

# FINANCE VIEW

The quarterly finance briefing from Positive Solutions



## Contents

Government Delays Pension Age Rise .....	P1.
New Junior ISA rules announced .....	P2.
What is a Final Salary Scheme ? .....	P3.
10 years to save your retirement .....	P4.
Looking out for the consumer .....	P5.
University to become more expensive .....	P7.
Everyone is talking about pensions .....	P8.
Market overview .....	P10.

## GOVERNMENT DELAYS PENSION AGE RISE

The government has put back plans to raise the state pension age to 66 in April 2020 until October 2020.

Earlier plans to speed up the equalisation of state pension age and a rise from 65 to 66 suddenly appear unfair to some women who received little notice of a two-year wait for their state pensions. This change means the longest delay anyone will experience is 18 months.

In an interview with the BBC, Joanne Segars, chief executive of the National Association of Pension Funds (NAPF), said: "This takes some of the sting out of what was a very raw deal for many women.

"This is a useful bit of leeway. People need time to prepare their finances for the transition into retirement, and there is now a clearer ceiling on what to expect.

"But a lot of women in their late 50s are still being told to wait another 18 months, and many will struggle to bridge the gap. The government could have done a bit more to give them extra notice."



## NEW JUNIOR ISA RULES ANNOUNCED

On 27 July the government announced its final rules for the new Junior Individual Savings Account (JISA).

Junior ISAs will become available from 1 November 2011 and will replace the defunct Child Trust Fund (CTF), which closed to children born after 3 January 2011. The one major difference between JISAs and CTFs is that there will be no contribution from the government. Anyone under age 18 and a UK resident is eligible for a JISA, provided they do not already have a CTF.

Just like conventional ISAs there will be two versions of the JISA – a stocks-and-shares JISA and a cash JISA – and all savings grow free of personal income tax and capital gains tax. No withdrawals are allowed before the child reaches the age of 18.

The earlier proposed annual investment limit was £3,000. However, in a positive move, the government has raised this to £3,600. This higher limit will also apply to CTFs from 1 November, increasing from its current limit of £1,200.

Ian Sayers, Director General, Association of Investment Companies (AIC) said: "Junior ISAs offer a straightforward way to save for children tax efficiently. The use of the well-established "ISA" brand should help build confidence and familiarity with the product.

"The Junior ISA will create even stronger incentives for those committed to saving for their children. An annual investment of £3,600 into the average investment company over the last 18 years would have grown to £147,541, which would be an impressive nest egg, whilst £50 per month into the average investment company over the same time frame would have also grown into a substantial £23,645. What will be important will be encouraging more parents to devote what they can to building a nest egg for their children's future."

Junior ISAs could play a significant role both in funding the growing costs of university education, and teaching children the importance of saving for the future.

# WHAT IS A FINAL-SALARY SCHEME?



A final-salary scheme is an employer's occupational pension scheme. There are two types of occupational pension scheme.

## Defined benefit schemes

These schemes set out to provide a guaranteed retirement income, usually calculated as a fraction of salary for each year of pensionable service. The salary may be salary at the point a member retires, in other words final salary. But, other definitions of salary may apply, for example, career-average salary.

A final-salary scheme is, therefore, a defined benefit scheme.

Because a final-salary scheme provides a guaranteed income, an employer must pay whatever it takes to meet the scheme's liabilities. We can, therefore, consider a final-salary scheme as 'known benefit – unknown cost'. This makes an employer's commitment open-ended.

## Defined contribution schemes

Here an employer decides on the contribution, usually expressed as a percentage of salary. These contributions when added to any employee's contributions are invested to produce an individual pension pot for each employee. When an employee retires, the pension fund that has built up is used to provide an income.

You may sometimes hear these schemes called money purchase schemes.

Because the contribution is fixed but the eventual retirement benefits are not, we can consider a defined contribution scheme as 'unknown benefit – known cost'. This is why defined contribution schemes are popular with employers as they are in control of the costs.



# 10 YEARS TO SAVE YOUR RETIREMENT

A SPECIAL REPORT PRODUCED BY METLIFE

**MetLife**

The UK pensions debate needs to move on from focusing on problems to delivering solutions. Consumers and independent financial advisers can only benefit from a debate which focuses on practical solutions to genuinely pressing problems.

The current generation of over-50s are ten years from retirement and are the first to face a series of challenges that no other generation has faced before. The key to saving your retirement is taking advice and your Positive Solutions IFA Partner has a vital role to play in helping you have the best retirement possible.

Pensions and the future of retirement is one of the biggest issues facing people today and in the future. The government is searching for solutions but it is the over-50s who are leading the way.

