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Rob Sandwith, Chief Executive

Summer is here and with it a new Finance Act and Mr Blair's third term to look forward to. Independent commentators suggest we are in for further tax increases and so identifying investment opportunities with tax exemptions makes greater sense than ever.

For those with children born since September 2002, the CTF offers an opportunity to invest £1200 p.a. together with an initial gift of £250 from the Government. This could provide a tax-exempt fund of over £40,000 on the child's 18th birthday – a very useful sum for further education bills, first wheels or 'broadening horizons' on gap years!

Autumn will see the release of the Turner Report on pensions, which is likely to include recommendations combining a higher state retirement age, greater government incentives to save, and possibly some form of compulsion for employers (along the lines of the Australian model where employers now have to fund 9% of employee salaries into a pension). To its credit, the current Government brings in a new pension regime from April next year which increases an individual's ability to invest – up to £215,000 p.a. with 40% tax relief – and at the same time brings wider investment choice, including residential property for the first time.

Our guide entitled 'Pensions – the new tax regime' explains the new rules and is available by contacting the office or emailing 'pensions@rosan-ifa.com' with your details.

I hope all our readers have a great summer.

Saving for the Future can be Child's Play

Giving children a financial boost when they reach adulthood is a priority for many. But finding the sort of money that will make a difference to an 18 or 21 year old can be a tall order.

To help with the cost of higher education or the deposit on a flat, you need a strategy. That means salting away funds in an environment where they can grow with minimum interference from the tax man.

According to the Children's Mutual, by 2023 it will cost over £41,000 to complete a three-year course. Getting on today's property ladder can cost around £160,000 – the average house price in Britain according to the Halifax. If the same house costs £300,000 in 2023, a 5% deposit would be £15,000.

What about a wedding? By 2023 the big day could cost £25,000.

There are many ways to save. Children born since August 2002 qualify for the Child Trust Fund. In other schemes there are ways to maximise tax benefits by

saving long-term. Of course, the tax rules could change.

How will you help your children meet their financial challenges?

in this edition. . .

Pensions, Planning and Property Purchase

The world of pensions will be transformed by the launch of the Inland Revenue's simplified pensions regime in April 2006. A huge volume of legislation and regulation will be replaced by a single set of tax rules for all tax-privileged pension arrangements, from large occupational schemes to individual stakeholder pensions. The reform has been widely welcomed, even if it is now not looking as simple as it did when the proposals emerged over two years ago. However, there is one area where the new rules will be less advantageous than today's regime: loans for commercial property purchase.

Under the *current regulations*, if you have a self-invested personal pension (SIPP), it can borrow 75% of the purchase price of a commercial property. Thus if your SIPP is worth £150,000, in theory it could buy a property worth £600,000 (ignoring expenses). 'Gearing up' in this way can be very attractive, because in most cases the interest on the loan should be covered by the rent.

Remember, it could ultimately be difficult to sell a property to generate pension benefits in retirement and the tax regime could change again. It is not generally possible to take benefits from a pension scheme before age 50 (or age 55 from 6 April 2010), and there are restrictions on how you can take the benefits.

Under the *future rules* from 6 April 2006, the picture will be very different. The maximum loan will be 50% of the net value of your SIPP. For example, if your SIPP is worth £150,000, it could only buy property valued at £225,000 (again ignoring expenses). That is less than 40% of what the current rules permit.

It is fair to point out that the new rules will permit much greater contributions to be made to the SIPP, but it could still take at least a couple of years for your SIPP to grow to the £400,000 needed to support a £600,000 purchase.

If you are thinking of buying commercial property in a SIPP, the message is clear: you probably should not wait for the new rules to arrive. In fact, it may be that the sooner you act, the better because:

- If you are going to transfer funds from other pension arrangements to build up your SIPP fund, that will take time;
- In today's tight commercial property market, finding the right purchase may not be quick. You do not want to be negotiating a price with a 5 April deadline looming; and
- Commercial property purchase is not something that can be undertaken overnight: your SIPP provider and mortgage lender will insist on adequate surveys, probably including a contaminated land survey.

The best news about the new regime and property purchase is that schemes will generally be allowed to buy property from connected persons – eg the scheme members. That is not allowed under the current rules.

