November 2008

Our MONEYmadeclear™ guides – here to help you

This guide is part of our Saving and investing series.

Available from our Consumer Helpline or website

www.moneymadeclear.fsa.gov.uk

No selling. No jargon. Just the facts.

If you would like this guide in Braille, large print or audio format, please call our Consumer Helpline on 0845 606 1234 or Minicom/Textphone on 08457 300 104 (call rates may vary).

To help us maintain and improve our service, we may record or monitor calls.

Plain Language Commission Clear English Standard Winning Document

No selling. No jargon. Just the facts about saving and investing.

MONEYmadeclear™

from the Financial Services Authority (FSA)

With our MONEYmadeclear™ range of guides, we cut out the jargon and give you just the facts about financial products and services, helping you to make an informed decision.

Just the facts about saving and investing.

We try to ensure that the information in this guide, some of which comes from sources outside the FSA, is correct at the time of print. It is possible that some of it is oversimplified, or may become inaccurate over time, for example because of changes in the law. You should check the current position before you take any action.

This is general information to help you make financial decisions. It is not advice, and cannot take account of your individual circumstances. When making decisions about your own circumstances you should consider whether to consult a financial or other professional adviser.

FSA®

The Financial Services Authority (FSA), set up by government to regulate financial services and protect your rights.

This guide is for you if

You want

to know what choices you have when putting money aside for the future.

It's about saving and investing and

- explains the differences between them;
- sets out how they work;
- points out some of the risks involved; and
- answers some of the questions you may have.

Contents

Saving for tomorrow

Saving tends to be for short-term goals or when you need to get at your money quickly (for example, a holiday, birthdays, Christmas or other festive occasion or an emergency such as replacing a household item).

Investing is for the longer term, if you're willing to tie up your money and take some risk to get a better return – balancing the risk of a short-term loss against the chance of a long-term gain.

See the *Jargon buster* on page 17 for an explanation of some words you may come across.

Get to grips with your money

Take the time to review your financial position as a whole. Everybody's circumstances are different, but these are the general rules:

- Pay off any expensive debts – such as credit cards. This is because the interest you pay on borrowed money is usually higher than the interest you get on a savings account.
- Protect yourself and your family – think about taking out insurance to cover you for unforeseen events, for example a house fire, illness, redundancy or death.
- Have an 'emergency fund' of money that's easy to get hold of, which would last you for three to six months if you lost your income suddenly. You can hold it in an easily accessible savings account – earning some interest until it's needed.

If you've met these priorities, you are in a good position to consider further savings and investments.

Think about your goals

Be clear about your financial goals; for example, how much money you'll need, and when.

You are likely to have a range of different financial goals with different timescales. Think about how you can balance your short-term goals, for example buying a car, with longer-term needs such as an income in retirement.

Your financial goals and timescales will determine how much you need to save or invest. And remember, even small regular savings can add up in the long run.

Saving for tomorrow

Remember, £10 today does not buy you what £10 did ten years ago. You get less for the same money over time as a result of inflation – making it harder to reach your target – see *Inflation* on page 5.

Savings and investments can help protect your money being eroded by inflation. There is also the possibility that your money may grow faster than inflation.

Key points

- Keep a spending diary so you can see where your money goes.
- Use our online **Budget calculator** to help you work out how much money you have left over every week or month after your expenses – see *Useful contacts*.
- Start an easy access savings account to use only in emergencies.

Saving for the short term

For short-term savings, you usually put your money into an account where it earns interest without the risk of losing any of it (short of a bank, credit union or building society collapse).

You can usually get your money out immediately or after a notice period, which could be 30, 60 or 90 days.

Your money grows because interest is added monthly or yearly. However, this can be a slow process and it can take many years for your original deposit to grow much. You also need to save regularly and not dip into the fund, if you can help it. Be aware of how inflation can affect your savings.

Saving with a regulated firm

Banks and building societies in the UK must be regulated by us to be able to take your money and hold it. We also regulate credit unions in England, Scotland and Wales. Always check that they're regulated by us before you hand over your money – see *Useful contacts*.

The Companies Registry in the Department of Enterprise, Trade and Investment regulates credit unions in Northern Ireland – see *Useful contacts*.

Banks and building societies follow a voluntary Banking code in the way they deal with their customers. You can get a copy from any branch.

If you have a complaint and can't resolve it with them directly, you may be able to take it to the Financial Ombudsman Service – see *If things go wrong* on page 15.

Savings accounts are deposit based. This means you'll usually get back the money you have put in plus interest, unless the bank or building society collapses.