On the one hand, the over-50s are benefiting from huge improvements in health and are living longer. The average man now lives to nearly 80 and the average woman to 82; many want to work past traditional retirement ages and enlightened employers are enabling them to do so. Yet on the other hand, retirement saving is under more pressure than ever before. Company pensions are less generous than they used to be, while the value of the State Pension has fallen. In addition, the global financial crisis has hammered private pension saving, leaving the over-50s battling to find enough money to save their retirement.

This is why MetLife's campaign focusing on 10 Years to Save Your Retirement is so important. Using a few simple guidelines it is possible to make a better future for yourself, even if you do have just ten years to save your retirement. Ask your Positive Solutions IFA Partner for a copy of the report today.

# LOOKING OUT FOR THE CONSUMER

The UK financial services industry is one of the most heavily-regulated industries anywhere. Although it fulfils a valuable role, occasionally something can go wrong.

Three organisations exist to oversee the market and protect consumers – the Financial Services Authority (FSA), Financial Ombudsman Service (FOS), and Financial Services Compensation Scheme (FSCS). These are independent organisations, set up by the Financial Services and Markets Act 2000. They play a key role in ensuring the smooth running of the financial services marketplace and in resolving disputes between firms and their customers.

## Financial Services Authority

The FSA is the independent watchdog set up to regulate UK financial services; it exists to protect consumers and ensure an orderly marketplace. The FSA does this by making rules and ensuring regulated firms follow these rules when doing business.

The FSA also makes the rules that govern FOS and FSCS. However, the FSA does not run these organisations. All firms regulated by the FSA automatically come under FOS and FSCS jurisdiction.

## Financial Ombudsman Service

The FOS was set up to provide a no-cost, independent dispute resolution service. In any dispute situation you should first complain to the firm; if this does not resolve your dispute, you have recourse to FOS who will investigate on your behalf.

If FOS upholds your complaint, it has powers to force the firm involved to put you in the position you would have been in had the transaction not taken place. This may involve financial compensation to make good any losses. FOS has powers to order firms to pay compensation up to £100,000 (£150,000 from 1 January 2012).

## Financial Services Compensation Scheme

The FSCS investigates complaints against firms it has declared in default. It is the statutory fund of last resort for UK financial services consumers. A firm is in default when FSCS decides it is incapable of paying claims itself. This will usually be because a firm has ceased trading, has inadequate assets, or is insolvent.

Any compensation that FSCS decides to pay is only intended to cover actual financial loss. Because of the FSCS status as the fund of last resort, there are limits to the compensation it can pay.

## Deposits

The current deposit compensation limit is £85,000. This protects savers should a bank get into difficulty by guaranteeing savings up to this threshold.

If you have more than £85,000 on deposit it makes sense to split it between banks. This is because the limit does not necessarily apply to every bank or building society; it depends on their how they are authorised by the FSA. Some institutions that are part of the same group may have a shared authorisation. Where this is so, the compensation applies to the authorisation, not each institution. This means you need to take care that, even where you have split your savings between banks and building societies, they each have their own compensation limit.

## Investments

For complaints against firms ruled in default from 1 January 2010 onward, the maximum compensation is £50,000. For all other complaints the maximum compensation is 100% of the first £30,000 and 20% of the next £20,000; this gives a maximum of £48,000.

Continued...

### Long-term insurance

This also covers life assurance and pensions.

For complaints against firms ruled in default from 1 January 2010 onward, the maximum compensation is 90% of the claim with no limit. For all other complaints the maximum compensation is 100% of the first £2,000 and 90% of the remaining claim.

### Invest with confidence

Considering the number of transactions that take place it's not surprising that occasionally there are disputes. It is reassuring to know that these independent bodies exist to ensure a fair outcome.





## UNIVERSITY TO BECOME MORE EXPENSIVE

If you have young children it may seem a bit early to begin thinking about university fees. However, with university fees set to increase from their current level of £3,200 a year to as much as £9,000 a year it's never too early to plan.

Recent research shows that children born today will need to find £85,000 in 2028 if they wish to go to university. This compares with £33,000 today. Although inflation over the intervening period will push living costs up, the major cause is fees. With most universities choosing to set their fees at the maximum of £9,000, it is estimated that university fees alone could reach £44,000 by 2028 for a three-year course. (Source: Money Observer, 25 March 2011.)

