



ETHIKOS

**Ethical & SRI
Investments
—
A Guide to
Financial Planning**

Contents

Foreword	2
Financial Planning	3
The Ethical Blueprint	6
Investing	7
Introducing the Asset Classes	8
History of Ethical Investing	12
Latest Developments in Ethical Investing	14
Checklist for choosing an IFA	16
About Ethikos	18
Our Services	19
Glossary	21

Foreword

We all need to plan our finances to provide a secure and happy life for ourselves and our loved ones.

Most of us need a pension for when we stop working, life assurance should we die prematurely, and a range of different investment opportunities to help us make the most of our money when we are working and in retirement.

More and more of us are making a conscious effort to recycle, to minimise our carbon footprint, to avoid buying goods and services from countries with poor human rights records and to try to buy from companies who make a positive contribution to our wellbeing.

Having made every effort in these areas it would seem to follow naturally that our financial planning should be aligned with our conscience.

We believe that ethical, environmental and socially responsible investment can, with specialist advice, provide a viable alternative to mainstream funds that have not been ethically screened.

We do not forget that it is your money not ours that we are advising on.

We recognise that you have your own personal and financial goals, and values, and beliefs, which are unique to you. We believe that our holistic service allows you the freedom to align your financial planning needs with your personal values.

This booklet is not a comprehensive guide to financial planning or a definitive guide to ethical and SRI investments. However, we hope that it will serve as an introduction to both subjects.

We have provided further details of who we are and the services offered at the end of this booklet. In the meantime please do not hesitate to contact us if you feel we can help you with your financial planning needs or if you would like to discuss how ethical investment can make a difference.

***We do not forget that
it is your money not
ours that we are
advising on***

Financial Planning

Financial planning is about looking at your financial circumstances as a whole rather than looking at each separate part in isolation. Whilst a full financial plan may be desirable, not everyone really requires one: financial planning comes into its own when you have a number of competing or complex financial goals. For the modest investor, or where there are easily identified simple financial goals, one of our other services may be more appropriate and cost effective. We will make sure that you are guided down the path which is right for you.

Financial planning comes into its own when you have a number of competing or complex financial goals

We are all at different stages in our lives. We each have our own unique goals and aspirations. We will have concerns which will affect our attitude towards our financial needs. Whilst recognising this individuality, there are some common threads which often appear when we are compiling a financial plan. There is a general assumption throughout that all planning will take into account your own social, ethical and environmental goals and concerns.

Guaranteeing a Lifetime's Income

This looks at questions such as:-

- What would happen to me and my family if I was unable to work through sickness, accident or disability?
- How am I to save for my retirement?
- How do I obtain the most appropriate income from my pension funds?

Building & Managing your Assets

Whilst this does look at areas such as investment portfolio management, it encompasses the whole of your assets including property and pensions. Our approach starts with analysing your present assets in relation to their usefulness in achieving the goals you set for your future. When building an investment strategy with you, we will take into account your own attitude to and tolerance of risk

Leaving a Legacy

With the increase in property prices over the last few years and despite the recent market downturn more and more people are being caught in the Inheritance Tax trap. We will help you to establish what you want to happen, and for whom, after your death. We will work with your accountant and/or solicitor, if you have one, to ensure that your Will is drawn up in such a way as to make best use of any allowances. If you do not have a Will or an

Don't get caught in the Inheritance Tax trap

existing working relationship with a solicitor we can arrange for expert advice. But leaving a legacy does not have to be left until after death we will work with you to help you make tax efficient gifts during your lifetime if that is your wish.

Protecting those you Love

What would happen to your family if a main breadwinner should die? There are very few state benefits available to help and a time of emotional tragedy should not be made worse by a financial crisis. Most families who have a mortgage have life assurance to cover the mortgage but what about ordinary living expenses, could these be met by the remaining income?

A time of emotional tragedy should not be made worse by a financial crisis

Reducing the Cost of Taxes

Whilst it can be argued that we all have a duty to pay our taxes, there is no necessity that we pay too much tax. We do not advise on exotic tax avoidance schemes, which usually fail as the loopholes are closed, but help clients to make full use of all their allowances and the legitimate tax mitigation schemes which the government encourages.

Planning for Retirement

It is clear that we can no longer rely on the State to provide the majority or even a reasonable contribution to our retirement income. Starting to build up a pension pot in the first decade of work is considered to be sensible decision, but this often coincides with other competing financial needs which can seem to be far more important. The financial planning process can help to clarify financial priorities.

Start to build up a pension pot early

Over time you may have started a number of pension plans. These should be reviewed at regular intervals to ensure that they are still performing as they should and are still providing value for money.

