

Fixed protection: could it be right for you?

Since 6 April 2006, the Government has imposed a limit on the amount of pension provision an individual can accumulate throughout their lifetime.

Called the lifetime allowance, for the tax year 2010/11 this limit stood at £1.8m. From 6 April 2011, it will reduce to £1.5m.

Anyone who would prefer their pension benefits to be measured against the existing £1.8m limit is able to register for fixed protection.

The downside to this is that no further contributions can be made to any form of pension provision and you are unable to be an active member of a defined benefits scheme, otherwise the protection is lost and you revert to the £1.5m limit.

Where you have pension assets valued at over £1.5m, but under £1.8m, it is likely to be in your best interests to register for fixed protection.

Fixed protection will give you a lifetime allowance of £1.8m, but if your funds grow to exceed this limit, there will be a tax charge on any excess.

Depending on the term left until you wish to crystallise your pension benefits, it is quite possible that the value of your existing provision could grow to £1.8m or more, even without any further contributions being paid into the funds. However, by obtaining fixed protection, your limit will at least be held at the higher level of £1.8m rather than drop to £1.5m.

To register for protection, you do not need to have existing pension assets over £1.5m, simply an expectation that your pension funds may grow to over £1.5m by the time you wish to crystallise the benefits.

Any excess over and above the £1.8m will be taxed at 55 per cent if you take it back as a lump sum or 35 per cent if you choose to use the excess fund to provide an income. These tax charges are harsh



and designed as a deterrent to anyone exceeding the prescribed limits.

If you are likely to be in this situation, you may wish to consider future contributions going towards a more flexible investment outside the pension regime or perhaps being invested in a way that could help make use of a spouse's tax status. In addition, as a result of the new legislation, we may well see an increase in the popularity of family pension trusts that involve capping the growth on

your fund and distributing it to a family member within the same scheme.

The forms to apply for fixed protection are not yet available but you have until 5 April 2012 to submit your application. There is no need to quote pension values at the time of the application – you simply need to inform HM Revenue & Customs of your name, address and National Insurance number. They will then register you on the system and send you a certificate.

Is the Retail Distribution Review achieving its objective of treating customers fairly?

When the Financial Services Authority (FSA) launched the Retail Distribution Review (RDR) in 2007, it was done in response to a belief that the traditional business model adopted by most Independent Financial Advisers (IFAs) was fatally flawed and unsustainable.

It was suggested that the level of qualification required for advisers was inadequate and needed to be increased. It would be difficult to argue against better trained and more knowledgeable advisers and, although our advisers were already well qualified, they have responded enthusiastically to the challenge of increasing their level of qualification.

One of the key issues, however, was a concern that commission payments by providers distorted investment advice to clients and would need to be replaced by a system of fees. This is a very fundamental change that has led to a great deal of discussion and negotiation amongst the trade bodies and it has now been confirmed that commission will be banned after 2012 and all fees must be agreed between advisers and clients.

They can, however, be deducted from the products and, in many ways, can work in a very similar way to commission, while achieving the key objective of ensuring that adviser remuneration is not determined by product providers.

There are, however, two issues that continue to concern us. One of these is the impact of VAT and the other is the level of charges being built into product pricing by the product providers, as both of these factors can significantly increase

costs to clients. It is difficult to see how this will benefit the client.

VAT is an issue because there is no VAT on commission but it is chargeable on fees. It is being suggested that VAT will not be charged on fees leading to the sale of a product but it will be applied to fees associated with portfolio management and advice not designed to lead to the sale of a particular product.

At best, that will be chaotic in terms of what HM Revenue & Customs will expect to collect and it will fly directly in the face of the FSA's objective of moving the emphasis of advisers' work away from product sales to the provision of an ongoing service.

When provider companies no longer have to pay commission to advisers we might have expected them to reduce their costs but current evidence suggests that the reverse is happening.

A number of companies have already released details of their RDR-compliant contracts and two high profile examples indicate costs are being increased. In the case of the Prudential With-profit Bond, the costs to the client will increase by 1.2 per cent per year, compared to the current commission paying system over a five-year period, and a £20,000 lump sum contribution into an Aviva Personal Pension will cost 0.5 per cent a year more under the RDR-compliant contract, compared to the current standard commission contract over a five-year period.

This does not seem to be achieving the objective of providing a better experience for investors.



Pension changes

The annual allowance for pension contributions will change to £50,000 from the 6th April 2011. The previous limit was £255,000, so this is a significant reduction. If you contribute more than £50,000 into a pension scheme you will not receive tax relief on the excess and if the contribution is made by a net pay arrangement or an employers contribution, then you will be taxed to ensure there is no benefit from tax relief at source.