Few people can fund this much expense from cash flow, so most will need to save to build up a fund of money to help put their children through university. The first place to start is by making use of your ISA allowance. You can invest up to £10,680 in 2011/12 and this limit increases each year, in line with the Retail Prices Index. As well as your own ISA allowance, from 1 November 2011 the new Junior ISA becomes available with an annual investment limit of £3,600. Because ISAs grow free of taxes on personal income and capital gains, they offer the most tax-efficient way of saving for university fees.

Of course, not everyone can make large single investments so it is worth making regular monthly contributions to an ISA. A £50 a month investment in the average investment company over 18 years to 31 January 2011 would have grown to £23,496. (Source: Association of Investment Companies, 14 February 2011.)

Annabel Brodie-Smith, Communications Director, Association of Investment Companies (AIC) said: "Students have never had it tougher, and at a time when austerity measures are starting to bite and inflation is becoming a concern, many parents will also be increasingly feeling the strain.

"But for those who are able to set aside a relatively modest sum, and who have a long time horizon, it's worth considering investing on a monthly basis into a pooled investment vehicle such as an investment company. By investing in a wide range of companies on your behalf, investment companies can spread investment risk across a variety of different companies, sectors, and risk profiles. While investors in the stock market need to be prepared for some ups and downs along the way, historically over the longer term, investors have been rewarded."

# EVERYONE IS TALKING ABOUT PENSIONS

Our rapidly improving longevity and the current economic situation has brought one thing into sharp focus: the pensions landscape as we know it is changing before our very eyes. What is becoming clear is that the pensions we, and our parents, may have taken for granted are now a luxury that employers and governments can no longer afford.

This is an issue that nobody can duck any longer so let's take a closer look at some recent developments in pensions.

## Private sector

The private sector has been refining its pension provision for some time now. The previously ubiquitous final-salary scheme, while not extinct, is a critically endangered species. Affordability and a need to control costs has ushered in a move to defined contribution schemes.

Maybe a bigger problem in the private sector is that 65% of employees have no access to a workplace pension scheme at all. (Source: HM Treasury, 28 July 2011.) The previous government recognised this and from 2012 employers have to set up a pension scheme or use the National Employment Savings Trust (NEST) as the default alternative. This creates the first form of compulsory pensions saving in the UK.

Over time, a minimum contribution of 8% – made up of contributions from the employer and employee, and tax relief – is the requirement, but this is to be phased in gradually.

## Public sector

Employees in the public sector have enjoyed generous final-salary schemes. Unlike private sector final-salary schemes, which are funded in an attempt to cover future liabilities, some public sector schemes, such as the civil service and NHS, work on a 'pay-as-you-go' basis. This means there is no investment fund to draw on: contributions collected from today's members go to pay pensioners. Unfortunately, those contributions are not enough so the taxpayer makes up the difference; now people live longer and collect their pensions for longer, the taxpayer is paying more and more. In 1970 the cost amounted to around 0.9% of GDP; it is now close to 2% of GDP. (Source: HM Treasury, 28 July 2011.)

The government asked Lord Hutton to look into public sector pensions. The resulting Hutton Report called for 'comprehensive reform' and contained proposals to move to a career-average salary rather than a final-salary pension, as well as linking retirement age to state pension age. Lord Hutton also suggested there was a clear argument for increasing members' contributions to relieve some of the burden from the taxpayer.

On 28 July, the Treasury announced its proposals for increases to members' contributions. The proposals state that those earning less than £15,000 will see no increase, while those earning up to £21,000 will see no more than a 1.5 percentage point increase by 2014/15. Higher earners will bear the brunt but any increase will be capped at 6 percentage points.



## State pensions

State pension age was already rising from age 60 to 65 by 2020 for women to bring it into line with men. However, there are proposals to accelerate that timetable from 2020 to 2018 while increasing state pension age to 66 for men and women by 2020.

Beyond this we don't know. However, the government has a stated aim to link state pension age to life expectancy. This means as our longevity continues to improve we can expect to wait longer for our state pension.

In April, the government also published its proposals for pension reform. One of the proposals is for a flat-rate pension for all of around £140 a week. There is no timetable for this yet but expectations are that it is some way off. If and when it does happen, the state second pension (S2P) will be abolished.

Increasing longevity has had a severe impact on another area of pensions: the annuity. A major factor in calculating the cost of an annuity is life expectancy. As people live longer on average, annuities pay out for longer; it follows that this has to affect the amount of income you will receive in return for your money.

Another major determinant in the amount of an annuity is gender. Because women, statistically, live longer than men, women have always received a smaller annuity than a man of the same age, though not for much longer.

In March 2011, the European Court of Justice ruled that gender based annuity pricing is incompatible with human rights. From 21 December 2012 this practice has to end and it is expected to reduce annuity rates for men by 8%.

