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Anderson Financial



Your financial safety net: How to protect what matters most to you

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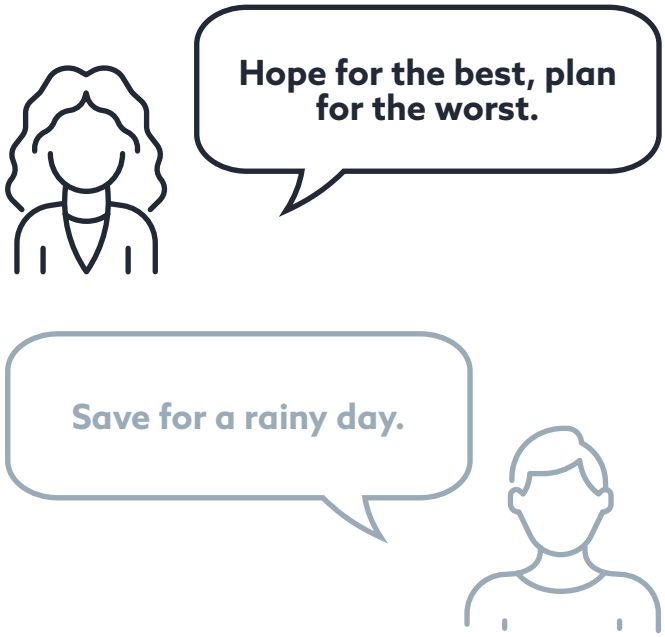


The English language is full of adages imploring us to use the good times in life to prepare for the more challenging ones.

Life can be plain sailing with everything going according to plan one minute, and then your world can be turned on its head the next.

Redundancy, illness, bereavement, and all manner of other events can come from nowhere and pose considerable challenges to your personal life, career, and finances.

And when the rains come, the best thing you can do is to have a storm shelter already prepared.

A financial safety net is a collection of savings, protection, and other buffers designed to shield your personal finances from life's unexpected twists and turns. Ensuring your safety net can support your lifestyle doesn't typically require lots of work or money. However, careful long-term planning is key.

In this handy guide, you will find out more about financial safety nets, including:

- What yours could include
- The role of cash savings
- Why you should consider protection, such as critical illness cover and life insurance
- Why your estate plan plays an important role
- How to fill your "protection gap"
- How we can help throughout the process.

Your financial safety net is not one-size-fits-all

Your safety net includes any financial arrangements you have in place to protect your finances from life's uncertainties.

Exactly what this comprises will differ from person to person, but a typical financial safety net might include:

- Cash savings
- Protection policies
- A broad collection of estate planning arrangements, including care plans, Lasting Powers of Attorney (LPAs), and an up-to-date will.

We will explore each of these components and the role they might play in your financial safety net in the following sections.

WHY IT'S IMPORTANT TO HAVE A FINANCIAL SAFETY NET IN PLACE

Life is unpredictable, and a safety net can be invaluable in the following circumstances:

- Redundancy
- A loss of business
- Illness
- Relationship breakdown
- Caring responsibilities
- Damage to your home or other property that isn't covered by insurance.



Why you need an emergency fund

An emergency fund is often what first comes to mind when people think of a financial safety net. It is a store of cash tucked away for a rainy day, and you don't touch it until you need it.

The key to building an emergency fund is keeping it in cash. This is because cash is generally secure and isn't susceptible to market dips in the way that investments can be. As such, you will know the exact value you have saved at any time.

Many cash savings accounts pay interest, although the rate you receive will depend on the type of account you hold and whether the interest rate is fixed or variable. However, over the long term, cash may be less likely to keep pace with inflation than market investments. So, it's important not to hold more than you need.

DID YOU KNOW

The Financial Services Compensation Scheme (FSCS) protects eligible deposits up to £120,000 per person per authorised bank, building society or credit union if that firm fails.



HOW BIG SHOULD YOUR EMERGENCY CASH FUND BE?

A commonly cited recommendation is to have **three to six months** of expenditure saved to cover everything you would need to spend in that time, though your needs may be different depending on your situation.

