money matters

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Pension planning: yet more changes

As people were preparing for 'pension freedom' from 6 April 2015, the Budget brought yet more changes to pension planning with a proposed cut in the lifetime allowance from £1.25 million to £1 million from April 2016. The lifetime allowance is effectively the maximum amount you can hold tax-efficiently in pensions.

The change will come with a new set of transitional provisions to protect people whose pension rights are already valued at over £1 million. From April 2018 the lifetime allowance will be index-linked – if the rules aren't changed again.

At current rates, £1 million will buy an index-linked pension with spouse's benefits of about £27,000, roughly equal to national average earnings. With further reductions to tax relief on pension contributions likely over the next few years, this could be a good time to maximise payments into pension plans while you can still claim tax relief on up to £40,000 a year at your highest rate. But you should also consider using other tax-efficient investment opportunities, such as ISAs, to provide for your retirement.

Annuities

Buying a pension annuity has become much less popular in recent years, and since 6 April 2015 it has become much easier to draw from pension savings in a more flexible way. However annuities should not be dismissed entirely because they are the only way to guarantee a lifetime income no matter how long you live.

Drawing income directly from your pension fund has several advantages, but it involves risks. If investment returns are poor in the future, your income could be reduced or you could even run out. The money might have to last for a long time. A significant number of people now in their 60s can expect to live well into their 90s and possibly even beyond.

The new pension rules allow a combination of income drawdown and an annuity. You could use part of your fund to buy an annuity, ensuring an income for life to pay basic bills, but keep the rest invested to boost overall returns, hopefully, and ensure your beneficiaries inherit in the event of early death. Or you might delay buying an annuity until later, if you do not need the income yet. If you opt for income drawdown, you should be aware of the tax implications. The most important is to remember that normally only 25% of your pension can be taken tax free. The rest will be taxed as your income as you withdraw it, at 20%, 40% or 45% depending on the level of the withdrawal plus your other income in the tax year.

Two methods of income drawdown allow you to draw any amount you wish. Flexi-access drawdown normally enables you to withdraw (or crystallise) your tax-free lump sum,

leaving the balance of your fund invested. This can be drawn as a regular amount or a lump sum, but there is usually no point in drawing from the tax-free environment of the fund sooner than necessary.

You can take funds out of your pension and invest into it in the same tax year. As long as you only crystallise the tax free element, you can continue investing the full £40,000 annual allowance into pensions. However once you start drawing income, your annual allowance for contributions drops to £10,000.

The other form of income drawdown is the generally less flexible 'uncrystallised funds pension lump sum' (UFPLS). When a lump sum is drawn in this form, 25% is paid tax-free and 75% is taxed as income. The balance of the fund stays invested. You can take a series of UFPLS payments, each of which is treated as a mix of 25% tax-free cash and 75% taxable funds. As soon as you take a UFPLS, your annual allowance drops to £10,000.

Professional advice is essential before making any decisions. Drawing a substantial sum from your pension early presents risks. Some schemes may not offer pension freedom, in which case you will have to change provider. There are additional considerations if you are in a final salary scheme. Please let us know if you need advice.

Cashing in on flexible ISAs

In his 2015 Budget, the Chancellor tried to put some much needed life back into cash ISAs with a substantial uplift to the investment limit. But the tax-free personal savings allowance announced in this year's Budget statement could actually make cash ISAs redundant for many savers from April 2016.

The idea is that annual savings income up to £1,000 will be exempt for basic rate taxpayers, with £500 exempt for higher rate taxpayers. Given current savings rates, a basic rate taxpayer will need around £45,000 invested before having to worry about an account's tax status. Higher and additional rate taxpayers should still find cash ISAs valuable, as will anyone aiming to build up substantial long-term savings.

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As something of a counterbalance, from this autumn the cash ISA investment limit is to become completely flexible. Currently, if you invest the limit of £15,240 and then withdraw it, no further investment is allowed during the same tax year. This restriction will go, allowing you to replace the money in your cash ISA.

Hope for first time buyers

There is one group of savers that will definitely want to stick with cash ISAs, and that is first-time home buyers. A help to buy cash ISA is planned for the autumn, with the key selling point being a 25% tax-free bonus paid by the government on both the amount invested and the accumulated interest. The bonus will be paid when the savings are used to purchase a home for up to £450,000 in London, or £250,000 elsewhere.