Included within the £50,000 limit are your own contributions, your employer's contributions and any increase in benefit from a Final Salary scheme above the standard CPI revaluation. In order to assess the increase in Final Salary benefits, you need to establish your pension entitlement at the start of the year (which can be increased in line with CPI), your pension entitlement at the end of the year and then multiply the difference by a factor of 16.

This means that a member of a Final Salary Scheme, whose pension benefits increase by only £3,125 over the year will use up their full £50,000 allowance ($£3,125 \times 16 = £50,000$ assumed contribution).

This will have a big impact on those within Final Salary Schemes and also on anyone looking to pay taxable redundancy payments into their pension scheme to save tax.

There are carry forward rules, which have been put in place to allow you to bring forward £50,000 from the previous 3 years, but you need to have been a member of a registered pension scheme to qualify and any contributions made in those three years will reduce the amount you are able to carry forward.

MARKET REPORT

GLOBAL REVIEW



Global events have been overshadowed by the devastating impact of the earthquake and tsunami that struck Japan on 11 March. With both the human and financial cost still unclear, the initial shock prompted an inevitable decline in financial markets.

As Japan is the world's fourth largest exporter and fifth largest importer, there are obvious implications for global demand and the manufacturing supply chain. This has been most strongly felt in the wider Asian equity markets due to the greater volume of intra-regional trade.

Financial markets were already struggling to come to terms with the growing civil unrest in North Africa and the Middle East, with concerns that higher oil prices could stall the global recovery. This compounded fears for growth in China, as the authorities continue with a cycle of policy tightening, and worries centred on the indebtedness of western governments, in particular those of the peripheral European nations.

UK



In unison with global indices, the FTSE 100 has struggled to make ground in the first quarter as the more positive sentiment that prevailed in December was gradually eroded by these headwinds.

Hopes that the surprise contraction in fourth quarter economic activity in the UK would be revised upward were also quashed as the Office of National Statistics confirmed that the economy shrank by -0.6 per cent, slightly worse than first estimated.

Falls in both business investment and household spending were to blame.

This latest economic blip eased the pressure on the Bank of England to raise interest rates in the face of surging inflation. Sterling has strengthened on the expectation that rates would be raised earlier than first predicted, given that the Consumer Prices Index has now been 1 per cent or more above the government target of 2 per cent for 15 months.

The Bank of England has argued that inflationary pressures will subside as January 2011's VAT increase and spike in food and energy prices fall out of the numbers but concerns remain that the Monetary Policy Committee are underestimating the upward pressures.

US



Economic activity in the US was also revised down as a result of reduced government spending but to a relatively more healthy annualised rate of 2.8 per cent in the fourth quarter.

This was below analysts' expectations of an upgrade to 3.3 per cent but still higher than the annualised rate of 2.6 per cent recorded in the third quarter. Given the impact of government on economic activity, President Barack Obama's recent pledge to halve the US deficit by 2013 through spending cuts and tax increases has clouded the medium-term outlook.

Federal Reserve Chairman Ben Bernanke has defended the US central bank's continued efforts to stimulate the economy via quantitative easing, citing the relatively subdued pace of the recovery and its minimal impact on the 8.9 per cent jobless rate. Mr Bernanke also noted that inflation was rising at less than half the Federal Reserve's 2 per cent target, while rejecting accusations that loose monetary policy was responsible for surging prices in other parts of the world.

EUROPE



Eurozone inflation accelerated to 2.4 per cent in February, prompting firm suggestions from the European Central Bank that interest rates could be raised the following month as a consequence.

The idea drew little support and may need to be reconsidered following the rejection of new austerity measures by the Portuguese parliament and the earthquake in Japan. Economic growth in the fourth quarter was an already disappointing 0.3 per cent and would be further subdued by higher borrowing costs.

The threat of higher interest rates also saw the euro strengthen and further moves may jeopardise exports, a key contributor to the latest fragile growth figures. Universal fiscal tightening, fragility in the banking system and continued concerns over sovereign debt also remain major threats to growth prospects.

The Portuguese Prime Minister José Sócrates recently resigned following his government's refusal to back proposed new austerity measures, moving sovereign debt issues back to the top of the agenda as fears of contagion were once again made real.

JAPAN



Despite being overtaken by China as the world's second largest economy and a downgrade for the country's sovereign debt, Japanese equity markets followed global indices higher at the start of the year as investor sentiment remained positive on global growth.

A brief sell-off at the end of February amid concerns of growing civil unrest in North Africa and the Middle East

inevitably turned to panic as one of the largest earthquakes in recorded history struck the country.

The uncertainty created by the unprecedented devastation of the earthquake and resultant tsunami has been compounded by the crisis at the Fukushima nuclear plant. While this is undoubtedly a human tragedy, initial concerns that the impact on one of the world's largest economies would trigger a dip back into global recession have receded as the situation in Fukushima has seemingly been brought back under control.

