Report for Alani Khan [CS2]

(prepared in Aug-2014 in tax year ending 05-April-2015)

1.Objectives

Review your existing investment trust holding and those inherited from your grandfather.

Advice on investing a cash sum arising from inheritance.

Understand the pensions changes and their impact on your planned retirement at 50 with net income £20,000pa in today's terms, and the rate of pension contributions and other provision required to achieve this.

I have identified further objectives:

- deposit for a mortgage should you get onto the property ladder
- flexibility to allow option of settling down and starting a family
- provide replacement income to retirement if long-term sick
- with continuing business growth, tax planning associated with incorporating your business and taking mixture of salary and dividends if more efficient than continuing as self-employed
- potential care costs.

2.Assumptions

I have used the following assumptions in the preparation of this report.

PA	
2.50%	Price_Inflation. Bank of England May-2014 Inflation Report . HMGovernment's CPI target 2%.
4.00%	House_Price_Inflation. In line with wage inflation assuming an approximate historic relationship of inflation+1.5%.
0.50%	Interest_rate_for_cash. Current Bank of England Base Rate.
3.00%	Return_on_Index-Linked_assets (inflation+0.5%).
2.00%	Return_on_Gilts (HMGovernment Securities) per redemption yields reported by Debt Management Office.
3.00%	Return_on_Corporate_Bonds assume approximate historic 1.0% credit spread over gilts.
6.00%	Return_on_Equities assume approximate historic equity risk premium of 4.0%, being the difference between expected rate of return from equities and the risk-free rate from gilts (Barclays Equity Gilt Study 2013).
5.00%	Return_on_Commercial_Property: 10year total return to 31-12-2013 per IPD-UK Annual Property Index was 6.3%pa, conservatively reduced by $^{1}/_{5}{}^{th}$.

All returns assumed to be total returns combining income and capital appreciation.

Average life expectancy is currently 82. Allowing another 10 years for luck we will also project to 92. Alani's assumed date of birth 01 August 1989.

Care costs in today's terms assumed to be £641pw residential and £874pw nursing, Lang & Buisson, Care of Older People 2013/14.

3.Assets_&_Liabilities

Your estate is summarised below. There are no reported liabilities although you may seek to get on the property ladder in the future with a mortgage. I have not included a value for your business.

Cash	
Savings	£4,000
Inheritance	£120,000
Investments	
Biotech Growth IT	£23,800
Aberdeen New Dawn IT	£9,125
JPMorgan Income&Growth IT Inc shares	£9,350
	£166,275

The JPMorgan Income & Growth Trust has income shares, capital shares and units. We have assumed the holding you have inherited is income shares as the holding size is similar to Aberdeen New Dawn. Please confirm.

4.Income,_Tax_&_Expenditure

Your income, tax and National Insurance contributions (NICs) are summarised below.

Self-employed earnings	£35,000	
Interest (gross)	£1,680	
Dividends (gross)	£613	
Total Gross Income	£37,293	£37,293
Less personal allowance	-£10,000	
Taxable income	£27,293	
Income tax	-£5,397	-£5,397
NICs	-£2,577	-£2,577
Net income		£29,318

Your stated expenditure £27,000pa is covered by net earnings. Due to the lumpy nature of your earnings, some months good and others not, you rely on your father to assist when cashflow is poor. You need to establish an accessible cash fund and I agree with setting aside £20,000 for this. I recommend NS&I Premium Bonds for tax-free deposit returning ~1.35%pa to “a person of average luck”.

Your expenditure is likely to increase with inflation. There is a need to commence pension provision and establish income protection so your expenditure will rise with the associated premiums.

I do not think there is much tax benefit in incorporating presently given your self-employed earnings have increased from £15,000 to £35,000. However if this is a trend they may again increase to £55,000.

Assuming gross earnings of £55,000 and keeping business costs similar, I estimate net self-employed income of £41,337 versus a mixture of salary and dividends of £42,451 net.

If earnings continue to rise I recommend seeking advice from your accountant about incorporating, and how best to introduce £30,000 to the business. For instance if incorporated it could be through a director’s loan account.

5.Attitude_to_Risk_&_Capacity_for_Loss

Allowing for £30,000 cash introduction to your business and £20,000 cash savings, there is £116,275 to invest, £74,000 being from cash.