A maximum bonus of £3,000 will be available when ISA savings reach £12,000, although a couple buying together can both qualify. Some £30,000 could therefore be available towards a deposit.

The initial investment will be limited to £1,000, with a maximum monthly saving of £200 thereafter. So given current interest rates, it will take about four and a half years to build up the savings necessary to qualify for the maximum bonus.

Although none of these changes are definite, it is now finally possible to transfer the savings in a child trust fund to a junior ISA. Better interest rates, lower fund charges, and automatic transfer into a normal ISA at age 18 are all good reasons to do so.

All change: tax on land transactions

The last few months have seen something of a sea change in the way that property transactions are taxed. Last December, stamp duty land tax (SDLT) on residential properties moved from a 'slab' basis to a 'slice' basis.

Land and buildings transaction tax (LBTT) has now replaced stamp duty land tax (SDLT) in Scotland from 1 April. Same tax rates, but different bands:

Rest of UK	Scotland	Rate
Up to £125,000	Up to £145,000	0%
£125,001 – £250,000	£145,001 – £250,000	2%
£250,001 – £925,000	£250,001 – £325,000	5%
£925,001 – £1,500,000	£325,001 – £750,000	10%
Over £1,500,000	Over £750,000	12%

For example, SDLT for a £450,000 house purchase in England will be £12,500. LBTT on a similar Scottish property is £18,350. The higher Scottish exempt band means that £400 less tax is paid on lower valued transactions, but more tax is due where values exceed £333,000. Unlike SDLT, grants of residential leases are not subject to LBTT.

There has been no change in the way that SDLT taxes commercial land transactions, with the slab basis still used in the rest of the UK. LBTT, however, is slice based, with rates being:

Scotland-commercial	Rate
Up to £150,000	0%
£150,001 – £350,000	3%
Over £350,000	4.5%

The treatment of commercial leases also differs,

although the basic approach is the same – both taxes charge a rate of 1% on the net present value of rent over the term of a lease on the value exceeding £150,000. For leases of over five years, SDLT takes the highest rent payable in the first five years and then applies it to the remaining years of the lease. LBTT instead uses the actual amount of rent payable over the lease term, using estimates as necessary. A revised return then has to be submitted to Revenue Scotland every third anniversary to ensure that LBTT reflects the rent actually paid. Any premium is taxed on the same basis as a freehold purchase.

Both taxes have similar reliefs, but sub-sale relief is an exception. SDLT sub-sale relief prevents a double charge where a property transaction happens in stages. There is no such across the board relief in Scotland, just a targeted relief for development transactions. Be warned that the anti-avoidance rate of 15% charged where companies buy residential properties valued at over £500,000 still applies in Scotland.

Ultra-low emission vehicles tax changes

An ultra-low emission vehicle is one that produces less than 75g/km of CO_2. Such vehicles benefit from a number of tax advantages, although somewhat less so since 6 April.

Electric cars: The use of an all-electric company car, with zero emissions, was previously a tax-free benefit. But this has changed, with the benefit currently based on 5% of the car's list price.

Over the next four years, the percentage used will increase to 7%, 9%, 13% and then to 16% for 2019/20. However, there is no fuel benefit, even if you charge up your car's battery at work. When you charge up your battery at home you also benefit from a 5% VAT rate on the electricity used, compared to the standard 20% rate.

For employers, the cost of a new electric car qualifies for a 100% first-year allowance (FYA). This allowance has just been extended to 31 March 2018.

Other ultra-low emission cars: Cars with CO_2 emissions up to 50g/km have the same benefit charge as an electric car. Where emissions are between 51 and 75g/km, the charge is 9%. This is a 4% hike from last year, and the charge will rise to 19% by 2019/20. As for electric cars, the 100% FYA is available, although since 1 April the qualifying emissions limit has been reduced to 75g/km. You also benefit from the 5% VAT rate when recharging a hybrid at home.

HMRC publishes advisory fuel rates which, for example, can be used to reimburse employees who pay for fuel for their company cars. There is also a set mileage allowance when reimbursing the use of private cars for business travel. There is no reduction to these rates for a hybrid car.