ASIA



By again raising banks' required reserves in March, the sixth such move since October, so soon after increasing interest rates to 6 per cent, the People's Bank of China clearly still view inflation rather than Japan's devastating earthquake as the major threat to economic growth.

The increase in reserves will lock up around \$53 billion of cash that would otherwise be available for lending in an attempt to quell pricing pressures with official year-on-year food price gains now exceeding 10 per cent.

The Indian government have been forced to introduce a Food Security Bill to provide almost 70 per cent of the population with a legal guarantee for cheaper rice and wheat. This follows reports that food price inflation continues to run in double digits, having peaked at 18 per cent at the end of last year. Of greater concern was the latest non-food manufactured products data that saw prices increase by 6.1 per cent in February, causing the Reserve Bank of India to raise interest rates to 6.75 per cent, the eighth such move in the last 12 months.

25 March 2011

Update on 2011 Budget

George Osborne delivered the 2011 Budget on 23 March, telling MPs that he was providing “fuel” for the economy.

He said his second Budget was the “Budget for growth” and an “urgent call to action for Britain”. His main ambitions, Mr Osborne said, were to “ease the economic burden on families and businesses while promoting Britain as the best place to do business in Europe”.

However, the effects of this Budget will not be felt for some time and Mr Osborne’s critics will have to wait before deciding whether he has delivered on his objectives.

Mr Osborne outlined a number of items that will affect our clients and we have summarised the main changes taking effect from 6 April 2011.

Tax

All income tax rates will remain at the same level this coming year, however the personal allowance has increased by £1,000 to £7,475 and there will be a £2,400 decrease in the basic rate band, reducing it to £35,000 to ensure higher rate taxpayers do not benefit from the increase in the personal allowance.

The age allowances for those over 65 are being increased, however when total income exceeds £24,000 per annum, they will be reduced at £1 for every £2 above this income level. The table below summarises the changes, comparing them to the 2010/11 tax year.

Individual Savings Account (ISA)

For the 2011/12 tax year, the ISA allowances have increased. The total allowance per person is £10,680, of which up to £5,340 can be held as cash. The full amount can, however, continue to be fully invested into equity-based investments where the cash element is not being used.

Capital Gains Tax annual exemption

The annual exemption will increase in line with statutory indexation to £10,600 for the 2011/12. This is an increase of £500 from the 2010/11 tax year and applies per person.

Inheritance Tax (IHT)

The IHT nil rate band remains unchanged at £325,000 and has been frozen until 6 April 2015. While estates will continue to be taxed at 40 per cent for any amounts above the nil rate band, a reduced tax of 36 per cent will be charged where 10 per cent or more of the deceased person’s net estate is left to charity. This measure applies only where death occurs after 5 April 2012.

Severance payments

This first £30,000 of qualifying redundancy lump sum payments will continue to be paid tax-free. However, from 6 April any surplus payments will be taxed on a week one, or month one, basis.

In previous tax years, a flat level of tax would be taken at 20 per cent, leaving the surplus tax to be paid through self assessment. This arrangement meant that HM Revenue & Customs (HMRC) would have to wait up to 18 months, in some cases, before the remaining tax was paid, enabling individuals to gain interest on the capital before paying the tax due.

Now HMRC’s approach is to tax leavers as if they were going to be paid their taxable sums every month for the rest of the tax year. While leavers will benefit from having their personal allowance included in the tax calculation, they are only granted 1/12th of it within the new calculation, therefore £7,475 reduces to £622.92 for the purposes of the severance calculation.

The remaining tax thresholds receive the same treatment, with only 1/12th of the basic rate tax allowance of £35,000 used at £2,916 and 1/12th of the £107,525 higher rate band at £8,960.41.

The result of these changes is that many more people will be paying more than the basic rate of 20 per cent on their severance at source. Any over payments of tax will be paid back through returning to work and having your tax code changed, enabling the repayment of tax to take place over the remaining months of the tax year.

Alternatively, those not returning to Pay As Your Earn (PAYE) employment can request a P50, allowing the over-payment to be returned earlier.

Tax Year	2011/12	2010/11
Personal allowance (under 65)	£7,475	£6,475
Basic rate of 20% on earnings between	£7,475 - £42,475	£6,475 - £43,875
Higher rate tax on earnings between	£42,475 - £150,000	£43,875 - £150,000
Additional rate of 50% on income over	£150,000	£150,000
Age allowance (over 65 - 74)	£9,940	£9,490
Age allowance (over 75)	£10,090	£9,640
Starting rate of 10% on savings income up to	£2,560	£2,440

Birchwood Investment Management Ltd, 8 Prospect Place • Welwyn • Hertfordshire AL6 9EN • UK

Telephone: 01438 840 888 (Welwyn) • 0161 932 1038 (Manchester) • **Fax:** 01438 840 097

Email: info@birchwoodinvestment.com • **Website:** www.birchwoodinvestment.com

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