

PENSIONS TAX TRAP

Don't get caught out withdrawing lump sums

ILLUMINATING FUND FEES

How to make sense of the acronyms

PLANNING YOUR LIFETIME GIFTS

How to make the best use of your nil rate bands



AUTUMN 2018

rosan helmsley
WEALTH MANAGEMENT

Quarterly Newsletter

Financing a child's future

Funding your children's path to adulthood is a long-term commitment



AUTUMN 2018

In this issue...

Welcome to the autumn edition of our newsletter, covering the latest developments as the country moves towards winter and the next Budget. Our feature story is about the lifelong journey of supporting children financially. We also look at lifetime gifts and possible changes to inheritance tax. For pensions we have essential advice for anyone planning their first lump sum withdrawal, and a look back at six years of auto enrolment. And for investment we offer help on decoding fund fees, and how to use market indexes in your investment planning.

03

Don't be caught by the pension tax trap

You may be over-taxed on your first pension lump sum withdrawal.

04

Financing a child's future

Supporting children financially is a long-term task that could need careful planning.

05

Auto enrolment six years on

Workplace pension membership is rising, but will your savings be enough in retirement?

06

Shedding light on fund fees

Despite efforts to improve the situation, fund fees are still complex to understand.

07

Thinking of making lifetime gifts?

The current generous treatment of gifts could be changed in the next Budget.

08

The ins and outs of market indices

Successful investment strategies should remember that companies in indexes can change regularly.

Back to school, and a 10 year old bull market

After a great British summer this year, many of us will now be focusing on a return to work, and for those with children in private schools or universities, looming education bills. The good news is that school fees rose this year at the lowest annual rate since 1994, though as always, school fee inflation rates bare little relationship to underlying CPI or RPI.

The average overall fee, excluding nursery fees, increased by 3.4% between 2017 and 2018. Boarding school fees average £33,684 this year and day school fees £18,750. If you are considering financing one or more children through a private education, then early planning is crucial and there are many naturally suitable investment schemes to help finance these liabilities.

ISAs remain the obvious first candidate, with an ability now to invest up to £40,000 per annum as a couple, you could expect to generate a fund over a decade of circa £600,000 with reasonable investment growth. All growth on ISA investments is tax free and any income taken from ISAs is also tax free.

Children might be able to assist their parents to a degree this year with Child Trust Funds (CTF) coming of age. Every child in the UK born between September 2002 and 2011 (when Junior ISAs took over), will have a CTF and if parents and grandparents had contributed the maximum investment of £1,200 per annum over the period (in addition to the Government's £250 or £500 contribution at outset), there will be an accumulated CTF fund of up to circa £25,000-£30,000 depending on investment growth. This sum will be particularly helpful for children planning a university education, where the education fees are now £9,250 per annum.

This week saw the extended bull stock market run reach a record 3,453 days – the longest in history without a single fall in prices of more than 20%. Inevitably, there are many pontificating a significant drop in equity prices. However, in my view, barring some geo-political event that will always have the capacity to disrupt markets, stock market values do not look over stretched.

The US market remains the most expensive on any valuation matrix at around 21 times earnings, but US earnings numbers are strong and generally continuing to significantly beat analyst's expectations. In addition, a much wider group of companies are contributing to earnings and revenue growth in the US – moving away from the narrow group of tech businesses that have dominated growth in recent years.

Our own UK market remains relatively undervalued against the US and other major markets, with the FTSE 100 on a PE ratio of 12.9 times and a dividend yield of 3.8%. In my view, once we emerge from the extended Brexit fiasco, the UK market is likely to get a positive re-rating.



The UK stock market offers relative value

This newsletter contains a number of articles on current topical industry and financial planning issues. Please do contact us if you wish to review any of the articles, or individual investment portfolios.

Rob Sandwith | Chief Executive

Cover image: iStock/pixdeluxe

This newsletter is for general information only and is not intended to be advice to any specific person. You are recommended to seek competent professional advice before taking or refraining from taking any action on the basis of the contents of this publication. The newsletter represents our understanding of law and HM Revenue & Customs practice. © Copyright 24 August 2018. All rights reserved.

