Financial Advice.net
MONEY NEWS

March 2018

A DIFFERENT KIND OF TAX YEAR END…

As we approach the end of another tax year, the planning process is going to be slightly different from other years for two reasons:

1. There will not be a Spring Budget. In 2016 the Chancellor decided to move to Autumn Budgets from 2017, thereby turning the old "Autumn Statement" into a "Spring Statement". The first of these is due on 13 March. Experience suggests that while a Statement is not a Budget, there may be some technical changes announced that take immediate effect, even if they are not legislated for until 2019. Usually these focus on anti-avoidance measures.

2. Easter falls just before the end of the tax year, with Good Friday being 30 March. If you are prone to leave things until the last minute, be warned.

In this newsletter we look at some of the areas that you may need to review as 2017/18 draws to a close and 2018/19 gets under way. As ever, space means only an overview can be given. If you need more information directly relevant to *your* circumstances, please contact us as soon as possible – March can be a very busy time.

INDIVIDUAL SAVINGS ACCOUNTS

Individual Savings Accounts (ISAs) have come a long way since their birth in 1999. There are now five types of ISA, although some people count more:

Type of ISA	Age Eligibility	Maximum contribution* 2017/18	2018/19
Standard Cash/Stocks & Shares ISA	18 upwards, but 16-17 year olds may start a Cash ISA	£20,000	£20,000
Junior ISA	Under age 18 without a Child Trust Fund (CTF) account	£4,128	£4,260
Help to Buy ISA	16 upwards	£1,000 initially then £200 a month	£1,000 initially then £200 a month
Innovative Finance ISA	18 upwards	£20,000	£20,000
Lifetime ISA	18-39 for opening and no contributions possible after 49.	£4,000	£4,000

* The general rule is that the maximum total contributions to *all* ISAs in 2017/18 and 2018/19 is £20,000. However, a 16 and 17 year old can benefit from maximum contributions to a standard ISA (including Help to Buy) and a JISA (ie a maximum of £24,128 in 2017/18 and £24,260 in 2018/19).

Basic features

ISAs have some features which are common across the different types:

- There is no UK tax on interest earned on cash or fixed interest securities.
- Dividends are free of UK income tax.
- Capital gains are free of UK capital gains tax (CGT).
- There is nothing to report on your tax return.

With the exception of Junior ISAs, all ISAs can effectively be inherited by a surviving spouse or civil partner.

Lifetime ISAs (LISAs) offer a 25% government bonus for contributions made before age 50, eg the maximum £4,000 annual contribution attracts an extra £1,000 top up. However, normally there will be a penalty of 25% of any amount withdrawn before age 60, other than towards the purchase of a first home (worth up to £450,000) and withdrawals when the investor is in terminal ill-health.

The importance of 5 April

ISA contributions are use-it-or-lose-it: there is no carry forward to future years of unused limits. Thus, to maximise the benefits of ISAs, you should aim to invest as much as you can each tax year. For example, had you placed the maximum in ISAs since they first were available, you would by now have sheltered over £185,000 from tax.

With very few exceptions, contributions must be in cash. However, if you hold existing investments in funds or shares it is usually possible to move these into an ISA by selling them personally and then immediately reinvesting within the ISA. This may involve costs and counts as a disposal for CGT purposes, but the gains could be covered by your annual CGT exemption (£11,300 in 2017/18).

In 2018, the 5 April is not only a deadline for contributions, but also the final day for a special terms transfer from a Help to Buy ISA to a LISA. If the transfer is made before the start of the new tax year, the value built up in the Help to Buy ISA to 5 April 2017 will receive the 25% LISA bonus with neither the transfer nor the bonus counting as a 2017/18 LISA subscription.

PENSIONS

In recent years, the Treasury has been attempting to cut the cost of pension tax reliefs by reducing the two main allowances, the lifetime allowance (based on total value of benefits) and the annual allowance (based on total contributions in a tax year). Unfortunately for the Chancellor, the Treasury's efforts have been somewhat countered by the Department for Work and Pensions, which has been more successful than many experts expected in encouraging automatic enrolment into work place pension schemes. The latest estimate is that over 9 million people have been automatically enrolled since October 2012.

Catching up on past years' contributions…

The annual allowance sets the maximum possible tax-efficient total pension contribution from all sources at £40,000 per tax year. However, this ceiling starts to be scaled back to as little as £10,000 if, very broadly speaking, your total income (not just earnings) plus employer pension contributions exceeds £150,000.

