CHANGES TO INHERITANCE TAX?
Simplified rules could alter your estate planning

SPOTLIGHT ON STUDENT FINANCING
Post-18 education review may lead to a shake-up in university fees

MANAGING THE FLOW
Future-proofing your retirement finances

rosan helmsley
WEALTH MANAGEMENT

AUTUMN 2019

Quarterly Newsletter

Taking the long view on your investments?

Holding steady in volatile times

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In this issue...

To say we're living in interesting times may feel like an understatement. It's almost impossible to avoid the headlines whether you focus on Brexit, international markets or climate change. But can that focus actually harm your long-term investment strategy? Recent research has shown almost three-quarters of investors are influenced by short-term political developments. However, as our feature explores, taking a long-term view may be more productive for your portfolio, and less stressful. We also investigate some developments on inheritance tax which could have important implications for your estate planning. And for those sending children to university this autumn, a report on the structure of student finances could play a role in future funding. With additional pieces on pension contributions and cash flow planning into retirement, that long-term view may work in more ways than one.

Cover image: iStock/Nikada

A time for reflection

Our job as wealth managers is fundamentally to focus on investment strategies and how best to meet client objectives through a range of investment solutions provided through asset managers around the world. The overlay of our deep experience in analysing the myriad of options available, and our close relationship with the asset management industry is what historically has driven our primary research and value add.

As I reflect on the last couple of years, it is certainly the case that our time is spent more and more on the influence of external factors on investment outcomes. Whereas the macro has always been an important part of the process, it seems to me that the current political situation is potentially distorting thinking both from our side as advisers and from our clients, many of whom are voicing very serious concerns about the future direction of the UK and it's political management. In 33 years as a wealth manager this month, I have never experienced a period where so much client interaction is driven by potential political outcome and the impact of this on accumulated wealth.

There is no doubt that here in the UK we should all be very concerned about the impact our parliamentary process is having on current events and perhaps more importantly, the potential outcomes on our financial futures. Globalisation and, to a degree QE, has had a very positive impact on those owning financial assets over the last decade – and as a result driven a wider gap between rich and poor.

This process is being challenged through politics around the world and the worrying dimension is the wider polarisation of views and policy that is creating further division, not unity, when unity and clever, inclusive thinking and leadership is what is required. I feel genuinely sad, and of course concerned as a custodian of invested wealth, that the leading political opposition party have announced this week and voted on a policy to abolish private education and enforce a right to buy for tenants in privately owned property. These are deeply Marxist policies borne from the leadership of a party who appear to care nothing for those who work hard and save for their financial futures. These policies, if introduced, will have a profound impact on investment in the UK.

The UK has always promoted choice when educating our children and a fundamental belief in capitalism has underpinned inclusive policy and the idea of meritocracy – these new policies are not conducive to these principles.

Capitalism, as we know it in this country, is under potential threat and, regardless of individual political persuasion, it is important to understand the ramifications a Labour government could have on those with invested assets. Seemingly, they would not be good.

A time for reflection

Understandably, the UK stock market remains historically very cheap and if there are positive outcomes to both Brexit and UK politics over the coming months, UK focused funds could actually perform very strongly over the coming two to three year period.

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

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TAX

Simplifying the inheritance tax rules

Major changes to inheritance tax (IHT) are proposed by the government's Office of Tax Simplification (OTS) which could alter your estate planning.

Inheritance tax is certainly complicated – especially for a tax that generates relatively little revenue. The OTS has spent some 18 months looking at it and has now produced two linked reports. The second and more important one, dealing with the structure of the tax, was published in July 2019, just as the man who commissioned it, Chancellor Phillip Hammond, was about to leave office.

The latest OTS report contains a wide range of proposals that could have a big effect on your estate planning. These include:

- You should only have to live for five years – not seven, as now – before a lifetime gift ceases to be subject to IHT. At the same time, the little-understood taper relief should also be abolished. This can reduce the amount of tax payable on lifetime gifts made more than three years before death, but it applies to relatively few estates.
- The rules for IHT business property relief (BPR) should be brought in line with those for capital gains tax (CGT), which would result in fewer businesses qualifying for the relief. Alongside this change, the CGT rules at death should be reformed.
- The current £3,000 annual exemption and the marriage/civil partnership exemption (up to £5,000 for parents) should be replaced with a new single 'personal gifts allowance'. The OTS made no specific recommendation but it pointed out that the annual exemption would now be worth just under £12,000 if it had been inflation-proofed since its last increase.
- The level of the small gifts exemption (originally set at £250 in 1980) should be reconsidered. Again, the OTS made no specific recommendation but it did say that inflation-linking would have increased the amount to just over £1,000.
- The rules for normal expenditure gifts should be reformed or should be replaced by a higher personal gifts allowance. This exemption is potentially valuable, but according to the OTS is regarded as confusing, difficult to claim and often not included in planning.
- Pay-outs under term assurance policies should be free of IHT. Currently, it is necessary to write such contracts under trust to keep them out of the policyholder's estate on death.