PENSIONS

Don't be caught by the pension tax trap

Pension freedom rules that make it easier for investors to access their pension savings may lead to excessive tax bills.

The pension freedom rules allow anyone aged 55 or over to access their personal pension funds, but there are complicated rules on how withdrawals are taxed. If you are looking to cash in all or part of your pension, you need to check that you are not paying too much tax.

The difficulties can occur if you decide to take a one-off lump sum – an 'uncrystallised fund pension lump sum withdrawal' (UFPLS) – from your pension, perhaps to re-invest, to buy a holiday or to pay off debts. This differs from using a personal pension to provide a regular income, through a drawdown plan or annuity.

Your pension provider will apply an emergency tax code, which assumes you are withdrawing the UFPLS on a monthly basis – unless the company has an up-to-date tax code for you. If you aren't planning to take monthly amounts, it's likely you will be paying too much tax.

“ *If you aren't planning to take monthly amounts, it's likely you will be paying too much tax.*

TAX ON UFPLS WITHDRAWALS

For example, if you take a UFPLS of £10,000 from your pension at the start of the tax year, HMRC may assume you will take an income of £120,000 across the year from your pension and will tax you accordingly.

The first 25% of a UFPLS withdrawal is tax free. Then, using the emergency tax code to calculate the tax on the remaining 75%, HMRC would apply only 1/12th of the personal allowance (the amount of income you don't pay tax on – £11,850 in 2018/19) and assess the remaining payment against 1/12th of the appropriate income tax bands. So, for example, someone who should be a basic rate taxpayer could end up paying 40% tax, or even 45%, on a slice of their pension, and it could take some time to get back any overpayment.

However, as emergency tax codes are generally only applied the first-time people access their pension funds, one option is to make the first withdrawal a nominal amount, say £100. The emergency tax code will be applied, but this triggers HMRC to adjust your tax code and send an updated and correct version to your pension provider. Once the new code has been issued, any further, larger withdrawals are taxed correctly.

CLAIMING REBATES

If you are taxed on an emergency code, you may be able to claim a tax rebate at the end of the tax year through your tax return. You can also apply for a rebate during the tax year.

Figures published by HMRC show 264,000 people aged 55 or over accessed their pension during the second quarter of 2018. Many of these are likely to have been taxed at the emergency rate.

It has been reported that HMRC is only processing an average of 10,500 rebate claim forms each quarter. This suggests some people may not realise they have paid too much tax, or are unaware that they can claim a rebate immediately.

If you are planning to withdraw a lump sum from your pension, or are concerned about a recent withdrawal, please get in touch.

✦ *The Financial Conduct Authority does not regulate tax advice.*

Levels and bases of taxation and tax reliefs are subject to change and their value depends on individual circumstances.

Tax laws can change.

PLANNING

Financing a child's future

Funding a child's path to adulthood is a long-term commitment for parents.



Any new parent will tell you a child is expensive from the outset: there is so much to be bought to cater for a new member of the family.

But this is just the first step of many building up to a child's financial independence.

The first ongoing cost encountered is often childcare. There is some government help available, which varies across the UK, but these schemes come with specific requirements and often need supplements because of time constraints or exclusions. For example, 'free' childcare for three- to four-year-olds in England may only cover 38 weeks of the year and may not include costs such as lunches.

EDUCATION, EDUCATION, EDUCATION

The costs can jump dramatically at the next stage of education if you choose private schools. Average junior school day fees are £4,342 a term, while at the other end of the

journey, sixth form boarding school fees are £11,821 a term, according to an April 2018 report from the Independent Schools Council (ISC). School fees also normally rise faster than general price inflation: fees increased by an average of 3.4% from 2017 to 2018, the lowest rise since 1994. Education increasingly has costs attached for children at state schools as well, whether it be requests for materials from schools or technology requirements, such as laptops.

