



GUIDE TO INVESTING

SAVING FOR CHILDREN

No parent will need reminding that children are expensive. Of course, there are the day-to-day running costs of clothes, shoes - and large telephone bills - but there are also some surprises: A recent survey in *The Times* suggested that four-fifths of first time buyers needed parental help to buy their home and the debate about university tuition fees indicates that higher education costs are likely to increasingly fall on parents. Add in private school fees

or a wedding and any thoughts of a quiet, comfortable retirement might appear to fly out the window.

Unless you are earning a significant amount of money, managing these expenses out of day-to-day income is likely to be almost impossible. We have therefore put together this short guide to give you some ideas - and tax efficient examples - which might help you to plan ahead.

DECISION TIME

In order to plan an investment strategy effectively, it is first worth clarifying your targets. For example, are you saving for a lump sum - to pay for university at 18 or for a wedding at 30? Or, do you need an income – perhaps to help with school fees?

Your time line and how you need that money will be the two most important determinants of your investment strategy. Afterall, if you have eighteen years or more over which to raise the money, you can afford to take more risk. However, if you need an income and you need it quite soon – in five or seven years for example, the amount of risk you can take may be limited.

TYPES OF INVESTMENT

Once you know what you need and when, the next thing to look at is how much money you have to invest and what investments there are to choose from. This guide will not go into detail about the actual asset classes available – your financial adviser is better placed to help there – but we can outline some of the questions you might need to ask yourself before you decide what approach is most suitable for you.

How much risk can I take?

Can you tolerate short-term fluctuations in your capital value in exchange for a higher potential return? In general, if you have a longer-term horizon you might find the potential of some volatile assets outweigh the apparent safety offered by lower risk options. However, even if you are saving for 18 years, if short-term losses will stop you sleeping at night, then the lower risk options are for you.

Will I be protected against inflation?

Inflation is a hot topic at the moment and retaining the purchasing power of your investment over the long term might be difficult without taking some risk. With interest rates at such low levels, many deposit accounts are not paying enough to make up for the price increases we are currently seeing. Over short periods, the risks of more volatile options might not be worth taking – but over 10-20 years, if you want your investment to grow in real terms and not just in absolute terms, you may need to consider other options.

How is the world likely to change as my children grow up?

If you are investing over 18 years, the world could become a very different place. China might overtake America as the world's largest economy. Countries such as Britain and France could fall behind the likes of India or Brazil. If you are willing to take a few risks, perhaps you could consider a little exposure to such opportunities, just in case.



Do I need an income?

If you need an income from your investment then at some point you will have to find a product that will pay one. Some investments are designed specifically to pay predictable levels of income so that you know where you are from month to month. Others offer the chance either for a higher income or one which has the potential to grow – but will be less consistent and may even require the odd subsidy from your capital to meet specific needs.





TAX

EFFICIENCY

ONCE YOU KNOW WHAT ASSETS YOU ARE LOOKING FOR, YOU CAN THEN DECIDE HOW TO ACCESS THEM – AND WITH CHILDREN BEING (MORE OFTEN THAN NOT) NON-EARNERS, THE LAST THING YOU WANT IS FOR THEIR HARD EARNED GROWTH TO END UP IN THE HANDS OF THE TAXMAN. THANKFULLY, WHEN IT COMES TO CHILDREN, THERE ARE PLENTY OF WAYS TO PROTECT IT:

1) Use your children's personal allowances

Children have a personal allowance, the same as an adults (£6,475 for 2010/2011). You can fill in a form R85 from HM Revenue & Customs to have any income received from their savings account or investment paid tax-free. However, you do need to be aware that if you give money to your child that produces more than £100 gross income a year, the whole of the income from that gift is taxed as if it were yours.

2) Individual Savings Accounts (Isas)

These are free from both income tax and capital gains and are likely to remain the first port of call for saving, including for children. Almost any investment (collective funds, cash,

shares) can be held within an Isa. There is no set holding period and every individual can invest up to £10,200 each year.

Note: Isas are not open to children in their own name until they reach the age of 16 for cash or 18 for stocks & shares.

3) Child savings bonds

These are offered by friendly societies and allow parents, grandparents, other relatives and friends to all save up to £25 a month on behalf of each child with the benefits then being earned free of further tax. The bond must have a term of at least ten years, mature on either the child's 18th or 21st birthday and the contributions must be maintained to earn the tax benefits. However, they do offer a valuable alternative, particularly if you are not the child's actual parent.

4) Pensions

These are still a niche choice for investing for children, but can provide a solution in certain circumstances. Investments into a pension attract tax relief on the way in, but tax is payable on any income received. From the age of 55 investors can take out 25% of the value of their fund as a tax-free lump sum which can be useful in paying for a wedding or helping your children find a deposit for their first home. You can also put up to £3,600 gross every year in a pension on behalf of your child. It will cost a basic rate taxpayer just £2,880 and tax relief is added by the government, but the child will not be able to access the money until they are 55.

5) Trusts

Legislation over the past few years has eroded many of the tax planning advantages of trusts. In general, these are now used to control access to the funds rather than for tax planning. A bare trust is the most common. Income and capital gains are treated as those of the children, which means that they can use all their allowances each year. It also gets round the problem that children cannot hold shares in their own name.

6) Child trust funds (CTFs)

Although CTFs were stopped in the 2010 Emergency Budget, millions of parents still have active CTF accounts for their children. Parents, family and friends can add a total of up to £1,200 to the account each year. There is no tax to pay on any income or any gains from the fund. However, as with savings accounts, it remains in the child's name and they will ultimately have control over how it is spent.

7) Life company regular saving plans

These tend to be used by more sophisticated investors, particularly offshore domiciliaries, expats and international executives. Investors can use them to build up a tax-free lump sum and then assign segments of it to their children. These segments are usually paid out tax-free as long as they fall within a child's tax free allowance but in the meantime, the policyholder retains control of the investment policy. However, minimum investment levels may be higher than some other options.



HOW TO INVEST

Investment trusts

These are a popular investment for children. They are a type of collective fund, so can invest across a range of assets in order to diversify risk, and are listed on the London Stock Exchange. There are lots of different underlying investment strategies available – from emerging markets to solid, global blue-chip stocks and even corporate bonds - so you can pick and choose the type of fund you require. They have some inherent advantages: They tend to be cheaper than other forms of collective equity investment. Also, they are accessible for smaller savers; using specific savings products you can buy in at a low minimum investment level – perhaps as low as £25 per quarter.

Unit trusts/OEICs

These are also collective funds. Again, they are available from a wide range of fund managers with a wide range of different investment strategies, including bonds, equities and alternatives. These tend to have slightly higher minimum investment levels than investment trusts. Savings plans usually start around £50 per month though some providers offer lower minimum investments to encourage smaller savers.

Individual shares

This is a higher risk option. Put simply, if one company goes bust in a collective fund, an investor may lose 1-2% of their money. However, if that company is the only share

that investor owns and it goes bust, he loses all his money. Nevertheless, the rewards can be impressive for those in a position to take the risk.

Conclusion

Investing for children is not so different from investing for any other purpose. You need to decide on your time horizon and attitude to risk and this will inform your investment strategy. You then ensure that saving is done in the most tax efficient way possible. There are a few short-cuts, but disciplined planning is the best way to ease the burden of your dear little things.

CONTACT US

We hope you found the information in this guide useful and informative.

If any of the points are of interest, or you would like to discuss your own situation in more detail, please call us on the number enclosed.