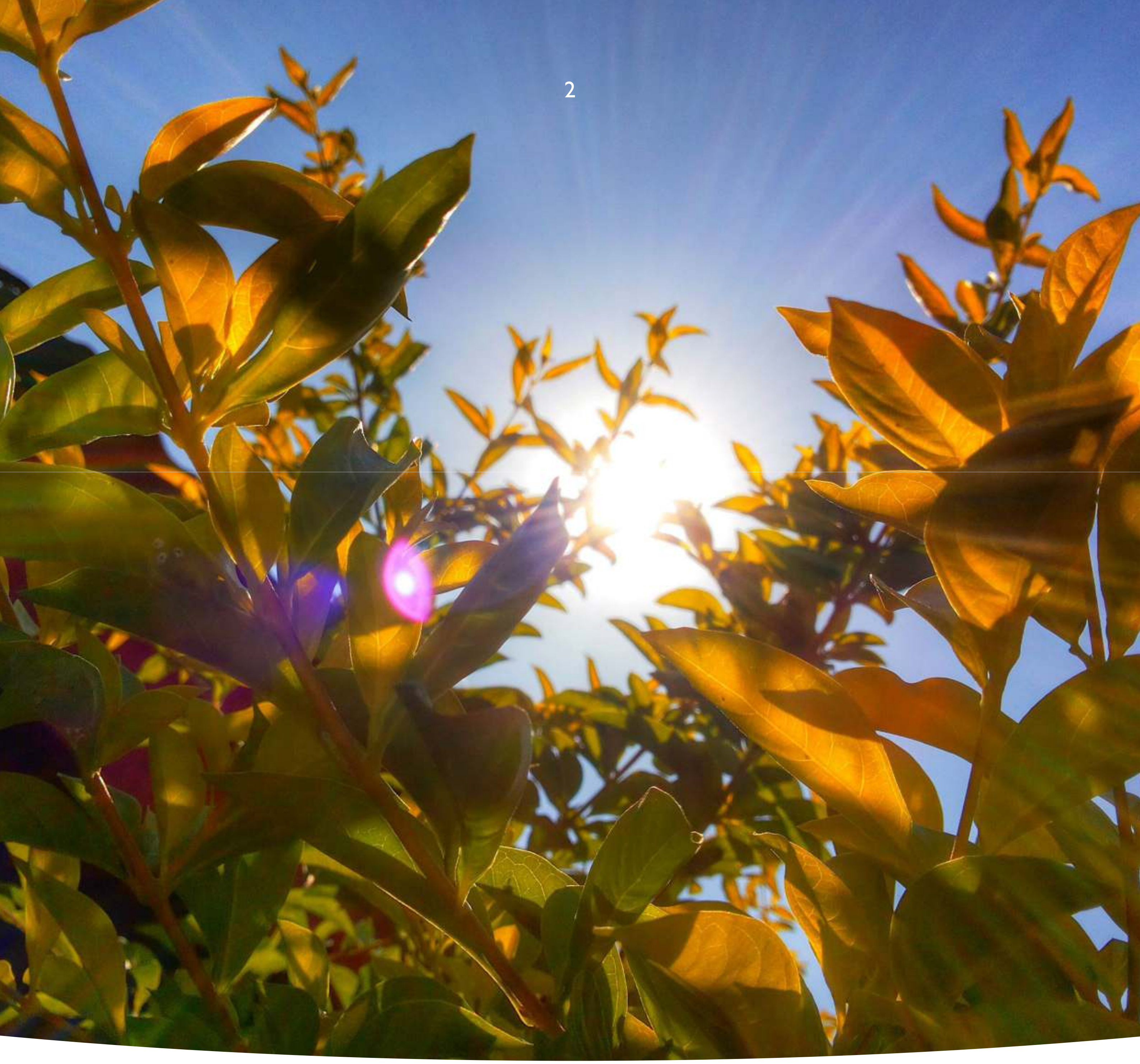
Sovereign
INDEPENDENT FINANCIAL ADVICE

Chartered Financial Planners

15 things your accountant might not tell you

Let your
future grow



Introduction

If you're a business owner, you might well have an accountant. Invaluable in helping with reporting and tax, you might think you're receiving all the financial advice you need.