Preparing for Retirement

You may have to live with the consequences of decisions made at retirement for the next 20, 30, or 40 years. This is a time of decumulation, of turning one's accumulated capital into income. There are more choices than ever before to utilise your pension fund, fixed rate annuities, escalating annuities, income drawdown and third way products, to name but a few.

Funding for Infirmity in Later Life

Dying prematurely can be a tragedy for our families and loved ones. But, increases in longevity are making the necessity to plan for the possibility of professional long term care even more essential. Whether the care is provided at home or in a nursing home, the costs are ever rising. None of us can forecast who is and who is not going to require additional help in later life, but sensible pre-planning can ease the financial worries.

Our Approach to Financial Planning

The Ethical Blueprint

Ethikos believes that financial planning is a dynamic, cyclical process that includes at least six steps: -

1. Before starting to design a portfolio we take time to find out what your own personal and financial goals are. These will be specific to you and we recognise that they can change over time. We then help you to identify your financial objectives and goals and establish the ethical and social framework you wish to adopt.
2. We collect and assess all the relevant financial and personal data including your attitude towards and your tolerance of financial risk.
3. We process and analyse the collected information.
4. We prepare a written plan for you and explain how the plan will help you to achieve the goals you have set.
5. Implementing the plan (including arranging any financial products, as appropriate).
6. We will review progress with you at our review meeting and modify the plan in light of any changes to your personal or financial circumstances.

This process is relevant to all, whether you are at the stage of accumulating, managing, protecting or sharing your wealth.

Investing

Why Invest?

Potential investors could be forgiven for thinking that the best place for their money would be under their bed: barring burglary, flood and fire, you get your money back when you need it. The problem is that over time the amount of goods and services you could buy with that money will decrease due to the effects of inflation. If you had placed £1,000 under your bed in 1990 it would only have been worth £610 in 2007, a loss of £390¹.

Cash is also perceived to be a safe store for wealth. Despite the relatively benign inflationary environment we have experienced over the last decade or so, interest bearing accounts have barely maintained their real value. As we seem to be entering into a time of far higher inflation fuelled by rising oil, food, and commodity prices we may see a return to the days of the 1970's and 1980's where interest rates were below the rate of inflation.

Over the longer term real assets such as shares, bonds and property have provided a far better defence against inflation than cash under the bed or in the bank, so that answers the question why invest.

This is all very well in theory but in the short term shares, bonds and property and the income from them can go up as well as down. The technical term for this is volatility. The greater the swing in an asset price the greater the volatility. Assets with a large volatility are considered to be of a higher risk than assets with a smaller volatility. This poses another question; how can we try to obtain these higher returns without losing the lot or suffering from excess volatility? The answer is diversification.

Income can go up as well as down

What is Diversification?

Diversification is defined as the spreading of your portfolio across different asset classes including shares, bonds, property, alternatives and cash. The main objective is to reduce the risk in your portfolio as opposed to risking investment into just one asset class.

Don't put all of your eggs in one basket

Much of the credit for the development of Modern Portfolio Theory and the underpinning theoretical basis for diversification in a portfolio goes to Harry Max Markowitz who was awarded the Nobel prize in 1990 for his pioneering work.

¹ Source MeasuringWorth

Simply stated the long term nature of portfolio planning means that all asset classes are likely to have their ups and downs from time to time. Normally the asset classes will not all go up and down at the same time so by holding a number of different assets in a portfolio it reduces the risk; as when one asset is under performing, the positive performance of another asset will help to compensate for it.

Diversification cannot remove risk altogether but it can help to reduce and manage risk.

Introducing the Asset Classes

Cash Deposits

Cash as an asset class does not include the notes and coins you carry or even the balance in your bank current account. It refers to monies held in an interest bearing account with a bank or building society, including Cash ISAs.

Keeping some cash available for emergency purposes is essential but cash can also play an important part in portfolio design.

Cash deposits are generally considered to be relatively safe with a low risk to your money, the main problem would be a bank or building society failing. Fortunately, the failure of banks and building societies is very rare. Over the long term the returns from cash deposits might not be sufficient to protect the value of your savings from the effects of inflation. The main role of cash deposits in portfolio design is to provide a low risk asset class.

Low risk does not mean the same as no risk

A poorly performing low risk investment can still lose you money; it will just do it more slowly!

Shares

Shares are also known as **equities** or **stocks**. When you buy shares direct in a company via the stock exchange, you are buying a part of that company and you become a shareholder, which usually means you have the right to vote on certain issues. Privatisations and the de-mutualisation of building societies and insurance companies increase the number of individual shareholders dramatically. The reason for holding shares is the hope that the value of your shares will grow over time as the value of the company increases in line with its profitability and growth. In addition, a dividend may also be received, which is an income paid out of the company's profits. Some growing companies tend to pay lower, or no, dividends with the profits re-invested into the business to try to boost the share value over time.

