LOWES

Where personal finances are cared for personally

January 2006

"A fall will always make a wise man wiser."

Ancient Chinese proverb

INSIDE – The tax you need not pay – see page 4

Our 2005 competition winner!

CONGRATULATIONS TO JOHN AGHA of Manchester. After 12 long months he has emerged as the winner of our 2005 'Predict the Indices Competition' and wins six bottles of Moët Champagne!

A year ago we asked you to predict how the three main indicators of global stockmarket activity – the FTSE 100, the EuroStoxx 50 and the S&P 500 – would close 2005 in terms of the top, middle and bottom performer.

Mr Agha predicted that in order of performance, the indices would be the EuroStoxx in first place followed by the FTSE and then the S&P. For the tie breaker he predicted that the EuroStoxx 50 would rise by 14.75 per cent.

The three indices started and ended the year as follows:

Index	Level start 1 January 2005	Level end 31 December 2005	% rise
EuroStoxx 50	2951.24	3578.93	+21.27%
FTSE 100	4814.3	5618.8	+16.71%
S&P 500	1211.92	1248.29	+3%

This year we are offering you the chance to enter another competition! For details see page seven.

Fraud is not an option with IHT

IN THE FIRST CASE OF ITS kind, the Revenue's Special Compliance Office in Edinburgh has successfully prosecuted a taxpayer for defrauding the Revenue of Inheritance Tax (IHT) mounting to £163,000.

John Lamberton took over responsibility for his aunt's share portfolio. He sold the shares and opened a stockbroker's account for himself which received the proceeds which were then passed through an offshore company and other offshore accounts. He then purchased a house in Spain and set up an estate agency but failed to declare the investments in his aunt's returns to the Revenue. His actions also defrauded another beneficiary of part of his entitlement.

Lamberton was found guilty of embezzlement and fraud and jailed for seven years. The Crown Office is currently trying to confiscate his assets.

● *See our article on IHT on page 6.*

Scotland's year for house price rises

NINE OF THE 20 TOWNS DELIVERING the biggest house price increases during 2005 are in Scotland, according to the third Halifax Estate Agent annual survey.

Other details which emerged include:

- Only 11 towns across the UK have an average price below £100,000. There were 38 in 2004 and 130 in 2003.
- Southern towns dominate the most expensive places with Gerrards Cross in Buckinghamshire the most expensive town and the only place with an average price above £600,000. Three towns have an average price above £500,000: Weybridge, Henley on Thames, and Richmond upon Thames.
- There are no towns outside the South East in the UK's most expensive 20 towns. The most expensive towns elsewhere are Ilkley in West Yorkshire (24th) and Altrincham in Cheshire (27th).
- The most affordable housing in the UK is in the North and the most affordable regions are Scotland, Wales, Northern Ireland and northern England.

Keep on working

THE TURNER REPORT ON PENSIONS HAS RECOMMENDED that people work longer – possibly until age 69 – in return for a more generous state pension.

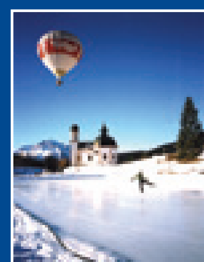
However, no changes in the current state retirement ages are proposed until 2020. In addition, no one currently aged over 50 would be affected while anyone aged over 40 would only have one more year added to state retirement age.

Turner also proposes that the universal basic state pension would be based on residence rather than a record of National Insurance contributions.

Retirement: How the UK compares

Country	Official retirement age	
	Men	Women
France	60	60
Japan	60	60
Australia	65	65
Germany	65	65
Italy	65	60
Sweden	65	65
UK	65	60
US	65.3	65.3

Source: OECD



The photograph used on this issue's cover was taken in Tyrol, Austria

Make your money work

Best bank and building society instant access/no notice accounts

Branch Based

Amount	Provider	Account	Gross Rate	Contact
£1+	Abbey	Flexible Saver	3.3%	Branch[1]
£2,000+	Bradford & Bingley	Premier Saver	3.55%	Branch[2]

Postal or Telephone

Amount	Provider	Account	Gross Rate	Contact
£1+	ING Direct	Savings Account	4.5%	0800 376 8844 to request application form and information pack[3]

Internet

Amount	Provider	Account	Gross Rate	Contact
£1+	Newcastle Building Society	Newcastle Net	4.9%	www.newcastlenet.co.uk

Note 1. Guaranteed to rise in line with base rate until 1 April 2006. Note 2. Guarantees to pay no less than one percentage point below base rate. Note 3. Account holders must be aged 18 or over, be a UK resident and hold a UK current account (with a cheque book and direct debit facility).

