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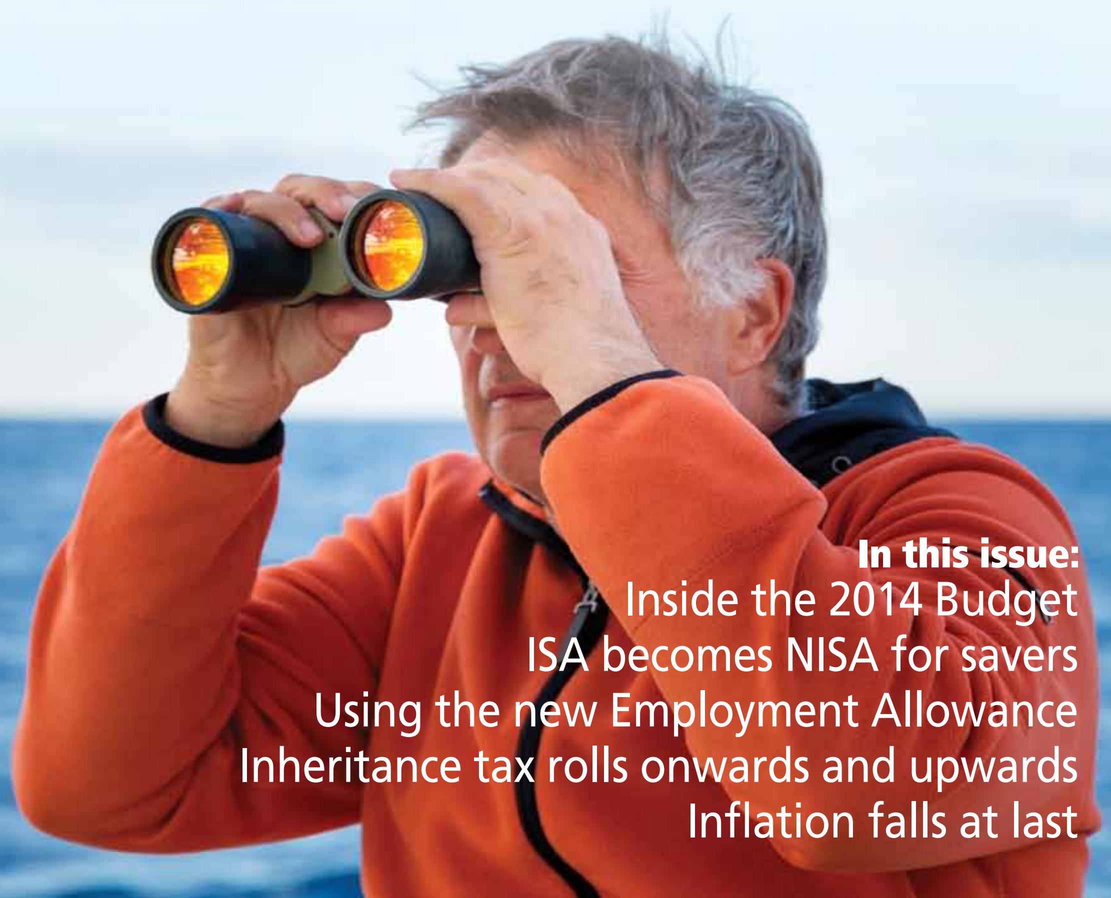
financial FOCUS

The pensions revolution:
changes on the horizon



In this issue:

Inside the 2014 Budget
ISA becomes NISA for savers
Using the new Employment Allowance
Inheritance tax rolls onwards and upwards
Inflation falls at last

Contents

Inside the 2014 Budget 3

There were plenty of changes in this year's Budget – many of them in the small print.

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The pensions revolution: changes on the horizon 4–5

The Budget hailed a private pension revolution which could affect your retirement planning.

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ISA becomes NISA for savers 6

From 1 July 2014, the new maximum annual investment level gives the ISA a boost.