High risk can mean high profits but it can also mean high losses

Over the long term, shares are the main asset class which has provided for real growth over and above the rate of inflation. However, with this potential for long term growth there becomes the possibility of greater risks in the short term.

Stock markets go up or down as the prices of the shares that are the constituents of that market go up or down. Markets rise and fall on market sentiment. This sentiment may have absolutely nothing to do with what is happening in the economy or how well an individual company is performing. To invest in shares you should be comfortable that the value of your investment will at times go down as well as up.

The value of your investment will at times go down as well as up

Holding individual shares is high risk – if you have put all your money into one company and that company becomes insolvent then you will probably lose most, if not all, of your money.

Pooled investments such as unit trusts and OEICS (open ended investment companies) reduce the risks of direct investment into shares, as a pooled investment will typically invest into 40 to 120 different companies. Therefore, if a company goes bust it only reduces the value of the fund by a small amount. However, this limited form of diversification does not guard against the risks associated with the whole of the stock market falling.

Bonds

Bonds are generally accepted as the next step up from cash in terms of risk.

A bond is a loan to a company, government or a local authority. Generally, interest is paid to you as the lender and the amount of the loan is repaid at the end of the term. There are many other names for this type of investment: for example, loan stock, fixed interest, debt securities, gilts (loans to the government), and corporate bonds (loans to companies).

The main benefit of these investments is that you normally get a regular stable income. They are not generally designed to provide capital growth.

Bonds have a **nominal value or par value**. This is the sum that will be returned to investors when the bond matures at the end of its term. Most bonds have a nominal value of £100.

However, because bonds are traded on the bond market, the price you pay for a bond may be more or less than £100. There are

several reasons why the price might vary from the nominal value, for example: -

If a bond is issued with a fixed interest rate of, say, 6% and general interest rates then fall well below 6%, then 6% will look like a good yield and the market price of the bond will tend to rise – perhaps from £100 to £110 or £120. The reverse is also true; if interest rates rise, the fixed rate of a particular bond might become less attractive and its price could fall below £100.

Buyers could be worried that an issuer may be facing difficulties and would want a higher return to compensate for the risk of failure. This would reduce the market value of the bond.

Bonds are generally less risky than having a share in a company. One of the main risks is if the company you have lent money to can not pay the interest due or cannot pay the money back at the end of the term (for example, if it has gone bust). It is generally considered that these risks do not apply to gilts – a government is expected always to pay in full – though there have been instances of certain countries having been unable to repay. Bonds issued by governments will usually pay a lower rate of interest as a result of the perception that they are less risky.

Most bonds are rated by independent agencies such as Standard & Poors or Moody's.

Property

Property is generally seen as the next rung up from Cash and Bonds on the risk ladder.

Although your own property does form part of your asset base, property as an asset class normally refers to commercial property. This includes warehouses, offices, shops, industrial units, shopping centres and business parks.

The main advantage of commercial property is the consistent long-term income stream with the possibility of some long-term capital growth. For most investors investment into commercial property is usually made via a pooled investment.

Commercial property does have its own risks. Valuations are very much a matter of opinion. The only time one can be absolutely sure of the value is at the time a sale is made, even the day after there can be no certainty regarding its value. It takes time to sell commercial properties so if a lot of investors want to take their funds from a property fund, the fund managers may not have sufficient cash resources available to satisfy the demand. In these instances the fund managers may delay repayment by six to twelve

months to allow for an orderly sale of properties. This happened in 2007 when there was a sharp downward correction in the price of commercial property funds.

Alternative Asset Classes

One final way to improve the investment mix of your portfolio is to include alternative asset classes. However, these are only suggested for the more sophisticated investors as they also, individually, carry a significantly high, and sometimes difficult to understand, level of risk. Except for the investor with a high-risk tolerance, they should only make up a relatively small portion of your portfolio.

Alternative assets may include hedge funds, private equity, fine wines, classic cars and antiques. For the ethical investor alternative asset classes could include sustainable forestry, micro finance and some types of private equity.

History of Ethical Investing

The history of ethical investing, as we now understand it, probably started in the early 1900's.

The Quakers being pacifists had sought to avoid any investment into the armaments industry and associated endeavours, with both their personal funds and their Church funds. The Methodists avoided investments into alcohol, tobacco and gambling.

The Methodist attitude towards investment can be traced back to John Wesley, founder of Methodism, who gave four consecutive addresses in the 1700's entitled: 'Earn all you can'; 'But not at the expense of conscience'; 'Not at the expense of our neighbours' wealth'; 'Not at the expense of our neighbours' health'.

