Newsletter Autumn 2011

Welcome to the latest edition of our new regular financial newsletter. We hope you find it of interest. If you know someone else who would also appreciate a copy, please just send us their email and we'll add them to the mailing list.

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This is the time of year when you should think about sorting out your financial affairs before the festivities begin.

And given the recent volatility in world stockmarkets and the economic crisis, perhaps it should be sooner rather than later.

In addition, and especially if you are retired, inflation can be a real concern. So how do you ensure that your savings are not effectively reduced by inflation? There's no easy answer to that question, but we look at the situation in this newsletter.

Savings certificates disappear again

Earlier this year, on 12 May, National Savings & Investments (NS&I) relaunched their savings certificates with a great fanfare.

They offered both fixed rate and index-linked certificates and these had not been available since July 2010.

But now they are gone again, as they have proved too popular and raised too much money.

On 7 September 2011, NS&I withdrew from sale all of its savings certificates. In its press release announcing the withdrawal, NS&I said that its action 'will ensure that the Net Financing target set by the Chancellor (£2bn) for 2011-12 should not be exceeded'.

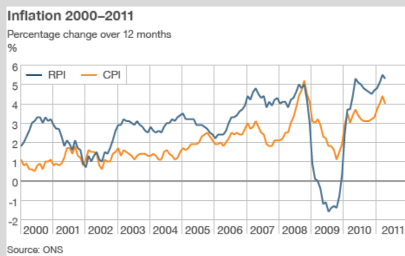
NS&I revealed that there had been nearly half-a-million applications for the latest issue of index-linked savings certificates. Not surprising, given their tax-free status and the level of inflation presently.

Although both certificates have been withdrawn, existing holders of maturing savings certificates can continue to reinvest in either 3 or 5 year index-linked certificates or the 2 or 5 year fixed rate certificates – regardless of which certificates they currently hold.

A number of other institutions are still offering inflation-linked deposits, see below, but these are all taxable unless you invest in them via an ISA. Of course, just like

savings certificates they could also disappear at any time.

It is now unlikely that any new certificates will come on offer until April or May next year, because NS&I have raised enough money in their current financial year, which runs to 31 March.



How can you inflation-proof your savings?

So now that savings certificates have gone, how can you inflation-proof your savings and can they be tax-free, like national savings?

There are government index-linked gilts available, but because of demand they are now actually offering negative real returns! That is, the overall return to maturity will be lower than inflation.

So you will have to consider investments offered by non-governmental organisations.

"As the latest rate of inflation - based on the retail prices index (RPI) - is 5.5% your savings will be shrinking fast in real terms"

And the first thing to say is that one big difference with any alternative is that none of them come with government backing. So you have to rely on the investors' compensation scheme if a provider defaults.

The best cash ISAs are paying above 3% per year, which is tax-free, but the maximum investment in those accounts is limited to just £5,340.

As the latest rate of inflation - based on the retail prices index (RPI) - is 5.5% your savings will be shrinking fast in real terms.

And recently we saw the Post Office have an inflation linked bond on offer, but that has been withdrawn "due to an unprecedented surge in demand". Hardly surprising now that savings certificates have been withdrawn.

There was also similar products on offer from National Grid, the people who run our power lines amongst other things, and the Cambridge Building Society, but both of these have now closed.

But the message is clear; investors have a great appetite for inflation-linked savings and providers of these accounts and bonds will hopefully announce new offers in future. But you may have to be quick off the mark!

In the meantime, you should consider if you are prepared to invest in asset-backed investments to try and preserve the value of your capital.

This does not mean investing in the stockmarket, there are many special investments nowadays that aim to preserve the value of your capital whilst giving you a prospective return that could beat inflation.

But these need to be carefully analysed to see if they would suit your circumstances. If this is of interest to you, let us know and we will be happy to explain them to you.

State pension age

Iain Duncan Smith, the Work and Pensions Secretary, confirmed in an interview with Andrew Marr that the current timetable for raising State Pension Age (SPA) to 67 was 'too slow'.

The plan had been to phase in the move from a national retirement age of 66 to 67 from April 2034 to April 2036.

But now a new piece of legislation, the Pensions Bill 2011, says that the initial step of changing the SPA to 66 will happen by April 2020. This is six years earlier than previously planned, as the change had been due to be made by April 2026.

So would the government then leave a 14 year gap before changing it to 67? That always seemed improbable and Mr Duncan Smith's comments confirm this.

The DWP has said in the past that 'To manage the ongoing challenges posed by changes in projected longevity, the Government will be considering the current timetable for these rises and will bring forward proposals in due course'.