These constraints on contributions mean that it is no longer possible to adopt the once common (if ill-advised) strategy of making large one-off pension contributions shortly before retirement rather than regular contributions throughout working life. The scope to catch up on contributions that could have, but were not made, is limited to just the last three tax years.

The mechanism involved, carry forward, sounds quite simple but in practice the calculations can be complex, particularly if you are or were an employed member of a final salary pension scheme during the period. *In theory*, in 2017/18 you and/or your employer could contribute as much as £160,000 without hitting any tax penalty. In practice, this is an area where there is no substitute for an in-depth personal assessment. The end of the tax year creates additional pressure, as 5 April 2018 will also be the last day on which unused contributions can be carried forward from the 2014/15 tax year.

And watching out for the future ones…

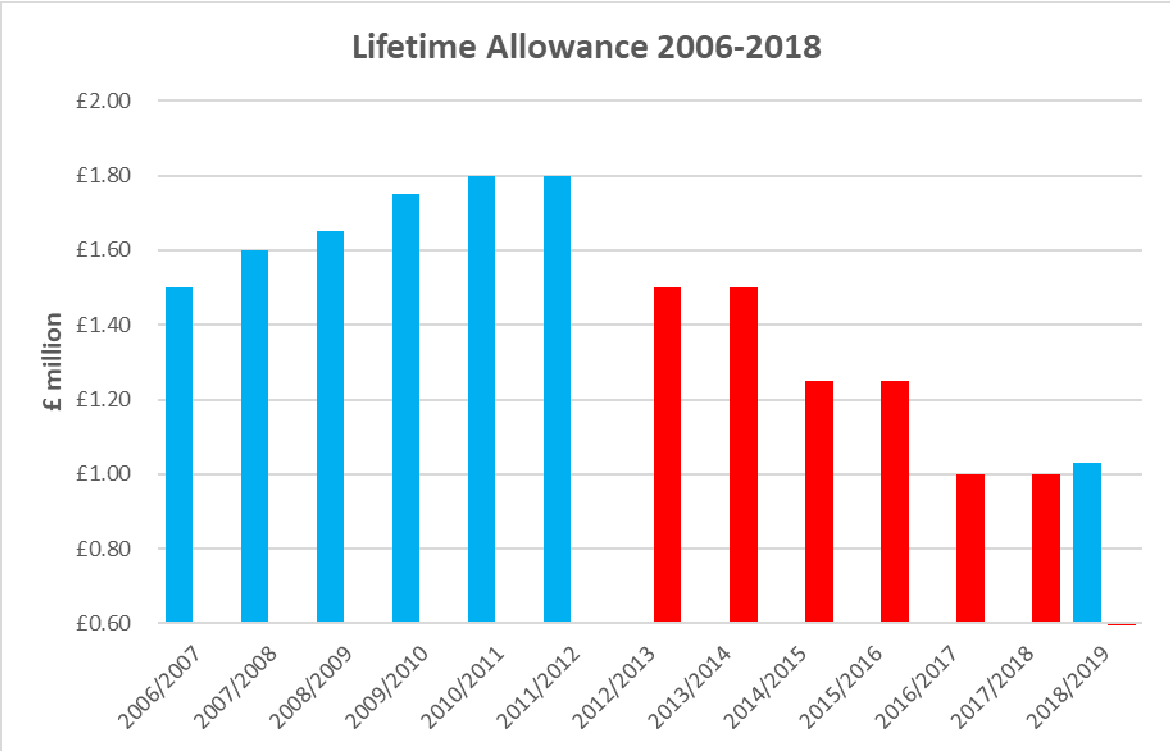
Once the 5 April is passed, many employers and employees will see their pension contributions rise because of increases to the automatic enrolment contribution rates scheduled long ago. The table below shows the changes and an example of the increased outlay based on an employee earning £26,000 a year

	Employer		Employee	
	2017/18	**2018/19**	**2017/18**	**2018/19**
Contribution rate (1)	1%	2%	1%	3%
On weekly earnings between (£):	157 - 866	162 - 892	157 - 866	162 – 892
Extra weekly outlay (2)	**£3.33 (+97%)**		**£5.37 (+196%)**	

(1) Usually no contributions are automatically required for employees whose earnings do not exceed £10,000 a year.
(2) Employee figure allows for tax relief at 20%. The employer will normally be able to offset contributions against profits for tax purposes.

For many employees, the increase in their auto-enrolment pension contributions will more than outweigh the savings from the tax year changes to the personal allowance and NIC bands (worth in total about £1.95 a week if you are a basic rate taxpayer), meaning net pay will drop in April by the equivalent of £3.42 a week. If you pay tax at the higher rate, the net extra outlay will typically equate to about £19 a month, as the increase in the upper limit for full rate (12%) NICs means an extra £1,350 of earnings on which you will have to pay higher NICs *and* auto-enrolment pension contributions.