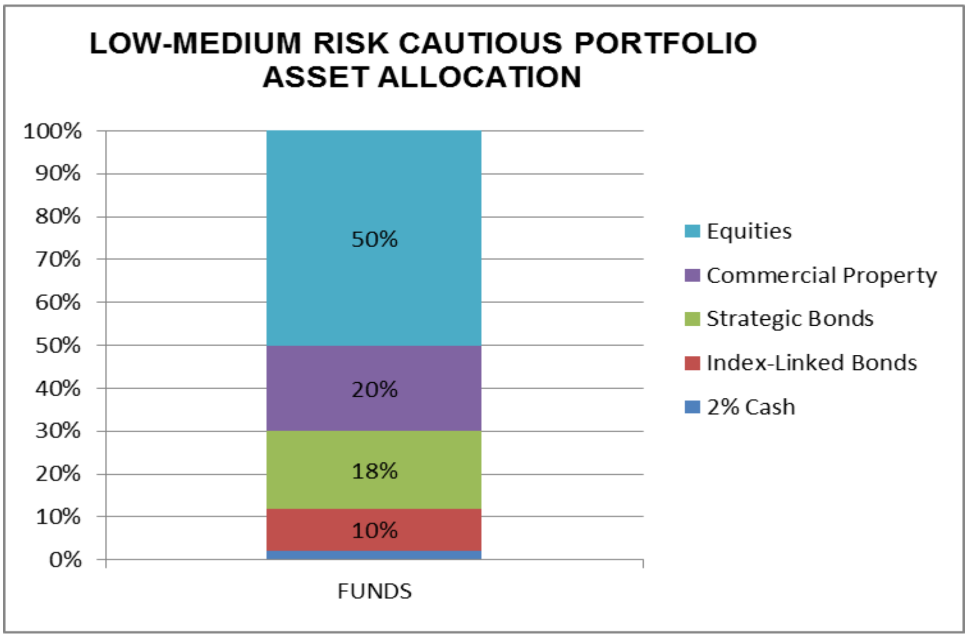
You describe yourself as a realistic investor and only want 50% exposed to global equities.

Allocating the residue to other asset classes like fixed interest and property, I would describe that as a low-medium risk cautious portfolio.

I view your capacity for loss as low-medium as you have a fledgling business with volatile earnings and it is possible you might decide to purchase a property in the next 5-10 years and/or settle down and start a family, when you would need to draw on your investments.

For pension contributions, I view your attitude to risk and capacity for loss as high. You will not have access for over 30years.

6.Proposed_Portfolio_Asset_Allocation



The allocation to cash will cover the wrap platform charges and provide a little liquidity.

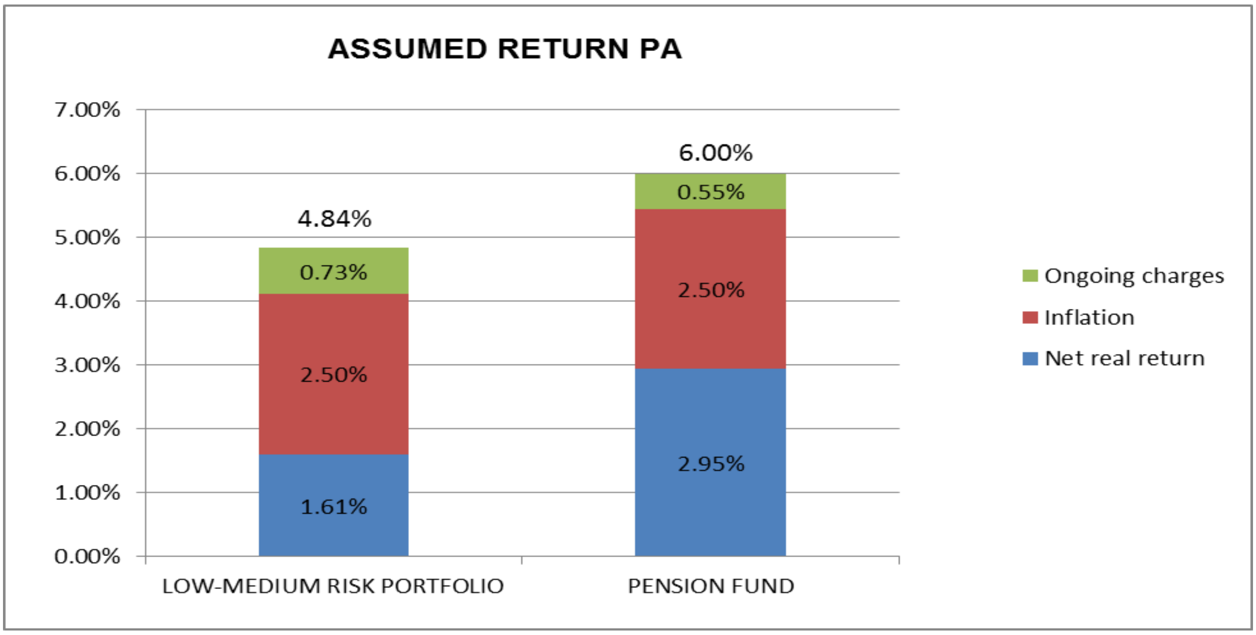
I have not allocated to gilts or investment grade UK corporate bonds which I view as unattractive given the outlook for rising interest rates. Similarly I have slightly reduced the allocation to bonds in favour of UK commercial property where the outlook is more positive.