The main options for saving cash

Easy access savings accounts generally allow you to withdraw your money when needed – some may have withdrawal limits or other conditions, and interest rates may vary.

Fixed-term savings accounts generally offer a fixed rate of interest for an agreed period of time. Access to your savings during this period may be restricted and early withdrawals, where permitted, may incur a charge or loss of interest.

Cash ISAs can be either easy access or fixed-term accounts, but any interest you earn in them is free from Income Tax, Capital Gains Tax, and Dividend Tax. In 2026/27, you can put up to £20,000 across all your ISAs in a single tax year.

Premium Bonds aren't technically cash savings accounts, but they are a secure way to hold your money and are backed by HM Treasury. Withdrawals normally take several working days. Whilst the amount you invest will not fall in value, inflation may reduce its purchasing power over time. Instead of earning interest, your eligible bonds are entered into monthly prize draws, with tax-free prizes ranging from £25 to £1 million. However, there is no guarantee that you will win a prize, so other savings options may be more appropriate depending on your circumstances.

Each option has pros and cons, and your emergency fund may contain a mixture of the above options. That said, it's a good idea to use your ISA allowance, if possible, as the interest will remain tax-free.

Any interest you earn above a certain threshold in non-ISA accounts is taxable. That threshold is known as your Personal Savings Allowance (PSA), and in 2026/27 the allowances are:

- £1,000 for basic-rate taxpayers
- £500 for higher-rate taxpayers
- £0 for additional-rate taxpayers

What to do if you can't work

If you are unable to work for a significant period due to illness, your employer may cover your salary for a while, or you might assume you can rely on benefit payments.

Depending on your employment contract, your employer may provide contractual sick pay for a period of time. If you are eligible for Statutory Sick Pay (SSP), this is payable at £123.25 per week or 80% of your average weekly earnings, whichever is lower (2026/27). SSP is payable from your first full working day of sickness absence for up to 28 weeks and may be considerably less than your normal earnings.

There are two main types of protection to cover you if you can't work:



CRITICAL ILLNESS COVER

Critical illness cover typically provides a tax-free lump sum if you are diagnosed with a specified illness or undergo a specified medical procedure that meets the definitions and conditions set out in the policy.

The illnesses covered, severity requirements, exclusions and other policy conditions vary between insurers. Being diagnosed with a serious illness does not automatically mean a claim will be payable.

Given the differences between the policies available, it's important to ensure you understand exactly what is and isn't covered before you take out a policy.

INCOME PROTECTION INSURANCE

Income protection insurance offers regular payments to cover part of your income if you're unable to work due to illness or an accident.

While policies vary, they typically pay out between 50% and 65% of your income, subject to the insurer's definition of earnings and policy limits.

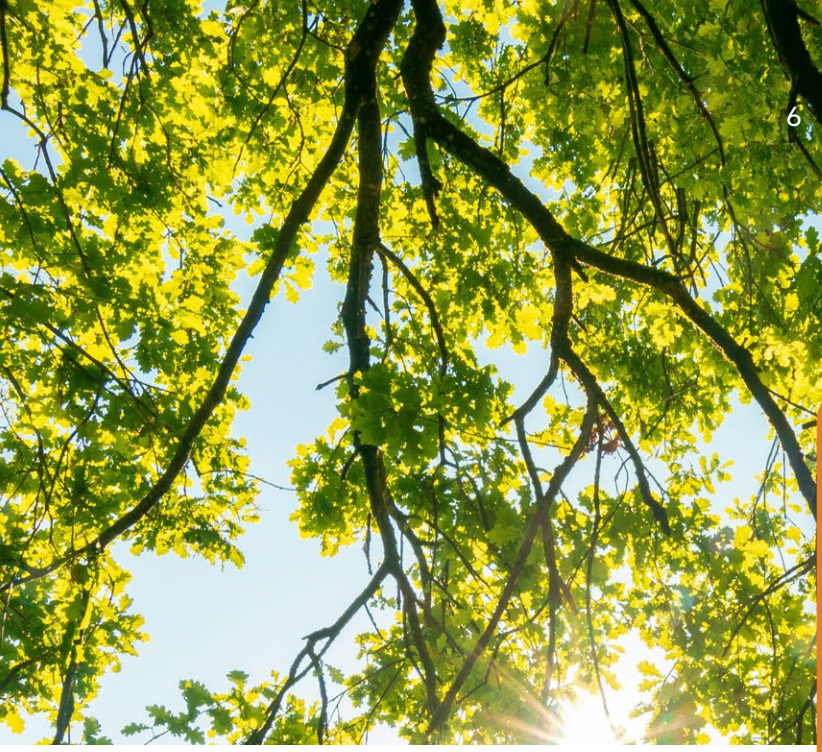
Policies often include a pre-agreed waiting period before payments start, typically ranging from four weeks to a year. Generally, the longer the waiting period, the lower the monthly premiums.

