# Your Retirement

Summer 2015

Could Alliance Trust Savings be an ideal home for your pension savings?

Why investors considering income drawdown must remember stock market risk – and how investment trusts can help investors cope.

A view from an adviser - understanding the options you have at retirement.

Alliance Trust Savings

# Welcome

When we decided to write this magazine we quickly decided that the working title would be 'Your Retirement' until we decided on a final name. The standard brainstorm ensued but at the end of day none of them seemed to fit as well as 'Your Retirement'.

Perhaps the reason why is because retirement is increasingly becoming a very personal, unique journey for people. Some may follow a traditional retirement journey and retire fully when they become eligible for the state pension, while many others are seeking to retire well in advance of the state retirement age with dreams of travel or living abroad.

For as many people who are looking to retire early, there is a growing segment of the population continuing to work after the state retirement age. This group is split between those who are doing so out of necessity due to financial pressures, and those who enjoy their work and the social interaction it brings and want to continue working through choice.

Whether you are reading this magazine as someone who is 40 years away from retirement, months away from retirement or already in retirement, the government, with their radical reforms to allow you access to your pension savings, have put your retirement future firmly in your hands.

In this first edition of 'Your Retirement', we take a look at the recent government reforms and the options now available to you at retirement. We also ask an award winning Financial Planner to bring retirement planning to life in a case study. We must also thank our investment partners for contributing articles to the magazine.

The cover image chosen for this first edition represents multiple streams of income coming together to form a 'pool' of retirement income. Understanding how to take an income from this pool is only one part of the jigsaw. Investing for growth in a way that fits your personal circumstances is also key.

I hope you find the magazine an enjoyable read. We plan to issue the magazine twice a year and I am keen to get your feedback on the first issue and what you would like to see going forward. Please email your feedback to marketingresponses@alliancetrust.co.uk

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# Now that the dust has settled

## SIXTH OF APRIL HAS COME AND GONE, THE NEW 'PENSION FREEDOMS' THAT FILLED THE PAPERS (EVEN THE FRONT PAGES) ARE NOW A REALITY. IT WAS HERALDED AS THE BIGGEST CHANGE TO PENSIONS IN A GENERATION AND NOW IT IS HERE – THE PENSIONS LANDSCAPE HAS CHANGED.

So what has changed? The simple answer is that the government have given you full control and responsibility over how you take an income from your pensions savings. People of minimum retirement age now have much more flexibility in terms of how they take an income from their pension.

But more choice can make some decisions harder rather than easier. In this article we cover the various options available to you. It is important to understand the options you have at retirement but first let's remember the basics:

- You normally have to be of minimum pension age (currently 55) to withdraw money from your pension
- The different retirement income options available under the new pension freedom banner are only available to money purchase/defined contribution schemes. This means that if you have a defined benefit/final salary scheme these options will not be available but remember these schemes are often regarded as the most generous schemes in terms of secure retirement income.

Let's have a look at the options that may be available to you in a little more detail.

Firstly let's go back to annuities. It is probably fair to say that annuities have had a bad press. In recent years annuity rates have continued to decline meaning many felt short changed for a lifetime of saving. Since the early 90s, there has been a general decline in annuity rates, meaning someone purchasing an annuity now would be likely to get less than half the annual income of someone who retired 25 years ago. Falling annuity rates are primarily market driven but annuities still have a key role to play in the retirement income market.

Before we cover the other retirement income options available, the fact is the only option that provides a secure income from the point of purchase until you die is an annuity and therefore for many will continue to play an important role in retirement income provision.

Let's now turn our attention to the other options. Please note with all of these options you will normally be able to take up to 25% of your pension as a tax free lump sum, with any subsequent income taxed at your marginal rate(s) of tax (and remember the tax free lump sum can be taken before purchasing an annuity).

The government has recognised that the increased choice and responsibilty that it has given individuals means access to either guidance or financial advice is important. As a result all individuals at or near retirement now have access to free impartial guidance from the government sponsored Pensions Wise.

NEW

Flexi-Access Drawdown

NEW

Uncrystalised funds lump sum

Free guidance at retirement

Capped Drawdown

Lifetime Annuity

> *"People of minimum retirement age now have much more flexibility in terms of how they take an income from their pension."*

## Capped Drawdown

This option only applies to you if you have taken tax free cash and or income from your pension (unsecurely i.e not from an annuity) prior to 6 April 2015. Capped drawdown as the name suggests allows you to take an income from your pension but this is capped at an annual amount. The cap is determined by HMRC based on your age, the gilt rate and the value of your pension. You may wonder why this option still exists if you now have the option to take as much income as you wish. Due to the tax relief available on what you pay into a pension from 6 April 2015 anyone taking an income from their pension for the first time has their annual allowance (value of contributions that you can pay to your defined contribution/personal pension pension plans and receive tax relief on) restricted to £10,000 or 100% of earnings. If you are in capped drawdown and remain so after 6 April 2015 your annual allowance stays at £40,000 or 100% of earnings.

## Flexi-Access Drawdown

This new form of income drawdown allows you take pension income which is taxable with no upper limit. You can take tax free cash (also referred to as pension commencement lump sum) with the remainder being paid as income over a period of time or in one payment. This option is available to all individuals of minimum pension age.

Flexi-access drawdown will replace capped drawdown for individuals setting up a drawdown plan for the first time on or after 6 April 2015. You can usually take a tax free lump sum but if you begin to take any income in addition to your lump sum, your annual allowance (value of contributions that you can pay to your defined contribution/personal pension pension plans and receive tax relief on) falls to £10,000. If you only take your tax free lump sum your annual allowance remains at the current annual allowance of £40,000.

## Uncrystallised Fund Pension Lump Sum (UFPLS)

A lump sum can be taken from uncrystallised pension savings with this new option. Uncrystallised means that this portion of your pension has not had any tax free cash taken and/or it is not providing you an income. Typically, 25% of the lump sum will be tax free with the remainder being subject to income tax. For example you could take a £10,000 lump sum from your pension with £2,500 being paid tax free and the remaining £7,500 being paid as income but subject to tax. This option leaves remaining monies in your pension pot uncrystalised. Remember, taking any UFPLS will result in your annual allowance being reduced to £10,000.