If this happens, and as long as the firm is regulated by the FSA, the Financial Services Compensation Scheme may be able to pay compensation to customers, up to a set limit – see *If things go wrong*. (There are different arrangements for credit unions – see *If things go wrong*.)

Firms not based in the UK

By law, most financial services firms must get our authorisation before they can do business in the UK. We may regulate firms from the EEA (European Economic Area) if they are operating in the UK.

However, if you are considering or currently doing business with a firm authorised in another EEA state you should ask for further information from the firm or its UK branch about its complaints and compensation arrangements. This is because the position may differ compared to a UK authorised firm.

Where you can save

You can save in a wide range of savings accounts available from banks, building societies, credit unions and National Savings and Investments (NS&I) – see *Useful contacts*.

In addition to regular savings accounts, you can also save in special Christmas savings accounts offered by some building societies and credit unions.

Inflation

Inflation happens when prices go up throughout an economy. The effect of inflation on your money means that the money you save will buy less each year.

To protect your savings against this, you should look for an after-tax interest rate that is more than the rate of inflation.

What to look out for

There are many savings accounts with many different features.

These features include:

- interest rates – some accounts have a higher interest rate for an introductory period, and then it drops. Others have a rate that goes up the more money you have in the account;
- notice periods for withdrawing your money without penalties – such as 30, 60 or 90 days;

- minimum deposits – some accounts require a certain amount to be paid in regularly;
- how long you have to keep the money in the account to get a high interest rate;
- the way interest is added – some accounts add it monthly and others once a year;
- additional bonuses – but these are usually payable only in certain circumstances, and you should make sure you understand what these are;
- tax-free savings – by using a cash ISA (Individual Savings Account) – see below.

Cash ISAs (Individual Savings Accounts)

There are two types of ISA – cash or investment. You can invest in two separate ISAs in any one tax year: one cash ISA and one investment ISA. For investment ISAs see page 10.

You can invest up to £3,600 (2008/09 tax year) in a cash ISA, and can only invest with one provider in any one tax year.

Cash ISAs usually pay a higher interest rate than normal savings accounts and the interest earned is free of income tax.

You can compare savings accounts, including cash ISAs, at **Compare products** on our website – see *Useful contacts*.

Tax

Interest paid on your savings is treated as 'income' and as such you may have to pay tax on it, just as you pay tax on your wages. You will usually receive your interest net of tax, with 20% tax already paid.

- If you don't pay income tax, you can fill in form R85, and receive your interest gross (before tax is taken off).
- If you are a basic-rate income tax payer, you don't get any tax back but you won't pay any more.
- If you are a higher-rate income tax payer you will need to declare this income on your tax return, and pay a further 20% on the interest you have earned.

Cash ISAs (Individual Savings Accounts) let you receive your interest free of income tax.

Some NS&I savings products, such as premium bonds, and saving certificates, are also free of tax.

For further information about tax and your savings – see *Useful contacts*.

Other types of savings

There are other ways to save, for example for specific items such as Christmas hampers or Christmas gift vouchers.

You can also save in saving schemes and clubs run by supermarkets, large retailers, local shops, social clubs, pubs and workplaces. You usually save what you can, and then exchange your stamps or scheme points for shopping or vouchers, or you can buy other goods and services.

With these options you're not earning any interest on your savings so your money is not growing. You're also restricted to using the stamps for specific purchases, depending on which type of shop you're saving with.

We don't regulate the companies operating these schemes, so if things go wrong with the company you may lose your money. Ask them about their arrangements before you use them.

Key points

- Decide what you want from a savings account – easy access, high interest, flexible saving – to get the right one for you.
- Find out how you can manage your account online, by phone, or in a branch.
- Ask for form R85 if you don't pay income tax or if the account is for a child.
- Make sure you use your tax-free allowance by saving in a cash ISA.

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Investing for the longer term

Putting money away for the longer term usually means investing your money in schemes or funds based on the stockmarket.

When investing, you take calculated risks to increase your chance of getting higher returns on your money, especially over the longer term (money you can afford to tie up for five years or more).

There are different types of investments but, basically, you take a risk with your money by investing in assets (usually on the stockmarket) that could rise or fall in value.

There is no guarantee you will make a return on your investment or even that you will get back the same amount you invested in the first place.

The upside is that you often get a greater return than you would with savings, giving you better protection against inflation over the long term.

