LFAMONEYTALK

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Are you losing money in cash ISAs?

A recent report reveals the true scale of losses people who keep their long-term savings in cash ISAs have suffered, compared with those taking a more diversified investment approach.

A recent report by Royal London highlights the fact that many people are using cash ISAs for their long-term savings, building up significant cash sums by adding to them year-on-year. And, the report suggests, they could be losing out substantially as a result. This highlights the dangers of holding long-term savings in cash.

£1,000 now worth just £910

The problem stems from the fact that although inflation has been low for some time, the cost of goods and services is still rising faster than the very low returns being paid on cash accounts (on average less than 1% each year since 2010). This means that although cash does slowly grow in these accounts, its buying power has been – and continues to be – gradually eroded. The report estimates that funds in cash ISAs have lost more than 9% of their purchasing power over the last 10 years. In other words, if £1,000 had been deposited in a cash ISA ten years ago it would now be worth less than £910 in real terms.

What are the alternatives?

People are often reluctant to put their savings into more complex investments like stocks and shares, seeing this as too risky. However, the report specifically compares investment in a cash ISA with investment in a 'multi-asset fund', which spreads your savings across a broad range of investments. The idea is that while some of your investments may drop in value during a particular period, others may do well, balancing out the overall returns over time. So while the value of multi-asset funds can fluctuate, they don't tend to experience the very high volatility that can hit riskier investments. The research shows that multi-asset funds have consistently outperformed cash deposits since 2008, making them more attractive for long-term savings.

£1,000 could now be worth £1,300

The report estimates that if the £1,000 mentioned earlier had been placed in a multi-asset fund rather than a cash ISA, its purchasing power could have increased by more than 30% in real terms. In other words, if you had invested your £1,000 in a multi-asset investment fund ten years ago, it could be worth more than £1,300 in today's values.

So, while it may still be wise to maintain some emergency savings in a cash account, you might consider placing your long-term savings in a well-managed and diversified multi-asset fund. There is a wide range of funds from which to choose, but not all are expected to deliver better returns than cash ISAs.

You could consider multi-asset funds that are constructed and managed to deliver consistent and anticipated customer outcomes within an entirely appropriate risk framework, thereby delivering customer expectations over the long term without causing sleepless nights along the way. To ensure that any funds you invest in reflect a suitable level of risk, and that they are aligned to your individual needs and circumstances, it's important to seek professional financial advice before investing.

Also in this issue

Find out more

To find out whether your savings are losing their value arrange a no obligation consultation with one of our professional financial advisers.

Call Richard Cakans on 07946 438807 or email richard.rakans@lighthousefa.co.uk.

It's time to talk about inheritance tax

HMRC recently published statistics revealing that the amount paid in inheritance tax has risen from £2.4bn in 2009/10 to £4.7bn (provisional) in 2015/16. That's a staggering 96% increase.

Tax year 2009/10 isn't simply a random year. It is the year since which the inheritance tax nil rate band (the amount above which inheritance tax is charged) allowance has been frozen at £325,000 and it will remain frozen until 2020/21. As a result more families are being dragged into the inheritance tax net.

How does the nil rate band work?

Inheritance tax is a tax on the estate (the total value of property, money and possessions) of someone who has died. Any part of the estate that is left to a spouse or civil partner will typically be free from inheritance tax. However, when their spouse or civil partner dies there could be inheritance tax to pay on their estate.

When someone leaves their estate to people other than their spouse or civil partner, such as children or grandchildren, inheritance tax is payable on the amount that exceeds the nil rate band. Tax rules make it possible to transfer any unused nil rate band to the surviving spouse or civil partner.

What about the £1m nil rate band?

If you have seen reports suggesting a £1m nil rate band per couple then you might be scratching your head. A new, additional nil rate band called the residence nil rate band is being introduced. It broadly applies when you leave your house to children and grandchildren. The allowance is being phased in over four tax years starting at £100,000 per person in 2017/18 and rising to £175,000 in 2020/21. The residence nil rate band will be gradually withdrawn for estates with a net value of more than £2 million.

What can you do to reduce inheritance tax?