**Important information**

*Alliance Trust Savings gives no financial advice.*

*Please remember the value of your investment and any income from them can go down as well as up, and you may get back less than you originally invested.*

*Before initiating a transfer you should seek professional advice on the merits of the proposed transfer that is specific to your circumstances. Your existing pension may have valuable benefits which you might lose when you transfer.*

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# Risk free path to pensions is a myth

## ARE YOU TAKING ENOUGH RISK? ROBIN GEFFEN, FOUNDER OF NEPTUNE INVESTMENT MANAGEMENT AND MANAGER OF THE NEPTUNE GLOBAL ALPHA FUND, DISCUSSES THE IMPORTANCE OF ACCEPTING ENOUGH VOLATILITY IN PLANNING FOR RETIREMENT.

We all have our own dreams for our retirement. The last thing any of us want is for our investments to be exposed to the sorts of risks that could jeopardise those dreams. Yet I believe the least understood risk by many pension investors today is not the risk that their pension pot will rise and fall over their lifetimes – on the tide of stockmarket movements – which we call 'volatility risk'.

Rather, the biggest risk for many people is that the sum of money they will receive on retirement will fall far short of what is required to meet their expectations. This is because they simply were not willing to accept enough volatility in the price of their investments when younger in life. Of course, for those who are approaching the point at which they are planning to start drawing down the money in their pension pot, volatility is very much the most significant concern as they need to safeguard the money they have grown over the years.

However, for those of us who are still some way from retirement, we must remember that our pensions are going to have to deliver the income we need for a prolonged period of time – and we can expect only very basic support from the state. The average length of retirement for those who are 65 today is 20 years – yet this could continue to grow significantly in the coming years. This is because the average life expectancy of each of us in the UK is increasing by around 6.3 hours a day for men and 4.6 hours a day for women.

Whilst it is a comfort to know that every time we wake up we are not quite 24 hours closer to the grave than we were the previous morning, it does mean we will require substantial pensions to take us through long, happy and active retirements in the manner to which we would like to become accustomed. Added to this, tax changes announced by the Chancellor in September last year have removed the 55% tax that was previously levied on our pension pots if we died and had sought to pass our investments on.

### Why do low volatility products dominate?

The recent pension changes may well encourage some of us to actively plan to pass on a portion of our pension pots. For these people it may be right to accept more volatility later in life as in reality the pot is designed for the next generation. However, I believe a number of forces have conspired to urge even younger investors, who are decades from retirement, into low-volatility products.

Firstly, the credit crunch persuaded many economists and fund management companies that the world economy will remain stagnant for years to come. A stagnant economy means prices rise more slowly. That in turn means that investors feel they only need to receive a lower level of growth on their investments – as they do not need to keep pace with such fast price rises.

Secondly, the government has moved to auto-enrol all of us in a workplace pension. The clear view taken has been that the new generation of investors this will create must be encouraged into investments that experience low levels of volatility – so as not to scare them away from the stockmarket. Finally, investors have been encouraged into low volatility investment products because the City has realised that if investors do not experience much volatility in

**Important Information**

*Forecasts are not a reliable indicator of future performance. The Fund may have a high volatility rating and past performance is not a guide to future performance. The value of an investment and any income from it can fall as well as rise as a result of market or currency fluctuation and you may not get back the amount originally invested. Investments in emerging markets are higher risk and potentially more volatile than those in established markets. These are Neptune's views and as such this article is deemed to be impartial research. We do not undertake to advise you as to any change of our views. This is not a solicitation or an offer to buy or sell our funds. References to specific securities are for illustration purposes only and should not be taken as a solicitation to buy or sell these securities. Some information and statistical data herein has been obtained from sources we believe to be reliable but in no way are warranted by us as to their accuracy or completeness. Neptune does not give investment advice and only provides information on Neptune products. Please refer to the Prospectus for further details.*

the price of their investments then they do not receive much volatility in the fees they receive each year.

### The importance of taking enough risk

However, none of the above is a good reason to avoid taking the sort of long-term risks that are needed to reach your pension expectations. I believe that rather than experiencing a long period of stagnation, the world economy is growing solidly. This will ultimately mean inflation will return.

The long-term pattern of returns teaches us that shares are the right investments to beat inflation over the long term. To illustrate this, between the years 1900 to 2013, the real value of global equities, with income reinvested, grew by a factor of 325.0 as compared to 8.4 for bonds and 2.7 for treasury bills.* I also believe that there are a number of stockmarkets around the world that have the capacity to grow significantly in the coming years.

In Japan, I believe that a powerful cocktail of reforms, put in place by Prime Minister Shinzo Abe, can lift the economy out of two decades of economic malaise. In addition, the US economic recovery sees no sign of abating, whilst there still remain exciting investment opportunities in the emerging markets, such as the Chinese technology sector. As a result, the Neptune Global Alpha Fund is primarily focused on these areas, with c. 90% of the portfolio invested in the US and Japan, whilst we also have exposure to select Chinese technology stocks, such as social media giant Tencent.

This positioning has paid dividends for the Fund, which has delivered strong returns over the last 5 years, despite short-term periods of volatility. However, an overly cautious approach – which slavishly works to avoid volatility in a portfolio – will likely find it near-impossible to fully exploit the opportunities that the Global Alpha Fund has benefited from. It is important to remember, however, that if you are unsure as to the suitability of any investment, you should speak to an authorised financial adviser.

