Technical Connection

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THOUSANDS OF ISA INVESTORS ARE HIT BY DECLARATION ERROR

The annual ISA subscription limit applies across the different types of ISA and it is essential that this limit is not breached.

When opening an ISA, investors are required to sign a declaration which states they have not subscribed more than the annual ISA allowance for the tax year in which they are making the subscription.

However, it has recently been reported that many investors have incorrectly signed the declaration for the Help to Buy ISA which has resulted in many providers having to write to investors who have breached this limit by failing to account for their full ISA range.

There are now 5 types of ISA available:

- Cash ISA
- Stocks and shares ISA
- Innovative finance ISA
- Help to Buy ISA
- Lifetime ISA

It is possible to put money into one of each kind of ISA each tax year provided the annual subscription limit is not breached - currently £20,000 for the 2017/18 tax year.

COMMENT

It is essential for those clients who wish to save in ISAs to keep a record of their contributions to

ISAs to ensure that they do not oversubscribe – this responsibility lies with the client because it is possible to open one of each kind of ISA with different providers.

THE TAX TREATMENT OF TERMINATION PAYMENTS

With effect from 6 April 2018 the rules on the tax treatment of termination payments are to be tightened, in particular the £30,000 exemption, which will apply to National Insurance contributions as well as to income tax. In addition, the unlimited relief for foreign service will be removed from 6 April 2018, although it will be retained for seafarers.

In light of this, the House of Commons Library has published a briefing paper, 'Taxation of termination payments', which explains the background to the legislative reform amending the tax treatment of termination payments included in Clause 5 of the Finance (No. 2) Bill 2017.

The paper covers the background to the Office of Tax Simplification review in 2013/14, the consultation on simplifying the tax treatment of termination payments and includes the legal background as an Appendix.

THE TRIPLE LOCK

On Tuesday 18th October the September CPI annual increase was revealed to be 3.0%. The following day average weekly earnings figures emerged from National Statistics putting the annual growth at 2.2% including bonuses and 2.1% excluding bonuses. The "Triple Lock" for increases to the basic and new state pension is the greater of CPI inflation, earnings growth and 2.5%.

CPI is thus the winner. As CPI increases apply anyway to state pensions other the basic state and new state pension, the net result is that all state pensions should rise by 3.0% from April. Give or take some rounding that means the new state pension (ie single tier) will rise from £159.55 a week to £164.35 and the old basic state pension (for those who reached their SPA before 6 April 2016) will rise from £122.30 a week to £126.00.

In its 2017 manifesto the Conservatives said that they would "maintain the Triple Lock until 2020, and when it expires … introduce a new Double Lock, meaning that pensions will rise in line with the earnings that pay for them, or in line with inflation – whichever is highest." The 2020 date reflects the previous 2015 manifesto pledge to maintain the Lock until what was expected to be the end date of that parliament. The validity of the 2020 break point is now uncertain given that the DUP, which provides the Conservatives with their working majority, said no change to the Triple Lock in their manifesto.

Although the Triple Lock appears to have cost nothing this time around, it is still having an indirect cost from those years when the 2.5% floor kicked in (2013 and 2017). In the long term, there is a growing consensus that the Triple Lock must be replaced by a less expensive increase mechanism. The only obstacle in the way is politics, although even that is starting to tilt with questions of intergenerational fairness coming to the fore.

The issue of young versus old is underlined by the forthcoming pension increases because most working age social security benefits are in the midst of a five-year freeze, and will not rise until 2020. When George Osborne announced that freeze in July 2015, inflation was virtually non-existent, so the measure looked much less punitive than it does now.

To add one further intergenerational twist to the picture, the 3% CPI implies a 3% rise in the standard lifetime allowance from April 2018 to £1.03m.

COMMENT

The failure of pay to keep pace with inflation remains one of the long-term effects of the great recession which continues to puzzle economists. Between April 2009 and April 2017, average weekly earnings increased by 15.3% and the CPI by 19.7%. The basic state pension, helped by the Triple Lock starting in 2011, added 28.4%.