In the 1960's anti-war groups in American universities began to question the ethics of companies who were profiting from the war in Vietnam. By the late 1960's and early 1970's organisations were questioning their own decisions on where they were to invest, but it could not be said at that time that there was a concerted ethical investment movement.

The catalyst for change was the anti-apartheid movement where boycotting was one of the main instruments used to bring down the South African regime. Many companies in the UK and US had built up strong links with and had investments in South Africa and were at worst considered to be either actively encouraging and supporting the apartheid regime or at best just ignoring the situation.

USA churches and some state pension funds began to seek ways in which they could identify South African involvement by companies and thus avoid direct investment into them. In the UK in 1971, the Public Interest Research Centre (PIRC), an offshoot of the Public Citizen network of organisations created in the US by Ralph Nader, was conceived and launched. Their first Chairman, Michael Young, was author of the radical 1945 Labour Party manifesto and founded numerous public interest organisations, among them Consumers Association and The Open University. PIRC is still active in researching issues which will directly contribute towards the long-term well being of society.

The UK based 'Christian Concern For South Africa' evolved the screening tools on which today's ethical fund managers rely. Christian Concern For South Africa was the forerunner of the Ethical Investment Research Society (EIRIS) which is now one of two independent ethical screening organisations in the UK.

'Earn all you can';

**'But not at the
expense of
conscience';**

**'Not at the expense of
our neighbours'
wealth';**

**'Not at the expense of
our neighbours'
health'**

John Wesley

Initially, ethical screening was only available to churches, pension funds and other large investors who could afford to invest through a stockbroker. The first retail ethical collective fund, Pax World, was launched in the US. Luther Tyson and Jack Corbett founded Pax World in 1971 with a well-defined mission. They had worked on peace, housing and employment issues for the United Methodist Church and wanted to make it possible for people to invest in keeping with their values. At the same time, they wanted to challenge corporations to establish and live up to specific standards of social and environmental responsibility.

Their vehicle was the Pax World Fund. Launched on 10 August, 1971 with \$101,000 in assets, it was the first broadly diversified, publicly available mutual fund to use social as well as financial criteria in the investment decision-making process. The mutual fund in the US is equivalent to a unit trust in the UK.

At the same time the Pax World Fund was launched, Charles Jacob, a Methodist Lay Preacher, who had become a partner in the top UK stockbroking firm of James Capel in the 1960's, changed direction to manage the centralised funds for the Methodist Church. To finance his work he took on board the management of various unit trusts and charity portfolios.

In 1972-1973 Charles Jacob, with others, formulated a proposal for a new type of unit trust to be modelled on the example of the Pax World Trust, but with the addition of a positive bias towards companies whose products and services were of benefit to the community. The unit trust was to be called 'Stewardship', alluding to the parable of the Talents.

Despite widespread support from a large number of churches and charities the Department of Trade and Industry who had to approve all new unit trusts refused permission. The grounds for the refusal of a licence being that such a trust (if constrained to invest only in stocks, which passed an ethical screening process), could not fulfil the obligation to seek the best possible return for investors.

The inspectors were apparently concerned with a conflict of conscience and capital

The inspectors were apparently concerned with a conflict of capital and conscience, and were not prepared to sanction the new concept. Charles Jacobs tried again in 1976 and was again turned down. However, two years later he managed to gain the support of the Chairman of the London Stock Exchange, Sir Nicholas Goodison, and their joint approach was met with an agreement in principle.

Concurrent with these developments, Friends Provident was involved in an internal debate on ethical matters. As its name suggests Friends Provident had been established on Quaker principles, and management was unsure whether they should stick with their ethical principles or follow the overtly commercial route. Due to pressure of work Charles Jacob was unable to undertake the

management of the approved fund but two trustees of the Rowntree Trust managed to persuade Friends Provident to undertake its management.

The Friends Provident Stewardship Trust was launched in 1984. The City was extremely sceptical and thought that the fund would attract no more than £2m in investment, if it were lucky. It was rather unkindly dubbed the 'Brazil Fund', as you would have to be nutty to invest in it.

Latest figures released from EIRIS² show that, as at 31 December 2007, there was £8.9 billion invested in Britain's green and ethical retail funds. The figure represents almost three quarters of a million accounts in ethical funds, up from around 137,000 accounts in 1997 when less than £1.5 billion was invested ethically.

The last few years have also seen the universe of UK ethical retail funds expand considerably. There are now almost 100 green and ethical funds available to UK investors - a decade ago there were just a couple of dozen.