Making gifts while you are alive can reduce the value of your estate. Gifts to charities, gifts up to £3,000 in a tax year and regular gifts out of income can all be immediately exempt from inheritance tax. This is useful if you have surplus income and, for instance, you make regular pension contributions on behalf of family members. You reduce the future inheritance tax bill and the recipient can enjoy a boost to their pension and tax relief. Other 'one-off' outright gifts are exempt, if the donor survives for seven years or more.

Using a flexible trust could be an option

If you need to remove larger amounts from your estate it may be appropriate to make gifts using a flexible trust where the trustees have control over who benefits and when. While this can be an effective strategy, it is a complex area and you should take professional financial advice before doing anything. A professional financial adviser can recommend inheritance tax planning strategies appropriate for your circumstances and future financial needs. As usual, the sooner you start planning, the more options you are likely to have.

Tax advice which contains no investment element is not regulated by the Financial Conduct Authority.

Find out more

To find out whether you could reduce the amount of inheritance tax likely to be payable when you die arrange a no obligation consultation with one of our professional financial advisers.

Call Richard Cakans on 07946 438807 or email richard.rakans@lighthousefa.co.uk.

The residence nil rate band

Harry died in 2015 and left his entire estate to his wife Sally. There was no inheritance tax to pay on Harry's death. He had not used any of his nil rate band. When Sally died in 2016, her personal representatives claimed Harry's 'unused' nil rate band as well as her own, giving a combined nil rate band of £650,000. This was before the residence nil rate band was introduced.

Let's now assume that they both lived longer. Harry died in February 2016 and left everything, including his share in the family home, to his wife Sally. No inheritance tax was due on Harry's death. In December 2020 Sally dies and leaves her entire estate to her two children. The nil rate bands available on Sally's estate are:

Sally's nil rate band	£325,000
Harry's unused nil rate band	£325,000
Sally's residence nil rate band	£175,000
Harry's unused residence nil rate band	£175,000
Total	**£1,000,000**

If Sally had not had children or had left her estate to nieces and nephews then the residence nil rate band would not have applied to her estate.

Decision time for additional pensions

Once you reach the age of 55 you are able to access any pension provisions you have that are not based on defined benefits whenever you want. You need to think very carefully about when to do so and what you do with these additional savings, as getting it wrong could prove costly.

Even if you are a member of a defined benefits (previously known as final salary or career average) pension scheme, you may have additional voluntary contributions (AVCs), pensions from other employers that are based on defined contributions (previously known as money purchase) or have taken out a personal pension. If you do, you can take advantage of pension freedoms when you reach the age of 55. So what can you do with your defined contribution pension?

Exchange it for an income for life

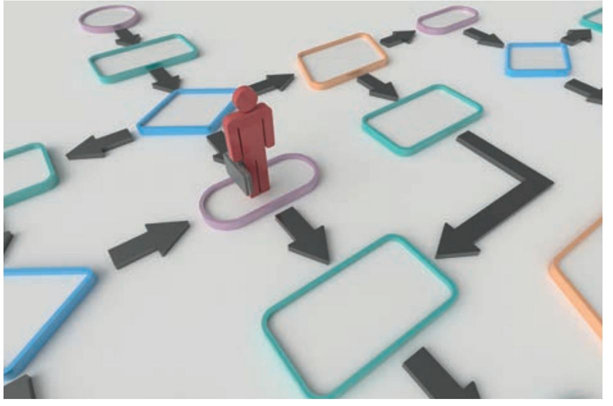
In other words buy an annuity. However, once you have done this you generally can't change your mind and you no longer own your pension fund. Also, you need to think about whether the income you get will keep pace with inflation – while it may cover your expenditure now, can you be sure it will do so in 10 or even 20 years' time? However, this might be an option to consider if you do not have a defined benefits pension that covers your regular expenditure when you retire.

Take all the money out

Only the first 25% of the money you take out is tax-free and if you take out more you could end up paying a lot of income tax and possibly moving to a higher rate tax band. You need to plan carefully to minimise the tax implications when you take income or capital from your pension. And clearly, the more you take out, the less you have for future needs.

Leave all the money in

You could do this if you are lucky enough to have sufficient income from other sources, for instance a defined benefits pension, and you want to pass on your pension fund to your loved ones.