AUTUMN BUDGET 2017 – A LITTLE CRYSTAL BALL GAZING

The Autumn Budget is now a couple of weeks away and so far there have been few rumours about it contents. There are several reasons for this:

- We are at the start of the new Budget cycle and there has been no Spring Statement - as there will be from 2018 onwards - to provide any clues.

- The backwash from Spring 2017’s fiscal announcement - the March 2017 Budget - is still lapping around parliament in the form of Finance Bill 2017/19. This reached Committee stage in the House of Commons on 11 October.

- The news recently released from the Office for Budget Responsibility (OBR) that it ‘is likely to revise down potential productivity growth in its November forecast, weakening the outlook for the public finances’ may have been holding up decisions. To put not too fine a point on it, the money isn’t there for giveaways.

- The political landscape for Mr Hammond is some way short of perfect. His March Budget was blown off course by a backbench rebellion over increasing Class 4 NICs. Back then the Conservatives had a parliamentary majority in their own right. Now the Government’s majority depends upon a confidence and supply agreement with the DUP, and there are plenty of Conservative backbenchers unhappy with the Chancellor’s Brexit stance. Ordinarily, the first post-election Budget would be the occasion to push through unpopular (tax-raising or controversial) measures, but these are not ordinary times.

With all that in mind, here are a few thoughts on areas of interest:

Pensions

The latest set of HMRC data showing the high cost of pension tax relief was enough to set the weekend personal finance columnists writing about a threat to higher rate contribution relief. In the political circumstances - remember Class 4 NICs - this looks very unlikely. David Gauke, who moved from the Treasury to the DWP after the election, told a conference in July that we “wouldn’t see any fundamental changes in the near future”. “Fundamental” does not preclude some technical tweaks which raise revenue without ruffling too many feathers – for example, a reduction in the annual allowance to £30,000.

One potential piece of good news is that the lifetime allowance is due to rise in line with CPI from 6 April 2018 (to about £1.03m) – unless Mr Hammond decides otherwise.

VCT, EIS and SEIS

The writing has been on the wall for venture capital schemes since the publication of the Treasury's paper on patient capital in August. Despite the overhaul to investment rules that took effect just under two years ago, another revamp now looks likely. The target will be schemes aimed at "capital preservation" rather than high risk growth - the classic example being pub-based EISs. One VCT has already pulled a share issue in expectation of such action.

There is a flood of VCTs and EISs on the market at present: by tax year end it may be only a trickle.

Capital gains tax

George Osborne's decision to cut CGT to a maximum of 20% (other than for carried interest and residential property) came as a complete surprise in his last (2016) Budget. Nobody had been lobbying for it, the result was a wider gap between income and capital taxation and it only benefited those few people (about 250,000 in 2013/14) with taxable capital gains exceeding their annual exemption. Mr Hammond could choose to revert to the old rates and win a few plaudits from the JAMs (just-about-managing), plus about £0.5bn a year.

SME tax

At present corporation tax is due to fall to 17% in April 2020. It is possible that Mr Hammond could kick this reduction down the road - or abandon it completely - in response to gloomier OBR numbers and to spike (partially) Labour's guns (their manifesto pledge was a 26% rate).

Lurking in the background is the Taylor Review of modern working practices, which is probably lodged on a dusty shelf after Mr Hammond's failure to push through Class 4 NIC changes. Equally problematical for the Chancellor would be any attempt to extend what amounts to presumed employment rules for contractors, which were introduced in the public sector in April 2017.

Income tax

The Chancellor still has unfinished business here in terms of the promise (repeated in this year's manifesto) to bring the personal allowance up to £12,500 and the higher rate threshold to £50,000 by 2020/21. That implies increases of £1,000 and £5,000 respectively over the next three years. Given the current inflationary outlook, the increased personal allowance will probably be covered by normal CPI indexation, but the lifting of the higher rate threshold will require a more concerted effort.