Sources: www.thisismoney.com, www.moneyextra.com, www.everyinvestor.co.uk 6/1/2006. All accounts subject to terms and conditions.

Brown hits property in Pre-Budget Report

Self-invested personal pensions
Chancellor Gordon Brown has used his Pre-Budget Report to reverse an earlier proposal to allow holders of Self-Invested Personal Pensions (SIPPs) to invest in a raft of exotic investments, including residential property, fine art, classic cars and race horses.

Dormant accounts
Millions of pounds lying in dormant savings accounts are to be used by the Government to fund youth facilities and community services.

Chancellor Gordon Brown revealed that he had reached an agreement with the banking industry to channel assets, which had remained unclaimed in savings accounts for 15 years or more into the community.

It's estimated that several hundred million pounds may have lain untouched for this long. A Commission on Unclaimed Assets is to be set up by the Scarman Trust with the support of a number of charities to examine how the money can be spent. Account holders would be able to reclaim their money at any time.

Property investments
The Government has given the go-ahead for Real Estate Investment Trusts (REITS). These will be tax effective collective investment funds, which will offer private investors exposure to the property market without the risk or complexity of direct property investment.

2006/7 Personal Allowances
The personal allowance for people aged under 65 will rise by £140 to £5,035 in April 2006, by £190 to £7,280 for people aged 65-74, and by £200 to £7,420 for people aged 75 and over.

Charities lost £691 million last year

UK CHARITIES LOST OUT ON MORE THAN £691 MILLION IN 2004 – £332 million more than in the previous year – by those giving to good causes not doing so tax efficiently reveals research from IFA Promotion (IFAP), which promotes the benefits of independent financial advice.

IFAP says 48.8 million Britons generously gave over £8 billion to their chosen charities, £1 billion more than in 2003. However, if donors had made the most of the tax allowances available, £691 million could have been re-couped by the charities.

COMMENT

Tax relief for the taking

"A FLOURISHING BRITISH VENTURE CAPITAL INDUSTRY is vital to growth"

The above statement was made by Chancellor of the Exchequer, Gordon Brown in his Pre-Budget Report of 10 December 2003.

He declared it was the intention of the Government to actively promote investment in successful small companies whose growth was being constrained by a lack of capital. He announced that for the following two tax years he would raise the annual investment limit for Venture Capital Trusts to £200,000 and the income tax relief to 40 per cent, even for basic rate tax payers.

These generous tax reliefs effectively made it possible to reclaim up to 40 per cent of an investment up to £200,000 as an income tax rebate with the rebate only limited to the investors total income tax bill for the year of the claim. These incentives are due to expire at the end of this tax year.

Investment in venture capital is a longer term investment as it involves small unquoted companies which are generally of higher risk than quoted ones. However, this risk has been somewhat mitigated by the tax reliefs of the last two tax years, with the Government effectively subsidising 40 per cent of the investment.

While the tax incentives are important, the ability of the managers of the Venture Capital Trust is even more so. The introduction of the enhanced tax incentives prompted some managers to offer VCTs for the first time, even though they had little experience of this specialised area. With this in mind and the scheduled reduction in the level of tax relief we feel it is appropriate to promote in this issue of our magazine, a VCT which we believe offers excellent prospects – the Matrix Income & Growth 3 VCT. For more information see page 8.

Wishing you all a prosperous 2006.

Ian H Lowes,
Managing Director

How you can avoid bec

Lowes' consultant, Barry Hopper, investigates how you can reduce your tax bill...

> *"The avoidance of taxes is the only intellectual pursuit that still carries any reward."*
>
> John Maynard Keynes

BRITISH HOUSEHOLDS WILL PAY AN average £603,697 each in tax during their lifetimes, with higher earning households easily paying £1 million in lifetime tax, according to an analysis by AXA of official UK statistics.

The AXA Investigation shows that the average British household aged between 30 and 50 years old needs a combined income of just £58,830 to end up being tax millionaires.

On average a British household pays around 35.5 per cent of its income in tax, with Income Tax and National Insurance accounting for £311,507 in their lifetime. Indirect taxes also make a significant difference to the average Briton, with fuel tax costing £25,294 over the household lifetime, and vehicle excise duty adding a further £7,244. When it comes to enjoyment, an average £15,333 is spent on alcohol duties alone.