Depending on the policy, payments may continue until you are able to return to work, reach the end of the agreed benefit payment period or policy term, retire or die.

Some policies provide payments for a limited period, such as one, two or five years.

Whether a claim is payable will depend on the policy's definition of incapacity, its terms, conditions and any exclusions.





Life insurance can offer vital support to your family after you're gone

Life insurance is a protection policy that may pay out a lump sum to your family and loved ones when you die.

It is designed to help ensure the security of those who financially depend on you and can be used to cover living costs, mortgage repayments, an Inheritance Tax (IHT) bill, or anything else they may need support with.

There are two main types of life insurance policies:

Term Life Insurance: This covers you for a specific period of time. If you die within this period, your policy pays out. If you outlive it, the policy ends, and there is no payout.

Whole-of-Life Insurance: This covers you for the rest of your life, no matter when you die. These policies are usually more expensive than Term Life Insurance. They are sometimes called "Life Assurance".

If you die during the policy term, the provider will pay out the agreed benefit, subject to the policy's terms, conditions and exclusions. It is important that your regular payments are maintained, otherwise your cover may end.

DID YOU KNOW

The vast majority of life insurance policies pay out.

The ABI (29 June 2026) reports that 96.7% of Term Life Insurance and 100% of Whole-of-Life policies paid out in 2025.