***£8.9 billion invested in
Britain's green and
ethical retail funds as
at 31 December 2007***

Latest Developments in Ethical Investing

As retail ethical investing comes up to its 25th anniversary the approaches to ethical investing have developed. There are broadly three different approaches which can be adopted by ethical, SRI and environmental fund managers to meet the needs of their investors. These are: -

- Positive Screening – or Support
- Negative Screening – or Avoidance
- Engagement

Whilst some funds combine all three approaches (positive screening, negative screening and engagement), others only use one or two.

Positive Screening or Support

Positive screening or support seeks to invest in those companies with a commitment to responsible business practices, positive products and/or services. Positive products can range from almost

² EIRIS is the leading global provider of independent research into the social, environmental and ethical performance of companies.

mundane areas such as food, clothing, electricity, water and housing to educational materials and safety products. Funds may also favour: -

Ethical

Good employee relations
Equal opportunities
Corporate governance
Socially progressive relationships
Strong community involvement
Charitable giving

Environmental

Recycling
Renewable energy
Pollution control
Waste management
Energy conservation
Supply chain management

Negative Screening or Avoidance

The most commonly recognised form of green and ethical investment is negative screening or avoidance. This approach involves avoiding companies or industries that do not meet the social, environmental or ethical standards by which the fund is run.

Typical avoidance criteria could include: -

Ethical

Arms trade
Oppressive regimes
Alcohol production
Tobacco production
Gambling
Pornography
Bad working practises
Animal exploitation

Environmental

Nuclear power
Air polluters
Water polluters
Ozone depletion
Rain forest depletion
Harm to wildlife

Engagement

This cannot be strictly counted as an investment approach as the fund manager neither refrains from investing in the company nor makes a positive decision to invest. The purpose of engagement is for the investor to encourage and support through dialogue more responsible business practices.

Engagement may be separate from screening or may be combined with it. It may apply to screened and unscreened funds. Normally, engagement with a company only takes place when there is a business case for change. In general, a company would not comply if there were no business benefit.

Checklist for Choosing an IFA

This list has been compiled from a number of checklists we have found on the web produced by the finance section of national newspapers and independent finance sites. It is not an exhaustive list and we would recommend you make a list of your own questions before speaking with an IFA.

- Check the IFA is fully authorised by the Financial Services Authority (FSA).
- Check the IFA really is independent. If an adviser is tied or multi-tied they won't be able to offer you whole-of-market advice.
- Ask how long the IFA has been established. That's not to say young advisers can't do a good job, but experience counts for a lot in this game.
- Book an initial meeting and make sure there's no charge at this stage.
- Check the IFA's qualifications. All IFAs need basic qualifications but choose someone with more advanced exams under their belt. IFAs with the new Diploma in Financial Planning, DipPFS (or equivalent) will have been thoroughly tested.
- Is the IFA a member of a relevant professional body such as the Personal Finance Society or The Institute of Financial Planning?
- Ask how the IFA will be paid. These days the option to pay by fee **has** to be on offer. Some work on a combination of fees and commission. Ask for details in writing before any work is done. Find out how fees are calculated. A fixed fee is preferable to a time cost basis because it's difficult to predict how many hours' work you'll have to pay for. Remember that investments that pay commission to advisers will usually suffer higher charges, which drag performance down so it may be better to pay a fee instead.
- Ask the IFA about their typical client. If you're 'HNW' (high net worth), make sure the IFA is able to deal with you. If your means are more modest, check he/she is equally interested in advising on smaller cases.

- Does the IFA have expertise in the area of your interest such as ethical investments? Is he/she a member of the Ethical Investment Association?
- Get any recommendations in writing and check you understand it all fully. If you have any questions, ask.
- Finally, find out how regularly recommendations are reviewed and evaluated to ensure your adviser is adding value.

Do You Need an IFA

The financial sections of the newspapers often give helpful guides. The financial press is definitely worth reading to give useful background and the knowledge will be useful when you deal with an independent financial adviser.

However, you should be very careful before taking any action which seems to be recommended in the press, as the journalist won't know about your individual circumstances, the advice will be very generalised, and it might not be the right thing for you. It is very difficult in limited space for journalists to cover all of the pros and cons. If you are in any doubt, you should still seek personal, independent financial advice.

About Ethikos

Ethikos was founded in 1996 by husband and wife team Peter and Christel Chesworth. Peter is the registered adviser whilst Christel is in charge of all administration related matters.

Ethikos provides independent investment advisory services and holistic financial planning. Our services are tailored to each individual's needs as we recognise that your financial goals and your social, ethical and environmental concerns are unique to you.

We provide comprehensive, ongoing advice for our clients – usually involving at least one meeting per year, to help you to be more financially organised and to help you to achieve and maintain financial independence.