Investing with a regulated firm

Firms advising on or selling investments must be regulated by us, or be the agent of a regulated firm. This means they have to meet certain standards. We monitor the standards and can take action if they don't meet them.

This also means that if you have a complaint and can't resolve it with them directly, you may be able to take it to the Financial Ombudsman Service or if a firm is unable or likely to be unable to pay claims against it the Financial Services Compensation Scheme may be able to help – see *If things go wrong*.

Their advertisements, product brochures and other promotions must be clear, fair and not misleading. You can check if a firm is regulated or report any misleading promotions to us by phone or online – see *Useful contacts*.

How investments pay out

There are different ways you can 'make money' with an investment. Some investments provide:

- capital growth – the original amount you invest grows; or
- income – a regular payment, for example dividends from shares; or
- a combination of income and growth.

Already got investments?

If you're saving in a pension, have a life insurance policy or are part of an employee share scheme, then you are already investing.

All these invest your money in the stockmarket with a view to making it grow over a long period.

What are investments?

A good way to understand investments is to think about investing in three layers.

Layer 1

The first layer, common to all forms of investment, is the **underlying investment** itself. It will fall into one of four **asset classes**. These are:

- shares – a stake in a company;
- bonds – loans to a company or the government;
- property – either commercial or residential; and
- cash.

You can invest in any one of these asset classes. However, it's usually a good idea to spread your investments over different classes and providers so that you reduce the risk of losing more of your investment if the value of those assets go down.

Layer 2

The second layer is called **pooled investments** – and provides a relatively easy way of spreading the risk of your investment by investing in a range of assets. This is because your money is 'pooled' with that of other investors, and is invested in one or more of the above asset classes by a fund manager. The most common types of pooled investments are open-ended investment funds, investment trusts and life assurance funds.

Layer 3

The third layer is what is sometimes known as a **tax wrapper**. This means that your investments are held in a 'wrapper' such as an investment ISA or a pension and you pay less – or no – tax. With a pension you get tax relief as well.

Understanding the risks

Risk and reward generally go hand in hand. The more risk you are prepared to take, the higher the potential reward.

If you are not prepared to lose any of your money under any circumstances then you have to accept a lower level of return.

If you see an investment promising a high return at little or no risk, be very wary. The old saying 'if it looks too good to be true, it probably is' almost always applies to investments.

The important thing to remember is that, even if your investment goes down, you will have only made a loss if you cash it in at that time; it is not a real loss until you sell.

You can't eliminate risk with investments, but you can reduce it by diversifying your investments.

What may be a small risk to one person may be huge to another. You must decide what level of risk you are personally willing to take.

Investment ISAs (Individual Savings Accounts)

There are two types of ISA - cash or investment. For cash ISAs see page 6. You can invest in two separate ISAs in any one tax year: one cash ISA and one investment ISA. This can be with the same or different providers.

You have an overall ISA allowance of up to £7,200 (2008/09 tax year) and up to £3,600 (2008/09) of that can be saved in a cash ISA and the rest in an investment ISA. Or you can invest the whole allowance in an investment ISA, but with one provider in any one tax year.

By using an investment ISA you invest in longer-term investments such as:

- individual shares or bonds, or
- pooled investments such as open-ended investment funds, life assurance investments or investment trusts.

You can transfer money from a cash ISA to an investment ISA – but not the other way.

You do not have to pay any income tax or capital gains tax on the growth of the ISA investments. This helps anyone who pays tax.

For more information, contact an ISA manager or get an ISA factsheet from HM Revenue & Customs – see *Useful contacts*.

Information you will get

Your adviser should give you some important documents setting out details of the service they are offering you – and the costs.

They will discuss your needs, and once they recommend a product, they will usually give you a Key Features document or, if they have recommended an open-ended investment fund, they will probably give you a Simplified Prospectus.

Key points

- Work out how long you can afford to be without the money you've invested. Investments are for the long term.
- Decide what you want your investment to provide – capital growth, income or both.
- Check you understand the level of risk involved.
- Read the documents you're given and ask questions if anything is not clear.
- Spread your investments to spread the risk – don't put all your eggs in one basket.

Your questions answered

Question

Where do I go if I want to invest?

Answer

A financial adviser can help you identify which investments are suitable for you, based on your own circumstances. You can find one in the Phone Book, or there are organisations that can give you a shortlist of advisers in your area. Always check that we regulate the firm to ensure you're protected if things go wrong – see *Useful contacts*.

Question

Where can I get an ISA?

Answer

You can get an ISA from many different organisations, including:

- banks and building societies;
- National Savings and Investments;
- investment firms.