A combination of the three options above

You could use part of your fund to secure any additional income you need and then draw the rest as income or capital as and when you need it or want to treat yourself. This may suit you if your defined benefits pension provides you with enough income to cover your regular expenditure.

The value of your investments can go down as well as up and you may get back less than you invested. A pension is a long-term investment and inflation will reduce how much your income is worth over the years. Your eventual income may depend upon the size of the fund at retirement, future interest rates and tax legislation.

Find out more

To discuss your options for accessing your pension arrange a no obligation consultation with one of our professional financial advisers.

Call Richard Cakans on 07946 438807 or email richard.rakans@lighthousefa.co.uk.

Passing it on

You are now able to pass funds remaining in your additional pension when you die, irrespective of whether or not you have started taking your pension, to any beneficiary you nominate. Pension funds generally fall outside your estate for inheritance tax purposes. However, your beneficiaries may have to pay income tax on the funds they inherit.

If you die before turning 75, they won't have to pay tax, providing that the money is paid to them within two years of your death.

If you die after turning 75, your beneficiaries will pay income tax at their highest marginal rate, unless the entire fund is withdrawn as a lump sum, in which case they will pay 45% tax (tax year 2017/18).

You therefore need to think about whether you should take income or lump sums from other assets before touching your pension, as this may be more tax-efficient. Also, pension funds are not taken in to account when calculating payment for long-term care.

Five things to put on your family protection ‘to do’ list

When you’ve got kids, you’ll do anything to look out for them. Yet a recent report shows many of us haven’t made plans to protect our children if we weren’t around any more – partly because it’s uncomfortable to think about.

The good news is there are some simple steps you can take to help protect them – from broaching the subject with your partner to making a Will. Here are five things to put on your family protection ‘to do’ list:

1. Start talking about it

In Aviva’s Family Finances Report, almost two in three people said they feel death is a taboo subject. Many also said they don’t want to talk about it because they just want to enjoy living their life.

It’s perfectly understandable that people prefer to avoid some topics of conversation, but if we can’t talk about something, it’s impossible to plan for it. So to get the ball rolling, pick a time and place when you won’t be disturbed and discuss things with your partner and/or immediate family. Once you start seeing making these plans as an unavoidable part of life planning, it becomes less of an emotional and more of a practical task.

2. Choose a legal guardian

Surprisingly, Aviva’s research shows more parents have a donor card than a formal, written plan of who’d look after their kids if they weren’t around any more. That’s why appointing a legal guardian is something a number of us ought to consider.

Put simply, a legal guardian is someone you appoint who will take care of your children if there’s no-one else with parental responsibility to look after them. It can be anyone over 18-years-old, so a family member or a close friend who has a connection with your children could be a good choice. While – thankfully – it’s unlikely that they’ll ever be needed, choosing a guardian really is a must-do. If you don’t appoint one and both parents die, your children could end up in foster care while the courts appoint a guardian of their choosing.

3. Make a Will

When you’ve discussed your plans and chosen a guardian, the appointment needs to be made official. One of the best ways of doing this is to make a Will, where you also say what you’d like to happen to your money, property and possessions when you die (otherwise known as your ‘estate’).

If you die without a Will, the law decides who gets what, and it may not be the people you’d have wanted. A Will can also help reduce the amount of inheritance tax that may be payable on the value of the money and property you leave behind – potentially leaving more for your children to enjoy.

4. Consider life insurance

Another way of helping to protect your children (and giving yourself some peace of mind) can be to take out a life insurance policy – as four in 10 UK families have done. In the same way that home insurance covers your property, life insurance covers you, and pays out if you die while you have the plan.

This means that if the worst ever did happen, your family may be able to use the money to pay for everyday bills and other expenses – helping them to maintain the lifestyle they currently have. Some life insurance providers will give you £15,000 of Free Parent Life Cover for one year if you have a child under four-years-old.

5. Get help from an expert if you need it

When it comes to making the sorts of plans we’ve mentioned above, the help of an expert can be invaluable. A professional financial adviser can help you work out what insurance you need and help you make sure you have appropriate paperwork in place.

Find out more

To check whether you and your family are protected financially against the unexpected arrange a no obligation consultation with one of our professional financial advisers.

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