*“The long-term pattern of returns teaches us that shares are the right investments to beat inflation over the long term.”*

**Neptune Global Alpha: Performance since launch**

*Source: Lipper, as at 30.06.15. A Accumulation share class performance, in pound sterling, with net income reinvested and no initial charges. The performance of other share classes may differ.*

| | Neptune Global Alpha Fund (% Growth TR £) | InvAssoc Flexible Investment av. (% Growth TR £) |
|---|---|---|
| 30/06/2014 to 30/06/2015 | 16.65 | 6.83 |
| 30/06/2013 to 30/06/2014 | 21.73 | 8.12 |
| 30/06/2012 to 30/06/2013 | 11.62 | 15.75 |
| 30/06/2011 to 30/06/2012 | -16.25 | -6.02 |
| 30/06/2010 to 30/06/2011 | 24.43 | 17.04 |

*Source: Lipper, as at 30.06.15. A Accumulation share class performance, in pound sterling, with net income reinvested and no initial charges. The performance of other share classes may differ. FE Crown Fund Rating applies to A Accumulation share class in pound sterling. FE Crown Fund Ratings do not constitute investment advice offered by FE and should not be used as the sole basis for making any investment decision. ©2015 FE. All rights reserved. The Morningstar OBSR Analyst Rating™ is subjective in nature and reflects Morningstar's current expectations of future events/behaviour as they relate to a particular fund. Because such events/behaviour may turn out to be different than expected, Morningstar does not guarantee that a fund will perform in line with its Morningstar OBSR Analyst Rating.*

**Credit Suisse Global Investment Returns Sourcebook 2015*

# Pensions don't have to be taxing!

IN AN EARLIER ARTICLE WE LOOKED AT THE DIFFERENT WAYS YOU CAN TAKE AN INCOME FROM YOUR PENSION, SUBJECT TO YOU BEING OF MINIMUM PENSION AGE WHICH IS CURRENTLY 55. THE KEY POINT TO REMEMBER IS WHEN YOU ARE TAKING AN INCOME FROM YOUR PENSION IT WILL NORMALLY BE TAXED AT YOUR MARGINAL RATE(S) OF TAX WHICH COULD MEAN PAYING TAX AT MORE THAN ONE TAX RATE (20%, 40% AND 45%). IT IS WORTH ALSO REMEMBERING THAT YOU CAN USUALLY ONLY TAKE UP TO 25% OF YOUR PENSION FUND TAX FREE, SUBJECT TO THE LIFETIME ALLOWANCE.

### To take an income tax efficiently you need to understand some basics:

**1.** The standard Personal Allowance is currently £10,600. This is the amount of income you are allowed to earn before you have to pay Income Tax. Your Personal Allowance may be bigger if you were born before 6 April 1938 or if you get Blind Person's Allowance. It's smaller if your income is over £100,000.

**2.** Income above £10,600 is currently taxed at the following rates:

| Tax rate | Taxable income above your Personal Allowance |
|---|---|
| Basic rate<br>20%<br>£0 - £31,785 | People with the standard Personal Allowance start paying this rate on income over £10,600 |
| Higher rate<br>40%<br>£31,786 to £150,000 | People with the standard Personal Allowance start paying this rate on income over £42,385 |
| Additional rate 45%<br>Over £150,000 | |

**3.** Any income you take from your SIPP will be treated as taxable income. So if you currently have taxable income of £40,000 and you withdraw £10,000 from your pension you will pay income tax at 40% on some of this income.

| EG - Personal allowance | £10,600 |
|---|---|
| Employment earnings | £40,000 |
| Pension lump sum | £10,000 |

Total: £50,000, of which £47,500 is taxable, as £2,500 is tax free from the pension.

Tax payable on income of £47,500

| Earnings | Tax payable |
|---|---|
| £0-£10,600 | £0 |
| £31,785 @ 20% | £6,357 |
| £5,115 @ 40% | £2,046 |
| **Total** | **£8,403** |

So in this example tax is payable at 20% and 40% because of the increased income.

### Some tips on taking an income tax efficiently

- **Remember the tax year** – If you need to take £40,000 from your pension and your current taxable income is £130,000 you can avoid paying 45% tax on the £40,000 by splitting the income across two tax years.
- **Will your taxable income change going forward** – If you are retiring from full employment and taking an income it is likely that your taxable income position will fall in subsequent years meaning taking less income in the first year of retirement could make you significant tax savings.

By taking income in smaller regular intervals you could ensure that you take an income from your pension as tax efficiently as possible, meaning more for you and less for the taxman.

Our Accessing Your Pension savings guide covers the Lifetime Allowance in more detail and is free to download at www.alliancetrustsavings.co.uk.

**The tables below show how much tax you would pay in different scenarios.**

| 1) Non taxpayer age 65 | |
|---|---|
| State pension income | £6,029 |
| Take lump sum from pension fund | £20,000 |
| 25% of £20,000 tax free | £5,000 |
| Remaining balance | £15,000 (subject to tax) |
| Total Income | £21,029 |
| Personal allowance | £10,600 |
| Tax payable @ 20% | £2,085 |
| Net payment of lump sum | £17,915 |

| 2) 20% TAX PAYER | |
|---|---|
| Earnings | £30,000 |
| Take lump sum from pension fund | £30,000 |
| 25% of £30,000 tax free | £7,500 |
| Remaining balance | £22,500 (subject to tax) |
| Total Income | £52,500 |
| Personal allowance | £10,600 |
| Tax payable at 20% (on earnings £0 - £31,785) | £6,357 |
| Tax payable at 40% (on earnings £31,786 - £41,900) | £4,046 |
| Total tax on earnings and lump sum | £10,403 |
| Tax on £22,500 pension lump sum | £6,523 |
| Net Payment | £15,977 |
| Total Net Payment including tax free lump | £23,477 |

| 3) 40% TAX PAYER | |
|---|---|
| Earnings | £80,000 |
| Take lump sum from pension fund | £100,000 |
| 25% of £100,000 tax free | £25,000 |
| Remaining balance | £75,000 (subject to tax) |
| Personal allowance | No personal allowance (as total income > £100,000) |
| Total Income £80,000 + £75,000 | £155,000 |
| Tax payable at 20% (on earnings £0 - £31,785) | £6,357 |
| Tax payable at 40% (on earnings £31,786 - £150,000) | £47,285 |
| Tax payable at 45% (on earnings £150,000 - £155,000) | £2,250 |
| Total tax on pension & earnings | £55,892 |
| Tax on £75,000 pension lump sum | £30,250 |
| Net Payment | £44,750 |
| Total Net Payment including tax free lump sum | £69,750 |

If you have any concerns about taking an income and the potential tax consequences please consult a professional adviser.