But, whilst the experience of a good accountant is highly valued, there are many areas of financial planning that their responsibility and expertise might not extend to. So, we've come up with 15 things that your Accountant might not tell you. And, depending on your circumstances, there are likely to be more.

1. Your aspirations and finances are inherently linked

Understanding your future aspirations will shape how you plan to achieve them financially. The first step is to establish your goals in the short and long term; the bigger picture. They might include having a family, buying a bigger home, travelling the world, having that car, or retiring as soon as you can.

Your accountant can identify your immediate financial situation, but financial planning looks to build financial security in your future.

2. How to invest appropriately

Now you've identified your aspirations, you need to save towards them. Ideally, this should be tax-efficient, but you also have to consider how long you're saving for and the most appropriate option available.

Typically, the security of cash savings and the interest they attract is more appropriate for short-term goals, under five years. But, if you're saving for the long term, like retirement, you are likely to want to invest it to help your money grow.

The suitability of investing in Stocks and Shares is usually driven by your circumstances. The level of investment risk you are willing to take and your capacity for loss will help define appropriate investments, as part of a diversified portfolio.

> **Many thanks indeed to the team at Sovereign. They have consistently given us excellent service and quality advice. They have always been flexible and have tailored their service to our changing needs.**

3. How your wealth is projected to change

An accountant is well placed to give you a snapshot of where your wealth stands now. But, with the help of cashflow planning, we can graphically show the effect that your income, expenditure, investment growth and big life events can have on your wealth over time.

Cashflow planning is especially helpful when thinking about retirement; indicating the level of saving required for the lifestyle you desire. Equally, if you're closer to retirement, cashflow planning can show if you can actually afford to retire sooner than expected.

Fundamentally, cashflow planning can also help you plan for sometimes unexpected scenarios, like:

- A loss of income
- The impact of large purchases
- Gifting to family and friends
- Passing away unexpectedly
- Long-term care costs
- Selling your business
- Receiving a windfall
- Downsizing your home

4. Most people underestimate their lifespan

When planning your retirement one of the most important considerations is how long your pension savings need to last.

Unfortunately, previous research found that almost 80% of people over the age of 50 significantly underestimate their longevity; by six years for men and eight years for women, putting them at risk of running out of income. A financial planner, with cashflow planning, can reduce that risk.

5. You should expect and embrace market volatility

Since the financial crash in 2008, we've experienced ten years of relatively steady investment growth. But, towards the end of 2018, volatility crept back into our lives and markets, temporarily, dropped. It's worth reminding yourself that market fluctuations are inevitable, especially at a time of political and economic uncertainty. History has demonstrated this, but it also shows that markets recover.

When markets do drop you only secure a loss if you sell your investment. On occasion doing nothing is the best course of action and making rash decisions certainly isn't. Also consider that when prices are low, if you are saving towards a long-term goal, making additional contributions could be a clever move, as you'll be getting more for your money.

6. Why pensions are brilliant for business owners

First, let's remind ourselves that your Income Tax Personal Allowance is £12,500 as of April 2019. Beyond that, you are taxed:

- 20% basic-rate from £12,501 to £50,000
- 40% higher-rate from £50,001 to £150,000
- 45% additional-rate over £150,000

On dividends, which are also not subject to National Insurance deductions you can receive £2,000 tax-free, then it's:

- 7.5% basic-rate
- 32.5% higher-rate
- 38.1% additional-rate

So, a combination of both is likely to provide the most tax-efficient income. However, a pension can provide an attractive way of extracting additional cash from your business. Naturally, the main benefit is increased security in retirement, but other incentives include:

- Employer contributions are an allowable business expense that can be offset against Corporation Tax. You also don't pay National Insurance.
- Thanks to Pensions Freedoms, access to your pension fund is now unrestricted after age 55
- Upon your death, pensions are usually free from Inheritance Tax
- Should your business fail, pensions are protected from creditors
- A Self-Invested Personal Pension (SIPP) or Small Self-Administered Scheme (SSAS) can be used to purchase commercial property
- A SSAS permits a secured loan back to you as the employer, which can be used to fund business activities and assets beyond the purchase of property

The various types of pension available and the difference between them can be complex. If you'd like clarification, or any other information, our contact details are in the footer of this guide.

7. How much you can save in pensions

Your pension is one of the most effective ways to save long term, but an accountant is unlikely to help you to understand the maximum you can tax-efficiently pay in annually or save over your lifetime.

