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INDEPENDENT FINANCIAL ADVISERS

## MoneyMatters

November/December 2009

### **A time for giving...**

Discover the rules on how to pay less inheritance tax

### **What not to be unaware of...**

Women without cover expose their family's future

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### **Thinking of investing again?...**

What type of investor are you?

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# The Pension

## shake up

## How will it affect you?

Next year the pension rules are changing, how will it affect you and what are the options for those considering retiring when they reach 50.

Many people have no idea that they will not be able to take their pension from age 50 from 6th April 2010. From this date the Government is increasing the minimum age that you can take pension benefits, from 50 to 55, therefore now is an ideal opportunity to review your pension planning arrangements.

The change will affect anyone born after April 6, 1955, so if you are in this age category and are thinking of drawing on your pension fund, you need to think about taking financial advice.

Since A-Day in 2006 the pensions system was changed and it has been possible to get your hands on tax-free cash and convert some of your pension into an income while continuing to work and save. However, the options open to you depend on the type of scheme that you are in. If you have a personal or stakeholder pension then you should have the most flexibility. The maximum that you can withdraw from a pension as tax-free cash is 25 per cent of the value of your whole fund, for example, £50,000 of a £200,000 pension pot. The

remaining 75 per cent must be either moved into an income-drawdown plan or used to buy an annuity. Drawdown, officially called an "unsecured pension", enables you to leave your fund invested with the option of drawing an income, or not each year. You must take the tax-free cash portion of the pension you are cashing in and if you move the rest into a drawdown plan, you can take an income of up to 120 per cent of the return that you would have received from an annuity, however, you do not have to draw an income if you do not need it.

On the plus side, for those who do not plan to retire and who have suffered a big decrease in the value of their pension funds due to the stock market turmoil over the last year, you do not have to do anything. You can still top up your pension funds and make contributions, so the change in retirement age does not mean an end to pension saving.

There is a lot to take in if you are in that "fifty-something" age bracket and planning for your retirement, so make sure you contact your financial adviser to help you choose the best option available to suit your individual requirements.

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

**To discuss how you can get the most out of your pension planning, please contact us for further information.**

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# Thinking of investing again

## What type of investor are you?

Everyone is playing a guessing game about the right time to start investing again. There are as many theories as there are pundits.

Is the recent rally in the stock market sustainable? If we are in for a recovery, will it be V-shaped (meaning a sharp increase), W-shaped (a rally followed by a dip before it really recovers) or a ladle (a longer time in the doldrums before it slowly climbs up)?

The real question is: what is your appetite for risk? Consider using the sleep test: if you can't get to sleep worrying about how your share-based investments are doing, then you probably have too much exposure to them.

The bigger the risk, the more potential there is for reaping rewards and for courting disaster. But no matter which type of investor you are, you can take certain actions to reduce the risk.

First, you should have six months' worth of living expenses in a savings account. Second, in turbulent times like these you should drip-feed your money in by saving regularly, so you don't have to worry about timing the market. Over the longer term, the ups and downs will be levelled out by regular investing.

Finally, spread your savings across the different asset types - shares, property, fixed interest and cash - and hope that if one falls the others will remain robust. However, all these asset classes have fallen in value in recent years, so there is no guarantee of future performance.

### Cautious

Even cautious investors face some risk. Advisers think this type of investor could have between 20 per cent and 30 per cent in equities, with an equal amount in fixed interest provided by corporate bonds and gilts, and the balance as a cash reserve. A cautious portfolio is low risk, not no risk. Only cash is as close to no risk as you will find and even then much can depend on the strength of the institution holding the cash. Even with cash holdings, unless you are earning more in interest than the rate of inflation, your capital will gradually be eroded.

Nervous savers poured billions into corporate bonds in the first quarter of this year. Here, the higher the yield, the more risk you take. Another favoured sector is UK equity income funds covering high-yielding shares, these absolute return funds, can profit from falling markets as well rising ones.

You can also buy a basket of shares through exchange traded funds (ETFs), which track a stock market or sector, such as the FTSE 100.