An increase to the lifetime allowance



The lifetime allowance sets your maximum possible tax-efficient total pension value and is currently £1.0m, unless you benefit from one (or more) of the various transitional protections which have been offered over the years. The standard lifetime allowance has been on a downward trend since 2012/13, as the red bars on the graph show. However, in 2018/19 it will rise for the first time since 2010. The increase is an inflation-linked 3%, taking the allowance up to £1.03m – just about visible in the final blue bar.

If you are planning to draw on your pension benefits in the very near term, it may pay you to wait until after 5 April, so you can take advantage of the potential tax saving offered by the marginally higher lifetime allowance.

Looking longer term, in theory the lifetime allowance should now increase annually in line with inflation, as measured by the Consumer Prices Index (CPI) – assuming the Chancellor does not have other ideas. A CPI-linked increase remains a constraint on contributions if investment growth is strong, a reminder that your pension arrangements will always need careful monitoring.

VENTURE CAPITAL TRUSTS (VCTs) AND ENTERPRISE INVESTMENT SCHEMES (EISs)

In the run up to the Autumn Budget 2017, many VCT and EIS promoters sought to raise fresh funds. The managers had rightly anticipated that the Autumn Budget would include changes in the wake of a Summer 2017 consultation paper on patient capital.

In the event the Chancellor's revisions were not as radical as some had feared, but they do mean the risk profile of these schemes will increase. For example, the minimum proportion of a VCT that must be held in "qualifying investments" will rise from 70% to 80% from 6 April 2019 and new loans from VCTs to companies will have to be unsecured from the date the Finance Act 2018 receives Royal Assent. On the other hand, the maximum investment for EISs will double to £2m in 2018/19, provided at least £1m is invested in "knowledge-intensive" companies.

Given the restrictions on pension contributions described above, VCTs and EISs will continue to play an important role in tax planning, particularly at the year end. As a brief reminder, the tax benefits of VCTs and EIS are:

Feature	VCT	EIS
Income tax credit on initial investment	30% on investments up to £200,000 per tax year	30% on investments up to £1,000,000 per tax year*
Backdating of investment	None	1 year, up to 100%
Minimum holding period to avoid tax relief clawback	5 years	3 years
Dividends	Tax-free and often paid from capital gains, not income	Taxable (but profits usually retained, not distributed)
CGT reinvestment relief	None	Gains may be reinvested in an EIS up to three years after realisation or one year before. No limit.
Capital gains on proceeds	Nil	Nil (except for reinvested gain)
IHT business assets relief	None	Usually available after two years' ownership

* Rising to £2,000,000 from 2018/19, provided at least £1,000,000 is invested in "knowledge-intensive" companies.

VCTs and EIS must be regarded as high risk investments, given their focus on small and relatively new unlisted companies. They should represent only a small part of a well-diversified investment portfolio. The level of investment risk is the primary reason that the government offers such generous tax reliefs, a point underlined by last November's Budget revisions.

CAPITAL GAINS TAX

2017 was a good year for the world's stock markets. The MSCI World Index rose by over 20%, although the UK stock market was not such a strong performer, partly down to Brexit-related issues.

Regular use of your CGT annual exemption (£11,300 rising to £11,700 in 2018/19) is one way to avoid the situation where gains built up over a period of years lead to a tax bill for rebalancing your portfolio or extracting some funds. The 2017/18 annual exemption could save you £2,260 in tax if you pay income tax at more than basic rate and the gains do not relate to residential property (where the saving would be a maximum of £3,164.)

