

# THE REDUNDANCY FINANCIAL PLANNING GUIDE

Managing Your Money in  
the Event of Redundancy



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# About the author

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Martin Bamford is recognised as one of the most influential financial advisers in the UK.

He is frequently quoted as a personal finance expert in the national press as well as on commercial and BBC local radio. Martin writes a monthly personal finance column for *Canary Wharf City Life* magazine.

Martin is the author of three best selling personal finance books, published by Prentice Hall. Two of his books – *The Money Tree* and *Brilliant Investing* – have been selected as WHSmith Business Book of the Month.

At only 29 years old, Martin is one of an exclusive group of advisers to be a Chartered Financial Planner and Certified Financial Planner professional. He holds an honours degree in Business Administration from the University of Winchester.

Martin is responsible for the day to day running of Informed Choice along with ensuring a high level of technical service to its clients.



# About Informed Choice

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Informed Choice is a family owned and managed firm of Chartered Financial Planners, established in 1994 by Nick and Andrea Bamford. We work with individuals and small business owners in Surrey and the surrounding counties to help them to build, manage and protect their wealth.



Informed Choice is one of only five IFA firms in the UK to hold the Gold Standard for Independent Financial Advice. This is the toughest award in retail financial services. We have been awarded the Gold Standard for three years in succession - 2006, 2007 and 2008.

We offer a friendly and professional advisory service. Our clients come from many different walks of life and typically have investable assets (including pension funds) between £200,000 and £1m. As a professional firm we charge fees for the advice, implementation and review of the solutions we provide.

Informed Choice is a firm of Chartered Financial Planners which means we have satisfied rigorous criteria relating to professional qualifications and ethical good practice. This means you can be confident that you are dealing with one of the UK's leading firms that is wholly committed to providing you with the best possible advice, service and support.

## Who should read this guide?

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- You should read this guide if you have recently been made redundant and need to consider the financial planning considerations before taking action.
- You should read this guide if you think you might be made redundant within the next twelve months and you want to find out the steps you should consider now in order to prepare yourself financially.
- You should read this guide if you have accepted a redundancy payment and need to decide how to best utilise this money.
- You should read this guide if you are considering early retirement as a result of redundancy.
- You should read this guide if your spouse or partner is being made redundant and you want to help them understand their choices and options.
- You should read this guide if you are a professional adviser, such as an Accountant or Solicitor, who has clients who are facing the prospect of redundancy.

**If you read this guide you will have a clear understanding of the choices and options you have to ensure your long-term financial well being in the event of redundancy.**

# Welcome to this guide

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Welcome to this guide from Informed Choice. We wrote this guide because the prospect of redundancy is becoming very real for more and more people, in light of worsening economic conditions.

Redundancy can occur for a number of reasons, but the current economic downturn is likely to increase the number of redundancies taking place across the UK. With every redundancy comes a whole series of important decisions to make about financial planning, in addition to the human and emotional impact.

Every redundancy is different because every person who experiences redundancy will have very different circumstances, goals and objectives. However, there are some common areas of concern that need to be addressed in most cases.

In this guide we look at some of the most common financial planning considerations in the event of redundancy. We look at how redundancy payments are treated for tax purposes, the things you need to consider if you have lost certain employee benefits, how to deal with your pensions in the event of redundancy and how to approach dealing with any debts you might have.

Most importantly, this guide is designed to put you in a very strong position to make decisions about the various financial planning issues you need to consider. It is designed to provide the questions you might need to ask and the resources you can call upon to get answers.

What this guide is unable to do is to replace the services of a professional independent financial adviser.

It is important to seek professional legal and financial advice at any early stage of the redundancy process, as any decisions made now can have a lasting impact on your long-term financial prosperity. Legal advice can ensure that you maximise the benefit of your redundancy package. Financial advice ensures that you structure your finances in the most effective way.

We have written this guide in plain English, to ensure that it is understandable. Where we have used a technical word we have tried to explain what we mean by it in simple terms.