You can use **Compare products** on our website to compare savings and unit trust ISAs – see *Useful contacts*.

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Question

Can I save or invest ethically?

Answer

Yes. For information about ethical saving and investing and details of financial services firms that provide this service – see *Useful contacts*.

Question

What is a tracker fund?

Answer

Tracker funds track the market in which they are invested. For example, a FTSE100 tracker would aim to copy the movement of the FTSE100. Trackers tend to have lower charges than actively managed funds because it is simpler to track an index than it is to research individual companies to invest in which is what a fund manager would do for you.

Question

I've just had a phone call from someone offering to sell me some shares at a really good price. Should I buy?

Answer

Beware of phone calls or mailshots 'out of the blue' offering great deals. There is nearly always a catch – if it sounds too good to be true, it usually is. Always check that the firm is regulated by us, make sure you understand the risks involved and are happy that the investment is right for you.

Dont be pressurised into buying over the phone.

Next steps

When saving or investing

Step 1

Pay off or get your loans and credit cards to a manageable level before you start saving. This is because the interest you'll be paying on these is more than the interest you could be earning on your savings.

Step 2

Start an easy-access savings fund for emergencies and try not to dip into it. Keep a separate savings account for holidays or other big expenses, and bear in mind that some accounts offer a higher interest rate the more you keep in them.

Step 3

It's never too early to start saving for your retirement. The sooner you start, the longer you allow for your investment to grow.

If you have any more spare money and are willing to take some risk, you could consider further investments – you may want to get professional financial advice.

Step 4

Whatever you choose to do, make sure you review your savings and investments regularly. Don't put your money away and then forget about it. Revisit your goals to make sure you're on track.

If things go wrong

Bank and building society accounts

Most banks and building societies follow the voluntary Banking Code when dealing with their customers. This sets out standards for dealing fairly with you and giving you the information you need to choose and run your accounts.

You can pick up a copy of the Code from any branch, or from the British Bankers' Association (BBA) – see *Useful contacts*.

Investments

Financial advisers and providers have to meet our standards when advising on or selling investments to you, so that you get the right product based on your own circumstances.

Complaints

If things go wrong contact the bank, building society, credit union, financial adviser or provider. They have a procedure to follow when dealing with complaints.

If you're not satisfied with their response, you may be able to take your complaint to the Financial Ombudsman Service. The firm should give you the details of this free service.

Compensation

If a regulated firm (for example a bank, building society in the UK, or a credit union in England, Scotland or Wales) is unable or likely to be unable to pay claims against it, you may be able to get compensation from the Financial Services Compensation Scheme (FSCS). It can pay compensation for financial loss of up to £50,000 for deposit claims, (which is 100% of the first £50,000).

If you hold multiple accounts in banks that are part of a larger group the amount of compensation depends on whether the bank is separately authorised or part of the parent group. For more information visit the FSCS website – see *Useful contacts*.

If things go wrong

For investments, the FSCS can pay compensation of up to £48,000 per person (100% of the first £30,000 and 90% of the next £20,000). For more information visit the FSCS website. The service is free to customers – see *Useful contacts*.

For complaints and compensation arrangements for credit unions in Northern Ireland check with the Companies Registry – see *Useful contacts*.

For information about making a complaint get a copy of our **Making a complaint** guide – see *Useful contacts*.

Firms based outside the UK

If you are considering or currently doing business with a firm authorised in another EEA state you should ask for further information from the firm or its UK branch about its complaints and compensation arrangements. This is because the position may differ compared to a UK authorised firm.

Other savings schemes

Christmas hamper schemes and other Christmas savings schemes and clubs are not covered by the Financial Ombudsman Service or the Financial Services Compensation Scheme.

For information about these schemes get the OFT's leaflet **Save Xmas** – see *Useful contacts*.

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Jargon buster

Some key words and phrases explained.

Asset classes
The underlying investments – shares, bonds, property and cash deposits.

Bonds
A loan to a company or the government.

Capital
The overall amount of money invested.

Capital growth
An increase to the original amount invested after charges and other deductions.

Collective investment scheme
A way of pooling money from lots of people into a single investment fund.

Diversification
Spreading your investments across different asset classes, or types of investments within an asset class.

Equities
Another name for shares in a company.

Fixed interest
The interest rate is fixed for a set period. So you win if interest rates fall, but you will be stuck on a poor rate if interest rates rise.

Fixed interest securities
Another name for bonds.

Gross interest
Interest paid before tax is taken off.

