Technical Connection

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NO EMERGENCY BUDGET

The Chancellor, Philip Hammond, has clearly stated that there will be no post-referendum “emergency Budget”. Instead, as further evidence of his (and the new Prime Minister’s) commitment to restoring calm, he has said that the government will be following the normal Autumn Statement and Spring Budget process.

Early indications are that this may see a move away from an austerity-based fiscal programme. Self-evidently, developments between now and the Autumn Statement will have a very strong influence on the direction that will be taken.

By all accounts, though, the new Chancellor will be more “inclusive” and less prone to “rabbit out of a hat” policies and initiatives.

We shall see….

INCREASE IN THE NUMBER OF ESTATES SUBJECT TO IHT

House prices boost inheritance tax (IHT) receipts (especially in London and the south east). Estates in London and the south east contributed almost half of the country’s inheritance tax receipts in 2013/14 because of rising house prices, which means an increasing number of people are being hit by (and potentially interested in planning for) IHT- especially in those parts of the country.

According to HMRC, the data shows that London and the south east contributed 49 per cent of IHT collected during the year to 5 April 2014.

Official forecasts also suggest the proportion of estates liable for IHT will reach 8.3% of all estates in 2014/15. This is the first time since 1976 that the proportion of estates subject to IHT has risen above 8%.

Properties, household savings and stocks, bonds and other financial securities make up the bulk of assets on which inheritance tax is levied. Among all estates that paid inheritance tax in 2013/14, 36% of assets were held in UK housing and 30% in securities.

The £4.8bn that the government is set to raise from IHT in 2016/17 is, however, a tiny fraction of forecast total tax receipts of £716.5bn, according to Office for Budget Responsibility forecasts.

COMMENT

The amount of IHT, as a proportion of the overall yield from all taxes, is very low. IHT does, however, generate a strong emotional response from those whose families may have to pay it. People see it as a form of "double taxation" to the extent that it represents tax on assets that are or were acquired by income that suffered income tax. Whenever there is a strong emotional resistance to a tax the motivation to "do something about it" will be higher.

Making individuals aware of what IHT can do to the family's net wealth and then explaining what can be done about it is a key part of the financial planner's role with those of their clients for whom IHT could be an issue. While, at 8.3%, the proportion of estates subject to IHT appears relatively low, the proportion of clients of advisers whose estates are likely to be subject to IHT will be greater.

Those who have estates where residential property is the main driver of the liability may well be interested in protection policies in trust to meet the liability if they want to avoid the sale of the house or arranging loan to pay tax. This is because effective planning to reduce the liability using residential property is in fairly short supply given the relative effectiveness of the gift with reservation and pre-owned assets tax provisions. To the extent that the liability is generated by cash and investments, the options for planning increase.

Tried and tested strategies founded on trusts, such as loan schemes and discounted gift arrangements, can deliver IHT reduction with continuing access and control for the settlor.

Especially given that it seems likely that both of these scheme types will remain outside of the (soon to be extended) Disclosure of Tax Avoidance Schemes (DOTAS) provisions this makes them potentially very attractive to many clients of advisers who are concerned about IHT but cautious about outright gifting – or even simply gifting into trust.

AUTOMATIC ENROLMENT: HOW AND WHEN TO USE POSTPONEMENT

Research by The Pensions Regulator (TPR) has shown that there is now almost universal understanding among business advisers of the tasks that need to be carried out for employers to comply with their automatic enrolment duties. However, an area which continues to prompt questions from advisers is postponement – a useful tool for employers, especially those who employ temporary or seasonal workers.

Key points

- An employer can temporarily postpone the assessment of workers for automatic enrolment purposes for up to three months.

- Postponement can be used for all of the employer's staff or just some of them.

- If an employer postpones from their staging date, the staging date does not change.

- If an employer chooses to postpone from their staging date, they still have duties (e.g. they must write to tell the staff who will be postponed, within six weeks of their staging date).

- The declaration of compliance date does not change; this remains as 5 months after their staging date.

- Postponement cannot be used with re-enrolment. If the staff meet the criteria to be enrolled on the re-enrolment date, then re-enrolment must take effect from that date.

Why would an employer use postponement?

- One of the main reasons your clients might decide to postpone the assessment of their workers is if they have temporary or short-term staff who they know will stop working for them within three months. For example, seasonal fruit pickers.

- Using postponement can also be helpful when assessing those members of staff whose earnings would usually fall below the automatic enrolment earnings threshold, but where an increase, such as a bonus, might temporarily take their earnings over the trigger level.

- If your clients apply a probationary period to new starters, then it can be helpful to use postponement to delay assessing these individuals until after their probationary period has elapsed (assuming it is not longer than three months).