### Balanced

Moving up the risk scale, you could have 50 per cent in shares and between 20 per cent and 25 per cent in bonds. You can be a little more adventurous by adding global funds to core

holdings, with a touch of spice from the east and emerging markets, plus higher yielding bonds.

### Adventurous

If you have a strong stomach, you could put between 80 per cent and 100 per cent of spare cash into equities. The longer your time horizon, the more risk you can afford to take. A general rule of thumb is that your age expressed as a percentage should equal the amount of cash you hold in your portfolio. So a 20-year-old should have 20 per cent in cash and the rest invested, while a 40-year-old should have 40 per cent in cash, and so on.

In any event, re-evaluate your portfolio regularly and also seek professional advice when reviewing your investment strategy.

*To discuss your financial requirements or to obtain further information, please contact us.*

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# Corporate Bonds

## Are they still worth it?

With stock market volatility and the bounce back this year, investors have been pouring their cash into corporate bond funds in a bid to boost their income.

The rally in the credit markets has been impressive and UK corporate bonds have surged from the market trough in early March 2009.

With deposit rates at historic lows and the typical corporate bond fund paying an income, or yielding, in the region of 5 per cent, it is easy to see why they are appealing.

Latest figures from the Investment Management Association show that the corporate bond fund sector, achieved the highest net retail sales of any sector for the tenth consecutive month, after consuming £338m in August.

### So what are corporate bonds?

Corporate bonds are a form of debt issued by companies or governments.

When you purchase a bond, you are essentially lending the cash for a set period of time, during which time you will receive interest on your loan.

While the value of corporate bonds can fluctuate, the main risk to your capital is if the firm issuing the bond goes bust and defaults.

### Advantages of corporate bonds

Corporate bonds provide a consistent income stream, offer low volatility and they are good diversifiers for equities.

The asset class has lower volatility, which, when combined with their current return potential, makes corporate bonds particularly attractive.

### Credit spreads are still favourable

Credit spreads, the additional yield that you receive by holding a corporate bond, over a government bond, continue to look attractive. The spread on UK corporate bonds are still wider than the peaks seen in the previous cycle.

Spreads have narrowed sharply since mid-March with corporate bonds sharply outperforming Gilts and more out performance can be expected, as business conditions improve.

Past performance suggests that the average rate of default on investment grade, the superior high grade of corporate bonds is 0.15 per cent and even in 2008 amid high profile corporate collapses, investment grade defaults only reached 0.4 per cent.

### Spreading your risk

It is possible to invest in a single corporate bond rather than in a fund.

Investors must remember that going for a single bond, is the same as investing in a single share, the risk of losing your cash, is far greater. By investing via a bond fund, savers spread their risk across a wide variety of different companies.

### Better performance with low interest rates

Low interest rates have made the outlook for bonds favourable. With the base rate at just 0.5 per cent, a bond fund with a yield approaching 5 per cent looks attractive. However, investors should remember that a bond is not guaranteed in the same way cash savings of up to £50,000 are.

By keeping cash rates low, central banks are actively trying to encourage lending in the economy and hence investors look to put their cash to work in productive places.

### High yield bonds

High yield or speculative-grade bond funds have also delivered some exceptional returns. They have greater yields because they are positioned at the riskier end of the spectrum.

The companies issuing them are more at risk of going bust: they don't have as good a credit rating as larger more robust firms. Many advisers feel there is more to come from the sector but investors will also have to tolerate more risk.

### Bonds versus shares and cash

Investors should have a balanced portfolio of investments typically made up of bonds, equities and cash, so that they are never too exposed to one area.

Bonds offer protection against deflation and slow growth; equities perform better with inflation and fast growth. Importantly, the risk profiles of the two asset classes are very different, switching out of corporate bonds into equities, substantially increases the risk profile of an investment portfolio.

As with many investments, bonds versus shares is a balance of risk and returns. In a market rally, bonds will fail to keep pace with shares, but if stock markets take another hit, investors could find corporate bonds a safer place to be.

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# Act now or repent at leisure

## The Government pre-credit crunch levels set to return

Consumers are being urged to act now to benefit from the series of measures that were introduced to stimulate consumer spending before they are due to end this year.