**Important information**

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# Five reasons why investment trusts will play a major role in the new retirement landscape

**The retirement landscape is changing. The raft of regulatory and tax changes that were introduced in April have made pensions a more attractive savings vehicle giving greater flexibility in regards to how and when people can release money from their retirement savings and also allowing people the opportunity to pass capital down to the next generation.**

We believe that investment trusts are well placed to play a key role in the new post-retirement landscape for five key reasons.

### 1. Inflation-beating income

In the new regulatory regime those approaching retirement will have to ask themselves a single key question: Should I buy an annuity or keep my pension fund invested, and draw an income from it (known as drawdown)? For those with no appetite for risk, annuities will still be attractive as they provide a guaranteed income for as long as you live. Looking at headline interest rates, an annuity might also still look financially appealing. According to the latest annuity tables a conventional annuity for a 65 year old pays a yield of around 5.8%*. At first glance this compares favourably to the yields paid on many equity funds which tend to pay between 2% and 4.5%.

But this is a false comparison. A conventional annuity pays a flat level income for life and over time the purchasing power of this income will reduce and many investors seriously underestimate the effect that inflation can have. For example, as you can see in figure 1, with an inflation rate of just 3.5%, the value of an annuity will effectively halve in less than 20 years. Put another way, an annual income of £5,800 twenty years ago would cover the equivalent purchasing power of about £2,900 today. Inflation linked annuities are available but these normally reduce the income paid at inception.

There are some specific reasons why investment trusts in particular are well-placed to help protect retirees' pensions from the eroding effects of inflation.

- Assets are still invested: Investment trusts generate differing combinations of capital and income which should help offset some of the effects of inflation on a static income.
- Long-term track record of dividend growth: There are a number of investment trusts that have good track records of paying rising dividends. Alliance Trust, for example, has increased the dividend it pays to investors for every one of the last 48 years.

- Structure: Investment trusts are structured like companies and as such they have independent boards that monitor the fund's performance. They have the power to appoint and dismiss the investment manager if investments under-perform. Furthermore, trusts can use gearing to finance further investment and boost income.

## 2. Control of Capital

There are, of course, annuities that provide an index-linked income (of around 2.5 - 3.5% at current rates**) and this is clearly more in line with the returns investors can expect from a well-managed investment fund. But collective funds, including investment trusts, offer one critical advantage: pensioners retain control of their capital.

Part of the income you receive from an annuity is simply the return of capital and when buying an annuity investors lose complete control of their pension fund. If they die within 10, or even 15, years of buying this annuity, the income that would have been paid out is likely to be worth less than the value of their original fund – and what is more, the residual sum can't be left to heirs unless the annuitant has paid out additional fees for 'value protection' on their capital.

By keeping your pension invested, you retain control of your capital and under the new rules, have more flexibility than ever before in regards to what you can take from it and when – including when you are in retirement.

## 3. Reliable Returns

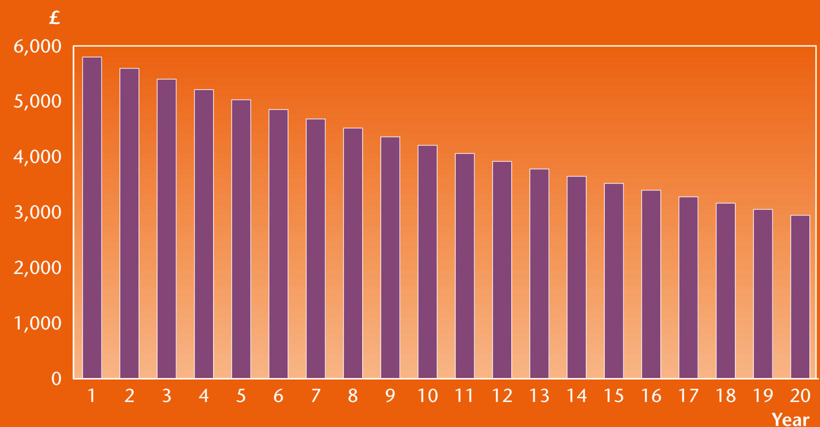
Pensioners who want to ensure their income keeps pace with inflation need a rising income stream. But they also need that income stream to be reliable. With any investment there is always the risk that market movements can impact on share prices, and companies' ability to pay a dividend.

However, the structure of investment trusts helps to mitigate against this risk compared to other investment vehicles. Unlike open-ended funds, investment trusts are not required to distribute all of the income they generate in a year and can retain up to 15% of their gross annual income, which enables them to build up distributable reserves which can be paid out during leaner periods. This has enabled many investment trusts to maintain, or even grow, their dividend at times when dividend distributions by the markets have fallen. At Alliance Trust we are extremely proud of our 48 year track record of paying an increasing dividend – something that we know is very important to many of our shareholders.

## 4. Tax

Retirement planning isn't just about pensions. Many people use savings, particularly tax-efficient ISAs to help provide an income. The New ISA (NISA) has substantially increased the amount of money that people can save in these tax-efficient wrappers. For individuals that annual limit is now £15,240.

**Figure 1: Inflation at 3.5% reduces the real value of a pension by 50% after 30 years** *Source: Internal 2015*




Although savers don't get tax relief on contributions into an ISA, any income taken from these funds is tax-efficient; it doesn't have to be declared on a self-assessment tax form.

Large global investment trusts also offer flexibility for ISA savers. These can be used to grow savings prior to retirement - by reinvesting dividends. Capital can also be used as and when it is needed; investors aren't constrained to the pension rules, which prevent people accessing the funds before the age of 55. After retirement these offer an income option for those that need it. There is no need to shift assets from one tax wrapper to another.

## 5. Diversification

It is one of the principles of investment that higher returns go hand in hand with higher risk. However, it's important to remember that diversification can help spread these risks.

Global trusts like Alliance Trust offer a good degree of diversification, not only because they hold a range of different companies within their portfolios, but also because their mandate allows them to invest in companies from all over the world, they can seek out the best companies, wherever they are listed, rather than being constrained by sector or market.