Each section of the guide contains some "top tips" for you to consider. We also ask a lot of questions throughout the guide which we hope will help you. You can use those questions when you speak with your employer, solicitor or financial adviser.

**Top tip: By asking lots of questions you should be able to get a good understanding of what your financial planning options on redundancy look like for you.**

In this guide we hope that you will find the answers to some of the questions you have. If the answers are not in the guide then email us at [hello@icl-ifa.co.uk](mailto:hello@icl-ifa.co.uk) and we will do our best to help you with your individual questions.

# Proactive steps

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The most powerful financial planning for redundancy takes place long before the subject is even raised by your employer. In times of economic uncertainty, when companies might well start to downsize or restructure, it is even more important to be proactive with your financial planning.

The two most valuable things you can do in anticipation of redundancy are to cut down on your committed expenditure and create an emergency savings fund. Later in this guide we take a closer look at dealing with debt.

## Emergency fund

A robust emergency cash savings fund will give you sufficient breathing space to assess all of your options and, if necessary, find new employment.

Most financial planners recommend an emergency fund equivalent to three to six months' typical expenditure. This money needs to remain accessible in the event of a real financial emergency but not too easy to access, in case you are tempted to dip into the fund during a non-emergency situation.

A cash Individual Savings Account (ISA) is often a sensible home for your emergency fund. Anyone over 16 years old can save up to £3,600 each tax year in the cash component of an ISA. The interest payable on your savings within the ISA is free of income tax. For the basic rate taxpayer this results in a saving of 20% and 40% for a higher rate taxpayer.

**Top tip: The most competitive interest rates are also often reserved for cash ISAs, because money saved within these tax efficient savings accounts is often left there for the longest period of time.**

## Unemployment cover

Another proactive step you can take is to put in place unemployment cover, but this needs to be done before impending redundancy or you will not be able to make a successful claim.

The terms of unemployment cover (which can be included within an accident, sickness and unemployment plan) will vary depending on the insurer.

These plans typically cover between 50% and 65% of your income up to a maximum benefit of £2,000 a month. Benefits received after a successful claim will only normally last for 12 months. This is because the insurer usually expects the claimant to have secured replacement employment during this time.

It is important to note that these policies only cover involuntary redundancy. If you volunteer for redundancy then this type of insurance cover will not pay a benefit in the event of a claim. The same applies if you are fired or resign from your job.

Payments will cease when you return to work, but it is usually possible to continue paying premiums to keep the cover in force. It is normally a condition of the policy that you are available to work and actively looking for a new job during the time you are claiming.

The other important feature of which you should be aware is a waiting period. Some policies will make you wait for 30 or 60 days before paying a claim. However, once this time period has passed the claim is often backdated to day one.

Some policies have a clause to prevent you from claiming until a certain amount of time has elapsed after you have taken out the cover. This would prevent you from taking out the cover and then making a claim the very next day. A typical waiting period before cover is activated is 120 days, so it is important to think about how you would cope financially during this time.

**Top tip: For all of these reasons, it is important to shop around to find the most competitive cover and also to read the small print so you can understand the terms of the cover you are putting in place.**

# Redundancy payments

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Assuming you have worked continuously for your employer for at least two years, you are entitled to a redundancy payment. Statutory redundancy payment is not subject to income tax or National Insurance contributions.

The amount of redundancy pay you receive will be covered in your contract of employment. However, it must be at least as much as statutory redundancy pay.

**Top tip: The first £30,000 of any payment on termination of a contract is tax-free.**

## Statutory redundancy pay

The total amount of redundancy pay you receive will depend on a number of factors, including how long you have been continuously employed, your age and your weekly pay. This last factor, your weekly pay, is subject to a legal limit which currently stands at £330 per week.

If you are under 22 years old, you will receive half a week's pay for each complete continuous year of employment. If you are between 22 and 40 years old, you will receive one week's pay for each complete continuous year of employment. If you are over 40, you will receive one and a half week's pay for each complete continuous year of employment.

