



On the lookout for LISA

Will next year's Lifetime ISA be a real pension alternative?

The rumour machine that operates before each year's Budget went into overdrive in 2016. First there was a steady flow of stories about changes to pensions that would see flat rate tax relief replace full income tax relief on pension contributions. Then, shortly before the Budget, there was a widely covered unofficial statement that the Chancellor had decided to make no changes. As it turned out, both rumours had an element of truth.

The good news is that full tax relief on pension contributions remains available for now, but Mr Osborne did not completely abandon tax reform of retirement savings. In a surprise move he announced the launch of the Lifetime ISA (LISA) from April 2017, which will only be available to the under-40s.

How LISA will work

The LISA will give investors a 25% government bonus on their contributions, up to an annual maximum of £1,000 (this being the amount of bonus payable on the maximum investor contribution of £4,000 a year). That's the equivalent of 20% basic rate tax relief. No bonus will be paid once an investor has reached age 50. Provided the LISA has been held for a minimum of 12 months, the investor can use the funds to buy a first home, or withdraw them from age 60 and use the funds towards retirement or for any other purpose. As with existing ISAs, LISA investments will be free of UK tax and all withdrawals will be tax free, but the LISA bonus is lost and a 5% charge will apply if the funds are withdrawn before age 60 and not used for first house purchase.

Many commentators made the observation that the new LISA looked remarkably similar to ideas for a Pension ISA which were floated by the Treasury last year. Some also saw LISA as a stalking horse for pension tax reform. It is not beyond the realms of possibility to imagine the LISA being made available to all investors in some future Budget, and tax relief on pension contributions being replaced by the LISA's 25% bonus.

In other words, the survival of higher rate relief may have been just a stay of execution...

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Budget 2016 tax changes: new moves

This year's Budget contained many measures which could affect your long term financial planning.

Budgets have become a regular feature of the financial landscape. The March 2016 Budget is the third in twelve months and it revealed some important tax changes:

Income tax For 2017/18 the personal allowance will rise by £500 to £11,500 and the higher rate tax starting point will increase by £2,000 to £45,000. This means the higher rate threshold will finally rise above its 2009/10 peak of £43,875. The Chancellor confirmed his goal of a personal allowance of £12,500 by the end of the Parliament (2020/21), but he made no comment about an earlier pledge to raise the higher rate threshold to £50,000 by the same time.

Capital gains tax One unexpected change was an 8% cut in the rates of capital gains tax, starting in the current year 2016/17. Gains that fall within your basic rate tax band are now generally taxable at 10%, while gains in higher and additional income tax bands suffer 20% tax. However, gains made on residential property (e.g. buy-to-let and second homes) do not benefit from this reduction, and continue to be taxed at the old 18%/28% rates.

ISAs The ISA contribution limit for 2016/17 is unchanged at £15,240 due to the fact that inflation was negative last September, but the Chancellor announced the limit would jump to £20,000 for 2017/18. He also promised the launch of a new Lifetime ISA (LISA) from 2017/18, which is designed to encourage saving by the under-40s. The LISA offers the equivalent of 20% tax relief on up to £4,000 of savings each year until the age of 50.

Corporation tax Mr Osborne had already earmarked a cut in corporation tax to 18% in 2020, but in the Budget he shaved another 1% off the rate, taking it down to 17%. However, he also proposed a number



of technical changes to corporation tax which will increase the Exchequer's tax take from some larger companies.

Other tax changes which were announced in earlier Budgets are being legislated for in the Finance Bill currently going through Parliament. Some of these need to be considered alongside the March 2016 measures. For example:

■ **Dividend taxation** The £5,000 dividend allowance, which was introduced from 6 April 2016, adds to the appeal of investing in shares and share-based funds. Not only will some investors escape tax on their dividends altogether, but the most tax any individual will pay on capital gains is now 20%.

The dividend allowance and future changes to corporation tax are also relevant to the way in which any business should be structured, and whether or not taking dividends is the best way to extract profits going forward.

■ **Pension protection** A 20% cut to the lifetime allowance (to £1m) was announced in the March 2015 Budget, along with two new transitional protections that can be claimed by those affected. These took effect from 6 April 2016.

If you think any of these changes could affect you, now is the time to talk to us about what actions you should take, if any.