Homeowners planning improvements to their properties and people looking to buy a new car risk losing out on the temporary 2.5 percentage point cut in VAT, which runs out at the end of December.

The government's car scrappage scheme, which offers a £2,000 lump sum if you trade in a car at least 10 years old, due to run out in February 2010 even with the government's extra £100 million funding.

And the abolition of stamp duty for property purchases worth up to £175,000 — rather than up to £125,000 — will also end in January 2010.

Experts expect a surge of activity in the next few months as consumers rush to benefit.

Here we look at ways to take advantage before the year end

### Home Improvements

The Federation of Master Builders is encouraging homeowners to finalise arrangements with builders now to avoid paying the higher VAT rate.

VAT was cut from 17.5 per cent to 15 per cent until the end of this year to help

stimulate consumer spending. Though the difference is small for most purchases, it could mean as much as £1,250 on a £50,000 home extension.

If you are making payments in stages, each instalment will have its "VAT point", when the tax is due. If the final payment is in 2010, you will have to pay this at the higher rate.

However, if you are planning a project now, you may be able to negotiate early payments, although this potentially puts you at risk if there is further work to be carried out after the payment is made. Builders can either send you an "application for payment" or a final invoice. With the application, the VAT point occurs only when the customer makes the payment. It means that if you are sent an application in December but fail to pay until the new year, you will be charged at the higher VAT rate.

### VAT on new cars

Drivers looking to buy a brand new car may have to pay at the higher VAT rate and may also miss out on the scrappage allowance scheme.

Many new cars, which are made to order, have a 12 to 14 week delivery time, meaning you should order as soon as

possible if you want your car before January.

Bills for new cars are usually settled on delivery of the vehicle. If this occurs in January, the higher rate of VAT is applied.

Those looking for smaller cars face the longest delays. Some models already have a January delivery time.

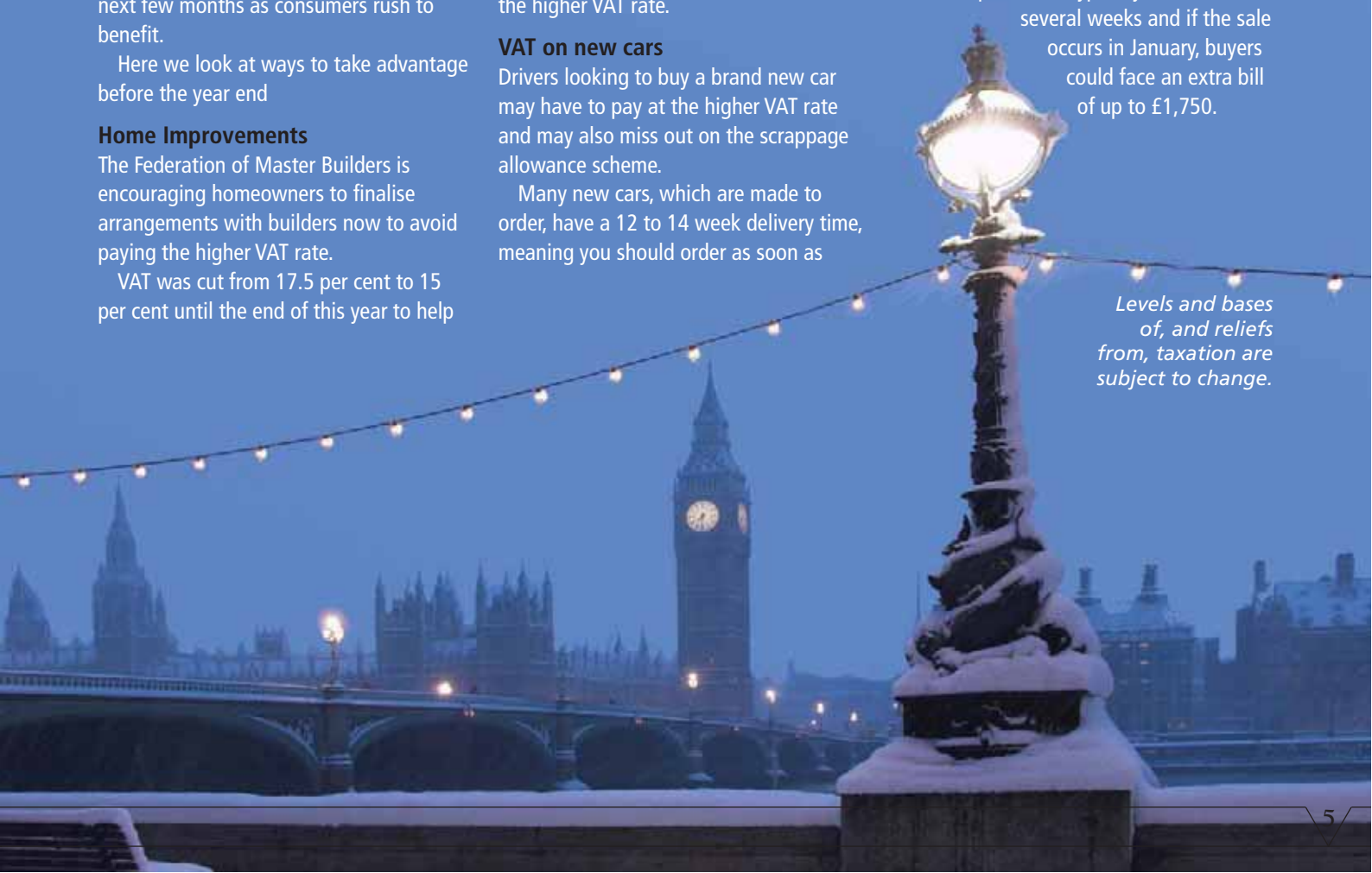
The best way to ensure you get your car delivered on time is not to specify added extras. Standard models with standard paint, speed up the delivery.