• The Annual Allowance

The most you can tax-efficiently contribute each year, your Annual Allowance, is set at the equivalent of your relevant UK earnings, up to a maximum of £40,000. If you pay more into your pension than your Annual Allowance, you won't receive tax-relief on the contribution.

The definition of 'relevant UK earnings' is important, especially for business owners, as it doesn't include dividend income you're probably taking. This could potentially limit your Annual Allowance to just £12,500 a year if you are only using your Income Tax Personal Allowance.

If you're doing particularly well, it gets worse! Anyone earning an income of over £150,000 could be subject to a Tapered Allowance. For every £2 of income over £150,000 your Annual Allowance will be reduced by £1. The reduction is capped to £30,000, so if you earn £210,000 or more, you can only save £10,000 tax-free into your pension.

There is an opportunity to pay in more if you haven't used your whole Annual Allowance from the previous three years, assuming you were a member of a pension scheme at the time. 'Carry Forward' lets you roll it up and use it now. It's worth checking with a financial planner what you could tax-efficiently contribute, especially if your income and therefore Annual Allowance is irregular over time.

• The Lifetime Allowance

Whilst there is no definitive limit on the value your pension can be, the Lifetime Allowance is the effective maximum without triggering additional tax. The 2019/20 Lifetime Allowance is £1.055 million and is set to increase annually with inflation.

There is no immediate charge when your pension grows above the limit, tax is only charged when you begin to take pension income over the allowance, at a rate of;

- 25% taken as regular income
- 55% you take as a lump sum

The Lifetime Allowance can be exceeded quicker than you might realise, it's worth checking the value of all your pension savings now and projecting them into the future to meet your aspirations.

8. How to save for your family

Like your Individual Savings Account (ISA) allowance, which is currently £20,000 and should be used each year if possible, your children have an ISA allowance too.

The Junior ISA (JISA) limit in 2019/20 is £4,368. Deposits can either be held in cash or invested, and interest or investment gains are not taxed, just like your ISA. Once your child reaches the age of 16 they're able to take control of the account, but withdrawals cannot be made until they turn 18.

9. Whether you can afford to open the 'Bank of Mum and Dad'

The long-established 'Bank of Mum and Dad' is playing an increasingly important role helping millennials get on the property ladder.

Research found that over a quarter of housing purchases require financial support from their parents, with the total lent during 2018 expected to reach almost £6 billion. On average, parents are lending or gifting £18,000, which is no small sum, requiring careful consideration and planning to ensure it remains affordable and doesn't negatively impact your financial security.

10. The steps to protect your wealth

Knowing how your finances stand is one thing, but you need to plan for the unexpected. It might be an unforeseen expense, or a sudden lack of income due to ill health or a downturn in business.

The first place to start is to build up an emergency fund. It's recommended that you have between three and six-months' expenditure readily available in a cash account. This will give you a financial buffer to fall back on, without having to compromise your lifestyle or jeopardise future plans.

Secondly, protection products can be used to underpin your long-term financial strategy. There are three broad types of cover available;

- Life Insurance which pays a lump sum on death
- Critical Illness Cover which can pay either a lump sum or income on diagnosis
- Income Protection which replaces a portion of earned income if unable to work

Which is appropriate for you depends on your circumstances, but it's entirely possible to require a variety of solutions.

11. How to build an exit strategy

Whether you're planning to sell your business or leave a legacy to your children, there are a lot of considerations.

If you're looking to sell your business, it must be able to function without you. If you are the business, it's not a saleable asset. As well as making your business more attractive to potential buyers, this will provide valuable time to align your business plan with your personal goals. After all, once sold, you could receive the single largest lump sum in your lifetime. Steps to do so include:

- Ensuring the business is profitable and sustainable
- Building a strong, reliable team and rewarding success
- Delegating key tasks to existing employees
- Making the most of technology available to you
- Formalising and documenting every process and agreement
- Preparing your financial accounts for presentation

In terms of succession planning, figures from **The Institute for Family Business** show there are 4.8 million family-owned businesses in the UK, generating over a quarter of GDP. But passing your business to your children isn't always a simple affair and in reality is logistically, financially and emotionally different to a typical exit strategy. You will also need to consider:

- Creating a formal handover plan
- Agreeing any involvement you might have
- Coaching your successors

12. That you can structure your retirement income

Don't just think about your pension, other assets are likely to play a fundamental role in your retirement income too. An accountant can help you understand the base figures and tax implications, but there are other areas to consider.

