ASSET

THE NEWSLETTER OF MURDOCH ASSET MANAGEMENT

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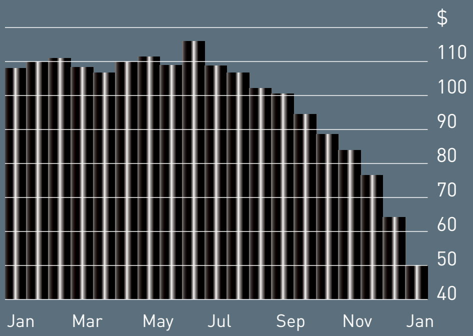
$50 a barrel.
Will the slide continue...?

IN THIS ISSUE

This month includes stories on big changes to pension death taxes and intestacy rules; new tax breaks for surviving spouses and civil partners; an option for inheritance tax exemption; and the Government's new Pensioner Income Bonds. We also look at the ups and downs of the market, bring you fund manager news and outline our new guides.



Oil price per barrel over the last 12 months

> In a big change to the current rules, the 55% pensions death tax is to be abolished.

See Pension Changes article for details

Market update

The biggest story of the last year is the falling oil price, with Brent Crude dropping below $50 per barrel – its lowest level since May 2009. OPEC has decided against reducing supply, the US is forging ahead with fracking and demand has fallen, particularly with cars travelling further on a litre than ever before. The Russian economy needs an estimated $103 per barrel to balance its budget so its production has hit a 20-year high to make up some of the shortfall, and exports from Iraq are back to 1980 levels. In combination, there is little indication of higher oil prices in the short term.

The Bank of England suggests that only sustained unemployment below 7% (currently 6%) and wage price inflation yet to come through would support a rise in interest rates, however with energy prices falling, there is potentially more scope for the tentative economic recovery to survive one.

The Eurozone is a concern, with GDP growth difficult to come by and member states imposing austerity measures to balance their budgets. Unlike the US and the UK, the European Central Bank has not initiated Quantitative Easing but its likelihood and the ultra low interest rates have already dragged the Euro down against Sterling and the US Dollar.

In Japan, the Yen has fallen 10% compared to Sterling, which in turn fell against the US dollar, with investors expecting interest rates to rise in the US first. Shinzo Abe's new 'Abenomics' fiscal policy includes depreciating the Yen to boost exports and import inflation into an economy that has flatlined for 25 years, however in our opinion, Japan remains broken.

Investment prospects for this year are mixed, particularly for those who are heavily invested in oil and other commodities, as well as in traditional supermarkets, which are being attacked on all sides by discounters, online shopping and higher quality offerings. However, there are still plenty of companies with good growth prospects, healthy balance sheets and decent profits to be harvested. And then there is the Swiss Franc...

Spouse to inherit ISA tax advantage

Chancellor George Osborne has announced several new tax breaks for people following the death of a spouse or civil partner, which come into effect on 6th April 2015. Whilst it remains unsaid, this probably sounds the death knell for the promise of a £1m personal inheritance tax threshold.

As of April, when an ISA saver dies, the surviving spouse or civil partner will be able to inherit the tax advantage. Survivors will be given a one-off ISA allowance equivalent to the value at the date of death and can use their own assets to fill it. This does away with the complexities of asset transfer and means that there is no need to alter wills that would ordinarily have left ISA assets to the next generation or to a Will Trust.

It is also proposed that widows' pension annuities are to be exempted from income tax, easing what is often a substantial reduction in pension income when a partner dies.

Better options for maturing cash ISAs

With interest rates still on their knees, the maturity options at the end of a fixed rate deposit account are poor, particularly within an ISA. If you are lucky, you can secure 1.5% interest or more by locking in to a minimum term of 1-5 years.

The good news is that better rates of return are available from the newly issued Government's Pensioner Income Bonds through National Savings & Investments. They offer a 2.8% gross interest rate for a 1-year tie-in or 4% for for 3 years and tax will be paid at your marginal rate. The bonds can't be bought with ISA money so you would need to cash in your ISAs to obtain them. An alternative is to transfer your cash ISAs to stocks and shares ISAs but only if you are prepared to accept the additional risk associated with it.