- Your clients might also choose to use postponement in order to align automatic enrolment with their other business processes. For example, if a client's staging date falls in the middle of a pay period, it may be helpful to postpone to the beginning of the next pay period.

When can postponement be used?

Your client can postpone automatic enrolment from:

- their staging date; or

- a staff member's first day of employment; or

- the date a staff member first becomes eligible for automatic enrolment.

If your client postpones from their staging date, it doesn't change their staging date. Your client can postpone for up to three months. They can postpone as many or as few staff as they like and the postponement period doesn't have to be the same length for everyone.

Note that staff can choose to opt in to your client's pension scheme during the postponement period. More information on what to do if this happens can be found on TPR's website.

What action to take?

An employer can postpone an individual, some, or all of their staff. If they do, they must write to those members of staff within six weeks of the date that postponement starts, to tell them:

- that their assessment has been postponed;
- the end of postponement date; and
- that they have the right to opt in or join a pension scheme at any time.

There's no need to tell TPR that a client has decided to use postponement. And remember – the declaration of compliance date will not change.

What happens at the end of the postponement period?

On the last day of the postponement period, your client will need to know whether each staff member, whose assessment they've postponed, is eligible to be automatically enrolled – if they still work for them. If they are eligible to enrol, your client must put them into a pension straight away - your client cannot postpone again. This is true even if your client postponed for less than the three months allowed.

However, if any members of staff are not eligible, then they will need to be monitored every pay cycle from then on to see if they become eligible in the future. If they do become eligible, your client could then apply postponement again in respect of them.

The most common postponement questions

Can postponement be used more than once?

Yes, but only for staff who are assessed as not eligible to be automatically enrolled on the last day of the postponement period. Where a member of staff is eligible to be enrolled, your client cannot postpone again and your client must put them in a pension scheme (as explained above).

If a member of staff asks to join a pension scheme during the postponement period, when does the employer start paying money into the pension?

If any member of staff writes asking to join a pension scheme, you need to assess what they have earned and how old they are in the pay period during which you receive the notice that they want to join.

GUIDANCE ISSUED ON CHANGES TO TAX RELIEF FOR RESIDENTIAL LANDLORDS

HMRC has issued guidance on the changes to tax relief for residential landlords which are to be phased in from April 2017. The changes will restrict relief for finance costs to the basic rate of income tax.

Despite calls on the Chancellor to review the government’s approach to taxing the buy-to-let sector, HMRC has released guidance that sets out how the new rules restricting tax relief for residential landlords will operate in practice.

Under the new rules – which were announced at Summer Budget 2015 - from April 2017 finance costs (such as interest on mortgages or loans taken out to furnish the property) will no longer be taken into account to work out taxable property profits. Instead, once the income tax on property profits and any other income sources has been assessed, a landlord’s income tax liability will be reduced by a basic rate ‘tax reduction’.

The rules apply to UK resident individuals that let out residential properties – whether in the UK or overseas – as well as to non-UK resident individuals who let out UK-sited residential property. ‘Individuals’ for these purposes include individuals who let such properties in partnership as well as trustees or beneficiaries of trusts liable for income tax on residential property profits. The rules do not apply to lettings of commercial properties; or to companies or landlords of furnished holiday lettings.

The restriction will be phased in gradually from 6 April 2017 – at the rate of 25% a year - and will be fully in place from 6 April 2020.

To sit alongside the new guidance, HMRC has also published a series of case studies which demonstrate the potential impact of the changes on individual landlords in a range of specific scenarios.

COMMENT

All individual landlords of residential property will need to consider their position. Existing higher/additional rate taxpaying buy-to-let investors with mortgage interest will be the most affected. However, the changes could also move some basic rate taxpaying landlords into higher rate tax and/or affect entitlement to allowances, such as child benefit, personal allowances, annual allowances for pension plans and whether chargeable event gains suffer higher rate tax or not.

VALUING PENSION BENEFITS FOR IP14 AND/OR IP16

HMRC has recently published a timely reminder as to how to value different forms of pension benefit for the purposes of electing for Individual Protection 14 and/or 16.

What follows explains, in a relatively straightforward manner, the calculations for:

- **Amount A:** Pre-commencement pensions
    - 25 times the current income if there have been no post A-Day BCEs; or
    - The adjusted value at the date of the first post A-Day BCE
- **Amount B:** Pensions crystallised from A-Day up to 5 April 2014 or 5 April 2016 as appropriate
    - The value based upon the percentage of the lifetime allowance at the time of the original BCEs adjusted to reflect the change in the lifetime allowance since then.
- **Amount C:** Uncrystallised pension benefits
    - The value of any uncrystallised pension funds, (insurance contracts should be valued in accordance with the agreed ABI protocol), plus
    - 20 times the value of any accrued DB rights and, where the pension cash lump sum (PCLS) isn't by commutation, add the value of any accrued PCLS, plus
    - The capital value of any cash balance arrangements.
- **Amount D:** Contributions made to a relieved non-UK pension scheme in respect of a relieved member
    - The total value of any UK tax-relieved contributions paid since A-Day.