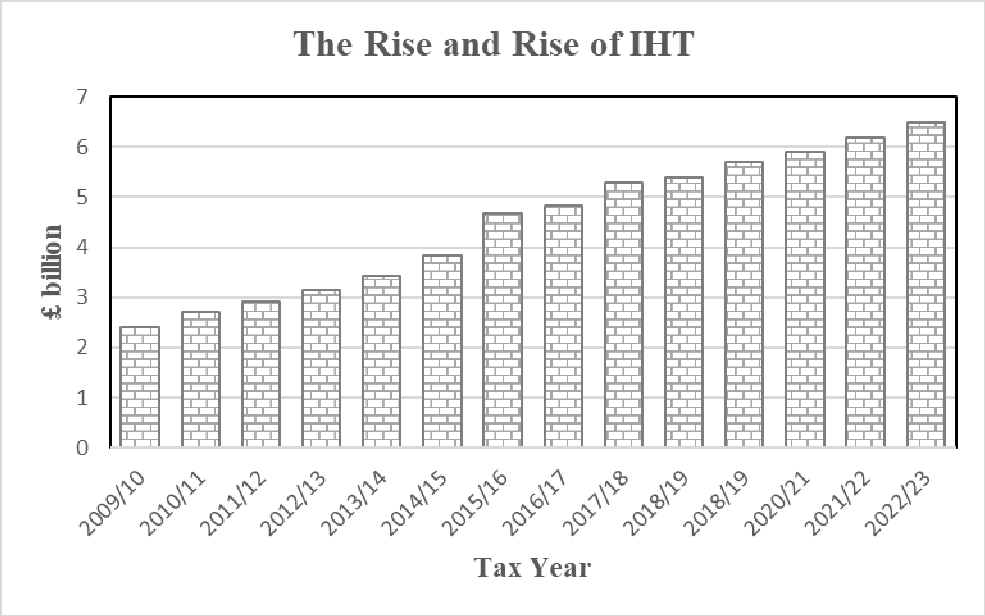
If you cannot sidestep a liability to capital gains tax, watch the timing of your gains:

- A gain realised on Thursday 5 April 2018 will mean tax payable on 31 January 2019.
- A gain realised on Monday 9 April 2018 will move the tax payment date to 31 January 2020.

One point to watch on residential property gains, eg from buy-to-let sales, is that from 6 April 2019, CGT is currently scheduled to be payable within 30 days of sale, so a further sale deferral until 6 April 2019 would *accelerate* tax payment.

When you realise any losses, the timing can be as important as when gains are crystallised. This is an easy fact to overlook when there is no tax payable. Tax law says that your losses are firstly set against gains made in the same tax year *before* the annual exemption is applied. You should therefore avoid making losses in the same tax year as the one in which you realise gains, unless your total gains exceed the annual exempt amount.

INHERITANCE TAX



Sources: HMRC, OBR

As the above graph shows, inheritance tax (IHT) receipts have been growing rapidly in recent years. This tax year's IHT payments are projected to be nearly double those of 2010/11. Despite the introduction of the residence nil rate band in 2017/18, the Office for Budget Responsibility (OBR) says future years will see more increases. One reason for that is that the nil rate band has been frozen at £325,000 since April 2009 and is not due to increase until April 2021.

Taking a yearly view

As part of your year end planning, there are three main yearly exemptions which you should consider using by 5 April:

1. *The Annual Exemption* Each tax year you can give away £3,000 free of IHT. If you do not use all of the exemption in one year, you can carry forward the unused element, but only to the following tax year, when it can only be used *after* that year's exemption has been exhausted.

   For instance, if you did not use the annual exemption in the last tax year, 2016/17, you can still use it by 5 April 2018, but only once you have fully used the 2017/18 exemption. Thus a gift of up to £6,000 (£12,000 for a couple) can escape IHT.

2. *The Small Gifts Exemption* You can give up to £250 outright per tax year free of IHT to as many people as you wish, so long as they do not receive any part of the £3,000 exemption. The more grandchildren, nieces and nephews you have, the more useful is this exemption.

3. *The Normal Expenditure Exemption* The normal expenditure exemption is potentially the most valuable of the yearly IHT exemptions. Any gift is exempt from IHT provided that you make it regularly, it is made out of income (including ISA income, but *not* from any capital) and its does not reduce your standard of living. No cash limits apply to this exemption. You can gift dividend or other investment income which would otherwise usually be reinvested, with the normal expenditure exemption covering the gift.

A point to note is that if you make a gift by cheque, what matters for tax year timing purposes is the clearing date. With the final week of the tax year including Easter Monday, you should aim to make your yearly gifts in March.

One good discipline for the annual and small gifts exemption is to use them at the start of every tax year – that way they do not get forgotten or overtaken by events. The start of this new tax year will mark a £25,000 increase in the residence nil rate band (RNRB) to £125,000. If you have not already reviewed your IHT planning and Wills in the light of the RNRB, which was introduced last April, now is the time to do so. One surprising side effect of the RNRB is that it may now make sense not to pass everything to a surviving spouse or civil partner on first death.

ACTION

The end of the tax year is coming ever nearer, as is the Spring Statement (on 13 March), which might produce the odd unwelcome surprise. With Easter straddled between March and April, the time to start your year end/year beginning planning is now.

Call us today to arrange for a comprehensive tax planning review. The sooner you contact us, the sooner we can begin work on your strategy and decide on actions for this tax year and the early part of next tax year.