Note: Small Self-Administered Schemes
The current rules for borrowing by small self-administered schemes (SSASs) are different from SIPPs. The maximum loan is, broadly speaking, 45% of the SSAS's value plus three times the regular employee and employer contributions. Thus the greater the contributions relative to fund size, the more the future simplified borrowing rule will bite. For example, if your SSAS is worth £150,000 and regular contributions are £50,000 a year, today's borrowing limit is £217,500, whereas the simplified regime will limit your borrowing to £75,000. So the advice is generally the same: do not delay.

Targeting Absolute Investment

Would you like a return that is higher than a building society or bank could offer on your cash?

The answer is obvious – of course you would, but achieving the desired result is not so easy. A golden rule of investment is that if you try to beat deposit interest rates, you have to accept some risk. How to achieve the additional return but limit that extra risk is the key question and it is now being addressed by a new generation of UK investment funds.

These new funds aim to achieve an absolute return, ie a total return that is higher than bank base rates, regardless of investment market conditions. They do not give you a 100% capital guarantee, but their structure and operation are designed to help protect your original investment as far as possible. So the value of your investment can fluctuate and you can lose some of your money.

The exact terms vary from one fund to another, but for example, one investment group's absolute return fund has its capital protection backed by its parent, a major German bank. In this case, the capital protection only operates every six months. You can access the funds in the meantime, but if you cannot risk any capital loss during the six-month period, you need to wait for the short six-monthly period of three days when capital security applies.

Absolute return funds are not in themselves new. Funds that target absolute returns have been around for many years, but access to them has largely been restricted to the institutions and the ultra-rich.

What has changed recently is that rules for publicly available funds, such as unit trusts and OEICs, have been revised to allow a greater range of investment strategies. The reform has

encouraged managers with experience of absolute return funds to make their expertise available to a wider audience. Past performance is not a guide to future performance.

The returns on these funds will never set the world alight – they typically aim for 2% to 3% above banks' base rate – but if they achieve their target, they should provide a better return than deposit accounts, even of the internet variety. But they do not offer the same degree of security. You take on some degree of risk to achieve that higher level of return. This promises to be a fast-developing area, so for the latest news of what is on offer, make sure you contact us. Not all products and services are regulated by the FSA.

Will You Get the Right Annuity Rate?

Nearly one in five new pension annuities are now arranged on an enhanced basis that reflects the ill-health of the purchaser, according to leading actuaries Watson Wyatt in March 2005. This means that the purchaser is receiving a better than normal rate. But normal rates are also coming down as a result because the remaining pool of standard rate annuity buyers is that much healthier.

If you are about to turn your pension fund into an annuity, check with us about what is on offer – for some companies you just need to be a smoker to qualify for their enhanced rates. Remember, once you have bought an annuity, it is almost impossible to change it. You should seek independent advice before making any decison.

Beware the Regulator

There is now a new pensions regulator called, appropriately enough, the 'Pensions Regulator'. The Pensions Regulator is pledged to be pro-active, whereas its predecessor, the Occupational Pensions Regulatory Authority (OPRA), was more reactive. If you employ five or more people, make sure that you have suitable pension provisions in place, or you could be one of the first to experience the regulator's new, improved powers.

Tax Deadline Nears

Sunday 31 July is the due date for the second payment on account for 2004/05 income tax and Class 4 national insurance contributions. One possible way to reduce the bill is to make a personal pension contribution now and backdate it to last tax year. However, this is the final year you will be able to do so – backdating will be a casualty of the simplified pensions regime.

Tax planning is not regulated by the FSA.

Watch Out for 59% and 77% Tax

You may think that the top rate of tax is 40%, but these days life is not so simple. The Chancellor's habit of tweaking the tax system has produced all sorts of different 'tax' rates, if you measure tax by what you lose from each extra £1 of income.

For a start, national insurance contributions will normally mean that the true top rate of 'tax' on your earnings is even higher than 40%. Then there is the potentially greater impact of Working Tax Credit (WTC) and Child Tax Credit (CTC).