The equities element is normally invested 50%:UK, 40%:Overseas and 10%:Emerging Markets, however there is emerging markets exposure through the global funds and indirect exposure through blue-chip UK equities.

Applying our investment assumptions to the asset allocation the estimated return is 4.84%pa for the low-medium risk portfolio.

Future pension contributions assumed invested 100% in equity funds returning 6.00%pa.

Reduction through charges shown below.



If we provide an ongoing service, our fee of 0.5%pa is in addition to the green ongoing charges. Our fee charge will increase if assets grow or decrease if assets go down in value.

7.Cashflow_Analysis

The cashflow analysis uses the following assumptions:

- Your earnings escalate at 4.00%pa in line with average earnings index

- Voluntary NICs paid from retirement to age 60 for 35year history. Full state pension based on new flat rate pension introduced in 2016 and commencing age 68, rising with inflation at 2.50%pa.

- Any pension premiums escalate with earnings and paid to retirement. The earliest date pension benefits can be drawn is age 57, with the 25% tax-free cash invested into the investment portfolio and the residual fund used to support income withdrawals under the new drawdown rules.

- Expenditure £27,000pa rising with inflation to retirement. Target retirement income £20,000pa net in today's terms. Please confirm the target retirement income should be less than your present living costs.

- Expenditure to include income protection premiums to retirement

- Income tax personal allowance rises with inflation. Conservatively basic rate band rises at 1.00%pa.

- Low-medium risk investment portfolio established of £116,275 using Alliance Trust Savings (ATS) Investment Dealing Account (IDA) and ISA

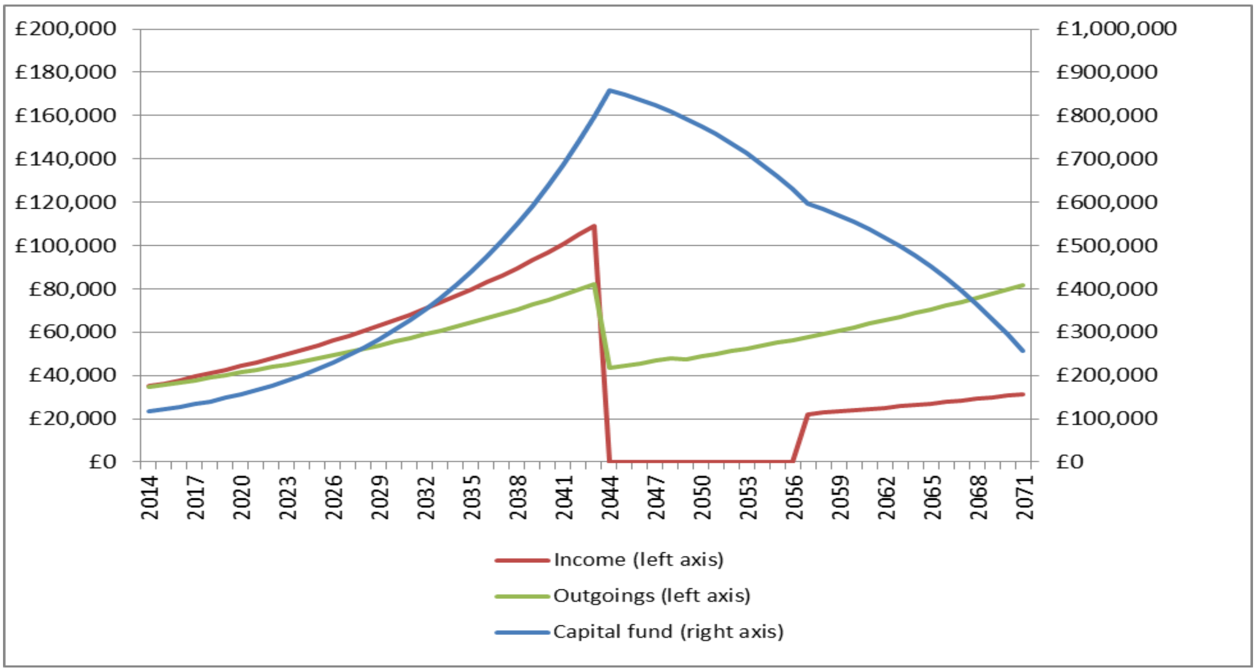
- Deficit in retirement income drawn from, and surplus income invested into ATS IDA run as low-medium risk portfolio. Portfolio alone will fund retirement income from age 50-57.