The taxes included in the AXA analysis include such items as Income Tax, NI contributions, Council Tax, VAT, alcohol, fuel and tobacco duties, vehicle excise duty, TV licences and stamp duty on house purchases. However, they exclude such taxes as Capital Gains Tax, CGT (see panel on right) and Inheritance Tax, IHT (see article on page 6).

Everyone has an annual CGT allowance (£8,500 in the current tax year). In practice, relatively few people pay this tax. Readers who do make capital gains on their investments can with some careful planning avoid having to pay this tax at all. Readers who do not have any capital gains can make very good use of their annual CGT allowance to reduce their income tax bill.

HM Revenue & Customs: tax take is increasing

Two taxes you can plan to avoid – Inheritance Tax and Capital Gains Tax

IHT	Number of inheritance transfers on death	Tax collected by UK Government
2004/5	34,000	£2.9 billion
1994/5	21,000	£1.4 billion
1984/5	25,000	£658 million
CGT	**Number of taxpayers**	**Tax collected by UK Government**
2004/5	180,000	£2.3 billion
1994/5	70,000	£926 million
1984/5	120,000	£730 million

Source: HM Revenue & Customs

coming a tax millionaire

How to reduce your income tax bill

Action 1 Use your annual CGT allowance

To do this you need to see income in a different light. Instead of regarding income as the interest or dividends paid by savings accounts and shares, consider it as the crystallised profits on your investments.

If you do this then you can gradually realise the profits on your investments and, by making use of your annual CGT allowance of £8,500 in the current tax year, you can take these profits as a tax-free income. Ideally, if you plan to do this then you should seek out investments where the emphasis is on capital growth rather than dividends.

Action 2 Avoid paying tax on savings interest

By using a tax-free cash mini-ISA you can avoid paying tax on at least some of your savings. This allows you to save up to £3,000 every tax year.

Action 3 Use a pension plan

You could reduce your taxable income (and your tax bill) by paying more into a company, personal or stakeholder pension, through one-off or regular contributions.

For example, if you were paid £100, this becomes £78 after tax for a basic rate income taxpayer and only £60 for a higher rate taxpayer. Even if you pay no income tax, you can invest up to £2808 a year into a stakeholder pension and have the contribution 'grossed up' to £3600.

Action 4 Use your spouse's allowances

If you're paying tax on savings interest or share dividends, you can reduce your tax bill by transferring this capital to a lower-earning spouse.

For example, if you are in a higher tax band than your spouse, you could put some of your savings and shares in his/her name to reduce your overall tax bill as a couple.

Action 5 Use your annual Venture Capital Trust (VCT) allowance

In the current tax year there are generous tax reliefs available on VCTs which enable you to reclaim up to 40 per cent of an investment up to a maximum of £200,000 as an Income Tax rebate. This rebate is only limited by your total Income Tax bill for the year of the claim.

Unfortunately, this tax relief is due to disappear at the end of this tax year and VCT investment is higher risk because it is based on unquoted companies and therefore only suitable for those prepared to risk their capital (see page 8 of this issue).

How to avoid paying CGT

Action 1 Bed and Spousing

The introduction of an enforced delay of 30 days between the sale and repurchase of equity-linked investments or shares spelled the death of 'bed and breakfasting'. However, there is an alternative called 'bed and spousing'.

If you transfer assets such as shares to your spouse, their gain on a subsequent disposal would be based on your acquisition cost and date. However, if you sell the shares on the open market and your spouse buys identical ones, the eventual gain made by your spouse on disposal will be based purely on their own period of ownership. The gain (if within the annual allowance) has been crystallised without a CGT liability arising and without the investment risk of a 30 day delay. Any taper relief for CGT purposes would be based on your spouse's sole period of ownership, not your combined ownership period.

Action 2 Bed and ISAing

An alternative approach is known as 'bed and ISAing' where you sell your investments on the open market and then buy identical ones back within an ISA. By doing this you can gradually transfer investments into an ISA shelter where there is no CGT liability on encashment.

There are certain conditions which must be met:

- The investments must not be purchased from the investor's spouse or from the investor.
- The investments must be bought at the open market price. Full stamp duty or stamp duty reserve tax (SDRT) is paid on the purchase of the ISA investments out of cash held in the ISA.