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Using the new Employment Allowance 7

Employers are in line to receive up to £2,000 from the Government.

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Inheritance tax rolls on 7

Inheritance tax is generating a rapidly rising income for the Government.

Inflation falls at last 8

Inflation is finally falling – after remaining stubbornly ahead of the Bank of England's 2% target.

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Getting to grips with life policies

Cover that qualifies for full tax relief can reduce the cost of life insurance.

If you are a basic rate taxpayer the tax relief cuts the effective cost by 20% and for higher earners, the tax relief can save 40% or even 45% of the premium. What's more, employers and employees do not pay national insurance contributions on the premiums – unlike many benefits in kind such as private medical insurance or the provision of a company car. So the effective cost saving is more than the pure income tax relief.

It isn't currently possible for individuals to take out a new life policy that qualifies for tax relief, but employers can arrange insurance on the lives of their employees and directors. Sadly, self-employed people do not qualify. The employer gets tax relief on the premiums and the employees and directors don't have to pay income tax on the benefit in kind of having the insurance.

If the employee then dies, their dependants can receive the death benefit payment free of both income tax and inheritance tax. These plans can be arranged on an individual basis, and they are called 'relevant life policies'. They are term assurance plans available to employers to provide an individual death in service benefit for an employee. Where there are several employees, they can be arranged on a group basis, known as 'excepted group life policies'.

The employer decides which employees should be included and also the levels of cover. As a broad indication, insurance companies that operate these policies generally allow employees to have cover of up to about 20 times earnings, including bonuses and commission for those up to 40 years of age, and about 15 times from 40 up to the maximum of 75 years. These policies can only pay a lump sum and they can't include any extras such as critical illness insurance, although some may pay out shortly before death if the insured person has a terminal illness.

Another advantage of these plans is that the premiums do not count towards the pension 'annual allowance' – currently an annual input of £40,000. And if there is a claim, they do not use up any of the individual's pension lifetime allowance (currently £1.25 million for most pension scheme members) above which there may be a tax charge on pension death benefits.

It is important to make sure that these types of policy are set up correctly. There is no guarantee that the favourable tax position will apply in all cases and there are also other circumstances when the plan might not pay out in full. The cost of the plan may rise, making it more expensive than you are willing or able to pay.

Inside the 2014 Budget

The small print revealed plenty of changes, not all of which made the Chancellor's Budget speech.

This year's Budget headlines were dominated by the reforms to pensions (see "The pensions revolution"), but there were plenty of other tax changes:

Income tax

The Chancellor set out changes for *next* tax year, i.e. 2015/16:

- The personal allowance is set to rise from the current £10,000 to £10,500. However, the allowance will still be phased out at the rate of £1 per £2 of an individual's adjusted income over £100,000.
- The higher rate threshold – the point at which you start paying higher rate tax – will rise by 1% to £42,285. This will still be almost £1,600 below its 2009/10 level.
- The transferable tax allowance will begin for married couples and civil partners. To be eligible, neither you nor your spouse/partner may be higher or additional rate taxpayers. You can transfer £1,050 of your personal allowance to your partner (or vice versa), making a maximum tax saving of £210 in 2015/16.
- The starting rate band for savings income will be increased from £2,880 to £5,000 and the rate of tax will be cut from 10% to 0%. This change is not as valuable as it sounds, because the savings rate only applies to savings income, which is deemed to sit on top of your earned income (including pensions) in the income tax hierarchy.

The Chancellor also confirmed that from autumn 2015 a new childcare scheme will start, providing parents with 20% of the cost of childcare, up to a maximum care cost of £10,000 per child, per year. In the first year of the scheme, it will be rolled out to all eligible children under the age of 12.