There are some different rules if you were made redundant before 1<sup>st</sup> October 2006, so this description of statutory redundancy pay only applies to redundancies which have occurred since this date.

## Help from the state

Depending on your financial circumstances, you might qualify for help from the state when you are out of work. Your first port of call should be Job Centre Plus, which will be able to tell you about your entitlement to payments or benefits.

If your redundancy payment exceeds £8,000 you will not be entitled to receive the income-based component of jobseeker's allowance.

However, you could still qualify for the contribution-based jobseeker's allowance, assuming you have paid or been credited with class 1 national insurance contributions in the relevant tax years. This can provide up to £60.50 per week if you are aged 25 or over.

**Top tip: Citizens Advice is another good source of advice on all aspects of benefits and housing.**

# Loss of protection benefits

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Redundancy often results in the loss of valuable employee benefits previously provided by your employer as part of your remuneration package. These employee benefits might include death in service and private medical insurance.

**Top tip: Redundancy (like any life event) should serve as a prompt to evaluate your protection requirements, identify any shortfall in cover and put in place a suitable protection arrangement.**

## Life assurance

Death in service benefit can be readily replaced with term assurance. This can be tailored to your specific circumstances, with the sum assured and term chosen to fit with your cover requirements and likely retirement age.

There is a great deal of difference between the most and least competitive premiums on offer from life assurance companies. For this reason it is very important to shop around or seek independent financial advice to ensure that you are paying the most competitive premium.

It is also important to consider all of your assets and liabilities before putting life cover in place. It is not always the case that you need to replace lost death in service benefits with the same level of sum assured from an individual policy.

Before deciding on an appropriate level of life cover, you first need to examine the likely financial position of your family on death. What debts will they have to repay, what assets or income will they have available to meet their lifestyle costs and what is the gap between the money they will have and the money they will need?

Remember to consider the use of a suitable trust. This will ensure that any benefits payable from a life assurance policy are paid to the right person (or people), in a timely fashion and in a tax-efficient manner.

A trust is a simple legal instrument and your financial adviser should discuss this with you at the time you set up any life assurance policies. It is also possible to put existing life assurance policies in trust, so if you already have suitable life cover in place you do not need to replace this with a new policy to benefit from a trust.

## Private healthcare

Some private medical insurers will allow you to take over existing employer-sponsored cover at preferential rates. This is often much cheaper than starting from scratch with an individual policy. It is also a way to ensure continuation of cover if you have any pre-existing medical conditions.

Just like life assurance, there is a great deal of difference between the most and least expensive providers. Unlike life assurance (where the only benefit is a payment on death) it is also important to consider the various features available under each plan.

**Top tip: Make sure you shop around to identify the most competitive provider of life assurance as the costs vary between the most and least expensive provider of these financial products.**

With private medical insurance it can be quite difficult to compare like with like. Different providers offer access to different hospitals, different levels of cover and different additional benefits. You also need to think about their track record for processing claims and providing information in the event of a claim.

For these reasons, you should always seek advice from an independent private medical insurance broker. They will be able to find the most cost effective and suitable cover from every provider in the market to ensure that you have cover in place that meets your personal requirements.

## Flexibility

Modern financial products such as these are designed to be reasonably flexible. This means that you can put arrangements in place and then cancel or adjust them in the future, if your circumstances change again.

As it can take a number of weeks to underwrite some forms of financial protection, particularly if you require substantial amounts of cover or have a complicated medical history, it is worth starting this process early when the topic of redundancy is first raised by your employer. This will put you in the position where you can put the new cover on risk as soon as existing benefits come to an end, therefore preventing any time gaps in your cover.

# Pensions

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Depending on your age at the time redundancy occurs, retirement is likely to be a serious consideration. As this is likely to be early retirement (or at least earlier than originally planned) you will need to look carefully at affordability. After all, you are younger so your pension benefits will have had less time to accumulate and will need to last for longer.