These represent a selection of methods for reducing your tax bill. There are many others. For more information, talk to your Lowes' Consultant or call us on 0845 1 484848.

Good planning can cut IHT bill

By Neil McLachlan, Lowes' Technical Manager

Figure 1: The rise and rise of IHT

IHT	Transfers on death	Tax collected
2004/5	34,000	£2.9 billion
1994/5	21,000	£1.4 billion
1984/5	25,000	£658 million

Source: HM Revenue & Customs

THE GOVERNMENT'S Inheritance Tax (IHT) tax take is projected to reach £3.4 billion in the current tax year as more and more people are sucked into this tax net.

Recent research by business and financial advisers Grant Thornton and economists Lombard Street Research shows that 3.6 million people will be liable to pay IHT by 2009, 70 per cent up on 2002, the last year full data was available. Looking ahead, based on the long-term average asset prices, the research predicts the number of estates above the IHT threshold will rise from 2.1 million in 2002 to 3.6 million in 2009.

The key problem faced by many readers is that the value of their home is becoming an increasingly significant inheritance issue.

Recent research by Halifax Bank says that almost one in three (31 per cent) of detached property sales in the UK are now above the current IHT threshold of £275,000. In addition, it says that the average price of a detached property in the UK is now £270,107, only 2 per cent below the current IHT threshold. And according to the property website, Rightmove, the average price of all houses will pass £200,000 this year. Five years ago, only 13 per cent of detached property sales in the UK were above the then IHT threshold of £234,000.

It's the children who pay!

IN THE SHORT TERM, THE rise in property values may not create an IHT issue, as it is common for one spouse to pass all their assets to the other on their death, which does not incur an IHT charge. The downside, however, is that when the other spouse dies, the children or other beneficiaries can face a huge tax charge.

An alternative approach is to make use of each spouse's IHT nil-rate band by bequeathing some of the assets elsewhere on the death of the first spouse. When it comes to the family home, the key is to do this in such a way that the surviving spouse can continue to live in it.

A common method of achieving this objective is for husbands and wives to own their home as 'Tenants-in-Common' whereby each owns a half share of the house (as distinct from a Joint Tenancy where the whole house is equally owned). Then, on the death of the first spouse, their share of the house passes to a Discretionary Trust rather than to their partner. This enables the deceased spouse to use their nil-rate band which may cover all or part of any IHT charge arising from the transfer to the Trust. So far, as the surviving spouse is concerned, at the discretion of the Trustees he/she can enjoy exclusive use of the property until death. At that point, their estate, including their share of the property, would pass to the Trust, with their nil-rate band again being used to offset any IHT charge.

However, the recent HM Revenue & Customs case of *Judge and Another* shows that great care must be taken to avoid creating what's called an 'interest in possession'.This is where the surviving spouse has an entitlement to use the whole house or has a say in whether or not it should be sold. In this case, HM Revenue & Customs argued that the widow of Thomas Walden had an interest in possession in the property she had exclusive use of and, therefore, that the value of the whole property would be taken into account in determining the IHT charge to the Trust.

In this case, the Revenue was unable to prove its view that there was an interest in possession. But the case clearly demonstrates that Discretionary Trusts alone may not always provide the answer when it comes to inheritance plans involving the family homes.

The Lowes solution

To get around this problem Lowes, in conjunction with the solicitor, Bennett Richmond, has designed a Will and Family Trust arrangement which offers great flexibility for the family and some protection against legislative changes. It provides extremely flexible benefits, and whilst it cannot be guaranteed to be immune to an HM Revenue & Customs challenge, it does meet all their requirements. It can potentially:

- Save IHT through up to three generations.
- Shelter assets for those three generations against a local authority challenge for long-term care costs.
- Protect against bankruptcy and divorce as well as provide IHT savings.
- *To find out more about this, contact your Lowes consultant or call on 0845 1 484848.*

Close friends or cousins can escape IHT

FRIENDS OR COUSINS OF THE same sex can pass on assets free of inheritance tax after their death thanks to the Civil Partnership Act 2004, which came into force on 5 December 2005.

From that date individuals of the same sex can have their relationships legally recognised in the form of a civil partnership. Civil partnerships were intended to give gay and lesbian couples legal recognition. However accountants and lawyers say they do not preclude any two individuals of the same sex, provided they are not direct family members, from forming a civil partnership to take advantage of the significant tax breaks.