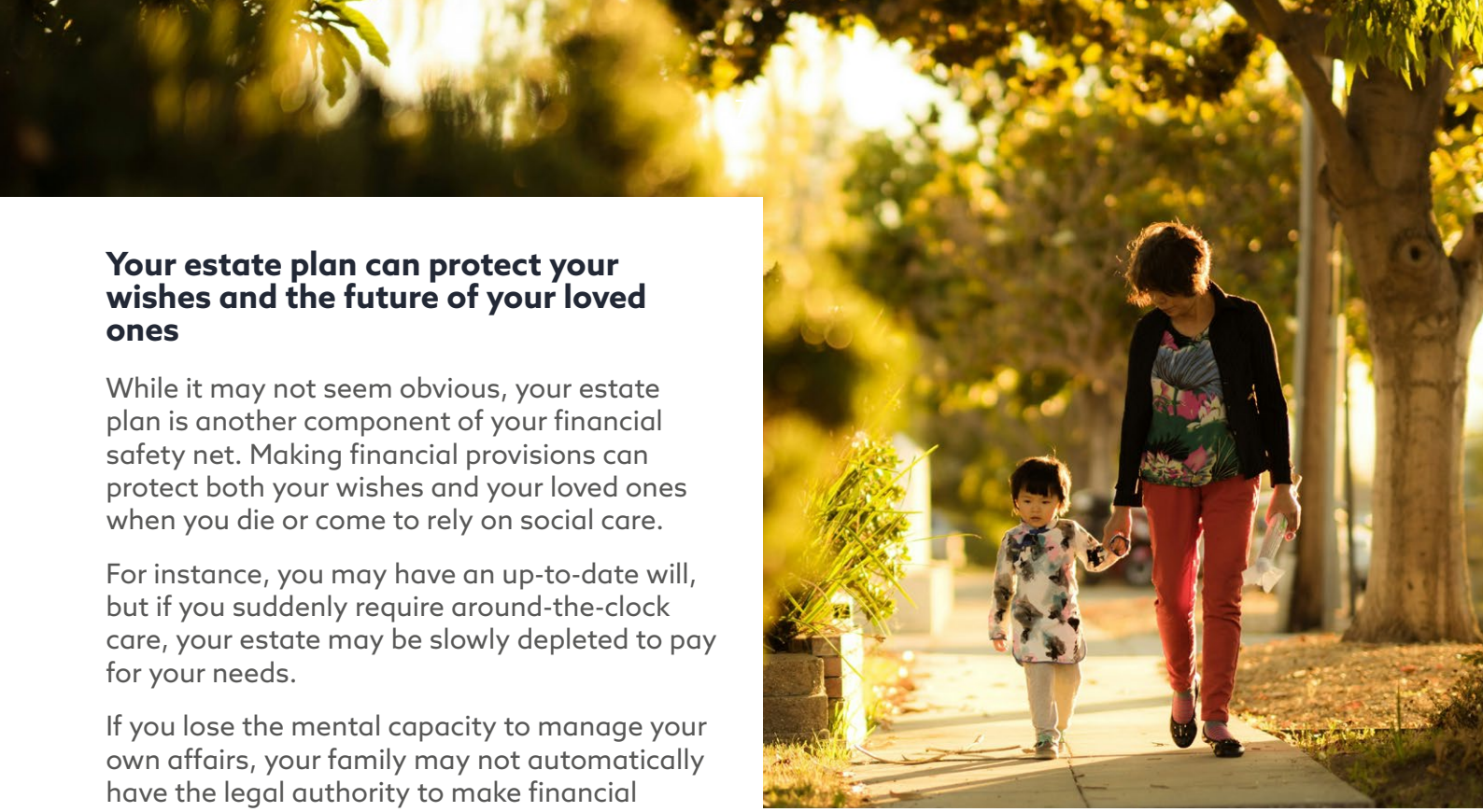
It is important to answer the insurer's questions honestly and accurately when applying for cover, as providing inaccurate or incomplete information may result in a claim being declined or the amount paid being reduced.

LIFE INSURANCE PAYOUTS MAY BE LIABLE FOR INHERITANCE TAX UNLESS IT IS WRITTEN INTO TRUST

Writing a life insurance policy into an appropriate trust may help ensure that the proceeds fall outside of your estate for Inheritance Tax purposes. It may also enable the proceeds to be distributed without waiting for probate.

Indeed, a report from Insurance Business (13 August 2025) found that up to £346 million may have been paid in IHT in 2022/23 due to life insurance policies not being held in trust.

However, trusts are not appropriate in every situation and can have legal and tax implications. A financial planner can help you consider whether a trust is appropriate for your circumstances, working alongside a legal or tax specialist where necessary



Your estate plan can protect your wishes and the future of your loved ones

While it may not seem obvious, your estate plan is another component of your financial safety net. Making financial provisions can protect both your wishes and your loved ones when you die or come to rely on social care.

For instance, you may have an up-to-date will, but if you suddenly require around-the-clock care, your estate may be slowly depleted to pay for your needs.

If you lose the mental capacity to manage your own affairs, your family may not automatically have the legal authority to make financial decisions on your behalf. Having appropriate arrangements in place such as a registered Lasting Power of Attorney (LPA) can help ensure that someone you trust is able to act on your behalf.

Therefore, it's important to consider multiple strategies when building your estate plan, including:

- Writing a will that you review either every five years or after every significant life event
- Registering an LPA so that someone you trust can make key financial or health decisions on your behalf if you are unable to do so
- Setting out clear nominations for your pensions
- Putting certain assets in trust to help shield them from IHT
- Developing a gifting strategy that reduces the value of your estate while also providing for your loved ones taking into account your own financial needs and relevant tax rules.

THE RULES AROUND PENSIONS AND INHERITANCE TAX ARE CHANGING IN 2027



Pensions have historically been exempt from IHT, so paying more into your pension used to be an effective way of mitigating tax on your estate.