Politics and the tight financial backdrop suggest Hammond will just stick with something close to CPI indexation for both in 2018/19 – say an £11,900 personal allowance and a £46,500 threshold (implying a £34,600 basic rate band).

Fiscal drag will be left to do its silent worst on the fixed thresholds for the high income child benefit tax charge (unchanged since January 2013), phasing out of the personal allowance and the additional rate (both of which are unchanged since their introduction in 2010/11).

Investment taxation

The dividend allowance cut to £2,000 from 2018/19 is already in the Finance Bill 2017/19, but a further cut – to zero – is possible for the following year or 2020/21. The latter timing could be justified if the corporation tax cut to 17% is not altered, as it could be argued to be a necessary counter to further incorporation. Other investment tax changes look unlikely, if only because of those restive backbenchers.

ISAs

The increase in ISA contribution limits to £20,000 only took effect in April, so any change beyond a CPI-linked increase looks unlikely. It will be interesting to see whether LISA attracts any attention – this Osborne inheritance has not had a particularly bright start to life.

Inheritance tax

Intergenerational equity is one of the flavours of the month at present. The Chancellor could use that as a starting point to initiate a review of capital taxes – IHT and CGT – which the Office for Tax Simplification called for long ago. This could examine something closer to a genuine inheritance tax, where the liability is based on the recipient rather than the donor. Such a structure encourages a greater spread of wealth.

In line with the likely moves against capital-preserving venture capital schemes, it is possible the Chancellor will tighten up the rules on business property relief for shareholdings in unlisted companies. This relief is looking increasingly anomalous when it extends to companies created and marketed solely for IHT mitigation purposes or to large AIM companies such as ASOS (with a market capitalisation of nearly £5bn).

Stamp duty land tax

SDLT is bringing in around £1.25bn a month to the Exchequer at present, 60% more than in 2013/14. Despite moans from estate agents about the stagnation of the £1m+ market, it is very hard to imagine Mr Hammond making any relaxation of rates or thresholds in the top bands. The politics of such a move would be highly dangerous. However, he might make a gesture by raising the lower threshold – currently £125,000 and even lower than the £150,000 proposed by the Welsh government – but do not expect much of anything else.

THE PENSIONS DASHBOARD – AN UPDATE

The general election in June 2017 created a break in the Government engagement with the pension dashboard concept. To retain momentum, the Pension Dashboard Prototype Project’s industry contributors agreed to a further project without Government involvement, focusing on four workstreams: consumer research, industry research and further work on data standards and service requirements. The findings have been published by the ABI in the document ‘Reconnecting people with their pensions’.

Each workstream was led by an industry chair and engaged closely with a wide range of stakeholders.

The Consumer Workstream held workshops with consumer organisations and industry associations, commissioned qualitative consumer research (jointly with the Money Advice Service (MAS)), and held interviews with representatives from countries who have implemented similar services.

The Industry Research Workstream conducted over forty interviews with senior stakeholders from across the industry.

The Data Standards Workstream worked with industry and regulators on refining the data standards and guidelines, as well as on a review of data quality across the industry.

The Service Requirements Workstream developed the requirements for live services.
Following this the Project has made 10 key recommendations:

1. All pension providers and schemes must make data available to consumers via regulated third parties, including occupational, personal and public service pension schemes. This compulsion requires a legislative change and a completion date stated by Government.

2. The DWP must make data about the state pension available alongside private pension information from day one.

3. A non-commercial service, endorsed by the Government, must be made available.

4. To enable innovation, the Government must enable an "open pensions" infrastructure that allows consumers to access their data via regulated third parties.

5. Dashboards and any other third party services showing consumers their data must be regulated to ensure consistency. Consumer protection requires legislation to establish one or more new regulated activities, which are most likely to be overseen by the FCA.

6. There must be an implementation plan and timetable, endorsed by Government and industry, including an approach to funding implementation and a major programme of communications.

7. An implementation entity must be charged with delivering the service and its governance. This will include establishing a governance body which oversees the network, establishes and manages data standards, data security and data sharing agreements, and which is sustainably funded.