The basic idea of tax credits was to target tax benefits onto people with low or modest incomes to encourage them to go out to work and to help with the costs of childcare. But the impact of these tax credits goes much further up the income scale than most people realise. When WTC and CTC were introduced in 2003, their effect on the tax system was not widely appreciated and many people wrongly assumed their earnings were too high to worry about tax credits. Since then, the picture has changed as both awareness and the credits have increased. Tax rules change.

If you are interested in finding out exactly how the WTC and the CTC can affect you, please contact us for a detailed analysis of your situation.

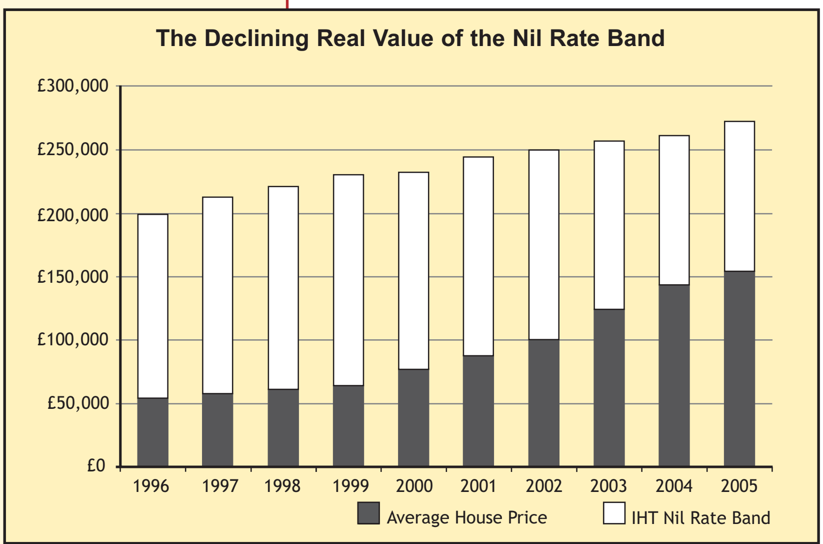
The point to appreciate is that you could be subject to an effective tax rate on part of your income of 59% or even 77%. And you might well not be aware of it – simply because for every extra pound of income you earn, you pay tax and lose part of your tax credit.

But if 77% or 59% tax is bad news, then the good news flip side is the potential for the same rates of tax *relief*. For example, a contribution to a pension will qualify for tax relief and, by reducing your taxable income, would also boost your tax credit entitlement.

An investment in an ISA could also reduce your taxable income and thereby improve your tax credit entitlement.

A Minor Easing on Inheritance Tax

In this year's Budget the Chancellor announced the inheritance tax (IHT) nil rate bands for 2005/06 and the next two tax years. The nil rate band is the threshold above which your estate is subject to IHT at the flat rate of 40%. For 2005/06 the nil rate band is £275,000, rising to £285,000 next year and a nice round £300,000 in 2007/08.



Sources: Taxbriefs and Tolleys, April 2005

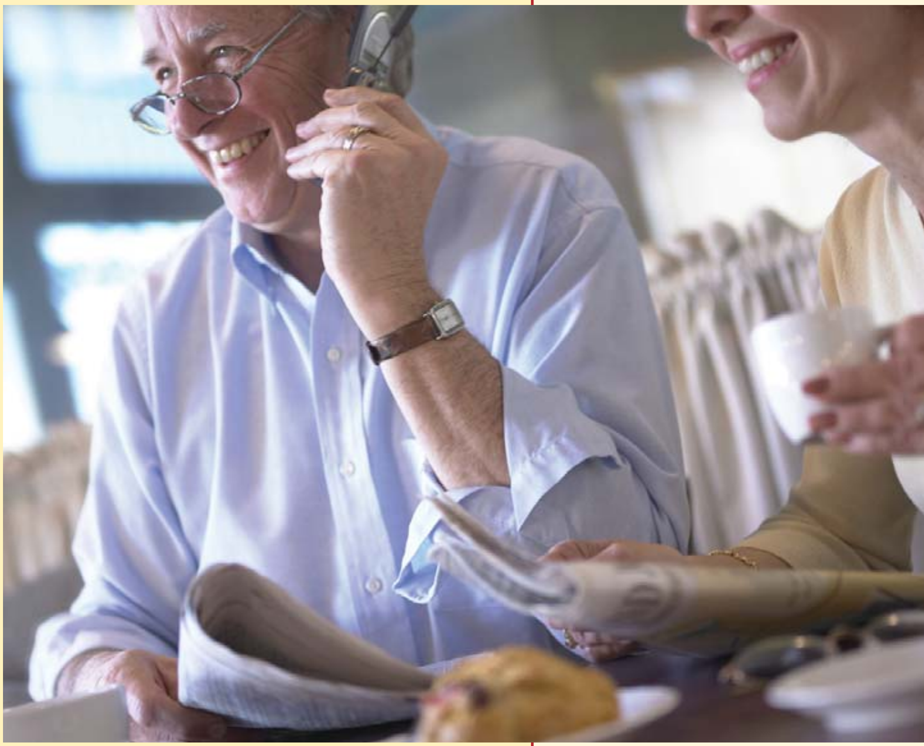
These increases average about 4.5% a year, which is more than the current rate of overall inflation and the government's target of about 2.5%. However, if you are a homeowner, there is little to celebrate. Since 1996, the increase in the nil rate band has singularly failed to keep pace with rising house prices, dragging more people deeper into the 40% tax band.