### Stamp duty

Stamp duty on properties valued up to £175,000 has been waived until the end of this year but analysts suggest up to 35,000 people may miss out. Previously, any property worth more than £125,000 incurred a 1 per cent charge on the entire value, and this rule is set to return.

House purchases typically can take several weeks and if the sale occurs in January, buyers could face an extra bill of up to £1,750.

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# The ISA advantage



## wonderful ways you can save tax

### **1. Basic rate income-taxpayers: save as much as £2,000 for every £10,000 income**

Basic rate taxpayers save 20 per cent income tax on interest from cash or fixed interest ISA. No saving on equity ISA, effective 10p tax paid on dividends before distribution.

### **2. Higher rates income-taxpayers: save as much as £4,000 for every £10,000 income**

Higher rate taxpayers save 40 per cent income tax on interest from cash and fixed interest funds and save 22.5 per cent income tax on dividend income from equity funds. For example, £100 gross dividend, £90 net dividend paid, if held direct, a higher rate taxpayer would pay an additional £22.50 in tax but if held within an ISA this is not paid.

### **3. 50 per cent income-taxpayers: save as much as £5,000 for every £10,000 income (2010/11)**

From April 2010, those whose income falls into the new 50 per cent band, above £150,000 of taxable income a year, save 50 per cent income tax on interest from cash and fixed interest funds. These super taxpayers save 32.5 per cent income tax on dividend income from equity funds.

### **4. For those earning £100,000 and over: save as much £2,590 on loss of personal allowance (2010/11)**

This is similar to age related allowances for the over 65s. ISA income is not only

free from further income tax but also does not count towards the new personal allowance "means" test. For those with taxable income of £100,000 or more, the personal allowance is eroded. For every £2 of income over £100,000 the personal allowance reduces by £1, completely extinguished by the time that income reaches £112,950 assuming that the personal allowance remains the same in 2010/11.

This is an effective tax rate of 60 per cent and for those with income of £112,950 will cost an additional £2,590 in income tax. However, ISA income does not count towards this personal allowance test saving up to £2,590 a year.