We don't just mean ISAs or investment portfolios either, increasingly people of varying wealth are using their main property to supplement retirement income. The Equity Release market is going through something of a transformation. According to The Equity Release Council for every £1 of savings withdrawn from a pension in 12 months, 50p of housing wealth was unlocked via Equity Release. And, product options available rose from 58 in 2017 to 139 a year later.

It's also worth noting that taking into account which assets to use is only half of the matter. The order in which you utilise them can affect tax and the longevity of your wealth. Pensions, for example, are usually free of IHT, so in some circumstances, it would be beneficial to use your pension savings after all other assets have been exhausted. We can help you build a bespoke retirement income strategy.

13. Ways to mitigate Inheritance Tax

Where applicable, Inheritance Tax (IHT) is charged at 40% on your estate, which includes the value of your home, savings, and other assets. According to **HMRC**, IHT collected during the 2017/18 tax year hit a record high. Estimates suggest that HMRC collected more than £5.2 billion, an increase of £400 million on the previous year.

You have two allowances available, up to which you don't have to pay IHT when you die:

- The Nil-Rate Band, currently £325,000 and intending to remain the same until 2021
- The Residence Nil-Rate Band currently £150,000 in 2019/20 and rising to a maximum of £175,000 in 2020/21

You can, therefore, have up to £475,000 each, and if you are married you effectively have a £950,000 exemption, as long as your entire estate is worth less than £2 million when deductions begin. There are several ways to reduce your potential liability, including:

- Having a valid, up-to-date will and Power of Attorney
- Making gifts, £3,000 p.a. are exempt but so are 'Gifts out of Normal Income'
- Using your pension to pass on wealth, as they are usually exempt
- Insuring against the likely liability

14. You can benefit from Business Relief

Business Relief is another IHT exemption, available for transferring ownership of particular business assets held for at least two years. You can claim 100% Inheritance Tax relief on;

- A business or interest in a business
- Shares in an unlisted company

You can claim 50% relief on;

- Shares controlling more than 50% of the voting rights in a listed company
- Land, buildings or machinery used in the business

This means that if you die prematurely your business won't need to be split and sold to cover potential IHT liabilities; you can pass your legacy on to loved ones.

There are other opportunities to utilise Business Relief too, via Alternative Investment Market (AIM) and Venture Capital Trust (VST) investments, where you are able to invest in small, unlisted qualifying UK businesses. There are risks associated, but there are also tax advantages if you'd like to explore Business Relief attracting investments.

15. How regularly your financial plan needs to be reviewed

Once you've set out a financial plan and followed the course of action, you can't just put your feet up. Regularly reviewing your plan with a financial planner is crucial for ensuring it remains suited to your needs and aspirations. It should be, at least, on an annual basis.

As with all of life's plans, things go awry, opportunities can present themselves or you may simply have a change of heart. Your aspiration, priorities and personal circumstances are all likely to change over time. Then you must consider political, economic and market influences beyond our control.

Who is Sovereign IFA?

We are a firm of Chartered, Independent Financial Planners based in Thornbury, North Bristol. Established in 1992, we have been serving the community for almost three decades. We love working with clients in the South West, but equally, enjoy working with clients throughout the UK.

From our experience, many business owners are concerned about growth, becoming more profitable and attracting new clients. Simultaneously, they want to ensure new and existing customers are given excellent levels of service.

With so much to juggle, you might have very little time available to address the wider company financials; even less to focus on their own personal finances. With our expert help, we will guide you every step of the way as you secure your business for success and work towards your own personal objectives and aspirations.

We are here to help answer those questions. Call one of the Sovereign team on 01454 416 653 or email **hello@sovereign-ifa.co.uk** to begin your journey.

Sovereign
INDEPENDENT FINANCIAL ADVICE

Financial Planners
Chartered

Sovereign, Unit 4, Thornbury Office Park, Midland Way, Thornbury, Bristol, BS35 2BS
01454 416653 hello@sovereign-ifa.co.uk www.sovereign-ifa.co.uk

Let your future grow