In April 1996, the average house price in the UK was just over a quarter of the then £200,000 nil rate band, according to Nationwide in March 2005. Today the average price of a house is more than half the amount of the nil rate band. In some parts of the country, the position is more extreme: in London the average price is now about 85% of the nil rate band, while the average detached house is now worth far more than the nil rate band.

Tax rules are subject to change, but if the value of your home – or other assets – means that your estate will be above the nil rate band, ask us for help. There are many IHT plans that could make a big difference. Not all products used in inheritance tax planning are regulated by the FSA.

Take Care With Retirement Income

If you are close to drawing the benefits of your pension plan, these are difficult times. Annuity rates remain at historically low levels because people are living longer than ever and long-term interest rates have seldom been lower in the last 50 years. Another factor is that next year's change in pension tax rules could mean you get more tax-free cash if you postpone retirement until after 5 April 2006.



So more than ever, specialist advice is an essential first step before you turn your pension fund into tax-free cash and an income that will last throughout the rest of your life. But whether you decide to draw benefits now or wait for the new tax regime, your choices will be as follows:

Fixed Annuities If you do not want to take risks with your retirement income, a fixed annuity could be your most attractive option. The company providing the annuity will guarantee payments, regardless of what happens to interest rates, investment markets or average life expectancies. But remember, once you have bought an annuity, it is virtually impossible to change.

An important decision is whether to fix your pension income or whether it should rise at a predetermined rate or be linked to inflation. An in-built increase can make good sense, because inflation erodes buying power. For example, in 12 years, inflation at 2.5% a year would cut the real value of a fixed-annuity by a quarter. But inflation protection is costly: for a 65 year old man, payments under an RPI-linked annuity will begin at little more than two-thirds of a level annuity. For a woman aged 60, the gap is even wider.

Investment Linked Annuities An investment-linked annuity does not provide a guaranteed income, or any guarantees will be very limited, so future income will fluctuate. This means investment-linked annuities are unlikely to be appropriate if they are likely to be your main source of income. But if your pension is just one income source then, by investing in real assets such as shares and property, you have the potential to outperform a fixed annuity, which invests in fixed-interest securities (or in index-linked securities if it is inflation-linked).

Within a broad range, you can choose the starting level of your investment-linked annuity. The higher your initial income, the smaller the scope for increases and the greater the possibility of reductions. Your initial pension and future income levels are dependent on the performance of the underlying funds. Remember past performance is not a guide to future performance and the value of investments can fall as well as rise.

Pension Fund Withdrawals Here your income is provided by regular withdrawals from your pension fund. Like the investment-linked annuity, fund withdrawals involve risk. Although your level of income will usually be fixed for the first three years, it could fall after that. So this option is not suited to everyone.

A major attraction of pension fund withdrawals is that the death benefits can be much higher than from an annuity. As a general rule, on death before age 75, there is a lump sum payable equal to the value of the remaining fund, after deducting a flat 35% tax charge. If the plan is set up under trust, the payment should normally be free of inheritance tax.