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Buy-to-let: strike five

The buy-to-let sector is under Treasury attack.

The government appears to have taken aim at buy-to-let investors in its efforts to help 'generation rent' become first time buyers. In the last year there have been five important announcements:

1. A phased reduction in tax relief for mortgage interest down to 20% by 2020/21;
2. The replacement in 2016/17 of the 10% wear-and-tear allowance with one based on costs the landlord has actually incurred;
3. An additional 3% stamp duty land tax (and building transaction tax in Scotland) on the purchase of second properties from 1 April 2016;

4. The maintenance of higher CGT rates for residential property in 2016/17, while other rates fall; and
5. A buy-to-let mortgage market review, which is expected to curtail lending.

The buy-to-let market boomed in the first months of 2016, but reports suggest a considerable cooling in the market since. Longer term, the market's fate is unclear. The tax changes have clearly reduced the potential returns from buy-to-let investment, particularly where mortgage finance played a key role. Some existing investors may find that in a few years' time, after-tax rental income may not cover their net mortgage costs.

If you are tempted to invest in the sector, make sure you consider alternative homes for your capital first.

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Your property may be repossessed if you do not keep up repayments on your mortgage.

The Financial Conduct Authority does not regulate some forms of Buy To Let mortgages.

Can you really avoid inheritance tax?

Inheritance tax (IHT) was once famously described as “a voluntary levy paid by those who distrust their heirs more than they like the Inland Revenue” by Roy Jenkins, a former Chancellor of the Exchequer.

When Gordon Brown was Chancellor of the Exchequer, he called IHT a ‘voluntary tax’ because he said there were many ways to avoid it.

It is clear, however, that not everyone has taken this message on board. The details of the estate of a well known and recently deceased figure in the world of entertainment were recently published. In the will, £15 million was to be divided between her three children. Each son will receive just over £3 million but the biggest beneficiary will be the Exchequer in the shape of a huge tax bill of nearly £6 million.

The billions that could be saved

The Office for Budget Responsibility released figures in 2014 which estimated that one in ten deaths would be subject to IHT in the 2018/19 tax year. This number is eventually expected to reduce as a result of the new main residence nil-rate band introduced in the Summer Budget 2015, but the Exchequer is still expected to receive receipts of around £5.6 billion of IHT a year by 2020/21.

If you aim to take advantage of the voluntary nature of IHT, it is essential to do your tax planning in good time. That means starting now – as soon as



possible – because most of us cannot foresee when we are going to die.

Start your estate planning

The first step is to make an appointment with us and put together a plan of action. This is likely to involve a number of aspects of your financial arrangements, such as making sure you have an up to date will in place, identifying which of the various exemptions you can use, and perhaps giving away assets now so that you see your heirs enjoy them during your lifetime. Personal pension funds

have taken on a new role in IHT planning due to recent changes, and it can sometimes make sense to delay taking benefits from these. Your adviser will also look at using trusts. Where ordinary ISAs form part of your estate on death, they can be converted into AIM ISAs which fall outside of your estate after you have held them for two years. There are schemes which make use of business property relief, and life assurance placed in trust is essential where you are not in a position to give much away.

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Stay covered for the rainy days

Whatever your view about the principle of providing people with social security benefits if they are ill or unemployed, it is inadvisable to try living solely on what the State provides in such circumstances. The so-called ‘safety net’ is lower than you may think it is.

After the recent U-turn on the Personal Independence Payments (PIP), the government has said there will be no more benefit cuts beyond those already planned, but that does not mean that you or your family could comfortably rely on State support to make ends meet during such times.

If you can’t work because you are sick or disabled, you may be able to claim Statutory Sick Pay (SSP) or Employment and Support Allowance (ESA). SSP is paid at a fixed rate of £88.45 a week for the first 28 weeks of sickness if you work for an employer. Otherwise, you should claim ESA.

Personal Independence Payments are an additional benefit for people aged 16-64 with a long-term health condition or disability who need help with everyday tasks or getting around. The standard daily living component is £55.10 a week and this can increase by the addition of a standard mobility component of £21.80 a week.

If you become unemployed when you are 25 or over but have not reached your State pension age, you will receive a maximum of £73.10 a week Jobseekers Allowance while you are actively looking for work. The rules are different in Northern Ireland.