For those wanting income, our balanced investment income portfolio is currently yielding 4.14%* – though this doesn't guarantee the future capital value of the fund, which can rise and fall in line with the underlying investments. By putting together a diversified portfolio of different assets from property, fixed interest and the stock market, you should also be able to secure reasonable growth over the long term.

*Current yield based on historic income payments, which can decrease and increase

1.5%

Current return expectation 1-5 year term

2.8%

NSI Pensioner Income Bond return on 1-year tie-in

4%

NSI Pensioner Income Bond return on 3-year tie-in

4.14%

Investment income portfolio current return

Fund manager news

Richard Pease is leaving Henderson early this year, taking his European Special Situations fund to the new Crux Asset Management venture where he will apply the same process as before. Pease is one of our longest-standing preferred managers and we have followed him for the last 15 years. Since the previous stock market peak at the end of 1999, he has returned an impressive 279.36%* compared to the sector average of 78.75%*, which is why we are likely to stay with him, subject to our normal reviews.

*Source: Financial Express Analytics, Total Return, Bid to Bid, GBP£, 31/12/99 – 6/1/15

Two years to IHT exemption: ISAs in the picture

For a long time, business property relief has exempted owners of certain qualifying assets from inheritance tax (IHT) once they have owned them for two years. Traditionally these are shares issued by smaller, less regulated companies listed on the Alternative Investment Market (AIM).

By nature, their risk level is greater than ordinary shares, which is why they receive the tax incentive, however this is an acceptable inheritance tax mitigation route for those prepared to take a much higher risk or who don't think they will live the seven years required for ordinary gifting.

As of a recent budget, AIM shares can now be held within ISAs and still qualify for business property relief, so we spent time researching this area of the market and have chosen two providers to run inheritance tax portfolios for our clients. These are well-established companies with a good track record of managing money in this area through good and bad markets. They can also manage the portfolios through certain platforms, so if you are in the right place you may not need to transfer your money.

This is an interesting area but with additional risks, so we would definitely recommend a meeting to discuss its suitability for you.

Rules change for intestacy

Changes to how an estate is divided up when there is no valid will (intestacy) came into effect on 1st October 2014, with new rules applying to married couples and civil partners with and without children.

In the case of married couples/civil partners without children, the estate will be inherited entirely by the surviving spouse or civil partner.

In the case of married couples/civil partners with children, the spouse or civil partner will inherit all personal possessions such as jewellery, furniture and cars; the first £250,000 of the estate (or all of it, if its value is less than that); and half of the remainder of the estate. As before, the remaining half goes to the deceased's children if they are over 18 or is held in trust until they reach age 18.

No change for cohabitants

An unmarried partner will continue to receive nothing at all, with the estate going to a pecking order of children (or grandchildren if no living children), then parents and finally siblings. An attempt to change cohabitation rules is currently underway in the form of The Cohabitation Rights Bill, which, if passed, will give cohabiting couples similar rights to married couples. In the meantime, making a will remains absolutely essential for unmarried couples wanting their partners to benefit from their assets.

Contesting estate distribution

In England and Wales, the Inheritance Act 1975 allows people to challenge the distribution of an estate if they feel they haven't been adequately provided for. That said, it's a complex, costly and uncertain route, and it can be easily avoided by making a will.

Pension changes

April 2015 will see a range of pension reforms including the much heralded pension freedom. The limits on income drawdown from defined contribution schemes such as personal pensions and SIPPs will be removed, allowing you to draw as much as you want – even all of it.

Although this freedom is welcome, it puts the onus on individuals to ensure that their retirement pension pot provides sufficient lifetime income. Those planning to take advantage of the new rules to boost income while semi retired will need to be particularly careful as once funds are withdrawn, future funding is limited to just £10,000 a year rather than the current £40,000.