**Source: Key Retirement Solutions*
***As at November 2014*

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**Risk Information**

*Investments can go down as well as up. You may get back less than you originally invested.*

*Laws and tax rules may change in the future without notice. The information here is our understanding in July 2015. This information takes no account of your personal circumstances which may have an impact on tax treatment.*

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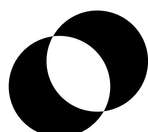


Alliance Trust

# Could Alliance Trust Savings be an

## AT ALLIANCE TRUST SAVINGS WE HAVE BEEN PROVIDING INVESTMENT ADMINISTRATION SERVICES FOR OVER 25 YEARS. SINCE 1986 THE BUSINESS HAS GROWN TO ADMINISTER MORE THAN £7BN OF ASSETS ON BEHALF OF MORE THAN 50,000 CLIENTS. WE HAVE A STRONG 'CLIENT FIRST' CULTURE THAT TRANSLATES TO EXCEPTIONAL SERVICE.

Many of you reading this will currently have an ISA or a Dealing Account with us but you may have your pension elsewhere or what is more likely is that you will have a number of different pension pots with different providers. So why should you consider Alliance Trust Savings for your pension savings?

Let's look at some of the reasons that apply irrespective of what product you hold with us.

### Award winning service

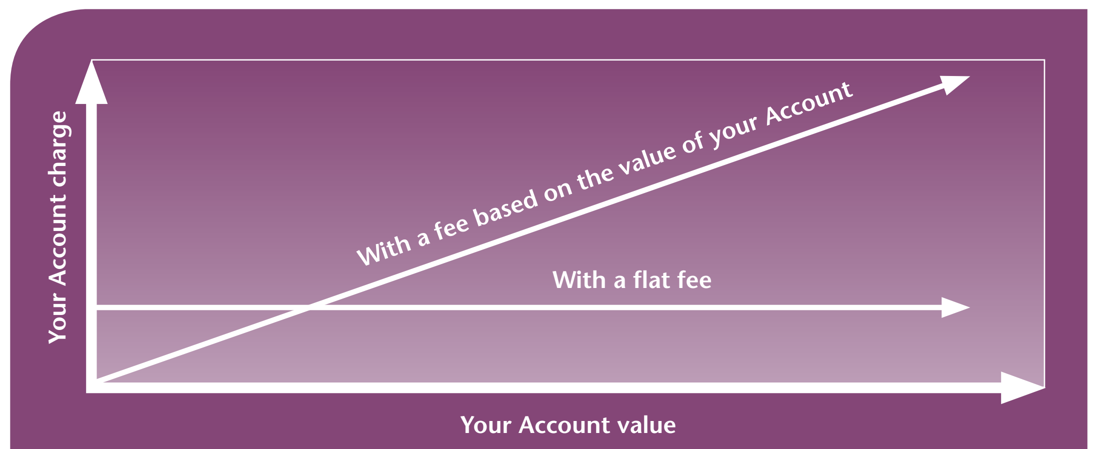
We have received best customer service award for three years running from Shares Magazine. We are really proud of this award as it is not decided by a panel of judges but by our customers voting for us.

### Account fees that don't grow with your investment

We don't charge a percentage of your assets under administration. Our services are provided on a flat fee basis. This means if your investment grows your charge doesn't. Conversely if your account value falls our charge remains the same. If you have a number of disparate pension pots bringing them together could make you significant cost savings. Before initiating a transfer however, you should seek professional advice on the merits of the proposed transfer that is specific to your circumstances. If you are transferring a pension, your existing pension may have valuable benefits which you might lose when you transfer.

### Investment choice

The investments that you can choose typically do not change per product (subject to a few rare exceptions). The wide range of assets available on our platform can help you select a portfolio of investments that suits your attitude to risk from gilts and other fixed interest securities to equities and investment trusts.



# ideal home for your pension savings?

### Manage your account online

You can check the valuation of your SIPP or look at your transaction history online.

Looking at our SIPP we believe that we offer one of the most flexible platform SIPPs in the market. Our SIPP can offer you complete income flexibility. When you decide to take money from your pension (you normally have to be of minimum pension age) we offer flexi-access drawdown, UFPLS and the ability to purchase an annuity from a life company.

If you are already in capped drawdown we will continue to support this option if you wish. Offering the required flexibility is only one piece of the jigsaw as it is important to offer these services at a fair price too.

Platforum is an independent research consultancy that researches the UK platform market. They published research on which provider is the most cost effective if you plan to take income via the flexi-access drawdown option.

Normally clients with this option take their 25% tax free lump sum and then income either regularly or as and when they require it. Platforum identified the lowest cost provider under three scenarios; a saver with a fund of £50,000; one with £100,000; and another with £250,000. Its analysis took account of pension administration fees, drawdown admin fees and drawdown set-up fees. Alliance Trust Savings topped the charts for savers with £100,000 and £250,000.

You may be surprised how much your various pension pots may be worth. Why not dig out your most recent statements, or ask your providers for a valuation? It may be time well spent. Ask yourself a question: are you paying too much for your pension savings? Before you choose a SIPP, make sure you understand its aims and risks. Alliance Trust Savings does not give advice. A SIPP requires active management and investment expertise. You should make sure you review your investments regularly.

### Jeremy Fawcett of Platforum says:

*“...those with large pension pots are likely to pay less on a service with a fixed annual charge like Alliance Trust Savings...”*

*“At £100,000, Alliance Trust Savings pushes Fidelity into second place with its annual fee for drawdown of £276. If you have a fund worth £250,000 Alliance Trust also offers the best value.”*

*Source: Times, 25 April 2015*

### Facts about Alliance Trust Savings

**Real time**
trading in listed securities

**Over 80**
Fund Managers

Comprehensive investment research tool from
**Morningstar**

**General Investment Account**
**Select SIPP**
**NISA**
And an equivalent set of products for children

**B strong**
AKG rating

**Over 10,000**
trades performed by our in-house dealing desk per year

**Over 2,200**
clean share class funds

**Important information**

*Alliance Trust Savings gives no financial advice.*

*Please remember the value of your investment and any income from them can go down as well as up, and you may get back less than you originally invested.*

*Before initiating a transfer you should seek professional advice on the merits of the proposed transfer that is specific to your circumstances. Your existing pension may have valuable benefits which you might lose when you transfer.*

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# *Managing investment risk*

UNLIKE YOUNGER INVESTORS, PEOPLE ENTERING RETIREMENT WHO CHOOSE TO GIVE UP THE GUARANTEED INCOME THAT ONLY ANNUITIES CAN PROVIDE MUST CONSIDER CAREFULLY THE RISK OF INVESTING IRREPLACEABLE CAPITAL.