### **5. Capital gains taxpayers (CGT): save £1,800 for every £10,000 profit**

CGT is 18 per cent after annual exemption of £10,100 (2009/10). CGT is only paid when a fund is cashed in or gifted.

Neither taper relief nor indexation exists now for private investors since April 2008. You cannot "bed and breakfast" anymore, which is sell a holding then buy it back the following day to rebase the base cost with the aim to save CGT going forward. However you can "Bed and ISA".

Bed and ISA is where you sell a fund or shares to the value of £7,200 then re-purchase them in an ISA, through a fund supermarket. This is done at the same days prices. Future growth and income are free of tax.

### **6. Employees in Save As You Earn schemes: can transfer shares to the value of the ISA contribution at maturity free of CGT. Saving up to 18 per cent on the gains**

Employees have 90 days to transfer maturing shares from SAYE schemes to ISA, the value counts as the subscription, but following this there is no CGT or income tax on dividends to pay.

### **7. For those aged over 65, with income of £22,900 or more: save as much as £603 in income tax**

ISA income does not count towards the age related allowance "means" test. For those aged over 65, the personal allowance increases from £6,475 to £9,490. However, for every £2 of income over £22,900, the additional age related allowance reduces by £1, completely extinguished by the time that income reaches £28,930. This is an effective tax rate of 30 per cent and for those with income of £28,930 will cost an additional £603 in income tax. ISA income does not count towards this age allowance test saving up to £603 a year.

So whatever your circumstances, it certainly seems worthwhile investigating the possible advantages of opening an ISA.

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# A time for giving

## Discover the rules and how to pay less inheritance tax

### IHT rules

IHT is charged at 40 per cent on all the assets that you leave above the nil-rate band, currently £325,000. However, the tax is not payable when an estate passes between a husband and wife or from one civil partner to another. The unused part of the tax-free allowance can be transferred to the surviving spouse or civil partner. So, the heirs of a widow who inherited all of her husband's money would have to pay inheritance tax only on assets above a combined total of £650,000. The tax is also payable on certain gifts made within seven years before death.

### Taking action

If you believe IHT will be payable on your or a relative's estate, action now could save money. The easiest way around this tax is to make gifts during your lifetime.

All gifts made seven or more years before a death are potentially exempt transfers (PETs) and free of IHT. Where someone makes a gift and dies within these seven years, the tax is payable at the full 40 per cent if death is within three years, and on a sliding scale if between three and seven years.

Certain gifts are clear of the tax, regardless of when they are made, including all gifts or bequests to charity. You can gift up to £3,000 a year free of IHT, or £6,000 if you made no gifts in the previous tax year. A couple who made no gifts last year could therefore reduce their liability by £12,000 with one gift to their children. This is your "annual exemption". Gifts of up to £5,000 on a wedding or civil partnership may also be exempt.

A second allowance is the "small-gifts exemption", which lets you make gifts of up to £250 to as many people as you like in any tax year. Note, however, that you cannot combine the two allowances to give one person £3,250.

More significantly, regular gifts from income are exempt from the tax, whatever their size, provided they do not affect your standard of living.

There are also a number of ways to reduce IHT by setting up trusts. A discretionary trust is effectively a gift, the donor must live seven years to avoid the tax, but it enables trustees to keep control of the money.

### After a death

A proactive approach after a death can significantly reduce an IHT bill. If it looks like there is a good deal of tax to pay, your first stop should be a good solicitor. He or she will be able to spot any loopholes and help you to negotiate with the Revenue.

### The good Will guide

If you do not make a Will, your estate will be distributed according to intestacy law, rather than your wishes. This could mean that your money is left to other relatives as well as your spouse — creating unnecessary IHT liability.

Be aware that marriage revokes a Will. This can cause problems, as any children from the first marriage may receive less than expected.

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**Putting in place an IHT strategy can be very complex and you should always receive professional advice before proceeding.**



# The risks and rewards of unsecured pensions

## Investigate before you decide

Older people enjoy greater freedom than ever about how they draw benefits from their savings – but they must beware of the risks, as well as the potential rewards, of unsecured pension schemes.

The UK has experienced unprecedented stockmarket turbulence in recent years and the value of many unsecured pension investors' pension pots have plummeted.