Capital taxes

There were a few small changes to capital taxes:

- The capital gains tax annual exempt amount will increase by £100 to £11,100 for 2015/16.
- The final period residential property exemption, which applies when a home is sold, has been reduced from 36 months to 18 months, with effect from 6 April 2014. The longer period will still apply for people moving into care.
- Stamp duty land tax (SDLT) saw no rate changes to the main bands, despite the increase in property values. However, the Chancellor did decide to reduce the starting threshold from £2m to £500,000 for the 15% rate on residential properties owned by companies and similar bodies.
- Inheritance tax was untouched, apart from some minor technical changes, including some related to trusts. Further changes to the treatment of trusts will follow consultation later this year.

Other taxes and measures

There was an important change on the business tax front, with the annual investment allowance (AIA) being increased from £250,000 to £500,000 from April 2014. The AIA will stay at this higher level until the end of 2015, after which it is due to fall to £25,000.

As usual there were several anti-avoidance measures, despite the recent substantial fall in the number of avoidance schemes being disclosed to HMRC. If you use such a tax avoidance scheme and it is disputed by HMRC or you enter into a scheme counteracted by the General Anti Abuse Rule introduced last year, you will have to make an upfront payment of the tax you hope to avoid.

To learn more about how these changes could affect you, please contact us.

The value of tax reliefs depends on your individual circumstances. Tax laws can change. The Financial Conduct Authority does not regulate tax and trusts advice and some forms of inheritance tax planning.

The pensions revolution: changes on the horizon

The Budget has started a new private pension revolution which is sure to affect your retirement planning.

The biggest surprise in this year's Budget was the Chancellor's decision to further break the link between pensions and annuities. As he said in his speech, "Let me be clear. No one will have to buy an annuity." Somewhat inevitably, matters are not quite that simple in practice. Legislation – let alone administrative systems – cannot be changed overnight, so we are now in a two stage process:

Finance Bill 2014 This year's Bill makes several interim changes to pension tax law for defined contribution (DC) pension arrangements (such as personal pensions and money purchase occupational pension schemes, but not final salary schemes):

- The limit for capped income withdrawals – making withdrawals from your retirement fund to provide an income – is increased from 120% to 150% of the broadly equivalent market annuity rate (for new plans and from the start of the next drawdown year for existing arrangements).
- The minimum secure income (broadly state pension, occupational pension or pension annuity) for flexible withdrawals has fallen from £20,000 a year to £12,000 a year. So if you have little more than double the basic state pension, in theory you have full access to your pension fund, with no cap on how much you draw and no regular reviews.
- You now have 18 months after drawing your tax-free lump sum before you must start to receive an income from your pension fund (which could be set at nil).
- New higher limits apply for converting small pension benefits into a lump sum (at least 75% of which is taxable). For example, the ceiling on the value of single personal pension arrangement you can convert to a lump sum has risen from £2,000 to £10,000 and the number convertible into cash is now three rather than two.

These changes will require your pension providers to make their own system and rule amendments, so you may not be able to take advantage of them all immediately.

Finance Bill 2015 and beyond The Budget was accompanied by a consultation document covering other pension changes, some of which are destined for next year's Finance Bill. These include:

- The introduction of full pension flexibility for defined

> radical reforms will almost certainly mean that your retirement planning needs to be reviewed.

contribution schemes from 6 April 2015. In effect this would scrap the £12,000 minimum income requirement, allowing you to draw from your fund as and when you think fit. The tax-free lump sum of up to 25% of the fund would remain, but the rest of your fund would be taxable as income.

- The treatment of benefits on death may change. Under the current rules any money remaining in your drawdown pension fund at death is subject to a flat tax charge of 55% if paid as a lump sum, a rate which the Government says "…will be too high in many cases in the future."
- The minimum age from which you can start drawing benefits from your pension is likely to increase – a change that would affect all private pensions. The Government is suggesting this minimum should rise in line with the state pension age (SPA), with the first move being from the current 55 to 57 in 2028, coinciding with SPA reaching 67.

These radical reforms will almost certainly mean that your retirement planning needs to be reviewed. In a world with much greater flexibility, both pre- and post-retirement strategies can look very different.