Pension fund inheritance

Two significant changes will come into effect in April concerning pension fund inheritance: the first is that anyone can be nominated to inherit pension benefits, including adult non-dependant children; and the second is that the 55% pensions death tax is to be abolished. Under the new rules, money in a pension pot of anyone who dies before age 75 can be inherited free of tax, and beneficiaries of those who die aged 75 and over will pay their normal rate of tax on money that they draw. On this basis, leaving money in a pension fund is a highly tax-efficient option, with beneficiaries in turn able to leave it to their own successors enabling pension wealth to cascade down the generations.

Importantly, the lifetime pension pot allowance of £1.25 million still applies and at the time of death, any undrawn amounts in excess of this figure will be taxed at 55% unless any applicable protection is in place. Inherited pension wealth, however, will not count towards a person's own lifetime allowance.

Below age 75
Uncrystallised (No funds drawn yet)
Current: Can pass on as lump sum completely tax free to any beneficiary, up to the deceased's lifetime allowance
From April 2015: No change
Crystallised (Funds drawn)
Current: 55% charge if paid as a lump sum or dependent can draw funds at marginal tax rate
From April 2015: Can pass on completely tax free to any beneficiary as a lump sum or as a drawdown pension
Above age 75
Uncrystallised (No funds drawn yet)
Current: 55% charge if paid as lump sum or dependent can draw funds at marginal tax rate
From April 2015: Any beneficiary can draw funds at their marginal tax rate or at a 45% charge if paid as a lump sum (Marginal rate from 2016/17)
Crystallised (Funds drawn)
Current: 55% charge if paid as lump sum or dependent can draw funds at marginal tax rate
From April 2015: Any beneficiary can draw funds at their marginal tax rate or at a 45% charge if paid as a lump sum (Marginal rate from 2016/17)

Helpful new guides

We have produced new guides to help you complete the relevant part of your self-assessment tax return for:

- Offshore bond chargeable event
- Reporting tax on fund rebates
- Reporting tax on overseas dividends (HICL and Amber)

We will also be publishing a practical guide to care fees funding and lasting powers of attorney in the next few months.

Please email Margaret at **margaret@murdochasset.co.uk** if you would like copies of any of our new guides.

Care fees: Fair or unfair? You decide...

Given that state help with care fees is very limited, most of us will need to meet the costs ourselves. Looked at in isolation, this seems like a very unfair burden. For many, financial constraints have meant that paying a mortgage has left little or no money to save or invest, and being forced to sell their home – their only asset – to fund their care is understandably galling. The broader picture, however, adds another dimension to the debate.

For the last forty years, Government financial policy has encouraged individual wealth so that fewer people need to rely on the state during their working lifetimes, in retirement and in later life.

During the 1970s, '80s and early '90s, MIRAS tax relief was given on mortgage interest to reduce the cost of borrowing, enabling people to buy and own higher priced homes. In 1980, the 'right to buy' scheme was introduced, which encouraged people living in social housing to buy their properties from the Government, often at 70% less than the market value.

Personal pensions were introduced in 1986, however the Government has remained liable for state pensions, which have been continually strengthened. In the '80s and '90s, numerous national treasures were privatised and sold off at very low prices, enabling individuals to increase their personal wealth and have an investment in the business of the United Kingdom. This continues today with the recent sell-off of Royal Mail at arguably less than its true value.

Finally, throughout time the Government has been fiscally supportive of property prices and the stock market, particularly in 2007 when it bailed out the banks, enabling house prices to remain at worst static then subsequently grow.

A positive perspective

Whatever your view on care fees, responsibility for meeting them is here to stay for most of us. Paying for your own care, in fact, has its benefits: it means that you can choose where you are cared for and perhaps with more comfort than if you were reliant on state provision.

It may mean that your children end up with a smaller inheritance but by making clear and decisive plans for maximising the returns on your estate and minimising the impact of inheritance tax, you'll ensure that you and your family are looked after in the best way possible.

Please get in touch if you would like to know more about our comprehensive care fee planning services.

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MURDOCH
ASSET MANAGEMENT

6 Oriel Court, Omega Park, Alton,
Hampshire GU34 2YT
T: 01420 83517 F: 01420 86180
E: info@murdochasset.co.uk
W: www.murdochasset.co.uk

CHARTERED FINANCIAL PLANNERS CII

design: www.prhdesign.co.uk