That is bad enough, but those who continue to take high withdrawals could see a high percentage of their pension savings wiped out within just a few years. However, the stock market's strong rally this summer demonstrates that share prices can rise as well as fall, without warning and that the past is not necessarily a guide to future performance.

An unsecured pension allows people to take an income from their pension savings whilst leaving it invested in the stock market. It is an alternative to an annuity, which involves you handing your pension savings to an insurance company in exchange for a guaranteed annual income for the rest of your life.

There are many people who have invested in an unsecured pension since this new option became available to pensioners in 1995 and a portion of all retirement income is derived from unsecured pension contracts. Typically these funds are invested in a combination of shares, cash and fixed-interest investments such as bonds and gilts.

But experts are urging unsecured pension investors, depending on your circumstances, to consider temporarily stopping or reducing their withdrawals if stock markets suffer another severe correction, to avoid their pension capital being eroded. You should try to keep your withdrawals within the natural yields on your investments, for example; the interest made on cash, the dividends paid on equities and the rental income from property. This way you will not be eating into your capital.

After stock market setbacks, reducing income withdrawals may allow the underlying pension fund to recover. But it means you may have less money to meet expenditure.

The majority of unsecured pension

providers allow you to specify which assets you want your income to be drawn from. Where circumstances dictate selling assets, take advantage of this flexibility to encash the assets that carry the lowest risk first – cash and Government gilts. This way you should avoid crystallising stockmarket losses by selling shares after prices have fallen.

Another upside to unsecured pensions is that you retain control of your money, which means your partner or dependants will be able to benefit when you die. An unsecured pension can be extremely flexible: you can take 25 per cent of your pension savings as a tax-free lump sum when you set up a contract, even if you do not want to draw an income straight away.

While an unsecured pension enables pensioners to retain ownership of their capital and some degree of choice about how and when they draw income, annuities provide a guaranteed income for life; in return for immediate loss of capital.

It can be a difficult choice to make at any given time but at least people are now allowed to choose how they access their savings.

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The value of your investment and the income from it can go down as well as up and you may not get back a significant proportion of your investment. Past performance is not an indication of future performance. Please contact a suitably qualified financial adviser for further information or advice.



# Reassuring the bank of Mum and Dad

## *“Insure” parent loans are protected*

Parents helping their children onto the property ladder are advising them to take out insurance to safeguard against a fall in their retirement income.

Traditionally, it's always been parents who have had to insure their lives for the benefit of their dependent children. Now, however, there could be a role reversal on the horizon as more and more parents help their children out financially and look to cover themselves against their offspring defaulting on payments.

That means requiring children to take out a life, critical illness or mortgage protection policy specifically mentioning borrowings from parents and the proposed repayments to them.

Despite the fall in property prices over the past two years, the UK's “Bank of Mum & Dad” is still booming, as parents help their struggling offspring, as property prices still remain stubbornly out of reach for many and lenders demanding larger deposits.

And it's easy to see why they feel they need to, as figures from the Council of Mortgage Lenders, show that first-time buyers are now paying an average deposit of almost £32,000, which is more than double the £13,194 in September 2007.

But there are serious implications to be considered especially for parents who are nearing retirement, and may rely on loan repayments from their children to help

fund their retirement.

When parents assist their children financially, often this entails a loan of some form or another. But this loan is more often being taken out at a time when parents are making serious plans for retirement or have even reached retirement age.

Therefore, as well as the normal protection advice for the new home and mortgage owning children, advisers are now having to include additional advice to cover, the parents loan or repayments. If parents are reliant on getting their cash

“There could be a role reversal on the horizon”

back to supplement their retirement income, then lending to your children can be a high risk strategy, so looking into some type of protection plan and getting proper advice is recommended.

### **How it may work**

A couple aged 58 and 56, are two years away from their planned retirement. They have a daughter aged 30, who is still living at home because she cannot raise

enough deposit to get on the property ladder.