We maintain close contact with a wide network of other professional advisers and planners who complement our services by their specialist knowledge in areas such as occupational pension transfers and property related matters.

Ethikos is a member of the UK Social Investment Forum and our Financial Planner, Peter Chesworth, is a member of the Ethical Investment Association. Peter has the Investment Portfolio Management qualification of the Chartered Insurance Institute. Peter is a Chartered Banker with a total of 36 years experience in the financial services sector. He also holds the advanced qualification the Diploma in Personal Financial Services and is a member of the Personal Finance Society and the Institute of Financial Planning.

We are predominately a fee based practice with any commissions that would normally be received being either invested back into the plan for our clients' benefit or used to offset the fees due. We do not believe that anyone should be excluded from receiving first class financial planning and we are happy, therefore, to discuss how we can best help according to your circumstances.

Ethikos is completely independent of any product provider and is directly authorised by the Financial Services Authority. Our FSA reference number is 445068 and our registration details are available at www.fsa.gov.uk/register/home.do.

Our Services

Ethikos offers a range of services that can be tailored to meet your needs.

The Ethical Blueprint

This is our holistic financial planning service. Financial planning is the process of meeting your life goals through proper management of your finances. Life goals can include planning for retirement, estate planning and making provision for your child or grandchild's education. The financial planning process helps you to understand where you are now, what you may need in the future and what you must do to reach your goals. We would recommend this service to all prospective clients.

We are aware that for many reasons some clients do not wish to undergo the full financial planning process. The following form part of our Ethical Blueprint but are also offered as standalone services.

Tactical Financial Solutions

This is for clients who have identified their own financial needs but require help in a specific area. It is designed to help with questions such as: -

- How much should I be saving for my retirement?
- Which is the most suitable pension plan?
- What ethical Maxi ISA should I invest in this tax year?
- Can you help me manage my investment portfolio?

Simplified Solutions

This is for the more modest investor. We can offer a simplified, cost effective, yet individual service. Contact would normally be by telephone/letter/e-mail. This does not result in the full client relationship but can develop over time.

Trustee Services

We provide an ongoing advisory investment service to Trusts where we are able to help Trustees meet the requirements of the Trustee Act 2000.

Ethical Alignment Programme

For clients with an existing investment portfolio who wish to align their holdings with their conscience.

The Giving Plus Service

For clients who feel they may have potential Inheritance Tax problems and who want to reduce their tax liability and increase the amount they gift to charities. Not all of this service is regulated by the Financial Services Authority.

Glossary

Annuity

An annuity is a type of insurance policy where you swap a lump sum for a regular income. If the annuity is purchased from the proceeds of a pension policy it is known as a Compulsory Purchase Annuity. All the annuity income is taxed as earned income. If an annuity is bought with your own funds it is known as a Purchased Life Annuity. Part of the income is taxed as investment income and part is paid tax free as it is considered a return of capital. (See also Enhanced Annuity, Impaired Life Annuity)

Assets

Any possessions or property that has a monetary value.

Asset Allocation

The process of dividing investments among different kinds of asset classes; such as shares, corporate bonds, commercial property, government gilts and cash, to try to meet specific financial goals. Asset allocation is used in an effort to reduce investment risk.

Bid Offer Spread

This is the difference between the buying price and the selling price of stocks and shares and some unit trusts.

Capital

Sometimes known as net worth or equity. Net worth equals the total of all of your assets less the total of all your liabilities. In mortgage terms, capital is the amount that you owe, not including costs and any outstanding interest.

Capital Gains Tax

The tax on the profits made after selling assets such as shares, a second home or a collectable item (stamps, antiques, figurines, etc). The current rate for Capital Gains Tax is 18% of any gains in excess of the annual exemption of £9,600 (for the 2008/2009 tax year).

Cash

In financial planning terminology or asset allocation this is not the money in your purse or wallet but monies held in an interest bearing account.

Cash ISA

An extremely low risk tax efficient savings method. Up to £3,600 can be invested into a Cash ISA every tax year. There is no upper limit on the amount of funds that can be accumulated.

Child Trust Fund

Child Trust Fund (CTF) is a savings and investment account for children. Children born on or after 1 September 2002 will receive a £250 voucher to start their account. The account belongs to the child and cannot be touched until they reach the age of 18. This is so that they have some money behind them to start their adult life. A maximum of £1,200 each

year can be saved in the account by parents, grandparents, family or friends.

Collective Investments

A fund which takes money from a number of private investors and pools it together to buy a portfolio of shares or fixed interest securities.

Corporate Bonds

One particular type of fixed interest securities. They are issued by companies as a way of raising funds as an alternative to bank borrowing. The corporate bonds are issued for a fixed period of time at the end of which they will be repaid at par at the redemption date. A fixed amount of interest is payable usually every six months during the life of the bond. Once issued the corporate bonds can be traded on a market.