8. Data must be made available in a standardised digitally consumable format. This needs agreed standards, which are being delivered by industry, but which must be mandated by Government and regulators.

9. An infrastructure must be set up to link schemes to dashboard providers so that consumers can find their pensions. This requires the Government's backing.

10. An identity assurance scheme must be agreed. This requires a policy decision about the use of Verify in this context.

DWP PUBLISHES RESULTS OF PENSION CHARGES SURVEY 2016

The DWP have published the full results and a summary document of the Pension Charges Survey 2016, which investigates the charges on occupational defined contribution pension schemes following the introduction of the charge cap of 0.75%.

The key findings are as follows:

- The charge cap had lowered charges in qualifying schemes to the level of the cap or below: as many as 98 per cent of members of qualifying contract-based schemes and 99 per cent of members of qualifying trust-based schemes now paid a maximum of 0.75 per cent.

- Among qualifying scheme members, the members of the smallest schemes, which previously charged higher than the cap, benefited the most. For example, ongoing charges for qualifying contract-based schemes with 12 or fewer members fell by 0.2 percentage points on average.

- Non-qualifying schemes, whose charges are not subject to the cap and were already typically higher than it, had not generally brought down their charges in response. In non-qualifying contract-based schemes just 21 per cent of members paid charges within the cap; and in non-qualifying trust-based schemes 50 per cent of members paid charges within the cap – both showing little change since 2015.

- Charges for unbundled trust-based schemes, measured for the first time in the 2016 survey, were typically comparable to their equivalent bundled trust-based schemes, although a relatively small number of closed, non-qualifying schemes charged markedly higher than the average.

- ‘Legacy’ charges that were banned under the charges measures (i.e. Active Member Discounts (AMDs), consultancy charges and member-borne commission) had been eliminated from qualifying schemes, and remained extremely rare even among non-qualifying schemes.

- There was virtually no improvement in providers’ abilities to report on transaction costs compared to 2015, with many providers, unbundled scheme trustees and their fund managers awaiting further guidance from the Government.

COMMENT

It is clear that the charge cap is working and those who were in high charging smaller schemes have benefited the most. It is a shame that those schemes not currently impacted by the cap haven’t reduced their charges in line with other schemes but there may well be good reasons for this.

HMRC TRUST REGISTRATION SERVICE - FAQs

The trust registration service (TRS) has been available for trustees since July but it is still not available for agents, although promised for October.

In the meantime HMRC has issued some guidance in the form of frequently asked questions which cover things like:
Who needs to register?
When is the UK tax liability triggered?
What are the reporting duties?
Details of the settlors, trustees and beneficiaries?
Details of the assets?
And so on…

STATE PENSION LUMP SUM AND INVESTMENT IN AN EIS

We were recently asked the following question: "Can the income tax payable on a deferred State pension lump sum be relieved by a subscription to an Enterprise Investment Scheme (EIS)?"

This is not an area we had previously explored and the results of our research are as follows:

EIS income tax relief takes the form of a reduction in an individual's income tax liability. The amount of the reduction is currently equal to tax at 30% on the amount of the subscription. However, the amount of the tax relief on a subscription to an EIS cannot exceed the amount of tax that would otherwise be paid without any EIS subscription.

Sections 22-32 of ITA 2007 set down the rules on how an income tax liability is calculated and include the rules for how tax reliefs can reduce the liability.

First total income is calculated – this is the income on which an individual is charged to tax. Then personal allowances and other reliefs (such as loss relief) are deducted. The tax liability is then calculated on this amount. EIS relief is then used to reduce the tax liability. However, this cannot result in a repayment of tax.

Although a deferred State pension lump sum is treated as income and taxed as such **it is not to be taken into account in determining the total income of any person** – section 7 Finance (No.2) Act 2005.

In conclusion then, the amount of income tax due on a deferred State pension lump sum cannot be relieved by a subscription to an EIS.

INCOME WITHDRAWAL RATE FOR NOVEMBER 2017

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 November 2017 is 1.75%.