COMMENT

Remember, the deadline for electing for Individual Protection (IP) 2014 is 5 April 2017. Therefore, it is still not too late to make such an election. Consideration should be given to making such an election for any client who had a pension valued as at 5 April 2014 in excess of £1.25m even if they already have an election for enhanced protection or fixed protection 2012 or 2014. As all of these protections can be lost then having a protective election for IP14 may prove beneficial for some clients who inadvertently lose their other protection.

A VARIATION OF TRUST CASE RECOGNISES THE RIGHTS OF SAME-SEX PARTNERS

A landed family, the Pembertons, has successfully varied an outdated trust to give any future same-sex partners of descendants the same rights as heterosexual spouses

In what is believed to be the first case of its kind, the High Court has approved a variation of a 51-year old trust to allow same-sex spouses and civil partners to acquire the same inheritance rights over property that are afforded to opposite-sex spouses of descendants of the settlor under the terms of the trust.

The terms of the trust in question, as originally drafted, were "much in the style of a 19th century dynastic family settlement" which did not include civil partners (naturally) or spouses under same-sex marriages. The Pembertons, who have lived in Trumpington Hall, Cambridgeshire, for three centuries, said they felt they had “a moral obligation" to future generations to modify the inheritance arrangements over their ancestral seat.

The variation, which ensures that future same-sex spouses and civil partners will have a life interest in Trumpington Hall following the death of their spouse, was approved on the basis that it would, in the words of the Judge, “be for the benefit of the family as a whole and therefore of benefit to each individual member”.

It is believed that the Pembertons are the first landed gentry to alter the definition of a ‘spouse’ in a pre-existing trust to ensure that it recognises same-sex marriages and civil partnerships.

The trust's lifespan was also increased for another 125 years, to 2141, and additional investment powers were conferred on the trustees.

COMMENT

The case highlights the progressive attitude of the Courts towards outdated family settlements that have not kept pace with changes to the law.

IS HMRC ATTACKING IN SPECIE PENSION CONTRIBUTIONS?

Over the last few weeks, there have been ongoing technical discussions between members of AMPS (the Association of Member Directed Pension Schemes; the trade body for SIPP and SSAS administrators) about in specie contributions. There appears to be growing evidence that HMRC is attacking SIPP/SSAS members over in specie contributions that have been made and withholding tax relief-at-source claims by scheme administrators. As might be expected this is starting to cause concern amongst scheme administrators.

We understand that law firm Pinsent Masons is intending to host a roundtable discussion, at which AMPS will be represented, to assess whether there is any appetite for a coordinated response to HMRC’s apparent change in how it is willing to deal with in specie contributions.

The topics that are likely to be covered are:

- The issues – contribution agreements, creating a debt, settling a debt.
- Possible alternatives to be presented to HMRC for discussion.
- AMPS steps so far with HMRC.
- Gathering samples of contribution agreements. Which ones are being challenged and which are not?
- Status of information notices. Ignore at your peril. How to respond.

- Running a test case, including: merits of remedy either to Tax Tribunal on availability of the relief or a judicial review on the decision to withhold relief; selection of test case; funding; and management of HMRC including information flow.

- Appetite for an action group

PERSONAL PORTFOLIO BOND CONSULTATION

Consultation on the permitted investments which can be held in a personal portfolio bond

At the 2016 Budget it was announced that the government would review the categories of permitted investments which could be held in a policy of life insurance, life annuity or capital redemption policy without it becoming taxable as a personal portfolio bond (PPB).

HMRC has now launched a consultation which invites views on the current property categories and further property types which may be held within a PPB.

Broadly, there are three types of investment vehicle which are being considered to be included within the permitted category list. These are:

- real estate investment trusts (both UK and foreign equivalents);

- overseas equivalents of UK approved investment trusts; and

- UK authorised contractual schemes.

The government is keen to hear from interested parties, especially policyholders and their representatives, members and representatives of the life assurance and funds industries and life policy administrators for whom these changes may have a material impact.

The consultation closes on 3 October 2016 and draft legislation is expected in advance of Finance Bill 2017.

INCOME WITHDRAWAL RATE FOR AUGUST 2016

The appropriate gilt yield, used to determine the 'relevant annuity rate' from HMRC's tables for an adult member commencing income withdrawals (or reaching an income withdrawal review date), in August 2016 is 2.0%.