> *The latest OTS report contains a wide range of proposals that could have a big effect on your estate planning.*

Philip Hammond responded to the report by saying that "The government will consider the recommendations...and will respond in due course" The new Chancellor Sajid Javid will probably echo his view, although in the short term his priorities are likely revolve around Brexit.

Like most reforms, the OTS proposals would create winners and losers. To understand which category you would fall into, and any pre-emptive actions that can be taken with your financial planning, please talk to us.

✢ The value of tax reliefs depends on your individual circumstances. Tax laws can change. The Financial Conduct Authority does not regulate tax advice.

The Financial Conduct Authority does not regulate will writing, trusts and some forms of estate planning.

For specific tax advice please speak to your accountant or tax specialist.

INVESTMENTS

Taking the long view on your investments?

Trade wars between the US and China, as well as Brexit and tensions in various parts of the world have all made markets more volatile in recent months. Unsurprisingly, private investors have become more nervous.

A recent survey by leading investment house Schroders revealed that almost three-quarters of UK investors said they were influenced by political developments and market movements and checked their investments at least monthly. Nearly one in five investors said that they were waiting for the dust to settle before making investment decisions.

So is it the wisest choice to allow political uncertainties and market swings to colour your investment judgements?

FIVE-YEAR PLANS

Most investment experts agree that five years is the minimum period that an investor should expect to hold share or bond-based funds. And the longer the holding period, the more likely it is that funds invested in shares will outperform cash deposits or bonds – although there is no certainty that this will happen.

Over five years or more, most of the headline-grabbing news normally fades away or is overtaken by other events. The value of taking a longer-term approach is well illustrated in the table on page 5 from the latest Barclays Equity Gilt Study, published earlier this year. This shows the probability of UK shares outperforming UK government bonds (gilts) and cash (as measured by Treasury Bills) over various consecutive periods between two and ten years, based on real data tracking between 1900 and the end of 2018.

For example, UK shares outperformed cash deposits in nearly three-quarters (73%) of four-year periods over the 118 years; and shares outperformed cash in over nine out of ten periods of ten years.

Just over the past five-year period from the start of 2014 to the end of 2018, the UK experienced two general elections, two

istock/Nikada

referendums, the resignation of a prime minister and the arrival of Donald Trump in the White House. Despite all these upheavals, investors in UK shares who stayed the course received an overall return of 22.2% against just 1.8% from cash. Adjusting for inflation shares were 8.4% ahead over those five years, while cash lost 9.4% of its buying power.

> *A very small number of days have historically generated a surprisingly large proportion of total long-term returns.*

THE RIGHT DAYS

Of course, stock markets can fall and sometimes they can drop very quickly. But the rebounds from falls can also happen quickly and are likewise hard to predict. A very small number of days have historically generated a surprisingly large proportion of total long-term returns. Over the last 30 years to 2018, about 0.2% of days generate roughly half of total performance.

So if you come out of the market, you could be missing out on key growth moments. For example, the US stock market as represented by the S&P 500 index of large companies had an overall market return of 1,000% over the 30 years to 2018. Removing the 10 best days would halve the performance to just 500%. It is a similar story with the European Stoxx 600 – the less stellar long-term performance of a 470% increase over 30 years would have been halved by leaving out the 10 best days on which the market moved upwards the most.

Ignoring the short-term noise in favour of paying attention to longer-term developments has two other benefits:

- Your investment turnover will be lower, reducing overall costs; and
- You can stop worrying unnecessarily about the daily changes in investment values.

✢ 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.

	Number of consecutive calendar years				
	2	3	4	5	10
UK shares outperform £ cash	69%	71%	73%	76%	91%
UK shares outperform £ bonds	68%	74%	75%	72%	77%

Source: Barclays Equity Gilt Study 2019

TAX

Homing in on capital gains

Draft legislation confirms a further tightening of the rules on capital gains tax and your home.

The government has been reforming the tax system to make investment in residential property less attractive. Actions have included increasing stamp duty land tax (mirrored in Scotland and Wales), reducing tax relief for mortgage interest and, from next tax year, creating a 30-day time limit for paying capital gains tax (CGT) on any residential property sale profits.