Early retirement prompted by redundancy is a good opportunity to re-evaluate your lifestyle and the associated living costs. Your pension might produce lower benefits than originally predicted, but this is all relative. Lower pension benefits are manageable when combined with a lower cost of living.

## **Tax-free cash**

One of the most attractive features of a pension plan is the tax-free cash (more properly called the pension commencement lump sum) available when you take retirement benefits. Under current rules, this is typically 25% of the value of the pension fund, although some older types of occupational pension schemes can provide higher levels of cash at retirement.

Remember that there is usually only one opportunity to take your tax-free cash from a pension fund. Once taken, the nature of your pension plan changes and this often has an impact on the tax treatment of the fund in the event of your death.

## **Annuity purchase**

One option for taking benefits from your various pension plans is to use the capital to purchase an annuity. This is a financial instrument used to convert the value of your pension fund, after any tax-free cash has been taken, into a guaranteed income for the rest of your life.

You can select various options such as an escalating income (to keep pace with price inflation), a guarantee period or a spouse's benefit.

Options like these can only be added to the annuity at the time of purchase, so you need to think carefully about the features you might need later in life. Once you purchase an annuity, you cannot change the 'shape' or frequency of payments, or the various options you have selected.

Your existing pension provider is likely to be able to offer you an annuity, but the golden rule is to always shop around. When buying an annuity with your pension fund you are able to exercise what is known as the 'open market option'. In our experience, the annuity rate on offer from the existing pension provider is rarely as competitive as the most competitive rate available on the open market. A higher annuity income can make a lot of difference over the number of years, particularly if you are taking early retirement.

### **Unsecured pension for flexibility**

Retirement ahead of your selected retirement age can result in the need to retain a degree of flexibility. An unsecured pension allows you to take the maximum available tax-free cash (more properly known as the 'pension commencement lump sum') from your pension benefits and this might be used to repay the mortgage or other debts.

You can then draw a level of income directly from your pension fund, which remains invested. Importantly, this income level can be varied each year depending on your requirements. If you find new employment then the income can be reduced to zero so as not to aggravate your income tax position.

**Top tip: By using the unsecured pension it is possible to take the tax-free cash from your pension, for example to repay expensive debts, without having to draw an income which would be taxable.**

The unsecured pension option is not suitable for everyone, but it can provide an attractive alternative to securing an annuity income at a time when the fund value might have fallen from its peak and you are too young to benefit from a particularly competitive rate.

### **Other retirement options**

In addition to annuity purchase or unsecured pension, there are other ways to take benefits from pension plans. These so-called 'third way' retirement products are relatively new to the UK market and have been criticised for being expensive and unnecessarily complicated.

However, it is always worth considering all of the options before making a decision about your income in retirement. Taking early retirement benefits introduces a whole series of other considerations, and retirement triggered by redundancy is typically an early retirement.

# Dealing with debt

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Debt is a drag on your ability to meet your other financial objectives. The global 'credit crunch' has highlighted some of the risks of funding your lifestyle with unsecured debt. What starts off as cheap and easily accessible can quickly become expensive and in short supply.

There are two main types of debt – unsecured and secured.

**Top tip: In light of the current 'credit crunch' the true cost of debt has been highlighted and this is an important area to tackle both before and during redundancy.**

Unsecured debt typically includes items such as credit cards, store cards, personal loans and overdrafts. It is usually a fairly short term form of debt (up to ten years) and more expensive than longer term secured debts.

Secured debt usually refers to your mortgage. It is secured because there is an asset (e.g. your house) guaranteeing the value of the debt.

Both forms of debt require the payment of interest. When facing redundancy you will need to consider how your ability to service all of your debts will be effected.

## **When you are able to repay your debts**

Some people who are made redundant are in the fortunate position to be able to repay their debts in full, often using the proceeds from any redundancy package. This puts them in the position of having no debts to fund at a time when they are not working.