The value of your investment and the income from it 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. The value of tax reliefs depends on your individual circumstances. Tax and pension laws can change. The Financial Conduct Authority does not regulate tax advice.

Self-assessment tax returns – October is around the corner

Is your self-assessment tax return already lost in your to-do pile? If so, you need to start working on it, because the deadline for paper-based tax returns is 31 October and you face penalties of up to £1,000 from 1 November. You do, however, get a three month extension to 31 January if you tell HM Revenue & Customs you wish to convert to an internet-based return before 31 October – if you haven't done it before you should know that the registration process takes around a week. Remember, even if you file personal tax forms online, you may still have a paper form with a 31 October deadline to return as a trustee or as executor of an estate.

ISA becomes NISA for savers

Pensions were not the only savings plans to see a boost from the Budget. ISAs received a welcome increase to the maximum annual investment level.

Yet it was only last autumn that Individual Savings Accounts (ISAs) appeared to be under threat. There were stories in the press that the Treasury was examining the possibility of capping investment at £100,000. As the Chancellor had announced the new ISA limits for 2014/15 in his Autumn Statement, the Budget was not expected to make any changes: cynics suggested any capping would be a post-election measure.

In the event, Mr Osborne produced several welcome ISA surprises, stating that he wanted to "help savers by dramatically increasing the simplicity, flexibility and generosity of ISAs." The changes are due to take effect from 1 July 2014, although as with the pension reforms, not every provider is likely to be up and running on day one:

- All ISAs will become New ISAs (NISAs).
- The overall annual investment limit will rise to £15,000 for 2014/15, an increase of £3,120 over the Autumn Statement figure. The same £15,000 ceiling will apply to NISAs for 16 and 17 year olds, but as now the investment may only be in cash.
- For Junior ISAs (JISAs), the contribution limit will increase to £4,000 a year.
- New subscriptions can be split in any proportion you choose between cash NISAs and stocks and shares NISAs. If you wish, you can place your entire £15,000 subscription in a cash NISA, not – as previously – a maximum of 50% of the overall limit.
- You can transfer your stocks and shares NISA into a cash NISA. A move in the opposite direction has long been possible, but as a one way ISA trip.
- The investment rules for stocks and shares will be relaxed. This will allow you to invest in funds, such as short-dated bond funds, that are currently ineligible for stocks and shares ISAs. The Government has also said it will consult on peer-to-peer lending and securities offered via crowdfunding platforms within NISAs.
- The 20% flat rate of tax on cash interest earned within stocks and shares ISAs will be abolished.

You will still be able to arrange two NISAs during a tax year – one cash NISA and one stocks and shares NISA. In theory the two could be combined into a single NISA, but before these appear the product providers will have to design them. Any subscriptions you made to an ISA or JISA between 6 April 2014 and 30 June 2014 will count against the new NISA subscription limit.

The new framework for NISAs means that now is a good time to review your existing ISA investments and decide where to invest your 2014/15 contributions. If you have cash ISAs, you could consider switching them to stocks and shares NISAs with the knowledge that you can now return to a cash NISA at a later date. You would lose the capital security that deposits provide, but you could significantly increase the income your (N)ISA provides and have scope for capital growth subject to your attitude and capacity for risk.

The value of your investment and the income from it 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. Investing in shares should be regarded as a long-term investment and should fit in with your overall attitude to risk and financial circumstances. The value of tax reliefs depends on your individual circumstances. Tax laws can change. The Financial Conduct Authority does not regulate tax advice.

Using the new Employment Allowance

If you are an employer, you're almost certainly in line to receive what is effectively a free gift from the Government worth up to £2,000, as part of an initiative to help smaller businesses.

Although there are exceptions, most employers qualify for the new Employment Allowance. This provides up to £2,000 a year off employers' class 1 national insurance contributions – the 13.8% payroll charge on employee earnings over £153 a week.

While you could simply 'bank' the savings, you might also consider using the money to improve your business. The £2,000 allowance could provide the seed corn for employee benefits such as additional pension contributions, health insurance or life cover for employees.