"....the initial step of changing the SPA to 66 will happen by April 2020. This is six years earlier than previously planned"

The 'most likely option according to Whitehall sources' for the new age 67 retirement date is 2026, a full ten years earlier than currently planned. So people now aged between 42 and 52 would have to wait another year longer for their state pension – and two years longer than currently, of course.

The government is already facing criticism for the impact that the increase from 65 to 66 will have on some women in their late 50s. A total of 161 MPs have signed a motion opposing the change in women's retirement age.

It is possible that a formal move to age 67 in 2026 could be accompanied by some tweaking of the female retirement age deadline.

And a move to an SPA of 67 has relevance beyond just state pensions. Under the government's current plans it would also mean bringing forward an increase in retirement ages for public sector pension schemes. That should be popular with the unions!.

All time low for drawdown annuities

If you are contemplating retirement, you will probably be shocked at the low level to which annuity rates have slumped.

This is because of a combination of low interest rates, rock-bottom yields on gilts and increasing longevity.

National Statistics said this week that there were more centenarians than ever and that life expectancy at birth in the UK was greater than ever before recorded. Not good news for the institutions paying them pensions!

An alternative to buying an annuity is to keep your pension fund invested and have a 'drawdown' fund. This allows you to take annual income within certain limits and you can then buy a conventional annuity when rates have improved.

Unfortunately, the annual income is based on gilt yields and these have now fallen to the lowest rate (2.75%) since drawdown was introduced sixteen years ago.

The one saving grace is that the investment fund is still being managed

(presumably) and that you are only subject to this rate for three years if you choose drawdown at the moment.

It is an inescapable fact that taking retirement benefits is a challenging exercise at the present time. At least, you should shop around for the best annuity rate and, if you have suffered an illness in the past, you should be eligible for an enhanced rate – but only if you ask!

Quotations are readily available; so if approaching retirement and you have a pension plan to encash, it would be worth letting us know your details so we can tell you the options available.

BUSINESS SECTION

NEST* part five – jobholders insisting on being included in the pension scheme

**National Employment Savings Trust*

So far, we have looked at when you have to automatically enrol jobholders in a pension scheme, such as NEST, and when the jobholder does not have to join.

But what if someone who is not eligible insists on joining your pension scheme?

Jobholder's right to opt into their employer's pension scheme

Where a jobholder with earnings above the level for automatic enrolment (£7,475 in 2011/12) is not automatically enrolled in a pension scheme, they can compel their employer to include them by giving their employer notice.

This situation could arise where the jobholder:

- is under age 22, or
- is over state pension age but under age 75, and
- has qualifying earnings between the National Insurance primary threshold and the income tax personal allowance, or
- is in the normal waiting period of up to 3 months (see previous newsletters).

"they can compel their employer to include them by giving their employer notice"

The notice requesting that they opt-in to the scheme must be given to the employer, be in writing and be signed by the member.

The notice could be given in electronic format, but in this case the requirement for a signature is replaced by a statement confirming that the jobholder personally submitted the notice.

Once this notice is received the usual automatic enrolment process will apply, except that membership will commence on the first day of the jobholder's next applicable pay period.

An employer does not have to take any action if the jobholder changes their mind before the enrolment date and withdraws the opt-in notice.

Where such an individual opts-in and has earnings in excess of the lower qualifying earnings level, they will also qualify for employer contributions at the minimum

level.

Where the individual's earnings are below the lower qualifying earnings level any employer contribution will be at the discretion of the employer.

But what if the employee does not have the qualifying earnings and wants to be included in your pension scheme?

Workers without qualifying earnings

Any worker who is aged between 16 and 75 without qualifying earnings, and who is not an active member of a qualifying pension scheme, can give notice to their employer that they want to become a member of the pension scheme.

If you receive such a notice, you must provide that employee with the following information:

a) a statement that a joining notice must be submitted in writing and signed by the employee or in electronic format including confirmation that they personally submitted the notice;

b) a statement that the worker may, in accordance with the scheme rules, choose how much to contribute; and

c) details of where to obtain further information about pensions and saving for retirement.

On receipt of the joining notice, the employer must make arrangements to include the individual as a member of their pension scheme.

You will not be required to make any contributions to the scheme for them.

If an employee ceases to be an active member of your scheme, any notice you receive from them in the next 12 months to opt-in again will not be a mandatory obligation on you and you do not have to re-admit the employee to your scheme (until the 12-month period has passed).

The information regarding taxation is based on our understanding of current legislation, which may be altered and depends on the individual financial circumstances of the investor. Past performance is not a guide for the future. The value of units can fall as well as rise. If an investment is surrendered in the early years, the surrender value may be less than the original investment. Currency fluctuations can also affect performance. If you no longer wish to receive this newsletter, please simply reply to the e-mail with "unsubscribe" in the subject line.

"You know it makes sense"