Beyond age 75 – assuming your 75th birthday falls after 5 April 2006 – you can continue to take withdrawals in a more limited form. While this means you avoid annuity purchase, continued withdrawals are unlikely to be advisable in many instances. The lump sum death benefit will no longer be available, but if you die leaving no dependants, your remaining fund can be transferred to another member of the same scheme (whom you can nominate). This transfer will probably be subject to inheritance tax, although the details are not yet clear.

Don't Let Your Child Trust Fund Voucher Gather Dust

Don't let your child trust fund (CTF) voucher gather dust earning no interest or growth. By now all vouchers should have been issued for children born before May 2005. Many of these seem to have been filed in the 'deal with later' pile, a common destination for Inland Revenue correspondence.

If you have not invested your child's CTF voucher yet, you are probably in the majority. Research published by Sainsbury's Bank in April 2005 suggested that three out of four vouchers had yet to be turned into investments. That delay could be costing your child money, because until the voucher is converted into a CTF investment, there can be no growth. The voucher itself is relatively small beer – most will be £250 plus a small interest compensation element – but that is not the whole story.

It is possible for you and/or friends and relations to add up to £1,200 a year to your child's CTF. CTFs have the same tax treatment as ISAs – no income tax on interest, no higher rate tax on dividends and no capital gains tax. Above all, you do not need to worry about the rules that mean the income from substantial gifts by parents to their children is taxed on the parents. Of course, tax rules can change.

To make matters worse, one year's top-up opportunity may disappear completely because of the way CTF's timings operate. Top-up years start with the child's birthday, so if your child has a birthday after 5 April 2005 but before you open their CTF, you will have missed one £1,200 top-up opportunity.

A CTF is a long-term investment – it will not mature until your child reaches 18.

Opening the CTF swiftly is important, but this does not mean you should rush to the nearest bank or building society without seeking advice. The evidence suggests that most CTFs will be deposit accounts, which could be another missed opportunity. A CTF is a *long-term* investment – it will not mature until your child reaches 18.

Over such a period, it may make sense to invest in something with real growth potential, such as share-based investments, rather than cash deposits (see 'A Long Term View of Investment Choices). While values may go up and down and it is possible you may not get back a significant proportion of your investment, the timescale means most short-term fluctuations do not really matter. Once the money has been invested in the CTF, it cannot be returned to the donor and it cannot be withdrawn until the child reaches 18.

There are 30 CTF providers according to the Inland Revenue and there is a range of funds and fund managers. To make the right choice, we can only repeat what the Inland Revenue says: 'If parents are unsure as to the suitability of a provider or their accounts they should seek independent advice'. And please, do it now, not later.

Levels, and bases of, and reliefs from taxation are subject to change.

A Long Term View of Investment Choices

Does it make sense to invest in shares? If you have your doubts after the past few years, take a look at the table below which shows the pre-tax annual returns from a variety of different investment classes to the end of 2004.

The results are good for terms of 20 years and longer, particularly when compared to cash, but more variable for ten years and less. In the last five years, which include the stockmarket's decline from its turn of the century peak, even money under the mattress earning no interest would have beaten shares. Past performance is not an indication of future performance. The value of shares and other investments can fluctuate and it is possible you may not get back a significant proportion of your investment.

If you feel hard pressed to draw any conclusions from these statistics, do not worry. They do not show that any one type of investment has been ideal at all times in the past. What they do reveal is that it pays to diversify across different investments rather than rely on one asset class. To make the point further, according to Investment Property Databank (IPD) in March 2005, the best-performing major asset class over the last one, five and ten years is not even shown in the table – UK commercial property.

Period to 31 December 2004	1 Year %	5 Years %	10 Years %	20 Years %	30 Years %	40 Years %
UK Shares	8.8	-5.4	5.0	7.2	10.5	6.1
Gilts	3.6	3.1	6.5	6.1	6.0	2.8
Corporate Bonds	3.3	5.6	8.5	N/A	N/A	N/A
Index-Linked	4.9	2.4	5.3	4.1	N/A	N/A
Cash	1.1	2.2	3.0	4.2	2.7	2.0

Source: Barclays Capital, February 2005

Company Cars – A Little Good News

If you have a company car, the chances are that the tax you pay on it will have increased this year because the CO_2 emission scales have once again been tightened. However, this year's March Budget did contain some good news for company car drivers.

