News – June 2015

Get ready for the second Budget of the year

Last month's unexpected election result has been followed by the more anticipated announcement of a second 2015 Budget. Quite what it will be about is unclear for now – the Treasury's press release gave little more than the date.

In terms of what was in the Conservative manifesto on tax, there are two measures that could be fleshed out next month that were not mentioned in the March Budget:

- More changes were proposed to the pension annual allowance, following the Budget statement that the lifetime allowance would be further reduced to £1 million from 2016/17. The manifesto suggested that for those with income of over £150,000, the allowance would be reduced by £1 for each £2 of excess income, subject to a minimum of £10,000 if income exceeds £210,000.

- The cut in the annual allowance was intended to fund a new main residence inheritance tax allowance of £175,000 transferable between spouses and civil partners on gifts to children or grandchildren. The allowance would be phased out for estates above £2m, again at the rate of £1 for each £2 excess. It would be much easier just to increase the nil rate band to £500,000. This may yet happen, as the manifesto proposals met with some criticism on various grounds, e.g. discouragement of trading down.

Either of these ideas could disrupt your existing financial planning, so do make sure you keep in contact with us for post-Budget news.

The value of tax reliefs depends on your individual circumstances. Tax law can change. The Financial Conduct Authority does not regulate tax advice.

Interest rate rise: now it's 2016

The latest Quarterly Inflation Report from the Bank of England suggests there will no base rate rise this year.

"Free beer tomorrow" is a sign that used to be spotted in some pubs before they were closed down or became eateries rather than drinking establishments. Of course, tomorrow was always one day away, so free beer was an illusion. It feels the same with increases to the Bank of England's (BoE) base rate, which has been stuck at 0.5% since March 2009.

"Interest rate rises next year" has become a variant on "free beer tomorrow", with learned predictions from pundits, experts and even the Bank of England's Governor, Mark Carney, proving to be mere shibboleths. In presenting the Bank's latest Quarterly Inflation Report, Mr Carney deliberately avoided making himself a hostage to fortune, saying that the Bank "… has long expected that these (economic) headwinds will likely merit not only a more gradual rate of increase in Bank Rate than in previous cycles, but also require levels of Bank Rate to remain below average historical levels for some time to come".

Look inside the Report itself and there is a graph showing how the money market (not the Bank) expects official interest rates to move over the next three years. At the same time, the BoE avoids confirming that the market's figures are built into the Bank's economic forecasts. As of May 2015 the market reading was that "…Bank Rate is expected to rise from early 2016, but to only 1.4% in three years' time".

That is a much slower pace of increase than in previous interest rate raising cycles, but it ties in with the Governor's remarks. It could also be wrong: as Mr Carney wryly remarked six days after the general election, "Last week, we were reminded of the difficulties in forecasting the outcomes of complex, interacting systems".
Fortunately there are plenty of ways of generating income that do not rely on base rates and some which, in recent weeks, have seen an increase in yields. For more information on your options, please talk to us. And do it today, not tomorrow!

Mary Poppins' Pension

Pension automatic enrolment is getting closer to home.

The roll out of automatic enrolment of employees into pension schemes started back in October 2012 with the largest employers. The logic was that these big organisations would have the necessary resources to start the process quickly and efficiently. Since those early days, the size of employers required to introduce automatic enrolment has been shrinking. As of this month, the threshold fell to fewer than 30 employees.

This is the minimum threshold and embraces nearly 800,000 small and micro employers. In this group, the precise timing ("staging date") for when automatic enrolment must be offered is driven by PAYE coding letters, which can have unusual effects. For example, two employers working from the same premises might have staging dates two years apart.

The first sub-30 group (with the last two letters of PAYE reference numbers 92, A1-A9, B1 – B9, AA-AZ, BA-BW, M1-M9, MA-MZ, Z1-Z9, ZA-ZZ, 0A-Z, 1A-1Z or 2A-2Z) have now reached their staging date of 1 June 2015. That has prompted some press coverage about the employment of nannies. Parents who employ nannies directly fall within the automatic enrolment rules, even if the recruitment of the nanny was originally via an agency. The initial pension cost will be modest – generally 1% of earnings above £5,824 – but the rate will rise to 2% in October 2017 and 3% a year later. For a nanny in London that could mean employer pension contributions of more than £1,000 a year from autumn 2018.

The pensioning of Mary Poppins is a reminder of the way auto-enrolment is working its way through to all employers.

If you are an employer – of any sort – make sure you know your staging date and understand your responsibilities.

Failure to do so could lead to escalating fines from the Pensions Regulator.

Deflation arrives

The official rate of inflation fell below zero in April: prices are now dropping year on year.

The April reading for the Consumer Prices Index (CPI) was an annual rate of -0.1%, which is the lowest level since the index was officially launched in 1990. On an unofficial ‘back-tested’ estimated you have to go back to 1960 to find a similar figure.

