

Why you should review your pension portfolio prior to A-day

The Inland Revenue recently announced that new pensions legislation will be implemented with effect from April 2005 (A-day) rather than April 2004 as originally planned. The main legislative proposals (Pensions Green Paper) were covered in our Spring edition. More details of the new tax legislation will be provided by the Government this Autumn.

The delay provides a breathing space, but there is likely to be considerable pressure on resources leading up to April 2005 and it is preferable to prepare well in advance. In particular, individuals should:

- value their pension portfolios to establish headroom for additional contributions prior to A-day;
- be aware of the selected retirement dates, any penalties for early transfer/retirement and guaranteed annuity rates in their policies or occupational pensions;
- understand their exit options regarding tax free cash and, for the balance of the fund, annuities, income drawdown and the Open Annuity;
- understand the death benefits position under the pre/post A-day regime;
- make additional contributions prior to A-day if likely to establish a fund value above the proposed lifetime limit of £1.4 million;
- review with profits holdings to consider withdrawals from providers where further terminal bonus and market value reductions may be forthcoming;
- review asset allocation to ensure that it is consistent with the time horizon to retirement, risk profile and income objectives.

The tax favoured environment for pensions still applies with up to 40p of tax relief for each £1 invested and normally 25% tax free cash at vesting - combining these results in a cost of just 47p for each £1 of income producing pension capital (up to the proposed lifetime limit of £1.4 million or higher as appropriate under the proposed new legislation).

A review by Saunderson House will investigate and report on all of the above and highlight any opportunities to transfer existing policies to a self invested personal pension (SIPP) providing access to a wide range of low charging investment funds.

Pension Contributions or Buy to Let?

Total returns from residential property have exceeded those available from any other asset class over the last 25 years. According to agents FPD Savills, residential property has returned 17% pa over the last 25 years, but investors should lower expectations for future returns to around 8% pa.

By contrast, the total return from the FT-SE All Share Index was just over 14% pa over the 25 years to 30 April. Analysts' forecasts for future total returns from equities are similar to those from residential property.

Whilst pension plans cannot hold residential property, tax relief is available on contributions. If analysts forecasts are anywhere near correct, £60,000 net (£100,000 gross) invested in equities in a pension plan over the next 25 years will be worth £684,000 at a return of 8%, with up to 25% of this available as a lump sum free of tax. The same net amount invested in a property would be worth £410,000, with the investor facing a substantial capital gains tax bill upon eventual sale.

Whilst annuity rates, which determine the income from a pension fund even if a non-annuity exit option is selected, have fallen, so too have yields from other asset classes. In our view, pension contributions remain the most attractive way to build a fund from which to draw income in retirement.

Single premium investment bond 5% pa allowance to continue

Contrary to expectations, the Chancellor did not remove the facility available in investment bonds to take a tax deferred "income" of up to 5% per annum of the original investment in the Budget.

The 5% allowance can be particularly useful when single premium bonds invest in higher yielding assets such as corporate bonds or property, where the income produced would otherwise be liable to tax at the highest marginal rate.

Pension Contributions to Equitable Life Unit Linked Funds

Equitable Life now charge 4.5% on further contributions to unit linked pension funds. The introduction of the charge was mentioned in the Annual Report being one of the unspecified anomalies.

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This note is for general guidance only and represents our current understanding of law and Inland Revenue practice as at August 2003. We cannot assume legal liability for any errors or omissions and detailed advice should be taken before entering into any transaction. The value of investments and any income from them may go down as well as up and you may not get back the full amount you invested. Levels and bases of, and relief from, taxation are those currently applying but are subject to change and their value depends on the individual circumstances of the investor. For income drawdown policies, it should be noted that: high income withdrawals may not be sustainable during the deferral period; taking withdrawals may erode the capital value of the fund, especially if the investments are poor and a high level of income is being taken - this could result in a lower income when the annuity is eventually purchased; annuity rates may be at a worse level when the annuity purchase takes place, and a certain investment return is required simply to "keep pace" with an annuity, because a pension withdrawal fund does not receive a benefit from the early death of other pensioners, 'mortality drag', as does an annuity.

PEP/ISA Tax Credit to be Abolished

Despite much lobbying from the industry, the Government did not back down on its decision to abolish the ability to reclaim the 10% UK equity dividend tax credit on PEPs/ISAs from April 2004. Income from bonds will continue to be entirely free of tax.

PEP/ISA holders should consider re-positioning their portfolios so that bond exposure is held inside tax free PEP/ISA wrappers and equity exposure is held outside.

Estate Planning - Eversden Case and Beyond

The loophole that permitted married couples to make a potentially exempt transfer into a trust but allowed one spouse to subsequently recover all or part of the trust fund without being caught by the gift with reservation provisions was finally closed by the Inland Revenue on 20 June. It was always likely that a scheme which complied with the letter but not the spirit of the law would come under attack.

Despite this, inheritance tax remains largely voluntary. Comprehensive financial planning advice can help you to decide how much should be given, to whom and when, and whether any gifts contemplated are affordable.

The main planning opportunities are (a) effective use of the nil rate band (b) use of appropriate trusts for pension and certain life assurance death benefits (c) gifts of capital where the donor survives for 7 years thereafter and (d) gifts within the specific annual exemptions or which form part of normal expenditure out of income.

With Profits funds

AMP has recently announced the closure of NPI and that equity exposure has now been eliminated in its London Life and older NPI With Profits pension funds. Policyholders should review whether to retain policies or transfer to funds which might provide more attractive growth prospects.

Until recently, the figures quoted by Equitable Life Assurance Society for the value of their With Profits pension policies were the fund value less a 20% charge for transfer without taking benefit. There was a lower charge of 10% if benefits were taken after the minimum contractual age which has now been consolidated meaning that the fund value has been reduced by 10%.

If Equitable Life's position deteriorates ie if claims of previous policyholders mushroom, the penalty might increase and/or further reductions in policy values could occur.

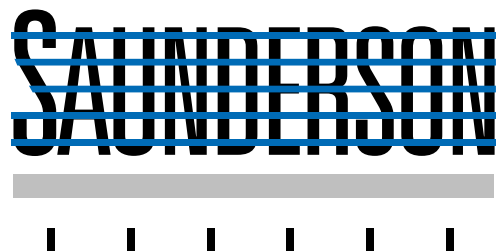
For those who are old enough, it may make sense to take benefits now but individual advice is recommended before any action is taken.

Autumn Seminars

Seminars on "Maximising your pension fund benefits with an update on the Pensions Green Paper" will be held at Ironmongers Hall, London EC1 on 1 and 9 October 2003. Please contact Sandra Pearson (telephone: 020 7315 6507 or email: sandra.pearson@saunderson-house.co.uk) to reserve your place.

Independent Fee Based Advice

We continue to see examples of advice biased by commission on product sales and remind prospective and current clients that Saunderson House is a fee based adviser working in a fiduciary relationship with clients.

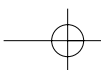


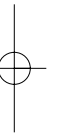
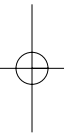
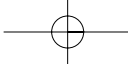
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| <input type="checkbox"/> The Pensions Green Paper | <input type="checkbox"/> Review of my with profits policies |
| <input type="checkbox"/> Maximising my pension contributions before 5 April 2004 | <input type="checkbox"/> Venture capital trusts |
| <input type="checkbox"/> Maximising my pension contributions before A-day | <input type="checkbox"/> 2003/4 ISA allowance |
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