

FIRST FINANCIAL

Retirement Planning

Creating Wealth

Protecting Assets ...



The taxation of pensions was drastically changed in 2006, opening up both opportunities and potential pitfalls. HM Revenue and Customs described the process of change as 'simplification'. In many respects, this description is correct. For most people, the tax rules will simplify the situation very considerably. The multiplicity of different tax regimes were abolished with effect from 6 April 2006 and very few people will find the new allowances for contributions or retirement benefits in the least restricting.

Pensions will still be the most tax-efficient way for most people to provide for their retirement. The large minority of the working population that are still members of defined benefits (or salary-related) pension schemes will have a generally attractive and secure means of building pension benefits. The remainder who depend on defined contribution (or money purchase) schemes will find that the tax advantages normally outweigh the restrictions on access and the other rules. If you are a business owner, you could find that your pension scheme is a useful tax vehicle for achieving your financial objectives.

The changes could mean that this is a good moment to review your pension arrangements. The FSA does not regulate tax advice. Tax rules are subject to change.

The new rules

Pensions have now become much simpler to understand, following the key changes to the tax rules that were introduced on 6 April 2006 (known as A-Day). The aim of this briefing is to explain the main changes. It is important to obtain specialist advice about your pensions strategy whether you are an employer, an employee or you are self-employed.

The new rules have genuinely had the simplifying effects intended by HMRC (Her Majesty's Revenue & Customs, formerly the Inland Revenue). But a few aspects have turned out to be very complex, and these changes are so crucial that you should be making a complete reappraisal of your financial planning strategy, if you have not already done so.

The changes mainly affect how much can be contributed to pensions, the limits on the benefits that can be withdrawn from them and how those benefits can be taken. The new rules generally apply to all pension schemes regardless of when they were set up. Further mainly technical changes are in the pipeline.

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Your Financial Needs in Retirement

Where are you now?

Working out your financial needs in retirement generally becomes easier, the closer you are to stopping work. However, the opposite is true when taking action to satisfy those financial needs. A shortfall identified 15 years before retirement is more readily rectified than one discovered two years before the golden watch arrives.

Wherever you are on the work to retirement timescale, it makes sense to review your position now and continue to do so regularly.

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Close to retirement

If you are within a few years of retirement, you are probably in a good position to estimate what your outgoings will be once you stop work. Sit down with some old bank statements and work out what your pattern of expenditure will be. Many items, such as council tax bills, will not change. Others may increase: your utility bills may rise as you spend more time at home and you will lose employment perks, such as health insurance, which you wish to replace. Some expenditure may fall: once you have stopped work, your commuting costs will disappear.

When considering your budget, it is a good idea to think how you will spend a typical month of retirement. What will you do that with all that free time? This is a serious question, and not only from the financial viewpoint. Many people think of retirement only in 'no more work' terms. Then, not long after retirement has begun, they find themselves pining for work again to fill their empty days.

As part of the budgeting process you should also think about what capital you will need at retirement. For example, you might have to replace a company car, pay for a cruise or clear outstanding debts. You may also want to increase your 'rainy day' cash reserve, because you can no longer rely on the monthly pay cheque.

On the income side of the equation, your pension provider(s) will be able to give you illustrations of the cash and pension income you should receive at retirement.

The numbers should be treated with some caution, other than for pension benefits paid from the state or a defined benefit (final salary) pension scheme. The final results from defined contribution (money purchase) pension arrangements depend on investment performance up until retirement and annuity rates at retirement.

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Longer to go

If you are further from retirement, matters are less clear cut. For a start, your actual retirement date may prove to be different from what you currently envisage. The state pension age for everyone will begin increasing from 2024, but on the other hand your employer could offer you an early retirement deal you cannot refuse. Similarly it is hard to predict your standard of living immediately before retirement.

The further you are from retirement, the greater the uncertainties. Even so, you should obtain illustrations of your retirement benefits from your current pension provider(s). If at all possible these should be in today's money terms so you get a feel for your retirement purchasing power. Unadjusted figures can give a false sense of security: £1,000 in 25 years' time is worth only £539 now if inflation averages 2.5% a year or just £295 if inflation is 5% a year.

A comparison between your projected pension and today's earnings will give a rough indication of how adequate (or otherwise) your current provision is. Do not be surprised if the gap seems wide – the gradual disappearance of generous private sector employer-funded schemes has left many people facing relatively low retirement benefits. With time, money and careful planning the gap can be narrowed, but as is so often the case in financial matters, the earlier you start to address the issue, the better.

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Retirement issues

There are many issues to consider about retirement outside of the bald income and capital numbers. These include:

Trading down

The rise in residential property prices has encouraged the view that retirement problems can easily be solved by trading down to a smaller home at retirement. In practice, this solution may be illusory. If you want to stay in the area you live in now, then you may find yourself having to make some difficult compromises to release enough capital. Moving house is a traumatic and costly exercise, especially if the end result is less living space and a poorer location.

Moving overseas

If you want to retire to abroad, then you need to start planning well in advance of retirement. One sound piece of advice is visit where you are planning to live in winter: sunshine can all too easily colour judgement. Living overseas will usually mean a substantial upheaval to your financial plans. You will need to come to terms with a new currency and different tax rules. Arranging your finances before you leave the UK is vital. For example, you might find your new home country will tax your pension scheme lump sum if it is drawn once you have moved.

Gradual retirement

You should not have to work once you have retired. If your retirement plan includes starting a part time job to make up an income shortfall, then it probably needs revising. You might be happy enough to work part time now, but for how long will you be willing or able to do so?

On the other hand, gradual retirement – cutting down the hours worked – could be a wise choice. If a sudden switch from full time employment to full time retirement looks too daunting – financially and/or personally – a phased approach to retirement can ease the transition. The FSA does not regulate tax advice. Tax rules are subject to change.

How we can help

As independent financial advisers, we are well versed in the many complexities of retirement planning. We can help you understand your retirement situation by:

- Obtaining details from your existing pension providers and putting the results into a coherent and consistent format.
- Guiding you through the options to improve your retirement benefits.

- **Setting out an appropriate strategy for your pension investments.**
- **Explaining the financial implications of retiring overseas.**
- **Showing you how to integrate your retirement plans into your overall financial planning – pensions are not the only route to building up income in retirement.**

It is vital that you make the right choice at retirement, as you may have to live with the consequences of the wrong decision for the rest of your days. As independent financial advisers we can help you by:

- **Providing illustrations of what the various options could mean to you and your dependants**
- **Sourcing the most competitive annuity rates in the market place.**
- **Recommending providers for fund withdrawals and phased retirement.**
- **Advising on appropriate investment strategies for fund withdrawals and phased retirement.**

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