However, from April 2027, pensions are set to be brought into the scope of IHT, which means the tax bill on your estate could significantly increase.

One way around this might be to use your pension to pay for life insurance held in trust. This helps ensure any surplus pension you have after you die goes directly to your beneficiaries IHT-free.

This is a complex strategy that involves many variables including reducing the funds available to fund your own retirement. It may also have income tax implications so it's important to consult a financial planner before adopting it.



How to build your safety net and identify your "protection gap"

The "protection gap" refers to the difference between the level of financial protection you need and the arrangements you currently have in place.

The following questions can help you understand your protection gap:

- What is my monthly expenditure?
- How much cash do I have saved?
- How long would my current cash reserves last?
- What sick pay would I receive if I were off work for a sustained period?
- What protection policies do I have in place?
- Does my current employer provide death in service benefits and if so, how much?
- Could my loved ones afford to live without my support?
- What outstanding financial commitments do I have, such as a mortgage or other borrowing?
- Do I have a plan in place for how my wealth can support my family if I'm no longer around or able to work?

In every instance, you want to work out what you have, what you need, and the gap between the two. For example:

- **You have:** £10,000 in your emergency fund.
- **You need:** £25,000 in cash savings to cover six months' expenditure in case you are unable to work.
- **The gap:** £15,000.

Going through each of the elements that make up a financial safety net (as laid out in this guide) can help you identify your protection gap.



THE KEY BENEFITS OF HAVING A FINANCIAL SAFETY NET THAT INCLUDES SAVINGS, PROTECTION, AND AN ESTATE PLAN

Greater peace of mind: Knowing you have enough money set aside and protection in place offers peace of mind during uncertain or difficult periods.

Protected long-term goals: Having a safety net may reduce the need to access our pensions or investments prematurely, which could jeopardise your long-term plans.

Reduced stress and anxiety: Being under financial pressure, especially if you are already sick, can be a considerable source of stress and anxiety. A safety net can help alleviate this.

Greater independence: A financial safety net may reduce your reliance on financial support from others such as family, friends, or additional borrowing.

Confident decisions: A safety net can give you time and space to make careful choices about your future, rather than being rushed into quick decisions.

A financial planner can help you build a safety net that protects you and your family

A financial planner can work with you to identify your protection gap. They can recommend protection policies you may be missing or strategies you might want to adopt, such as putting assets into trust or developing a plan to make regular gifts to your loved ones.

Once you have determined your protection gap and explored the various options available to you, a financial planner can help you create a plan that gets you from where you are to where you need to be.

They can use cashflow modelling to show how your finances may be affected in different scenarios, and you can then develop a financial plan designed to help you manage potential financial challenges, taking account of your individual circumstances, priorities and affordability.

A financial planner can also conduct regular reviews to help ensure your financial safety net continues to reflect your changing circumstances, needs and objectives.A financial planner can also conduct regular reviews to ensure your safety net continues to reflect your circumstances and that you and your family are fully protected.

To speak to a financial planner, get in touch.

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Please note: This guide is for general information only and does not constitute advice. The information is aimed at individuals only.

All information is correct at the time of writing and is subject to change in the future.

Please do not act based on anything you might read in this guide. All contents are based on our understanding of HMRC legislation, which is subject to change.

The Financial Conduct Authority does not regulate estate planning, cashflow planning, tax planning, trusts, Lasting Powers of Attorney, or will writing.

A pension is a long-term investment not normally accessible until 55 (57 from April 2028). The fund value may fluctuate and can go down, which would have an impact on the level of pension benefits available.

The value of your investments (and any income from them) can go down as well as up and you may not get back the full amount you invested. Past performance is not a reliable indicator of future performance.

Note that life insurance and financial protection plans typically have no cash in value at any time and cover will cease at the end of the term. If premiums stop, then cover will lapse.

Cover is subject to terms and conditions and may have exclusions. Definitions of illnesses vary from product provider and will be explained within the policy documentation.

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