Thanks to reforms in tertiary education, costs can now rise further once university education starts. Again, the rules vary throughout the UK's constituent parts. Tuition fees are up to £9,250 for English residents at English universities, £9,000 for Welsh residents at universities in Wales, £4,160 for Northern Irish residents at universities in Northern Ireland but nothing for Scottish residents attending Scottish universities. Fees are typically financed

by loans, which also provide for student maintenance. This is often the first time a young adult will manage their own finances.

OUT INTO THE WORLD?

The result is that graduates can emerge into working life with significant debts, to be repaid out of earnings. For example, in England, repayment is set at 9% of income above £25,000 a year (for a plan 2 loan for courses started on or after 1 September 2012), and loans carry a variable inflation-linked interest rate, currently up to 6.3%. The relatively high interest rate and, in England and Wales, a 30-year write-off period for plan 2 loans, mean that five out of six student loans will never be fully repaid, according to the Institute for Fiscal Studies.

Student debt, potentially running on until a graduate reaches their early 50s introduces another issue for parents supporting their

PENSIONS

Auto enrolment six years on

Pension savings have grown after six years of automatic enrolment, but more progress is required to provide most people with adequate funds for retirement.

“ *The relatively high interest rate and, in England and Wales, a 30-year write-off period, mean that five out of six student loans will never be fully repaid.*

Automatic enrolment has sharply reversed the downward trend in workplace pension membership, which hit a low of 55% in 2012. Membership was at 84% in 2017 according to the Department for Work and Pensions.

In April 2018 the overall minimum contribution rate – normally made up of employer and employee contributions – rose from 2% to 5% of band earnings (£6,032 - £46,350 in 2018/19), with another increase to 8% due in April 2019.

The impact of automatic enrolment is welcome, but it is no guarantee of adequate retirement provision. For

some, the state pension (up to £164.35 a week in 2018/19) and their auto-enrolled pension may be enough once work stops. But for many others, such as those with patchy employment records or who are already close to retirement, it won't.

If you are worried about your retirement, start by asking us to project what your current pension arrangements may produce.

✦ *Occupational pension schemes are regulated by The Pensions Regulator.*

The value of your investments, and the income from them, can go down as well as up and you may not get back the full amount you invested.

children: funding the first home. The so-called 'Bank of Mum and Dad' has come to the fore in recent years as many first-time buyers have to rely on family assistance to gather enough for a deposit.

The picture that emerges is one where a child will need varying degrees of financial support for perhaps the first 25 years of their life. There is no single way for you as a parent – or grandparent – to handle these demands. In some instances, outright gifts may be the answer, whereas in others the use of investment via trusts or even drawing on existing pension arrangements may make sense.

The key to any solution is to start planning as soon as possible with professional advice and to integrate the process into your overall financial strategy.



INVESTMENT

Shedding light on fund fees

Despite renewed pressure on fund managers to be more transparent on fees, the jargon can make it hard for investors to understand exactly what they are paying.

Fund factsheets can contain a mix of different acronyms, but the most important is the OCF – the Ongoing Charges Figure. The OCF includes the annual management charges on the fund (also known as AMC), as well as a variety of other operating costs and administration costs.

All regulated funds now must display their OCF, which is expressed as a percentage. This makes it a useful way to compare charges between different funds. If a fund has an OCF of 0.5%, this means at least 0.5% of the value of your fund is paid to the manager each year in charges. There will be additional costs to pay on top of this, explained below.

Remember, this charge is applied to the total value of your fund, including investment growth. It is not just a percentage of the contributions you have paid in.

KEEPING UP TO DATE

If you have been investing for several years you may remember the 'Total Expense Ratio' (TER), which was supplanted by the OCF in 2012. The two terms are broadly similar – both include the AMC plus some other fund expenses. The main difference is that the OCF includes some additional charges, such as the cost of producing reports and the fund manager's research costs.

A 'Total Expense Ratio' implies that this includes all costs paid by the investors, which is not the case. Unfortunately, the OCF is also a slightly misleading name as it does not include all fund charges.