Until recently, anyone with a pension fund had to use it to provide an income by buying an annuity. For years this wasn't an issue but improving longevity and historically low interest rates mean today's annuity rates are not as attractive as they once were. However, now there is an alternative called income drawdown.

Income drawdown allows you to draw cash direct from your pension fund, which remains invested, rather than buying an annuity. There are limits to protect against your pension fund depleting to nothing but income drawdown offers a useful alternative.

The original thinking behind pensions was sound; however, it has been overtaken by events. Until now, living longer has meant being retired for longer; in the future, it will also mean working for longer. If we want to influence how long we spend retired, then it is, more than ever, down to us as individuals to take control of our own retirement plans.

# MARKET OVERVIEW

After a relatively uneventful second quarter, global stock markets took a beating in the third quarter, as Europe's sovereign debt crisis led to a continued lack of investor confidence. Greece continued to teeter on the brink of default, leading to more concern among investors. Much of the blame for the quarter's underperformance can be laid at the door of current investor uncertainty.

In the UK the FTSE 100 fell heavily across the quarter, turning in its worst quarterly performance since the third quarter of 2002. Inflation and unemployment continued to rise, and the economy continued to stall, amid fears of a fall back into recession.

For a further quarter, Greece dominated Europe. As the quarter came to a close, Greece announced a new property tax. This and other austerity measures led to more support from the wider European Union but mainly Germany.

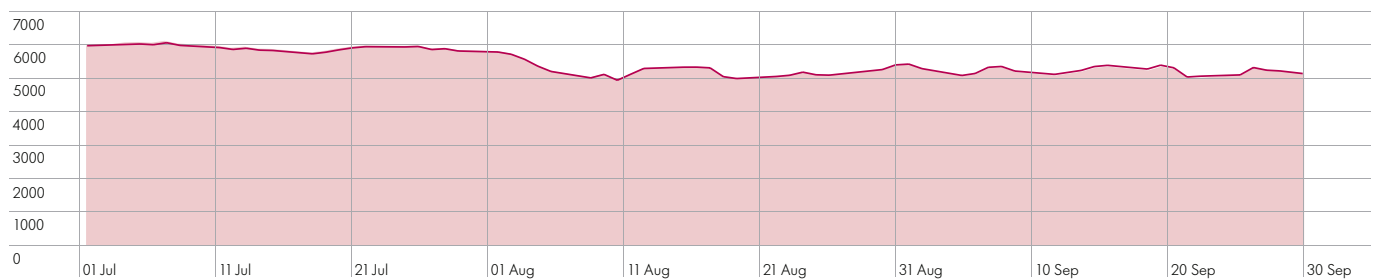
A political stand-off over raising the debt ceiling led the US to the brink of default, resulting in Standard & Poor's cutting the country's AAA credit rating for the first time. In September the US Federal Reserve announced Operation Twist, a \$400bn package of measures designed to kick-start the US economy.

In Japan production and exports continued to rise as it continued its recovery from the earthquake and tsunami. Japan's central bank reported that it expects to find that the country emerged from recession during the third quarter.

All markets suffered a nose-dive in the third quarter. From its opening position on 1 July the FTSE 100 closed on 30 September down 13.7%. In the US the NASDAQ at -12.7% and the Dow-Jones Industrial Average at -12.1% turned in similar performances. Japan, despite its continued recovery, closed the quarter down 11.9%. Perhaps unsurprisingly, Europe suffered the most with the Dow-Jones Euro Stoxx 50 down by a startling 23.5%