HMRC
HM Revenue & Customs – responsible for collecting taxes and paying tax credits.

Individual Savings Account (ISA)
A tax-efficient way of saving or investing with limits on how much you can pay in each tax year.

Instant access accounts
These let you take out your money whenever you want, without penalty.

Interest
Your savings earn interest. This can go up or down or may be fixed. Once interest is added to your savings, your money grows.

Investment trusts
A pooled investment. You are buying shares in a company that invests in other investments. It has shares and is quoted on the stock exchange. It is a **closed-ended fund** as the number of shares available is fixed.

Net interest
Interest paid to you based on your savings from banks and building societies with tax already taken off.

Notice period
A set number of days before you can make a withdrawal without charge from a bank or building society account – 30, 60 or 90 days are common notice periods.

Pooled investments
A way of putting contributions of various amounts from lots of people into a single investment fund. There are different types and they work in different ways.

Shares
A stake or share in a company.

Stocks
Another term for shares.

Tax year
6th April one year till 5th April the following year.

Unit trusts
A pooled investment, which is an **open-ended** investment that gets bigger as more people invest and smaller when they take money out.

Variable interest
The interest rate goes up or down in line with the Bank of England base rate.

Useful contacts

Call rates may vary – check with your telephone provider for their charges.

To order other MONEYmadeclear™ guides, check our Register, report misleading promotions or for general information or guidance

Financial Services Authority (FSA)
Consumer Helpline: 0845 606 1234
Minicom/Textphone: 08457 300 104
www.moneymadeclear.fsa.gov.uk

Other MONEYmadeclear™ guides
- About the Financial Services Authority
- Borrowing money
- Credit unions
- Getting financial advice
- Insurance
- Making a complaint
- Mortgages
- Pensions

On our MONEYmadeclear™ website you can find:
- a **Budget calculator** to help you work out how much money you have available each month.
- **Compare products** tables to help you compare products including savings accounts and ISAs
- information on savings www.moneymadeclear.fsa.gov.uk/products/savings/savings.html
- information on investments www.moneymadeclear.fsa.gov.uk/products/investments/investments.html

Other organisations that can help you

For information on bank or building society accounts or a copy of the Banking Code

British Bankers' Association (BBA)
www.bba.org.uk

Building Societies Association (BSA)
www.bsa.org.uk

Tips on how to stay safe online

Banksafe online
www.banksafeonline.org.uk

For information on credit unions

Association of British Credit Unions Ltd (ABCUL)
www.abcul.coop

Find out if there is a credit union near you.

For information on ISAs or employee share schemes

HM Revenue & Customs
www.hmrc.gov.uk

Factsheet:
Individual Savings Accounts

For information on government-backed savings

National Savings and Investments (NS&I)
www.nsandi.com

National Savings certificates, premium bonds and other savings accounts

For information on investments

Association of Investment Companies (AIC)
www.itsonline.co.uk
Order line: 0800 085 8520

Guide to investment companies plus various factsheets

Association of Private Client Investment Managers and Stockbrokers (APCIMS)
www.apcims.co.uk

Online information on sharedealing

Investment Management Association (IMA)
www.investmentuk.org
Information line: 020 7269 4639

Factsheet:
Introducing investment

Other factsheets are available.

London Stock Exchange
www.londonstockexchange.com

Online information for first-time investors

Ethical Investment Research Services
www.eiris.org

Information about product providers and other sources who provide ethical investments

For information on tax, benefits and employee share schemes

Directgov
Money, tax and benefits section

www.direct.gov.uk

HM Revenue & Customs
Helpline: 0845 980 0645

www.hmrc.gov.uk/calcs/r85

Check if you can receive tax-free interest on your savings.

For information on other savings schemes

Office of Fair Trading (OFT)
Order line: 0800 389 3158
www.oft.gov.uk

Leaflet: Save Xmas – A quick guide to paying for Christmas

Complaints and compensation

Financial Ombudsman Service
South Quay Plaza
183 Marsh Wall
London E14 9SR

0845 080 1800
www.financial-ombudsman.org.uk

Financial Services Compensation Scheme (FSCS)
7th floor, Lloyds Chambers
Portsoken Street
London E1 8BN

020 7892 7300
www.fscs.org.uk

The Companies Registry
Department of Enterprise, Trade and Investment

1st Floor, Waterfront Plaza
8 Laganbank Road
Belfast BT1 3BS

0845 604 8888
www.companiesregistry.detini.gov.uk

For credit unions in Northern Ireland