The OCF represents the ongoing costs to the fund, which includes the AMC and other charges for services such as keeping a register of investors, calculating the price of the fund's units or shares and keeping the fund's assets safe.

“ *The OCF is a slightly misleading name as it does not include all fund charges.*

However, the OCF leaves out the transaction costs of buying and selling assets within the fund, including any commission paid to stockbrokers, dealing charges and stamp duty – which is levied on the purchase of nearly all UK shares.

These costs vary significantly from fund to fund, partly depending on how frequently the manager buys and sells shares. Since January 2018 fund managers have been required to include information on their transactional costs alongside the OCF. Transactional costs are projected based on previous actual dealing charges and can be a useful way for investors to understand what these additional expenses might be.

The new figures won't include any initial charges, nor the cost of buying and holding a fund through a platform.

If you would like to discuss your investment choices further, please get in touch.

+ The value of your investments, and the income from them, can go down as well as up and you may not get back the full amount you invested.

Past performance is not a reliable indicator of future performance.

Investing in shares should be regarded as a long-term investment and should fit in with your overall attitude to risk and financial circumstances.



TAX

Thinking of making lifetime gifts?

If you are considering making gifts, make sure all your inheritance tax (IHT) liabilities are covered.

Today's treatment of lifetime gifts is extremely generous, which is why interest in IHT has increased ahead of the Budget. If you make an outright lifetime gift to an individual:

- There is no immediate IHT charge, regardless of its size;
- There is nothing to report to HMRC (unless you die within seven years);
- If you survive seven years, there is no IHT to pay and the gift is outside your estate; and
- If you die more than three years after making the gift, any tax payable on it may be subject to taper relief.

Different rules apply if the gift is being made to a trust, but the net tax result will be generally much the same unless the gift exceeds your available nil rate band.

A point to consider when making lifetime gifts is the potential effect on the remainder of your estate. Any gift could reduce your available nil rate band if you do not survive for the following seven years, so your remaining estate may suffer more tax than you might expect. The example highlights the issue.

A simple way to address the problem is to arrange a seven-year term assurance to cover the extra tax on early death. For lifetime gifts that come to more than the available nil rate band, special 'inter vivos' cover can be set up to match the sliding scale of tax liability.

ALTERNATIVE INHERITANCE TAXES

The Office of Tax Simplification has been



Any gift could reduce your available nil rate band if you do not survive for the following seven years.

considering the simplification of IHT and while this simplification could mean less administrative hassle, it could herald more reforms.

The final report of the Resolution Foundation Intergenerational Commission this year has suggested introducing a 'lifetime receipts tax'. This tax would replace IHT and would be payable on lifetime receipts of gifts or inheritance in excess of an allowance of £125,000 (rising with inflation). The tax rates would be lower than the current 40% IHT rate, but the various reliefs would be restricted. The net effect is forecasted to raise an extra £5 billion in tax, almost equal to the current revenue from IHT.

If you are contemplating pre-Budget gifts, make sure you ask us about your liabilities.

EXAMPLE

Lifetime gifts and the nil rate band

Hilary has an estate of £600,000 and all of her nil rate band available. She gives her niece Ann £300,000. She then amends her will to leave her residual estate to her nephew, Andrew, who is at present going through a divorce. Two years later, Hilary dies:

- Ann's £300,000 has no other allowances to offset against the gift, but is covered fully by Hilary's nil rate band, (which is £325,000 in 2020 because the band is frozen until at least 2021/22).
- Andrew's legacy has only the remaining £25,000 of nil rate band to offset against it. There is therefore an IHT bill of £110,000 on the rest of the estate, leaving Andrew with a net £190,000.

✦ *The Financial Conduct Authority does not regulate tax advice.*

HM Revenue & Customs practice and the law relating to taxation are complex and subject to individual circumstances and changes which cannot be foreseen.





TAX

iStock / ChesireCat

Are you in the top 10%?