By Ian Cowie, Sunday Times columnist, in association with J.P. Morgan Asset Management

Beware the danger that if share prices fall soon after retirement it may prove difficult – or impossible – to regain losses. Pensioners who rely on income drawdown – investing for income to fund retirement – should consider the risk that their money might run out before they die.

### Pension reform creates new choices and risks

New freedom of choice created by reforms of the pension rules that took effect on April 6 mean that everyone – not just the wealthy – are able to retain ownership of their life savings after they reach the age of 55 or retire, if they choose to do so[1].

There is no longer any compulsion to invest any of a pension fund in a guaranteed income for life that only an annuity can provide – although everyone remains free to do so, if they wish. Annuity purchase usually requires the saver to irrevocably transfer his or her capital to the insurer that guarantees to pay them an income for life.

Annuities are protected by a statutory safety – enforced by law – that provides a high degree of safety for savers[2]. No such guarantees apply to stock market investments. Share prices can fall without warning and you might get back less than you invest.

### Why pensioners must be particularly careful

Unlike younger investors, people entering retirement who gives up the guaranteed income that only annuities can provide must consider carefully the risk of investing irreplaceable capital. Unlike younger investors, pensioners who rely on income drawdown and do not have any other income may be unable to top-up their fund if share prices fall.

In addition to the existing ability to draw up to 25% of the fund at retirement as tax-free cash, everyone aged 55 or older will also be allowed to drawdown some or all of the remainder of their pension fund. However, it is important to beware these withdrawals will be subject to income tax – possibly at higher or top rates, depending on the amount withdrawn – and could also cause capital erosion of the fund. So it is important to carefully consider the danger that income drawdown might mean pensioners' money runs out before they die.

### A tale of two pensioners

Many people are aware of the risk that share prices can fall and you might get back less than you invest in the stock market. Fewer people may understand the risk of bad timing and how the sequence or order in which events occur may substantially affect fund values.

If share prices fall soon after retirement it may prove difficult – or impossible – to regain losses. For example, pension consultants calculate[3] that if two pensioners both invested £100,000 in income drawdown and both enjoyed average annual investment returns of 7% while drawing £7,000 annual income during the next 10 years, they could end the decade with very different outcomes, depending on when their investments went up or down in value.

To be specific, a pensioner who suffered stock market losses of 11% and 3% in the first and second years of retirement, followed by gains for the next eight years, might end the decade with a fund worth nearly £72,000 (£71,952). However, a pensioner who enjoyed exactly the same gains but during the first eight years of retirement, followed by losses of 11% and 3% in years nine and 10, might end the decade with a fund worth more than £120,500 (£120,537). That's more than half as much again as the pensioner who got off to a bad start.

J.P.Morgan
Asset Management

J.P. Morgan Asset Management are the UK's leading investment trust manager and provide a wider range of investment trust choice than any other UK provider. (Source: Association of Investment Companies as at 30 June 2015, in terms of assets under management and number of investment companies.)

### How investment trusts can help cope with the risks of income drawdown

While investment trusts cannot provide any guarantees and the past is not a guide to the future, some funds – including JPMorgan Claverhouse – have a long history of maintaining or raising dividends over several decades[4]. Investment trusts also seek to diminish the risk to capital by means of diversification and smoothed income payouts. Income and capital are important issues for anyone considering income draw-down.

Investment trusts set out to help individual investors reduce the risks inherent in stock markets by spreading our money over dozens of different companies' shares – and, in the case of international funds, they can also allocate assets over dozens of different countries. The objective is to reduce individual investors' exposure to the risk of setbacks or failures at any one company or country.

### Investment Trusts' Unique Advantages

Unlike other pooled funds – such as unit trusts, open-ended investment companies (OEICs) or exchange traded funds (ETFs) – investment trusts can help smooth income payments by retaining up to 15% of returns from underlying assets in good years in order to top-up payouts in bad years.

Other key characteristics of investment trusts include independent boards of directors – whose job it is to represent shareholders' interests, rather than those of the fund manager – and, in many cases, increasingly frequent payments of income. Five years ago, fewer than one in five investment trusts paid quarterly dividends. Now nearly one in three investment trusts pays dividends every three months[5].

### Look before you leap

Anyone entering retirement who is considering new freedoms to opt for income drawdown rather than the guarantees provided by annuities should remember the risks inherent in stock markets. Share prices can fall without warning and you might get back less than you invest. If you are in any doubt about the best course of action, you should seek independent financial advice specific to your individual circumstances.

Bad timing – or the sequence in which events occur – can substantially affect fund values. If share prices fall soon after retirement it may prove difficult or impossible to regain losses and pensioners' money might run out before they die.

However, while investment trusts provide no guarantees, some – including JPMorgan Claverhouse have maintained or raised dividends for several decades, Investment trusts can help to diminish risk by diversification and smooth income payouts by retaining up to 15% of underlying returns in good years to top-up dividends in bad years.

*1. Source: HM Treasury: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/301563/Pensions_fact_sheet_v8.pdf 2. Source: Financial Services Compensation Scheme: http://www.fscs.org.uk/ 3. Source: Cazalet Consulting, see page 109, table headed: "Sequence of returns" 4. Source: Association of Investment Companies "Dividend heroes" 5. Source: Association of Investment Companies "Dividend Payments increasingly regular: AIC publishes list of investment company dividend dates".*

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*The opinions and views expressed here are those held by the author at the time of publication, which are subject to change and are not to be taken as or construed as investment advice. If you are unsure about which investment options are right for your circumstances please speak to a financial adviser. JPMorgan Asset Management Marketing Limited accepts no legal responsibility or liability for any matter or opinion expressed in this material.*