The civil partnership extends the same rights and responsibilities enjoyed by husbands and wives, the biggest tax advantage being the ability to leave assets to a surviving partner without them incurring IHT.

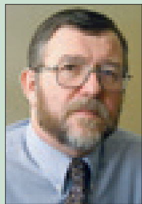
There is no express requirement in the Act for the two individuals to live together, to be of any particular sexual orientation or to be in a sexual relationship. However, parents, siblings, grandparents, aunts and uncles and those in adoptive relationships are barred from registering as civil partners.

It is possible to terminate the relationship by a process equivalent to divorce called 'dissolution'.

- *For more information, contact your Lowes' consultant or call 0845 1 484848.*

MARKET COMMENT

There's value in the markets



By Melvyn Bell, Lowes' Investment Manager

IN THE LAST LOWES Magazine I assessed the likelihood of a reversal of the equity market recovery which started in March 2003 and concluded timing purchases or sales would require luck and judgement.

The need for accurate timing has been graphically illustrated in the last few months. After hitting a high at the end of September the UK equity markets experienced a correction, with the FTSE 100 falling from a high of 5,515.00 on 3 October to 5130.90 on 21 October. However, by 2 December there was a new high for the year.

No one factor is responsible for the markets' continued climb. But a key one is increased merger and acquisition activity. Recently, JP Morgan Chase Bank noted that: "Rather than using profits to invest, return them to shareholders as dividends, or commit them to their pension funds, UK corporates are piling up cash." JP Morgan says this cash is being stockpiled to take advantage of good investment opportunities.

However, it seems companies outside the UK believe these opportunities have already arrived – on 31 October the London Stock Exchange was informed of a number of bids for major UK companies:

- £18bn bid by Spain's Telefonica for O2.
- £2bn bid by Japan's Nippon Sheet Glass for Pilkington.
- £3.3bn bid by Dubai Ports World for P&O.
- BPB rejecting an initial offer from France's Saint-Gobain, but subsequently recommending accepting an increased offer of £3.9bn.

More recent deals include:

- Punch Taverns taken over by private equity group, Spirit, in a £2.68bn deal.
- Boots acquisition of Alliance Unichem.
- Reg Vardy set to be taken over by Pendragon in a £450m deal, unless a rumoured counter bid by Lookers comes to fruition.
- EMI rumoured to be a target for a £2bn bid from Time Warner.

What are these deals saying? Quite simply that there is significant value in the markets. Consider this: the PE ratio (the most commonly used method of comparing relative value of share prices) of the FTSE 100 Index 1 April 2004 was 14.53 (i.e. the average price of a share in the FTSE100 was 14.53 times its earnings).

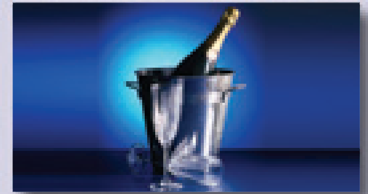
Since April 2004 the index has risen around 25 per cent, but the PE ratio has fallen to 13.73. In short, although the rise in the market might suggest that UK equities are less attractive than in April 2004, the fact is that the rise does not reflect the recovery in corporate earnings.

COMPETITION

Predict the FTSE in 2006

WHERE WILL THE FTSE 100 Index be at the end of 2006? Do you think the steady growth of 2005 will be repeated in 2006, with the markets continuing to recover more of the losses they suffered in the first few years of this century? Or do you think they'll head down?

It's your call and all you have to do to enter our competition is to write your prediction and your details on the pull-out reply paid coupon inside this magazine and then return it to us by 14 February. The client whose prediction is closest to the actual closing price at the close of business on 31/12/2006 will be declared the winner. Any tied entries will be placed in a draw.



The prize will be an enormous helping of bubbly – six bottles of Möet Champagne!

To help you, our table shows how the FTSE 100 has finished each of the last five years:

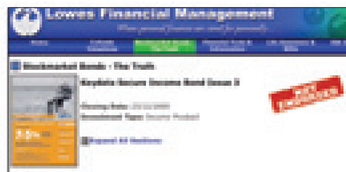
Closing values of the FTSE 100 Index over the last 5 years

Close of business	Level of FTSE 100 Index
31/12/2005	5618.8
31/12/2004	4814.3
31/12/2003	4476.9
31/12/2002	3940.4
31/12/2001	5217.4

Our aim is to add value

AT LOWES WE PRIDE OURSELVES on the efforts we make to keep you fully informed about the products we believe are best suited to your needs.