In May, HMRC released data about the top 10% of income earners.

The top tenth of income earners is projected to be anyone with an income of at least £57,500 in 2018/19. HMRC estimates that this 10% will pay about £110 billion of income tax, just under 60% of the total for 2018/19, compared to £81 billion and 53.5% in 2010/11.

The statistics reinforce the feeling of many higher earners that they are paying a growing share of tax. Above-inflation increases in the personal allowance have been matched by frozen, or barely moving, thresholds at the other end of the tax scale.

If you want to cut your tax bill, the HMRC statistics suggest you should seek professional advice, not wait for the Chancellor.

✦ *The Financial Conduct Authority does not regulate tax advice.*

Levels and bases of taxation and tax reliefs are subject to change and their value depends on individual circumstances.

For specialist tax advice please refer to an accountant or tax specialist.

INVESTMENT

The ins and outs of market indices

Stock market indices change more than you might imagine - despite their iconic image.

The well-known Dow Jones Index consists of a select group of just 30 companies. General Electric (GE) - was a founder member of the Dow Jones Index in 1896. Until late June, GE had been a continuous Index member for over 110 years, but it has now been replaced by Walgreen Boots Alliance, a pharmaceutical retailer. As is often the case with index demotions, GE had gone through a hard time and its share price fell by almost half in 2017.

In the same month that GE and the Dow Jones Index parted company, MSCI, another leading index provider, made some important announcements and changes. The MSCI Emerging Markets Index (EMI) is a key yardstick for measuring emerging market performance; about \$1,900 billion of money either tracks or is benchmarked against the MSCI EMI.

In June, a first round of Chinese mainland shares (A shares) were added to the EMI, and more will be included later this year. Then further adjustments to the EMI are scheduled for 2019:

- Saudi Arabia will be added, with a weighting of approximately 2.6% of the Index.

- Argentina will return to the Index. It was a member of the EMI until 2009, when it was demoted to the Frontier Market index in the wake of a financial crisis in the country.

UK MARKETS

FTSE Russell undertook its quarterly review of the FTSE 100 Index in June. This failed to produce one widely predicted change - the replacement of the High Street retailer Marks & Spencer (M&S) by the online-only grocer, Ocado. Ocado did enter the FTSE 100, but M&S survived for another three months.

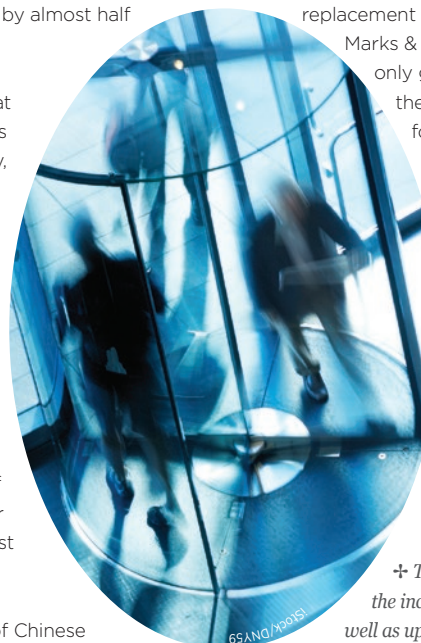
Whether you hold index-tracking funds or active funds which try to beat their benchmark index, June's changes are a reminder that indices are by no means fixed.

Let us know if you would like to discuss your investments in light of these changes.

✦ *The value of your investments, and the income from them, can go down as well as up and you may not get back the full amount you invested.*

Past performance is not a reliable indicator of future performance.

Investing in shares should be regarded as a long-term investment and should fit in with your overall attitude to risk and financial circumstances.



rosan helmsley
WEALTH MANAGEMENT

Rosan Helmsley Ltd, 1000 Cathedral Square,
Cathedral Hill, Guildford, Surrey, GU2 7YL

01483 90 40 40 | www.rosan-ifa.com

Rosan Helmsley Ltd is authorised and regulated by the Financial Conduct Authority (FCA).