But if she can raise £50K she will have sufficient cash. The couple has calculated they need a combined income of £23K to support their desired income in retirement and they have the following projected income of £12,000 from their pensions, a buy-to-let income of £4,000 with the same amount tied up in investments. This leaves them £3,000 short.

They, however, have savings of £100K. With a combination of investment and deposit-based savings, they could make up the retirement income shortfall.

But if they lend £50,000 to their daughter, they cannot make up the income shortfall without taking disproportionate investment risk and leaving insufficient capital reserves. The couple may feel this is not a problem because their daughter is going to repay the loan over a period of, say, 10 years; this is where the potential need for more insurance and protection arises.

In terms of cost of the insurance, which would take into account, life, critical illness and income protection, based up on the above example, the total monthly premium could be circa £27 according to comparison websites.

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# Trust in the family

## A way to pass assets to future generations

Family trusts are a means of avoiding inheritance tax and they can provide an effective way for parents to retain some control of assets, while passing them to adult children.

Governments have viewed family trusts as a tax avoidance ruse and have imposed increasingly unfavourable taxes; most recently in 2006 with the introduction of 20 per cent inheritance tax (IHT) on setting up a trust worth more than the nil rate band (currently £325,000 per person). From April 6 2010, many trusts will also be liable to tax at 50 per cent on income it receives, so the tax incentives for creating trusts are diminishing.

However, the history of trusts is very different; their purpose was not to avoid tax but to provide a very effective way of protecting assets, typically family wealth, for future generations. Protecting assets, not just from the taxman, but in some cases from legal challenges, marriage breakdown and children who may be tempted to spend too much too soon.

Trusts can be set up at different times and for various reasons. During an individual's lifetime they may want to make provision for someone, on special occasions such as the birth of a child or the marriage of an adult child; or upon death, a trust can be created in a will.

Where a trust is created through a will, the trustees chosen are often a mixture of

close friends of the parents, grandparents or professionals who are able to take responsibility for the trust and run it long after they are no longer around. The parents' or grandparents' wishes for the trust can be expressed in the trust deed and sometimes in a separate letter to any incoming trustee.

It would not be unusual for parents to draw up a trust with very tight powers enabling the trustees to give children very limited access to income and capital, depending on the beneficiary.

For children under the age of 18 who lose their parents, a trust will be created statutorily but once they turn 18 the money is theirs. So having a trust in a will or created during an individual's lifetime is well worth considering, unless parents are happy that their hard-earned wealth could pass to their children at a fairly young age.

Trusts created during an individual's lifetime can be useful for tax planning. This is because they can remove the value from the estate so that, if timed correctly, future IHT at 40 per cent can be saved and more wealth left to the children.

However, lifetime trusts are often used for early protection of assets; say on the

occasion of a marriage, so that the child knows that some money has been set aside for them. For the parent, by putting the money in trust and not gifted directly there is the possibility that the gift is protected should the marriage break down.

For lifetime trusts, the individual creating the trust, the settlor, can also name themselves as one of the trustees, meaning that they retain control of the trust fund during their lifetime.

So, with a combination of protection and tax advantages, trusts retain some significant advantages whether they are drawn up during an individual's lifetime, on a special occasion or on death, via the will. Putting any tax advantages aside, the prime function of trusts is to provide protection for assets held, preserving that wealth for the family's future.

Putting in place a Trust can be very complex and you should always receive professional advice before proceeding.

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# What not to be unaware of



## *Women without cover expose their family's future*

Based on tradition, where males have often been the only or chief income earner, many families have only ever felt the need to insure his position and not that of the female. This is frequently a short-sighted move because the question that has to be asked is, what if the alternative occurred?

Nowadays more women than ever are contributing substantially to their families' incomes and a predicted one in four women will be the main breadwinner by 2030. But many still have an old-fashioned attitude when it comes to their insurance. Half of women in the UK have no life insurance, critical illness cover or income protection in place and a quarter of them rely on their partner's insurance policies instead.

Without adequate insurance, some families could find themselves dangerously under protected should the worst happen. One of the biggest potential health threats is breast cancer, which is diagnosed to one in nine women during their lifetimes. Despite this, almost a third of women believe they would have to sell their home, borrow money, or seek help from family and friends if they were faced with serious health and financial issues. With the right cover, however, many of these concerns could be eased.