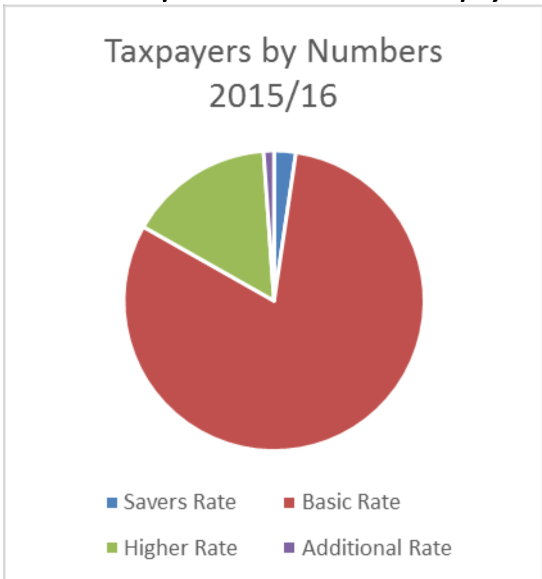
Negative inflation – deflation in the economist’s jargon – had been in the offing for some time, but the consensus forecast for the April inflation figure was that it would stay at the 0% recorded in February and March. What seemed to have made the difference in April was the timing of Easter and its effect on transport costs. The year’s peak Easter air and sea fares missed the data collection dates for the inflation number crunchers, helping to keep down that element of the index.

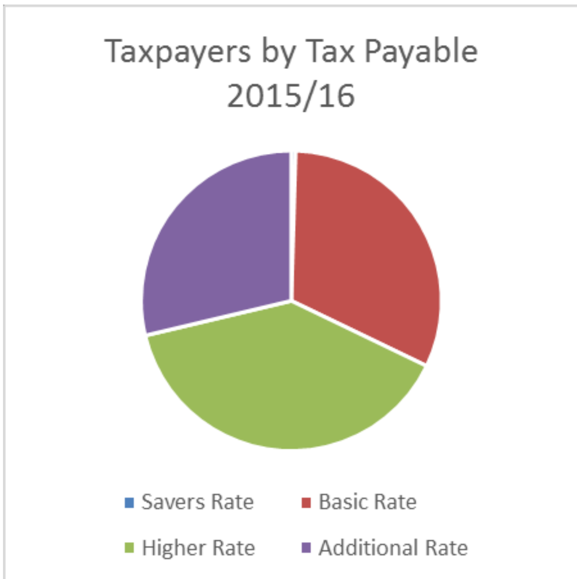
The Retail Prices Index (RPI) – no longer an official inflation measure – was still in positive territory at +0.9%. Similarly ‘core inflation’, which strips out the volatile elements such as fuel from the CPI, was +0.8%, down from 1% in March. The main drivers for the current ‘lowflation’ numbers are falling food and oil prices over the last 12 months. Oil prices have already recovered from their lows, so as the year moves on, positive CPI figures will probably return. The Bank of England still expects the CPI to be running at around its central target figure of 2% in two years’ time.

No inflation means that, for now, the miserable interest rates available from banks and building societies are not causing the buyer power of deposits to drop. However, this temporary phenomena is no excuse for leaving long term capital languishing in short term accounts.

1 in 6 pay more than basic rate tax

HMRC have updated their income tax payer data.





HMRC regularly updates data on income tax payers and last month it produced a revised set of numbers. These give an interesting insight into the drivers behind tax policy, and in particular, the emphasis on reducing tax avoidance.

- HMRC estimates there will be 29.7 million income taxpayers in 2015/16, 1.6 million fewer than in 2010/11, despite increased employment. The drop is mainly due to the significant increases in the personal allowance over recent years combined with low earnings growth.
- Of that near 20 million, almost 5 million will be higher or additional rate taxpayers at the margin – just over 1 in 6 of all taxpayers. In 2005/06 – with additional rate tax not yet invented – the proportion of higher rate taxpayers was less than 1 in 8.
- While 81% of taxpayers are basic rate, in 2015/16 they will only provide 32% of the total income tax receipts of £171 billion. Higher rate taxpayers will supply 39%, while additional rate taxpayers (numbering 332,000) will account for nearly 29% of all income tax paid. The average rate taxpayer will have a tax bill of £148,000.

The heavy dependence on additional and higher rate taxpayers helps to explain why pension tax reliefs have been squeezed and the relentless attack on the more aggressive forms of tax avoidance.

If you are in the 1 in 6 who pay more than basic rate, the second pie chart is a reminder why the Chancellor will not rush to reduce your tax bill. Fortunately there remain plenty of tried and tested opportunities to cut your contributions to the Treasury. Please call us to discuss the income tax planning options which are relevant to you.

The value of your investment 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.