- Care costs in last 5years, with 3years residential followed by 2years nursing care. Costs escalate 4.00%pa (primary overhead wages).

- General expenditure reduces ½ when care commences

- No future inheritance.

Although you would benefit from making future pension contributions from your earnings, you do not have sufficient disposable income to afford this. Assuming no future pension contributions, net retirement income of £20,000pa in today's terms and no provision for care, the earliest age you could retire is 55 (per illustration below).



Projecting to 92 your earliest retirement age would be 57.

The Capital fund represents your investment portfolio.

Between 55 and state pension age 68 the Capital fund is heavily depleted.

Extending this to an 18 year period through retirement at 50 is too much for the Capital fund to support.

Bringing retirement age down to 50 (again without consideration for care) would require additional provision by way of an annual pension premium starting at £2,000pa, escalating with earnings. Projecting to 92 this rises to £3,000pa.

Taking care costs into account requires an annual pension premium starting at £7,400pa, escalating with earnings. Projecting to 92 this rises to £8,000pa.

Still taking care costs into account, changing the target net retirement income to £27,000pa in today's terms requires an annual pension premium starting at £11,100pa, escalating with earnings. Projecting to 92 this rises to £12,450pa.

Stopping work at 50 denies your arrangements additional years of accrual and accumulation. Your financial planning objectives will be more affordable if you:
- plan on working to a later age say 55 or 60
- continue working part-time in your 50s
- sell your business giving a capital sum to re-invest.

Also you should build pension contributions into your business overhead for scope to make sustainable future contributions.

8.Pensions

You do not get tax relief buying investment company shares. To buy investment company shares within a pension plan would require a self-investing personal pension which is too expensive for a small pension pot.

The new pension rules:

-Allow 25% tax free cash at retirement and then unrestricted drawdown of your residual fund, with drawdown payments treated as taxable income. You do not have to buy an annuity.

-Reduced the Lifetime Allowance (the maximum pension fund allowed before additional tax charges) to £1,250,000

-Schedule an increase in minimum pension age to 57 from 2028

-Include a guidance guarantee giving you impartial information on your options at retirement.

I recommend commencing pension contributions to an Aviva stakeholder pension using their Global Equity Income fund. Overall annual charge 0.55%pa.

The minimum investment term is 32years so 100% in equities is appropriate.

Your premiums will attract immediate basic rate tax relief, for each £80 you pay £100 is invested. I recommend starting contributions at this level (using cash savings to fund initially if you have to) and then increasing as your business grows. Ideally they should be 15%pa of your earnings.

If you subsequently incorporate, I recommend the premiums are paid as employer pension contributions to benefit from corporation tax relief.

9.Investment_Recommendations

You have £124,000 in cash savings and investment trust holdings valued at £42,275.

Existing Arrangements

	OCF	Gearing	Income Yield	Discount/ Premium	Book Cost	Current Value	Gain/ Loss
Biotech Growth IT	2.09%	8.00%	0.00%	-10.09%	£12,400	£23,800	£11,400
Aberdeen New Dawn IT	1.06%	7.00%	2.00%	-9.17%	£9,500	£9,125	-£375
JPMorgan Income & Growth IT Inc	1.30%	30.00%	4.60%	-12.37%	£10,200	£9,350	-£850
					£32,100	£42,275	£10,175

Biotech Growth is pregnant with gains exceeding your annual capital gains tax (CGT) allowance of £11,000. It has a high ongoing charge of 2.09% pa and is invested in global equities narrowly focused on the biotechnology industry, with 85% in US presently.

