

**SUPPLEMENTING
RETIREMENT INCOME**

Pensions rightly provide the main source of retirement income, but they have their limitations. The rates of return from the conventional fixed rate annuities into which most individual pension savings are converted are the lowest for many years, and with increasing lifespans inflation can substantially reduce the value of the income received.

In this situation, investment-based retirement provision has growing appeal. Many advisers are now advocating With Profits annuities as a means of protecting capital values and providing the potential for an increasing income. The fact that an annuity fund is not subject to premature withdrawals makes this a natural home for With Profits, and annuitants can enjoy the full benefit of the smoothed investment returns.

But advisers are also looking beyond pensions, and for most people it makes eminently good sense to complement their pensions with income from other sources, such as Unit Trusts, OEICs and ISAs. These have the advantage that they permit the investor to retain control of their capital and to decide whether to use this for their own purposes or to pass the benefit to their dependants, possibly via tax-efficient gifts.

Some funds also offer the facility for investors to take regular monthly payments of a fixed proportion of the capital value of the fund, in addition to or instead of drawing the natural income. The payments will suffer no Income Tax and will be free of Capital Gains Tax provided they do not exceed the annual CGT exemption (currently £8,800 p.a.) or if they are made from an ISA.

Investors could also use this mechanism to reduce the value of

their estate which would be subject to Inheritance Tax on their death.

A suitable fund for this purpose would be one which provided similar diversity to With Profits by spreading the investment between shares, fixed interest securities and possibly property. The ultimate investment spread would be achieved by selecting a multi-manager Fund of Funds, which employed the talents of a range of leading fund managers.

ISA SEASON

Many people delay making their annual ISA investment until the end of the tax year – which is unfortunate because the best time to buy investments is when other people are not doing so. So the best advice is – don't delay!

As to the question of where to invest, clearly the overriding concern must be to select investments which sit happily alongside the other holdings in each individual portfolio. This means achieving a balance between the three main types of investment - shares, fixed interest investments and cash – in such a way as to reflect both the return the investor needs and the amount of excitement he or she can stand.

Since investment should be for the medium to long term, it would be wrong to base decisions on the expectation of short-term market movements. Equally, however, investors should not ignore clear signals that particular investment markets may have become over-bought. The conspicuous case in point at the present time is the UK commercial property market.

As an asset class property is closer to fixed interest than to shares and is bought primarily for income, but prices have been chased up by hungry investors and yields are now lower than the returns available on cash deposits. So anyone considering property investment

would probably be advised to look overseas rather than in the UK.

The UK fixed interest market is also seriously over-bought as a result of pension funds having to buy fixed interest securities to cover their liabilities to their members. Again, deposit rates are currently more attractive and arguably money which might normally have been invested in fixed interest might now be directed instead to cash.

Up to £3,000 can be invested in a cash ISA and any additional investment up to the £7,000 annual ISA allowance must be placed in a share fund. However, the Government has announced that it intends to abolish the distinction between mini and maxi ISAs and to permit holdings in cash ISAs to be transferred into share ISAs (but not the other way round).

EQUITY RELEASE

There have for long been two types of Equity Release scheme – Lifetime Mortgages, under which interest is rolled-up and repaid out of the eventual proceeds of sale of the home; and Home Reversions, under which a proportion of the value of the property is sold for cash. However, it is only now that regulation (and consumer protection) are being extended to cover both types of scheme.

In consequence, there will in future be a formal requirement that anyone advising on Equity Release must consider both alternatives. In general terms Lifetime Mortgages provide more flexibility but are suitable for shorter time frames, whereas Home Reversions provide certainty as to the value to be retained by the householder. The overriding principle, however, is that Equity Release should be regarded as a last resort, to be considered only when other all means of raising cash (or reducing the taxable value of an estate) have been eliminated.

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