*The value of investments and the income from them can fall as well as rise and investors may not get back the full amount invested. Past performance is not a guide to the future. Investment trusts may borrow to finance further investment (gearing). The use of gearing will increase the volatility of movements in the Net Asset Value (NAV) per share. This means that a relatively small change, down or up, in the value of a trust's assets will result in a magnified fall or rise, in the same direction, of the investment trust's NAV per share.*

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# Retirement Planning

## – A view from an adviser

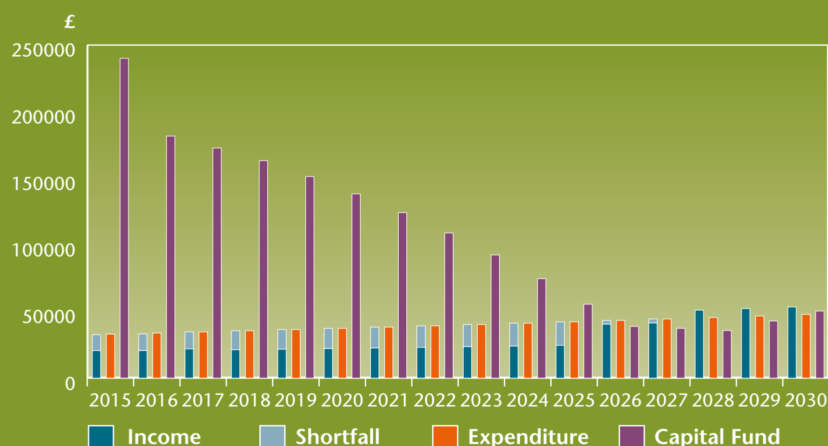
UNDERSTANDING THE OPTIONS YOU HAVE AT RETIREMENT IS ONE THING, UNDERSTANDING WHICH ONE OR BLEND IS BEST SUITED TO YOUR NEEDS CAN BE MUCH MORE CHALLENGING.

We are fortunate that financial adviser Robin Keyte has kindly agreed to bring this topic to life through a case study. We need to be clear that this case study and Robin's response does not represent advice from Robin, his firm or Alliance Trust Savings but is a useful way of getting you to think about retirement planning and it's many intricacies.

Please note the people in the case study below are purely fictional and any likeness to any person is purely coincidental.

### Setting the Scene

Martin and Moira Wilson recently popped a bottle of champagne to celebrate paying off their mortgage on their 3 bedroom bungalow in Somerset.




Martin is 62 and already drawing an NHS pension of £10,000 pa. He has continued working in management on a self-employed consultancy basis 4 days a week earning £30,000 pa. He wants to scale back to 2 days a week to spend more time with his wife Moira, and then to stop altogether at 65.

Martin has a collection of personal and stakeholder pensions worth around £200,000 relating to work before the NHS, and an old retirement annuity from the 1980s worth £40,000, about which he knows little other than the death benefit is a return of premiums, equating to just 1/6th of the actual fund value.

Moira is 54 and left employment with the County Council a few years ago with a deferred pension of £12,000 pa.

Martin has qualifying National Insurance contribution record of 40 years and Moira 32 years. They each have £20,000 in NS&I Premium Bonds and Martin has £40,000 in a Stocks & Shares ISA.

Their son Robert and his wife Paula are both 30 and have just become the proud parents of twins Jack and Emma. They work in the south-east and are in good jobs but are renting a flat as they are saving for a deposit to buy a place.

## The Challenge

Martin and Moira require a net income of £33,000 pa in today's terms, and want to raise a capital sum of around £50,000 to pass to Robert for a deposit on a new family home.

They want to know how they might use the new pension rules they have read about to meet their goals, and whether there are any issues they need to watch out for.

## Quantifying the Shortfall

The target income in retirement of £33,000 pa is after tax, and is assumed to increase each year with inflation. For instance if inflation was 2.5% per annum the target income next year would become £33,825.

Moira does not presently have any income, and Martin's income relates to his NHS pension of £10,000 and self-employed earnings of £15,000. Allowing for some National Insurance Contributions (NICs) and income tax I estimate Martin's net income as £21,350, meaning there is a shortfall this year of £11,650.

Looking ahead, the shortfall will continue at a similar level for another two years until 2018 when Martin retires from work at 65 and his state pension commences.

The shortfall will continue through to 2026 when Moira reaches 65 and starts to receive her Local Government pension. However as Moira was born in 1961 her state pension will not start until age 67 in 2028.

So we can see that it is not until 2028 that the combination of their final salary pensions and state pensions will cover all of Martin and Moira's living costs.

Please note the new state pension regime being introduced in 2016 requires 35 years of NICs to qualify for the full pension. Moira only has 32 years so I recommend she applies for a state pension forecast and enquires about making 3 years' worth of voluntary NICs.

## Meeting the Shortfall

The return of premiums death benefit for Martin's old retirement annuity is often associated with the presence of guaranteed annuity rates (GARs). GARs can be around double open market annuity rates, so it makes sense to let that policy run to age 65 then look very closely at taking the GAR from age 65. This will help to plug the gap to some degree, perhaps around £4,500 pa gross from age 65.

The bulk of the shortfall can be met by Martin's personal pensions, if they are transferred into a flexi-access drawdown arrangement. This will allow income withdrawals to be varied each year to meet the income shortfall.

If the combination of Martin's pensions and income withdrawals is close to the higher rate tax threshold, he can top-up by making withdrawals from the Stocks & Shares ISA, rather than incur higher rate tax.

The cash flow forecast summarises the position. The shortfall in light blue

decreases from 2018 to 2025, and then disappears altogether from 2028. The purple column represents the capital fund which is the combined value of Martin's flexi-access drawdown and ISA and is used to meet the shortfall.

The capital fund is reduced substantially in 2015/6 as I suggest the pension tax free cash of £50,000 calculated as 25% of the fund is drawn out to provide a house deposit for Robert and Paula.

This allows Martin and Moira to help, without diminishing their own accessible cash savings. Allowing for unused exempt capital gift allowances for both of £3,000 last year and £3,000 this year, £12,000 would be treated as an exempt gift and the remaining £38,000 would be treated as a potentially exempt transfer (PET), which would become exempt from inheritance tax (IHT) if they survive the gift by 7 years.