The risks associated with a corporate bond are that the issuing company could go bust and be unable to pay the ongoing interest payments and the capital amount at the redemption date. This risk can be reduced by using a collective investment. The other risk is that general interest rates may rise making the issued corporate bonds less attractive and reducing their value.

Debt

Most people have debt of one form or another at some time in their lives. Whether this is a house mortgage or three years free credit on a car purchase. Debt is only a problem when it cannot be managed and then it can become a very heavy load indeed. For companies, incurring debt (bank loans or by issuing corporate bonds) may be a cheaper alternative to fund expansion than issuing further share capital. Once again too heavy a load of debt can lead to the collapse of a company if trading conditions change for the worse.

Debentures

A fixed interest bond. In the event of the liquidation of the company, the owners of debentures would be paid before the holders of ordinary shares.

Decumulation

This term is not in the dictionaries as yet but is starting to be used in financial planning circles. It refers to the use of your assets to fund the cost of your retirement. In other words, how to secure retirement income in the most beneficial way.

Defined Benefit Scheme

Defined Contribution Scheme

See Final Salary Scheme

Depreciation

The fall in the value of an asset. There are two common forms of depreciation: the first is when you buy a new car and see the price tumble as soon as you leave the garage forecourt; the second is leaving monies in a non-interest bearing account and over time watching inflation reduce the purchasing power.

Derivatives

Used by professional and institutional investors to make or lose large sums of money, sometimes the second immediately after the first.

Diversification

Spreading the risk of your investments by having a mix of different asset classes held within a portfolio

Dividends

Payments made by a company to its shareholders. When a company makes a profit it can either be re-invested in the business, known as retained earnings, or distributed to the shareholders as a dividend.

Endowment

A life assurance policy that pays a specified lump sum on death within a specific term and can be used as a savings plan. If the life assured survives to the end of the term, normally between 10 and 25 years, a cash amount is paid. The cash amount is not guaranteed. Endowment policies have fallen out of favour in the last ten years or so.

Enhanced Annuity

These can pay more than an ordinary annuity for smokers and those who live in certain postcode areas. No medical underwriting is required. (See also Impaired Life Annuity)

Equity Release

A process by which homeowners can get cash out of their property. Not a financial arrangement to enter into lightly as the consequences of a wrong decision can be catastrophic.

Estate Planning

Ordering one's affairs in such a way as to reduce the impact of Inheritance Tax.

Expression of Wish

Also known as a nomination form, this indicates whom the pension policyholder wishes to receive the death benefits from the pension plan or scheme. It is not binding on either the pension trustees or the executors.

Face Value

See Par Value

Final Salary Scheme

Also known as a defined benefit scheme.

A pension arrangement supplied by a decreasing number of employers.

The pension benefit is dependent on the number of years of service and the leaving salary. Due to the rising costs of providing a final salary scheme some employers are offering pensions that are based on the average earnings over the period of employment or abandoning the schemes altogether in favour of defined contribution schemes.

Defined contribution schemes are when the employer pays in a set amount to a pension plan. The resultant pension will depend on the investment performance.

Financial Plan

A comprehensive strategy designed to help you achieve specific financial goals and prepare for unexpected life challenges or events. A Financial Plan may include some or all of the following: investing, tax planning, asset allocation, risk management, retirement planning, education funding, accumulation funding, estate planning and insurance.

Financial Services Authority (FSA)

The FSA is the independent regulator overseeing all the providers of financial services and products. All firms of financial advisers have to comply with the rules and regulations of the FSA.

Fixed Interest Securities

A loan made to a company, local authority or government. The loan is normally for a fixed period of time and will be repaid at par (usually the issue price) at the redemption date. Fixed interest securities can be traded and the capital value will depend on the prevailing interest rates. Increases in interest rates usually cause the capital value to fall, rising interest rates cause the capital value to rise. See also Corporate Bonds

FTSE 100

This is an index used to measure the performance of Britain's 100 largest companies by market share. This is the index referred to in Television and Radio news bulletins. It was launched in January 1984 with a start value of 1000. The FTSE 100 reached its peak on 30 December 1999 at 6930.20.

Gilts

UK Government bonds or securities issued to raise public funds. As they are backed by the government, they are considered to be one of the lowest risk investments, if held to maturity.

Impaired Life Annuity

An increased annuity payable where the annuitant has health issues which may reduce the expected life expectancy. These will usually involve medical underwriting and the enhancement to the annuity will depend on the severity of the condition.

Income Drawdown

An arrangement to take income from your pension whilst leaving the rest invested.