An example of this is the ongoing research we conduct of structured investment contracts which purport to offer good returns for the minimum of risk. This research is featured on our website and is regularly updated with information on products and the reasons why we either endorse or don't endorse them.



We usually only review structured investment contracts that are stockmarket-linked because there is a clearly defined underlying measurement. We have, however, had many enquiries about a contract from Keydata, the Secure Income Bond Issue 3 which closed for business on 23 December. We have therefore decided to publish our opinion.

This is the third tranche of this particular contract, and none of the previous ones been reviewed on our website. When first launched, the high headline income rate coupled with the lack of stockmarket exposure at first sight seemed to be the answer to many clients' demands for income.

However, on closer examination, we felt unable to recommend it. Our view on the contract has not changed since the original one was launched; whilst there is no stockmarket exposure, the risk to capital is not only unquantifiable, but if there was any ultimate loss of capital it would be almost impossible for us to verify the justification for the loss.

The problem as we see it is that a part of the underlying investment comprises a portfolio of insurance policies which produce returns either on their sale or on maturity. The returns on these policies are not subject to precise measurement, as are stockmarket returns, but are down to the discretion of the insurance company actuaries.

We hope that the investment 'does exactly what it says on the tin' but for the above reasons we felt unable to endorse the proposition.

Experienced, Stable and Successful

AS MENTIONED ON PAGE 3 THERE ARE less than three months left to invest in Venture Capital Trusts before the scheduled withdrawal of the Government's very generous 40 per cent income tax break. With this in mind, we have selected a VCT – the Matrix Income & Growth 3 VCT – to promote, which we believe offers excellent prospects.

It is our belief that Matrix Private Equity Partners are one of the most experienced, stable and successful teams managing VCTs. They currently provide fund management for four VCTs and their performance has been impressive, demonstrating their ability to deliver good levels of income and also to protect capital.

From April 1999 when they started operations through to 30 June 2005, their generalist VCT investments have made a total return* of +65.9 per cent, which compares very favourably with the FTSE All-Share Total Return of +2.9 per cent over the same period. Please note, however, that past performance is not an indication of future performance.

By focusing on Management Buy Outs (helping a company's management team acquire the business they have been managing, but do not own), Matrix Private Equity Partners ensures that the companies they invest in have the same aims as the VCT – maximising income and making a profitable sale of the company when appropriate.

The Matrix team's long tried and tested strategy is to invest in profitable, cash generative businesses that can afford to pay regular high levels of interest to the fund. Furthermore, the team only targets companies where there is clear potential for making a capital gain on exiting the investment.

Matrix expects most exits to be through trade sales, where the investee company is bought by a competitor, although flotations on the AIM market may also provide exit opportunities. Whenever investments are sold at a profit, the capital gain generated in the fund can be converted into income which the fund will pay out as additional tax free dividends.

To invest in the Matrix Income & Growth 3 VCT it is important that you first read the prospectus fully to ensure that you understand the investment and, in particular the Risk Factors detailed on page 5 of the prospectus. Please note that the value of an investment in a VCT may fall as well as rise, and an investor may not get back the full amount invested. An investment in venture capital is generally held to be higher risk than investment in quoted companies and a VCT should be considered a longer term investment.

Once you are satisfied that a VCT is an appropriate investment for your personal circumstances, please complete and return the application form to us together with your cheque in the reply paid envelope provided.

The minimum investment is £5,000 and the maximum investment which attracts tax relief is £200,000 per investor. If you have any questions about the suitability of the Matrix Income & Growth 3 VCT for you then please call your Lowes' consultant or this office on 0845 1 484848.

*Total Return based on valuation of current investments, capital returned in cash to the fund and income received from the investee companies. FTSE All-Share return calculated bid-to-bid, gross income reinvested.

Lowes may be required to approach a third party in order to verify the identity of a client or any person providing funds on behalf of an investment made in a client's name. Where further information is required to verify identity, Lowes reserves the right to delay applications or withhold settlement until sufficient identification has been provided.

If you would like to receive further information on any of the subjects featured in this issue of **LOWES** please call **0845 1 484848**, fax **0191 281 8365**, e-mail **client@lowes.co.uk**. Or write to us at: **Lowes Group PLC**, FREEPOST NT197, Holmwood House, Clayton Road, Newcastle upon Tyne NE2 1BR.
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