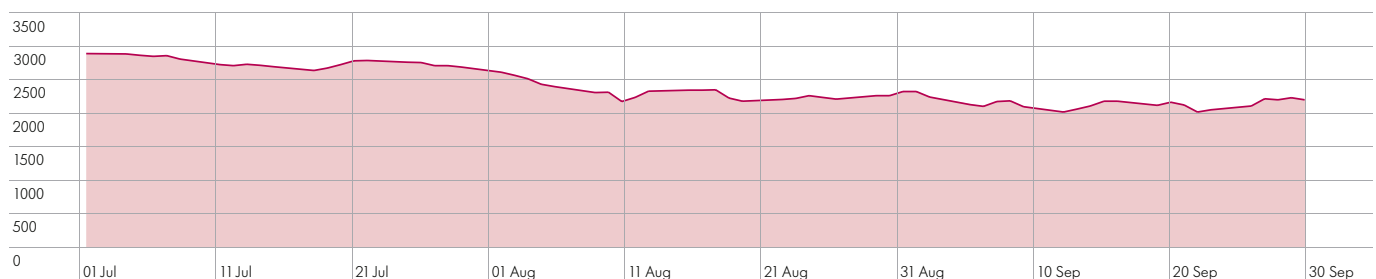
## FTSE 100

From 01.07.2011 to 30.09.2011



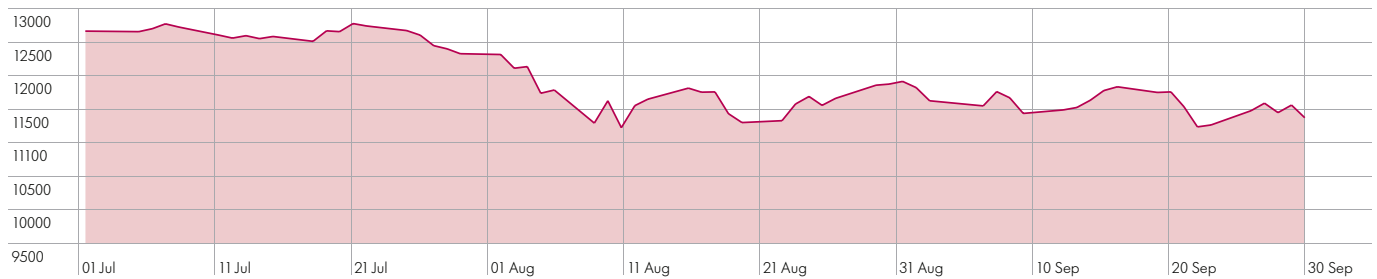
## EURO STOXX 50 PR

From 01.07.2011 to 30.09.2011



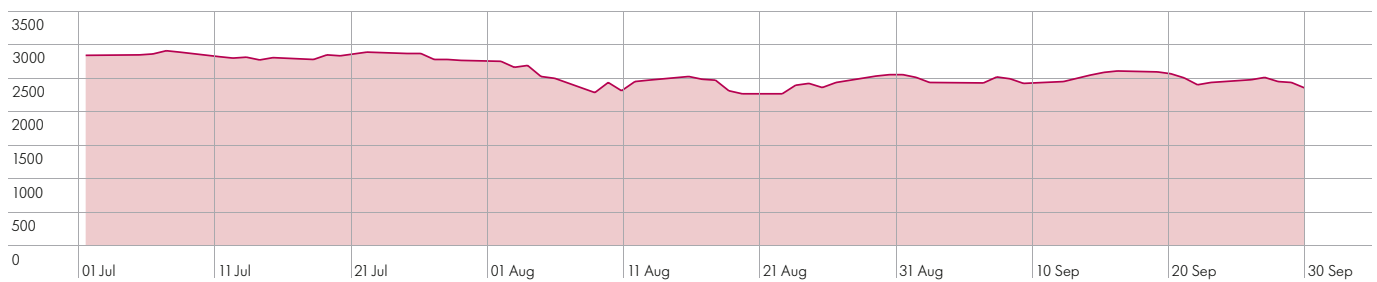
## DOW JONES INDUS AVG

From 01.07.2011 to 30.09.2011



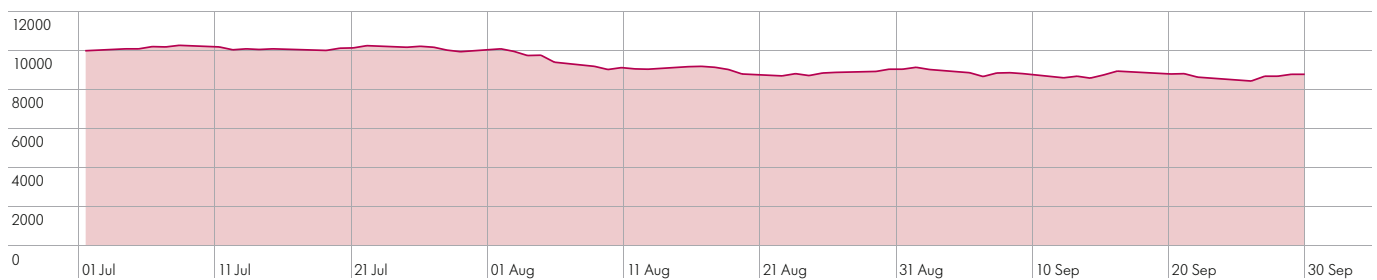
## NASDAQ COMPOSITE INDEX

From 01.07.2011 to 30.09.2011



## NIKKEI 225

From 01.07.2011 to 30.09.2011



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