The most common form of life cover is term assurance, which pays out if the policyholder passes away within a set period of time. The amount paid out, however, can remain level, increase or decrease over time. The policy should be written into a trust to curtail tax liability.

Premiums are determined by age, pre-existing medical conditions and lifestyle, so smokers and those with weight problems will have to pay more.

There is also the option to have the cover paid as an income with family income benefit. It is one of the cheapest means of protection because instead of paying a lump sum, it provides a monthly, tax-free income from the time of the claim for the duration of the plan term. So, if the plan term was 20 years, a claim made after 15 years would result in benefits being paid for the remaining five years.

While life cover is typically inexpensive for women, illness protection is usually costlier because there is a higher likelihood of claims, yet it can still be a vital form of protection.

Women generally live longer but are more likely to fall seriously ill, so some form of income-producing plan is worth considering. Relying on state handouts is desperately inadequate and are often not available if the spouse is still working.

With critical illness cover, a tax-free sum is paid out upon diagnosis of life-threatening conditions, which are specified in the policy. Cover can either remain level throughout the term, or decrease over time, commonly to reflect a reducing mortgage.

Income protection insurance is a common alternative to critical illness cover and pays out for an inability to work, rather than a specific illness, until the policyholder has either recovered or retired. A deferment period is set beforehand to determine how long after falling ill the policy would start providing a monthly income. Generally, those who opt for a longer deferment period can lower their premiums.

With both life insurance and income protection, the younger and healthier policyholders will be offered cheaper premiums so it is advisable to take a policy out sooner rather than later. Smokers should also try to give up as this can dramatically reduce premiums.

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

# Start **building** up your pension savings

Britain used to have a pension system that was the envy of many. But a decade of firms closing their final-salary schemes, mis-selling scandals and a multi-billion pound government pensions tax grab has largely put paid to this. Now, there are vast numbers of people who are putting nothing away for their old age.

We are all living longer, and as things stand, the full basic state pension only offers £95.25 a week for a single person and £152.30 a week for a couple. It's easy to see how thousands of people, have no option but to sell their homes to pay for either a more comfortable old age, or, if they become infirm, nursing-home fees. Living longer is a double-edged sword financially, and the key is to prepare for the twin challenges of building up sufficient retirement income while protecting it from the ravages of long-term care costs. So what can you do today to lay the financial foundations for old age?

## Your 20s and 30s

It is difficult to assess the level of income you will need in retirement, but it is still vital to start the savings habit early. It is considered by many, as a rough rule of

thumb, you should save 10 per cent of your income at age 20, 15 per cent at age 30, and so on.

There is a general misconception that retirement planning means just paying money into a pension, but having other savings vehicles is equally important, to diversify risk. A range of savings plans, as part of a larger retirement portfolio is the safest way to save. Individual Savings Accounts are particularly important because of their tax efficiency as are any pension contributions offered to you by your employer.

## Middle age

Your forties mark the need to start some serious planning. The first thing is to estimate the annual income you'll need when you retire. Consider your mortgage, marital status and whether you have, or plan to have, any dependants. Crucially, inflation and tax will have to be taken into account. The Financial Services Authority has useful annuity comparison tables which you can use to work out how much of a pot you'll need to secure the right income. Annuity rates do

change, though, so it's a good idea to recalculate and amend your target every year.

With a final figure in mind, you can work out how much you need to save each month to hit that target.

## Your 50s and 60s

Decide how you plan to draw benefits. If you wish to take out an annuity, a relatively modest approach to risk is advisable.

Many people still make the mistake of buying their annuity from their pension provider, which will typically offer poorer rates than elsewhere in the market. Ask your adviser to shop around. Also, you may have a medical condition or lifestyle issue such as smoking, which qualifies you

for an impaired life annuity and therefore guaranteeing a higher income.

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For more information on any subject that we have covered in this issue, or on any other subjects, please tick the appropriate box or boxes, include your personal details and return this section to us.

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