Aberdeen New Dawn is at a small loss and invested in Asia-Pacific-ex-Japan equities.

JPMorgan Income & Growth holding is at a small loss and mostly invested in UK equities. It has a higher gearing meaning the trust has borrowed money to invest, representing a higher risk compared to a standard UK equity fund.

With historically low inflation and interest rates we are in a low return environment. I recommend focusing on holdings with lower ongoing charges, keeping more of the return for you.

For exposure to global equities I have recommended alternative investment trusts with lower ongoing charges and gearing.

This is contrary to your request to retain your investment trust holdings as part of your portfolio. However they do not fit with your attitude to risk, capacity for loss or need for low charges.

If all are sold the small capital losses for Aberdeen and JPMorgan will offset the gain on Biotech, avoiding any CGT liability.

Outline_Proposals

For your £20,000 cash savings I recommend NS&I Premium Bonds which are accessible and provide a tax-free return ~1.35%pa to “a person of average luck”. Allowing for £30,000 cash introduction to your business, there is £116,275 to invest, including £74,000 from cash.

Whilst pension rules allow scope to make large single premium contributions, I do not recommend doing so for the following reasons:

- Your chosen retirement age is 50 whereas a pension plan cannot commence payment of benefits until 57

- You may seek to buy a property in the next 5-10 years and require capital for a deposit. Not accessible if tied up in a pension

- You may settle down and start a family in the next 5-10 years and require your investments to support your early years. Not accessible if tied up in a pension.

Your overriding need is for flexibility whilst at the same time achieving tax efficient returns ahead of inflation, which is best achieved with a portfolio of investments trusts, OEICs and unit trusts making full use of your annual NISA subscriptions allowances.

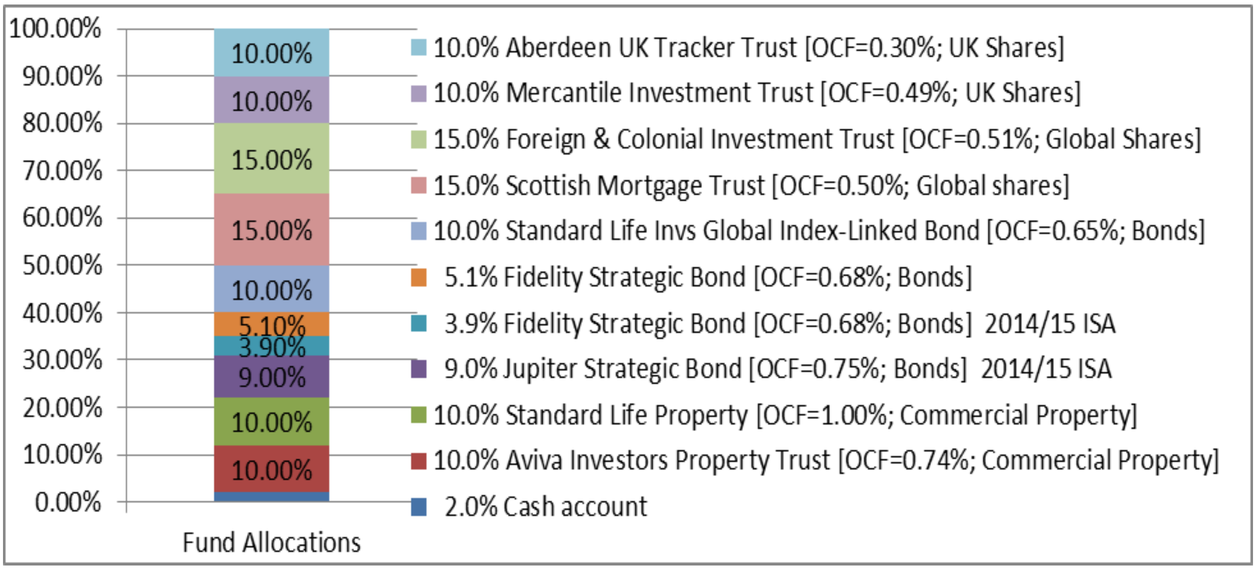
Recommendations

Invest £15,000 into ATS ISA focusing on fixed interest and property where income yield is gross tax-free.