Electric vans: The exemption for company provided zero-emission vans is being withdrawn on a tapered basis. For the current year, the charge is 20% of the £3,150 van benefit. This will rise in steps until 2020/21, when the full benefit charge will apply. As for electric cars, there is no van fuel benefit, and zero-emission goods vehicles are eligible for the 100% FYA.

And there are other advantages. Cars with CO_2 emission rates up to 100g/km do not pay any vehicle excise duty. Electric and plug-in hybrid cars with emissions up to 75g/km can qualify for a grant of 35% off of the car's cost, subject to a grant cap of £5,000. For vans, the grant is 20%, with a cap of £8,000.

There is also the ultra-low emission zone to be introduced to central London from September 2020, with drivers of non-compliant vehicles charged to enter.

Shared parental leave arrives

Parents can now take shared parental leave (SPL) where an employee's baby is due after 4 April 2015. Maternity leave rights are unchanged, but now there is an extra option of ending maternity leave early in exchange for SPL for the other parent.

With SPL, parents have more flexibility in taking parental leave. A father could previously take additional paternity leave, although fewer than 1% actually did so. They could not take paternity leave until 20 weeks after birth, and then only after the mother's return to work. With SPL, parents can take leave together or separately, and leave can be stopped and restarted, with a return to work in between – because each parent is now entitled to three separate blocks of leave.

Employers cannot refuse a request for a single period of leave, but they can turn down a request for multiple blocks. For example, an employer has to accept a request for eight weeks, but they can refuse or negotiate about, say, two blocks of four weeks if this request is not acceptable. Each block must be for complete weeks, with eight weeks' notice required before any SPL starts.

Employed mothers qualify for maternity leave from the first day of their employment, but SPL is only available if certain conditions are met. The parent taking SPL must satisfy a continuity of employment test, and their partner an employment and earnings test. A self-employed spouse cannot take SPL, but could meet the employment and earnings test so that their spouse can. That spouse might prefer the flexibility of SPL to maternity leave.

For SPL to start, the mother must return to work or give notice of when maternity leave will end. However, two weeks of maternity leave immediately following birth is compulsory. Two weeks of ordinary paternity leave are also available. The remaining 50 weeks of maternity leave can be exchanged for SPL. Although there is no need to make any immediate decision, partners must give their employers at least eight weeks notice. Where a couple take SPL, shared parental pay will generally be received instead of statutory maternity pay. The rates are the same.

Couples who adopt a baby can also qualify for SPL by giving up their entitlement to adoption leave. And from 5 April, adopters are given the same rights as birth parents, with entitlement to adoption leave now being granted from the first day of employment. SPL is not straightforward for employers to manage, and if you offer enhanced maternity rights, you should consider offering the same for shared paternity. If not, you could end up facing a discrimination claim.

Curtains for the annual tax return?

Millions of taxpayers will no longer have to make annual tax returns if plans outlined in the Budget come to fruition, although the timetable is ambitious.

It's hoped that digital accounts will calculate an individual's tax position. This will include details that HM Revenue & Customs (HMRC) already holds, such as pensions and income taxed under PAYE, and third party material including savings income. Data will be added in real time so taxpayers will know how much they owe through the year. Taxpayers will be able to register, update and file information at any time. They will also make tax payments directly from the account with an option to 'pay as you go'.

As a first step, the UK's five million small businesses and the first ten million individuals will be moved onto the new electronic tax system by early 2016. Early beneficiaries are likely to be higher rate taxpayers who entered self-assessment because they or a family member receives child benefit.

Taxpayers remain responsible

Taxpayers will remain responsible for reporting any other income and chargeable gains and, crucially, for the accuracy of their tax bills. Small businesses and companies will still have to supply details of their income and expenses. But the plans include the prospect of business accounting software feeding data straight into digital tax accounts so that most businesses will log in just to check their details with no need to send a return. They will be able to let agents manage the account on their behalf. HMRC promises 'extra help and support' for people who have difficulty going online.

Another benefit for businesses will be that information about all their liabilities, including VAT and PAYE, will be held on the same digital account. In time, small businesses will be able to use their digital accounts to access tailored government support to help their business grow.

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