In practical terms, Martin should transfer his collection of personal and stakeholder pensions worth around £200,000 into a self-invested personal pension (SIPP) to gain access to a wider choice of investment funds.

Whenever transferring out of a pension arrangement however, policyholders should first check whether there are any beneficial contract terms that are worth holding onto, such as guaranteed annuity rates (GARs), tax free cash greater than 25%, state funded benefit escalation (pre88 GMP) etc It is also wise to check whether there are any nasty transfer penalties and the total costs associated with the new arrangement (for instance fund charges, platform charges, product charges and adviser charges).

In terms of how to invest the SIPP portfolio, this will depend on Martin's attitude to risk, however he should bear in mind the need to generate returns ahead of inflation and that his capacity for loss will be reduced as he is reliant on the fund to meet his income shortfall.

The new flexi-access drawdown rules allow a pension fund to be inherited so I recommend making a death benefit nomination in favour of Moira, and thereafter Robert and the grandchildren.

More generally, if Martin and Moira have not already done so, I suggest that they engage a solicitor to establish Wills in favour of each other and then on second death, in favour of Robert and their grandchildren. They might also ask the solicitor to arrange Lasting Powers of Attorney (LPA), or alternatively they can organise these themselves online. The Office of the Public Guardian registration cost is £110 per LPA.

We hope you agree that Robin's case study has been thought provoking and has got you thinking about your retirement planning. The key thing to remember is that you are not alone when considering your retirement planning. As a provider we can supply you with guides and also up to date valuations of your SIPP or other investments that you hold.

If you are 55 or approaching 55 you also have the option of contacting Pensions Wise the free and impartial government guidance scheme. Remember, though Pension Wise can only give guidance they cannot and will not make any recommendations this can only be sought from a qualified financial adviser.

**Robin Keyte is a director of KEYTE Ltd who are authorised and regulated by the Financial Conduct Authority (FRN 136129). He is a longstanding fee-based adviser and is both a Chartered Financial Planner and a Certified Financial Planner CM certificant, and has been certified to ISO 22222 for Personal Financial Planning. Robin is a graduate of Imperial College, London and has a science based PhD.**

**In the Money Management Financial Planner of the Year Awards, Robin has won the following:**

- 2014 Overall Financial Planner of the Year
- 2013 Investment Company Planner of the Year
- 2012 Investment Planner of the Year
- 2012 Pre-Retirement Planner of the Year
- 2009 Cautious Investment Planner of the Year
- 2009 Wealth Management Planner of the Year (2010 & 2011 Runner Up)

**Robin has had success in the Personal Finance Society (PFS) Chartered Financial Planner of the Year Awards:** 2013 & 2014 Finalist Chartered Financial Planner of the Year

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# Pensions in facts and figures

## State Pension

**1908**

The first state pension in the UK was the Old Age Pension. The law was passed in August 1908 and the first pensions paid on 1 January 1909 to around 500,000 people aged 70 or more.

**53%**

53% of pensioner income (2011/12) is from state provision versus private pensions. *(Source: Pensions Policy Institute – Pension Facts)*

**£116.30**

Current Basic State Pension is £116.30 and represents 17.9% of weekly National Average Earnings of £649.
*(Source: Pensions Policy Institute – Pension Facts)*

## Market Stats

**£15,800**

Average retirement income in 2014 was £15,800. In 2009 it was £17,779 and £18,663 in 2008.
*(Source: Prudential)*

**1 in 7**

One in seven people will retire without a pension, and women are nearly three times more likely than men to be entirely reliant upon the state pension, because they made no provision of their own.
*(Source: Prudential)*

## Demographics

**89.3**
**86.7**

Women aged 65 today expected to live until 89.3 years while men expected to live until 86.7 years.
*(Source: Pensions Policy Institute – Pension Facts)*

**12,000,000**

Currently there are over 12 million people of State Pension Age or older, by 2050 the figure will be over 16 million.
*(Source: Pensions Policy Institute – Pension Facts)*

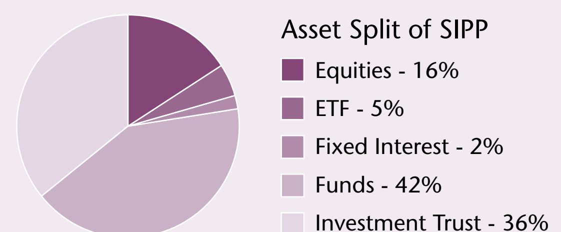
## Our Customers

Average age of our SIPP book **52**

**64** Average age of clients taking an income (clients in drawdown)

Average SIPP value **£167k**

**£211k** Average SIPP value of clients over age of 50




*Source: Alliance Trust Savings July 2015*

# Ways to do business

## ONLINE

**Manage your account online at www.alliancetrustsavings.co.uk**

- Buy and sell online from £12.50
- Same day set-up and trading (conditions apply)
- Online monthly dealing from £1.50 per transaction
- Make use of our research facility investment selectors powered by Morningstar

## PHONE

**01382 573737**

Our real-time telephone dealing service is available during normal UK market opening hours. You can also do this online for a reduced charge. Calls may be recorded for security and monitoring purposes.

## POST

**Alliance Trust Savings Limited**
**PO Box 164,8 West Marketgait**
**Dundee DD1 9YP**

Send us your instruction form and cheque and we'll process your trades. However, you can also do this online for a reduced charge.

For full details of all charges please visit alliancetrustsavings.co.uk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### Risk Warnings

*Specific investments may have additional risks and commitments. You must ensure that you read all documentation regarding any investment you choose to make such as key features and further information brochures.*

*Please remember past performance is not a guide to future performance. You may not get back the amount you invest. The value of your investment and any income from it may fall as well as rise.*

*Laws and tax rules may change in the future without notice. The information here is our understanding in August 2015. This information takes no account of your personal circumstances which may have an impact on tax treatment.*

*Exchange rate changes may cause the value of overseas investments to go down as well as up.*

*Investment trusts may borrow to finance further investment (gearing). The use of gearing is likely to lead to volatility in the Net Asset Value (NAV) meaning that a relatively small movement, down or up, in the value of a trust's assets will result in a magnified movement, in the same direction, of that NAV. This may mean that you could get back nothing at all.*


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