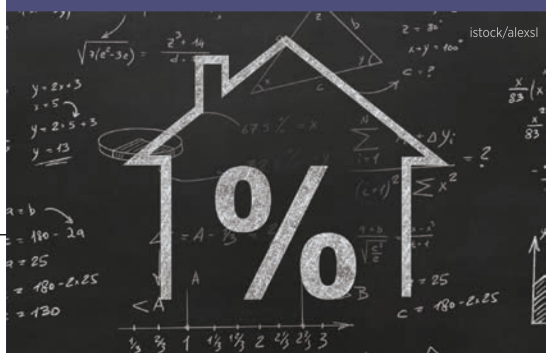
There will be two further new changes from April next year:

- A reduction in the 'final period exemption'. This is the period in which no CGT applies to a former main residence, and it will be halved to nine months in most circumstances. a problem if you buy your new home before selling your old one.
- Letting relief, which exempts up to £40,000 of gain from tax, will only be available if the owner remains in shared occupancy with the tenant. So it won't apply where the owner moves out.

The government's explanatory note says that "These changes are intended to make private residence relief fairer and...better targets... reliefs at owner occupiers, in line with broader tax strategy to promote home ownership".

If you are thinking of moving home but retaining your current property, both measures provide food for thought.

✢ The value of tax reliefs depends on your individual circumstances. Tax laws can change. The Financial Conduct Authority does not regulate tax advice.



istock/alexsl

EDUCATION

Time for a university fees shake-up?

A review of post-18 education in England has put student financing under the spotlight yet again – and could be the subject of another bout of reform.

The review was partly in response to growing criticism of the level of university tuition fees. But it also comes as new National Statistics methods mean that student financing will soon account for a substantially larger proportion of the national debt.

Fees vary throughout the four constituent parts of the UK, with England having the highest overall. English students will pay up to £9,250 wherever they study in the UK, unless they go to Wales, in which case the maximum is £9,000. Scottish students studying in Scotland remain free of tuition fees, while those from Northern Ireland who stay home only pay £4,160.

The review, chaired by Dr Philip Augar, suggested several major reforms. While these focused on the system in England, they could well prompt a response from other parts of the UK as well.

- The cap on university tuition fees should be reduced to £7,500 a year by 2021/22, frozen for 2022/23 and then should be inflation-linked from 2023/24.
- For new students from 2021/22, the annual income threshold at which loans start to be repaid should be cut from £25,000 to £23,000 (in 2018/19 values). The loan repayment rate should remain at 9% of income above the threshold.
- The maximum repayment term for new students should be extended from 30 to 40 years.
- A cap should be put on lifetime repayments at 120% of the initial loan amount, adjusted for inflation.
- Means-tested maintenance grants should be reintroduced and the eligibility thresholds revalued in line with inflation.

A surprising consequence of the proposals is that the total repaid by the highest-earning graduates would be less than under the current rules. But those on 'middle of the range' graduate earnings could end up paying a lot more as a result of the ten-year extension of the repayment term.

These proposals would change important aspects of student financing, but most graduates would still start their working lives with a substantial amount of inflation-linked debt. Some will end their working lives 40 years' later in a similar situation.

If you have children or grandchildren heading for university in the coming years, you should factor their education costs into your planning.

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PENSIONS

Workplace pensions – good start but not enough

This October marks the seventh anniversary of the start of workplace pension auto-enrolment, perhaps proving that some grand government schemes can be a success.

There was much scepticism when the first phase of automatic enrolment into workplace pensions began in October 2012 – an earlier attempt to encourage workplace provision through the launch of stakeholder pensions had been a failure. After the initial phase focused on the largest employers, there was doubt around how small and micro-employers would handle the administrative burden.

INCREASED PARTICIPATION

As it turned out auto-enrolment has hugely increased the number of people in workplace pensions. Back in 2012, before the start of the initiative, only about four out of ten eligible private sector employees were members of workplace pension arrangements.

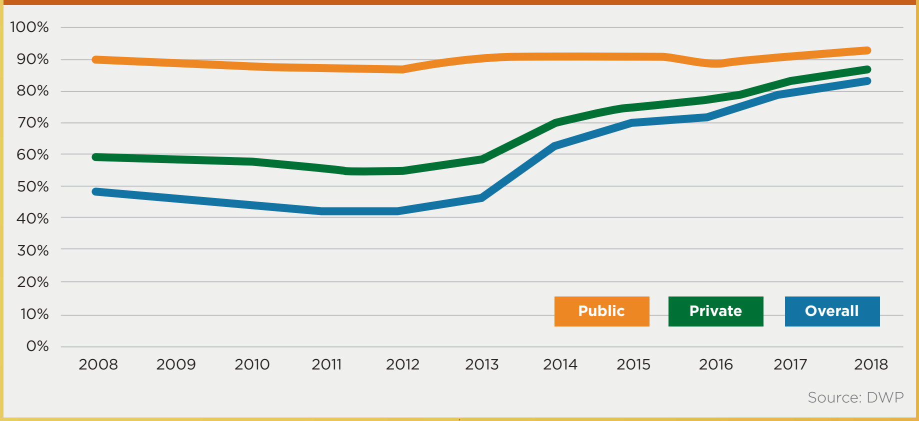
By April 2018, nearly nine out of ten eligible employees were workplace pension members (85% in the private sector, 93% in the public sector), according to recently issued figures from the Department for Work and Pensions (DWP). A sharp rise in the minimum level of overall contributions from April 2018 does not appear to have dented employee enthusiasm. Another minimum contribution increase took effect from this April, seemingly with similar acceptance, although there are no firm figures yet.