The full new State pension is £155.65 per week. Your National Insurance record is used to calculate your entitlement, and you will usually need 10 qualifying years to get any new State pension and normally 35 years to claim the full amount.

You might be able to claim Bereavement Allowance of up to £112.55 a week for up to 52 weeks if you are widowed between 45 and State pension age, together with a one-off £2,000 bereavement payment if you are under your State pension age when your husband, wife or civil partner died.

Whilst we cannot cover the full range of State



benefits here, it should be sufficient to indicate that for most of you the amounts payable are inadequate to maintain the kind of standard of living that you would want to maintain. Get in touch with us to discuss a range of plans that could help bolster your financial defences.

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How much lower for longer...?

March 2016 marked the seventh anniversary of a 0.5% Bank of England base rate, but other interest rates are still falling.

"Lower for longer" is now a commonly used phrase when economists and bankers discuss the future of interest rates. The view is supported by banks and other deposit takers, which continue to reduce savers' rates. Shortly after Easter, National Savings & Investments (NS&I) joined the rate cutters. From June Income Bonds and the Direct ISA will then pay only 1%. In its announcement NS&I said "...downwards movements in interest rates across the cash savings market mean that our rates have risen in the competitor tables."

If you need income, then the continued downward pressure on deposit rates is unwelcome news. However, if you are prepared to forgo capital security, there are plenty of investment options capable of providing a higher income return. For example:

■ **UK equity income funds** typically yield

around 4% and offer potential for long term growth in income. The reforms to dividend taxation that took effect at the start of this tax year mean your first £5,000 of dividends now attracts no personal tax, regardless of your marginal tax rate

- **Global equity income funds** generally have a lower income yield than their UK counterparts, but offer a valuable element of diversification.
- **Property funds** which invest directly in property (rather than shares in property companies) offer attractive yields. The current rental return on commercial property is around 5% according to Cluttons, the property agents.
- **Fixed interest funds**, such as sterling corporate bond funds, have long been popular with investors seeking income. The range of income yields on offer is

wide, with the highest income generally coming from funds investing in the lowest quality bonds.

If any of these investment opportunities interest you, do make sure you take advice before investing: simply picking the funds with the highest initial income can be a fatal mistake.

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The potential costs to a business of not complying with the rules for automatic enrolment were recently highlighted in press reports about Swindon Town football club. In the words of The Pensions Regulator, the club "repeatedly failed to comply with its automatic enrolment duties," and was ultimately fined £22,900. If your business is yet to start auto-enrolment, you need to begin preparation early to avoid incurring penalties. Occupational pension schemes are regulated by The Pensions Regulator.

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Don't fall into the gifting tax traps

New tax rules introduced in April have changed your options when investing for children.

If you give money or investments to your unmarried minor child, then the tax rules can catch you out. HM Revenue & Customs (HMRC) is suspicious that such gifts are an attempt to avoid tax on the part of the donor, so the law says that if the total income generated from all such gifts exceeds £100 in a tax year, that income is taxed as that of the parent. The rule operates on a per parent, per child basis, but it can still be difficult to avoid crossing the £100 threshold.

Several ways of sidestepping the problem have been developed over the years. The government has provided a partial solution by introducing the Junior ISA, which allows up to a total of £4,080 per tax year to be invested with no tax consequences upon parental donors, and no personal UK tax on the underlying investments.

Two new tax allowances, which came into effect at the start of this tax year, have changed the picture somewhat:

- **The personal savings allowance** means that if you are a basic rate taxpayer you can receive up to £1,000 per tax year of interest free of tax. If you pay tax at 40% the allowance is £500, but there is no allowance if you are a 45% taxpayer.
- **The dividend allowance** gives you up to £5,000 of dividends free of personal tax per tax year, regardless of your tax rate.

Both allowances could be useful if a gift to a child would lead to the £100 threshold being breached. Unless the relevant allowance is exceeded based on the total of your and your child's income, there will be no income tax to

pay. However, direct investment in the name of a child is not always an ideal solution, as it gives the child access to the funds when they reach the age of majority, and there could be inheritance tax consequences.

You should therefore always seek advice before making gifts to your children.

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