Flexibility is often important when considering the repayment of debts, particularly a mortgage, following redundancy. Whilst you might have sufficient cash savings to repay your mortgage, you may not wish to do so, particularly if you have plans to return to work in the near future.

Your options in this scenario might include using the cash savings to continue making mortgage payments or using some of the cash to offset the mortgage balance, using an offset mortgage. This latter option cancels out the interest due on your mortgage balance with any interest that would have been earned on the equivalent savings balance. However, it also means that you can continue the access the cash if you need it in the future.

Before making the decision to use any cash to repay your mortgage, you should seek professional financial advice

## Time for advice

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As a result of the complex interplay between the different areas of your personal financial planning, it is important to seek professional independent financial advice to ensure you have considered all of your options and made the most suitable decision based on your personal circumstances.

This is one area of financial planning where it pays to use a fee-charging adviser. He or she will be able to look for solutions, including the repayment of debt and restructuring of existing financial arrangements that could be overlooked by a traditional financial adviser who needs to sell a financial product to generate a commission.

**Top tip: You will need to work closely with your financial adviser and keep him or her informed of the situation as things develop and change.**

Again, it makes sense to seek advice at an early stage of the process. We often deal with clients facing redundancy and in a panic to make important decisions ahead of tight deadlines that have been imposed. It can take time to request detailed information and conduct analysis ahead of providing advice to a client who is being made redundant.

### **Finding an adviser**

Finding a competent independent financial adviser who you trust to provide you with the best advice is not always easy. The best way to find a good adviser is usually to ask your friends, family or colleagues for a recommendation. They should be able to point you in the direction of an adviser they have used in the past where they have been satisfied with the advice and service provided.

An alternative method is to search for a local adviser online using one of the many internet search engines. These include [www.unbiased.co.uk](http://www.unbiased.co.uk) from IFA Promotions or [www.findanadviser.org](http://www.findanadviser.org) from the Personal Finance Society. The latter allows you to search for a Chartered Financial Planner which is a higher level of professional qualification for financial advisers.

It is important to have a first meeting with a financial adviser before making a decision to use their services. This first meeting is typically without charge or obligation. The adviser will want to ask you lots of questions about your financial circumstances and objectives. Remember to use this opportunity to ask them lots of questions about their experience, qualifications and services.

At or before this first meeting, the adviser should give you a copy of their Client Agreement letter. This sets out the important protections you receive by dealing with an independent financial adviser. Take the time to read it carefully and make sure you ask the adviser if you have any questions.

If you are not comfortable with the financial adviser for any reason, there is nothing to stop you from meeting with other advisers to find one who suits you. A working relationship with a financial adviser should be long term, but you can switch advisers at any time if you feel that another adviser would be more suitable.

# Summary

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Redundancy, whilst becoming more common in the current economic climate, is always a scary prospect. The fear associated with having your role made redundant is usually linked to uncertainty; so many aspects of your life becoming unknown in a short space of time.

The financial aspects of redundancy are only one area to consider, but they are an important area.

By taking control of your financial planning – both before, during and after the event of redundancy – it is possible to remove one type of uncertainty and reduce the level of fear that is associated with losing your job.

In an uncertain world economic climate we are confident that levels of redundancy will continue to rise for some time to come. Even during periods of economic growth, redundancy continues to occur as companies restructure or change their strategy.

Taking control over your financial planning is a crucial activity that needs to be taken as seriously as your health, family and relationships. By working closely with a professional independent financial adviser it is possible to construct, and then regularly review, a comprehensive Financial Plan. This will enable you to face the future with a greater degree of certainty.

Reducing stress and worry in our often hectic lives is a valuable investment to make. The modern professional adviser is no longer an insurance salesman keen to push sometime inappropriate financial products. Instead, they form close working relationships with a relatively small number of clients to ensure that your financial plans remain relevant to your changing life circumstances and goals.

Engaging with a professional independent financial adviser is a worthwhile thing to do; regardless of the prospects for your own employment in the near future.