Cash health plans can provide payments when your staff visit the dentist, the optician, or physiotherapist, as well as paying a daily sum when they are in hospital. Buying this cover as a group, even a small one, is generally more cost-effective than individual purchase.

Beneficial for all

These plans can help you as well as your employees. Knowing that you have funded or part-funded payments should help reduce absenteeism or sickness, according to cash plan provider Bupa. Some plans offer help with backache or stress, both common causes of absence.

If you are prepared to dig deeper, then consider group private medical insurance. Private hospitals can treat problems without long waiting lists – again improving staff morale and reducing time off. Life cover offers peace of mind to employees who may never choose it for themselves.

But bear in mind that choosing the right plan for your purpose, working out the cost and tax considerations can be a minefield; so you'll need some expert financial advice.

If your organisation is approaching your staging date for auto-enrolment or if you are in the throes of introducing this pensions innovation, there can be extra costs. You might well need the extra funds to help smooth the path. Auto-enrolment should not present too many difficulties with good preparation, but it does need to be taken seriously and you are likely to need specialist help.

If things are going well, you could spend the money on a staff party or outing, perhaps at Christmas or during summertime. Such events can help lift employee spirits – especially if your workforce is young – and provided the total of such events cost under £150 per employee in a tax year, there should be no tax or national insurance charges to pay.

Inheritance tax rolls on

The unloved tax is generating a rapidly rising income for the Government.

The inheritance tax (IHT) nil rate band has been frozen at £325,000 since 6 April 2009 and measures in this year's Finance Bill will maintain that freeze until at least 5 April 2018. Such a prolonged freeze is inevitably dragging more estates into the IHT net and increasing the IHT paid. The Office for Budget Responsibility projects that the tax will raise almost 75% more for the Exchequer in the final year of the freeze than it did in 2012/13.

If you have not reviewed your estate planning in recent years, you could be surprised at the slice of your wealth destined to disappear in IHT rather than pass to your children or grandchildren. 40% of today's house price rise could be tomorrow's IHT bill.

Fortunately there remain a variety of planning opportunities that can help you reduce the impact of IHT. As is so often the case, the sooner you can start the planning, the better. Why not arrange for an initial discussion with us to assess your IHT liability and the options open to you?

The Financial Conduct Authority does not regulate tax and trust advice and inheritance tax planning.

Inflation falls at last

Inflation is finally falling – after remaining stubbornly ahead of the Bank of England's 2% target.

The headline Consumer Prices Index fell from 1.7% to 1.6% in the year to March 2014. The Retail Prices Index, which includes housing costs, rose by 2.45% over the same year.

But if you feel your personal costs are mounting faster than these figures suggest, you could well be right. An index assumes a typical spending pattern – and we are all different.

The over 75s and under 30s have the highest inflation rates, according to the Economic Research Centre at Alliance Trust who have looked at the impact of rising prices on five different age bands. Older people use more gas and electricity when price changes remain high, while rising student tuition fees are a significant burden on younger people. Those aged 50 to 64 come off best – thanks to a fall in petrol prices.

Even moderate inflation at 2% a year can upset long term financial planning goals. Someone who today takes out a £100,000 life or critical illness policy over 20 years would need £148,590 in 2034 to match today's spending power. A 30 year-old looking at retirement 40 years ahead would need £220,800 to equal a £100,000 pension pot today.

The costly company car – is it worth it?

This year's Budget set out increases in company car tax for 2017/18 and 2018/19. Alas, that does not mean there are no increases beforehand, as earlier Budgets have set tax rises in place through to 2016/17. The increase basis generally means that the lower your car's CO_2 emissions, the greater will be the proportionate rise in tax payable. The same effect will apply to fuel benefit, if your employer still provides you with 'free' fuel. Next time your car is due for replacement, it could be worth looking at alternative, more tax-efficient benefits.

The Financial Conduct Authority does not regulate tax advice.

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