Income Replacement Insurance

An insurance designed to replace 50% to 65% of your income if you are unable to work through accident, sickness or disability. Income will be paid until you return to work, for a defined length of time, or until a pre notified retirement age. There is normally an exclusion period until the benefits start, typically this will be either 13 or 26 weeks.

Inheritance Tax

The tax payable on an estate after death based on your assets over the threshold is known as the Nil Rate Band. The Nil Rate Band for the 2008/2009 tax year is £312,000. The tax rate for Inheritance Tax is 40% on the portion of the estate in excess of the Nil Rate Band.

Interest Rates

High interest rates are bad for borrowers but many savers welcome high interest rates. Do not forget that high interest rates usually coincide with high inflation so the real value of your money may be decreasing.

Individual Savings Accounts (ISAs)

Tax efficient savings plans that can hold Cash or Stocks & Shares. The maximum cash subscription into an ISA is £3,600 per tax year within an overall ISA limit of £7,200. The Cash ISA and the Stocks & Shares ISA can be with either one or two providers.

Large-Cap

One of a trio of terms in common use, the others being 'small cap' and 'mid cap'. Everyone agrees that the terms refer to market capitalisation, but no one can agree what the thresholds are. What is certain is that large caps refer to the very largest companies with the highest market capitalisations. So companies in the FTSE 100 would certainly be large caps and those in the FTSE MID 250 would be large caps or mid caps.

Long Term Care

A general term to cover the possibility that health problems could mean that paid help to stay in your own home or that a move into a nursing home is required.

Mattress

Not somewhere to keep your money under unless it is fireproof, burglar proof and inflation proof!

Mid-Cap

(See Large Cap)

Morbidity Risk

Used in financial planning to describe the statistical incidence of serious illness, disability and the results of injury that could have major financial implications for an individual or their family.

Mortality Risk

The risk that a life assured or annuitant will die sooner than statistically expected.

National Savings

Government backed savings products which can sometimes have a useful role in a well balanced investment portfolio.

Occupational Pension Scheme

See Final Salary Scheme

OEIC (Open Ended Investment Company)

Form of collective investment, similar to a unit trust. Rather than issuing units, OEICS issue shares. They normally quote a single price for buying and selling.

Par Value

The price for which a share was first sold to the public. Also called the maturity value or face value - the amount that the issuer agrees to pay at the maturity date.

Pensions

This can be a rather confusing catch all term, as this could refer to the basic state pension, state second pension, personal pension or occupational pension, the income you are receiving in retirement or how much you are putting aside for retirement. The term becomes far clearer when used in context.

Policy

A document that sets out the terms and conditions of a contract such as an insurance policy, a life assurance policy or a pension policy.

Pooled Investment

Another term for a collective investment.

Portfolio

A collection of investments usually comprising different asset classes such as shares, fixed interest securities, cash and commercial property.

Risk

There are whole books about investment risk and academics have even received the Nobel Prize for work on the subject. There is no suitable, one paragraph, definition. There is a brief chapter in this guide on the subject.

RPI (Retail Prices Index)

This is one of the official measurements of the rate of inflation used in the UK. It measures the increase in price of a sample basket of goods which a typical household might buy.

Shares

Where ownership of a company is divided into a number of equal parts or "shares", ordinary shareholders are entitled to a distribution of the profits (known as dividends) and have the right to vote at company meetings. If the company is wound up, ordinary shareholders are entitled to any assets left after all other obligations have been met. These residual assets are known as the equity of the company, hence the term "equities", sometimes used to describe ordinary shares. Ordinary shares rank after debentures and are known in the US as common stock.

Share Capital

The value of a company as calculated from the total market worth of its shares.

Small Cap

See Large Cap

Stock

A term used to describe the total capital of a company divided into shares. In the US shares are called stocks. In the UK stocks and shares tend to be used interchangeably.

Stock Market

The market place for the sale and purchase of shares, bonds and Government Securities. The UK stock market is known as the London Stock Exchange whereas the main US stock market is Wall Street.

Tracker

A collective investment fund that reproduces the make up of a market index such as the FTSE 100 Index. Tracker funds are also referred to as passive investment funds.

Will

Every adult should have a Will. Dying without a Will can cause serious problems for those who are left.

Yield

This is the amount an investment earns expressed as either a percentage of the market value of the investment or the original amount put in. Yield can alternatively be known as the return on an investment.

LLP Members Peter J Chesworth ACIB DipPFS • C P Chesworth
Ethikos LLP is a Limited Liability Partnership registered in England
number OC315223

Registered office: 48 Longworth Avenue • Tilehurst • Reading •
Berkshire • RG31 5JY

Ethikos LLP is authorised and regulated by the
Financial Services Authority