The car benefit scales will stay the same for the next two years, so your car benefit tax will not increase unless you change to a car in a higher emission band or your marginal tax rate increases. However, there is one trap to watch out for – if you drive a diesel. The extra 3% diesel charge will apply for all new diesel cars registered after 31 December 2005, not just those older vehicles which do not meet Euro IV emission standards.

There was also some limited good news if you receive 'free' fuel from your employer: the base figure for calculating the value of the benefit was unchanged for this tax year. However, 'free' fuel is still an expensive benefit. If you are a higher rate taxpayer, the minimum tax you will pay is £864 and the maximum is over £2,000.

Unless your private mileage is high, it could pay you to give up 'free' fuel, particularly if your employer will compensate you for the loss, eg with higher pension contributions.

Whether to give up the company car is a more difficult decision. Like many company car drivers, you may not want to give up the peace of mind that comes with a company car, even if it could save you some tax. If you keep the car, then do not forget that there will be no company car when you retire. And the chances are that your employer will not count your company car as earnings when it comes to calculating your pension entitlement. Nevertheless the benefit clearly counts as earnings in the eyes of the Inland Revenue, so *you* can 'pension' it. Tax planning is not regulated by the FSA.

Student Debt Rises

£13,501 is the strangely precise sum representing the average amount of debt that this year's graduates in England and Wales will have on leaving university, according to Barclays in April 2005.

The figure is 12% up on last year, but is still well below debt levels that are expected for students in a few years' time. Today's graduates have faced annual tuition fees of a little over £1,000, whereas when top-up fees are introduced in autumn 2006, virtually all new students will be paying £3,000 a year.

The government originally set £3,000 as the upper limit for top-up fees, but a survey in the *Guardian* at the start of this year revealed only one college out of 85 that did not intend to charge the full £3,000. That response is hardly surprising given the precarious state of many universities' finances, but it does mean that graduate debt will be much higher by 2009, when the first graduates emerge with their student loans boosted by three years of top-up fees. An average total debt figure of over £20,000 seems likely.

Debt is already a worry or at least a concern for nearly two in five graduates. The average £13,501 debt is just over two-thirds of the starting salary of the average graduate. Not all of the debt is from the Student Loan Company, whose loans are relatively cheap to service. Students tend to borrow from friends and family as well and the average debt here is close to £2,500, according to the Barclays survey.

If you do not want your children (or grandchildren) to start their working life weighed down by education debt, the answer is to undertake some financial planning. Just as school fees planning is best started early, so too is funding for higher education. And, as with school fee funding, you (and the potential student) will have to accept that it may not be possible to cover all of the cost in advance. Fortunately, with higher education funding there is more scope to save tax, because your student son or daughter is unlikely to be paying much, if any, tax when they are at university. To take full advantage of this needs careful investment selection, so do speak to us before taking any action. Not all products and services are regulated by the FSA.

Invest Early, not Late

It is the same story every year: there is a rush to invest in Individual Savings Accounts (ISAs) at the last minute, just before that tax year ends.

'Use it or lose it' is the message about your ISA allowances in March, but there is also another message that gets forgotten in the following month: 'Invest early for maximum benefits'.

There is a simple logic behind starting your ISA early in the tax year. The longer your money is invested, the more it benefits from the ISA's favoured tax treatment. This is still worth having, particularly if you are a higher rate taxpayer and/or pay capital gains tax. If you do not have the cash available at present, it may make sense to sell an existing investment and then repurchase within the tax-efficient ISA wrapper. Before selling investments, seek independent advice as it may not be suitable and you could incur changes.

This year some of the rules for ISAs have changed. The little-used life assurance component has been consolidated into the stocks and shares component, so there are now just two ISA investment components – cash as well as stocks and shares. If you want to invest in two mini-ISAs rather than one maxi-ISA, then the limits are now £4,000 for the stocks and shares plan and £3,000 for the cash plan.

The current total contribution limit for ISAs is £7,000 per tax year, which the Chancellor announced in the Budget would stay until at least 2009/10, a year longer than previously planned.

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