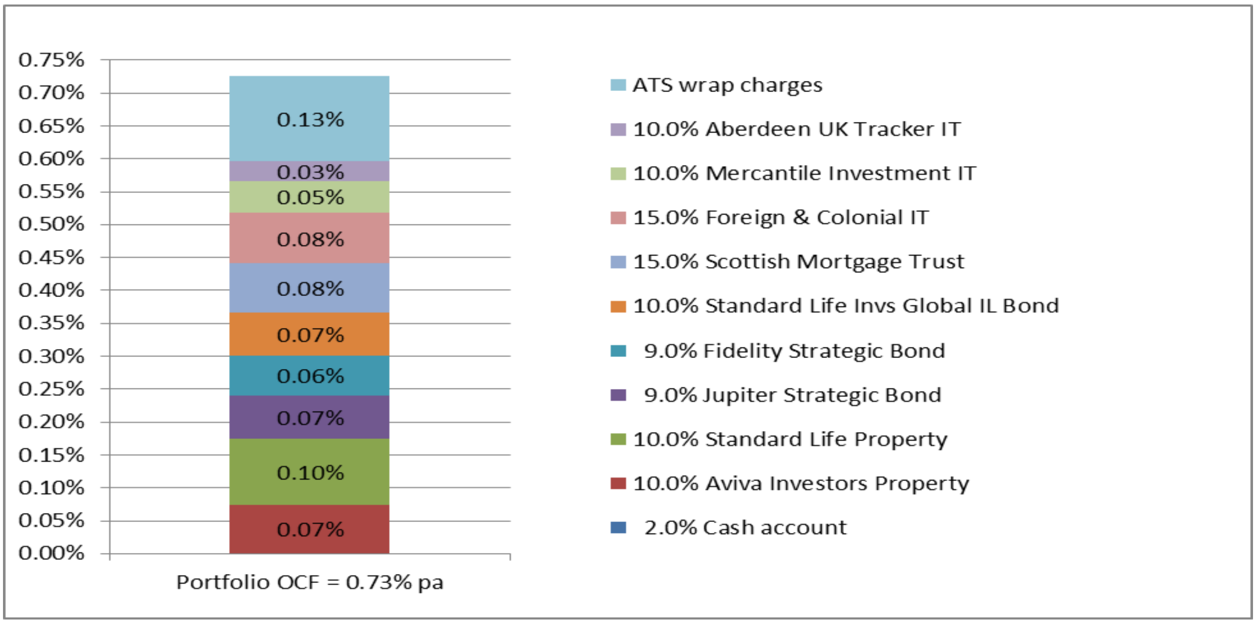
Re-register your investment trust holdings to ATS IDA with a view to disposing and re-investing, together with additional £59,000 from cash.

In future years, arrange bed'n'ISA transactions moving holdings from IDA to ISA, focusing first on fixed interest and property before moving to equity funds.

The ATS platform charge is £75pa per account and dealing charge of £12.50per deal. I recommend the following portfolio as a good match to your attitude to risk and objectives.



The overall OCF including ATS platform charges is 0.73%pa, illustrated below.



I have focused on investment trusts for equity exposure:

- Scottish Mortgage Trust has 15% gearing and Foreign & Colonial 7%, so less overall exposure to gearing
- Aberdeen UK Tracker has an appealing 5.80% discount not available through unit trust/OEIC trackers
- Mercantile and Foreign & Colonial have attractive discounts of 11.70% and 10.14% respectively.

I have used active-managed funds for fixed interest and commercial property as I am not satisfied an index tracker fund is suitable presently. I have assumed new investments will be made keeping to the same asset allocation and annual portfolio re-balancing.

10.Protection

Protecting income against incapacity to retirement using personal income protection.

Cheapest quote on standard rates with premium and benefit rising with earnings; Friends Life £11.50pm premium and £17,496pa cover with 6months deferred period.

Consider Private Medical Insurance to obtain faster treatment times to speed up return to work from ill-health.

You could also consider critical illness cover although this is a lower priority.

11.Will_&_Power_of_Attorney

Engage a solicitor to establish a Will and Lasting Power of Attorney (LPA).

Alternatively organise LPAs yourself online. The Office of the Public Guardian registration cost is £110per LPA.

12.Next Steps

Item	Who	When
a)NS&I Premium Bonds	Client/planner	Immediately
b)Re-registrations to IDA	Client/planner	Immediately
c)IDA and ISA investments	Client/planner	Immediately
d)Income protection	Client/planner	Immediately
e)Stakeholder pension	Client/planner/accountant	Immediately
f)Self-employed versus incorporated	Client/accountant	2015/16
g)Will and LPA	Client/solicitor	Next 12 months

Your plan will be reviewed annually.

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