CONTRIBUTION GAP

Pension contributions for employees are still too low however and need to be increased, as the government acknowledged in a review issued in late 2017. The review suggested that around 12 million people were "under-saving for their retirement", with most of those under-savers earning more than £25,000 a year.

Higher earners are more likely to be not contributing enough because there is no longer any earnings-related element to the state pension. The new flat rate state pension introduced in April 2016 (£168.60 a week in 2019/20) represents a smaller proportion of earnings at retirement for those on higher pay.

ELIGIBLE EMPLOYEE PARTICPATION IN WORKPLACE PENSIONS APRIL 2008 – APRIL 2018



Source: DWP

However auto-enrolment has left one sector of the working population untouched – the self-employed. Their numbers have been growing rapidly – think gig economy – to the point where they account for about 15% of the UK labour force in 2017. Yet pension participation among the self-employed has fallen. According to the DWP, "the self-employed group has seen a continuous decline in [pension] participation from 27% in 2008/09 to 15% in 2017/18".

MEETING THE GOALS

The government will probably find some mechanism to raise minimum contributions again, although this may not happen until the middle of the next decade.
Meanwhile:

- If you are an **employer**, remember that every three years, or earlier if they meet certain criteria, you must re-enrol any employees who have left your pension scheme.
- If you are an **employee**, talk to us about whether you need to pre-empt that contribution increase to meet your retirement goals.
- If you are **self-employed**, make sure that you are not among the 85% who do not contribute into a pension.

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PROTECTION

Mind the insurance gender gap

Women generally insure themselves for much smaller sums than men, although both buy life insurance and critical illness cover in roughly equal numbers.

The average level of cover for a man's life insurance policy is around £130,000, but only around £85,000 for women's policies, according to an analysis of policies by software company IRESS. The gap is even larger with critical illness policies, which pay out if you are diagnosed with one of the listed critical conditions. Here, the average cover taken out by women is, around half the average cover for men.

On average, women earn less than men, by about 10% according to the latest gender pay gap figures. But that isn't enough to explain the huge difference in levels of cover, which indicate that women seem at higher risk of being under-insured than men.

Insurance experts say couples tend to buy more life insurance for the higher-earner. But both partners should have adequate protection — most families depend on two incomes and a reasonably equal share of childcare.

PLANNING

Future-proofing your retirement finances

The unknowns in your financial outlook can always shift, especially when you come up to retirement.

One of the best tools for looking at the future is using long-term cash flow planning to project your expenditure and the income you'll need to meet it. You may not be able or wish to continue working to shore up against future financial challenges, so estimating your likely expenditure before considering your potential sources of income and capital over the coming years is a good place to start.

CHARTING EXPENDITURE

Balancing this equation becomes even more important as you think about how stopping or reducing work will impact on your lifestyle and spending habits. Housing is a major issue. You may have paid off your mortgage, but you might want to move to another property or even another area or country.

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For many people, early retirement is a time for high activity levels in terms of travel, social life and pursuing interests; later this might reduce as they decide to take life easier.

Your expected levels of expenditure will vary as these assumptions change. It helps to define your expenditure as core and essential – such as utility bills which are unavoidable – and what could be dropped if the financial resources were not there to cover it, such as eating out regularly.

MAPPING INCOME SOURCES

The other side of the picture is assessing the income and capital resources with which to meet your expected outgoings. These could include earnings from work, state and other pensions and rental income, as well as total returns from savings and investments. It makes sense to explore a range of scenarios for investment performance across your different sources of income. Projections can range from the very positive to the more pessimistic.

The actual cash flow projections will map these potential expenditure and income outcomes to show whether you are likely to have a deficit or a surplus over your expected lifetime.

For a surplus, you might want to consider whether to increase your expenditure, which could include making gifts to your family. A deficit forecast may mean you should reconsider your spending plans and see where you can make cost savings. If you have the choice, you might want to rethink your retirement date and focus on additional pension or other saving.

It is hardly surprising that long-term cash flow modelling has grown into one of the most valuable tools for financial planning.

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