Topical commentary

Possible pre budget planning

As you will know from the media, the Labour government is expected to increase tax on assets in the budget on 30th October.

Only those with access to the draft budget proposals can know exactly which taxes will rise or be introduced, or what the changes will be.

However, core targets for existing taxes are Capital Gains Tax (CGT), Inheritance Tax (IHT) and the taxation of pension funds.

There is also the potential of a new wealth tax or a tax on unrealised capital gains.

In addition, we could see current exemptions withdrawn or curtailed. The ending of higher-rate tax relief on pension contributions seems a high probability. There is a possibility of restrictions on the yearly allowance for ISA funding and perhaps also a limit on how much can be held in an ISA, or the extent of the tax exemption.

These days, budget changes normally come into effect at the start of the new tax year, giving ample time to prepare for them. However, changes could come into effect without any delay, thereby scuppering options for those who have waited to see what happens rather than taken pre-emptive action on a "just in case" basis.

The trouble with pre-emptive action is there could be downsides if the feared changes don't materialize, or other measures that negatively impact the actions taken.

A brief summary of our thoughts on the main changes we see as on the cards is below.

Capital Gains Tax

There seems a high probability that rates will increase. For assets such as investments held outside a tax wrapper they are currently 10% on realised gains that fall into the basic rate tax band and 20% if they fall into the higher or additional rate tax bands. Gains realised on property that isn't your main residence are taxed at 18% and 24% respectively.

Capital gains tax rates may well move to align with income tax rates, so become 20%, 40% or 45%, depending on the tax band they fall into.

We may also see the exempt allowance removed. In the past two years it has fallen from £12,300 a year to just £3,000, so it's unsafe to assume that trend won't continue.

A smart move for the Government would be to announce the increase but have it come into play from 6th April. That way, many would choose to realise gains after the budget but before 5th April, paying the lower rates, thereby generating a windfall tax for HM Treasury.

In contrast, an instant increase in rates is likely to lead most to decide against realising gains in the hope of a future change of government reducing taxes.

However, there is a risk a change would be immediate so if you have unrealised gains, it is worth considering realising them before the budget and paying the current relatively low tax rates. That could, though, backfire as a change might include some form of relief for gains built up to date, such as reintroduction of the exemption from tax for gains that merely reflect inflation.

There also seems a high chance that the exemption for CGT on death will be abolished, so beneficiaries inherit the CGT liability if the assets are sold or perhaps even if they are not.

Unrealised Capital Gains

These attract no tax at present but that could change. However, there is no forward planning we can think of, beyond realising gains ahead of the budget as discussed above.

Inheritance Tax

Other than using the £3,000 per donor annual exempt allowance, there is no forward planning as gifts beyond that are already potentially taxable.

We think the best approach is to see what changes come along and then review the impact of these, once they are known.

Pension funding

If you are a higher rate taxpayer and have not taken advantage of all your funding allowance, it may be wise to do so before the budget.

Pension tax free cash entitlement ("Pension Commencement Lump Sum")

The general view seems to be that it is highly unlikely there will be any further restriction to that already in place, where the maximum tax-free cash available is £268,275 or, if there is, that the change will take effect from 1st November rather than a later date or without any transitional relief for pension funds already built up.

However, while that may be the consensus view, it could obviously turn out to be wrong.

If we do see a further limitation on the entitlement to tax free cash or a change to make the withdrawal only free from basic rate taxes, and it comes into force immediately with no transition reliefs, then taking out any remaining tax-free cash entitlement ahead of the budget would prove a smart move.

It may be an "own goal" though, as a pension fund is normally exempt from IHT. That exemption may go, but if it doesn't and there is no change to the tax-free cash entitlement, leaving it in place may well prove the better choice.

It's a conundrum faced by everyone who has an estate over the IHT limit and hasn't withdrawn all their pension tax free cash, so a huge number of people.

ISA allowances

We can think of nothing that can be done to prepare for a possible cap on the total value of funds that can be held tax free in an ISA but using this year's allowance head of the budget seems smart, just in case the allowance is reduced or withdrawn, and the change comes into force at once.

However, it seems much more likely that a change would be from the new tax year, as doing it halfway through would be an administration nightmare for HMRC and ISA providers alike.

A wealth tax

This is another where preplanning is not really an option. If it does get introduced, the threshold will probably be set too high to impact on the vast majority of us, so we think it's a case of waiting to see and worrying about it if we find we need to, although avoiding its impact will probably be almost impossible, bar leaving the country.

Conclusion

Without knowing what will actually change, and with pre-emptive action having a possible downside, our general view is it is best to wait and hope there is time after the budget to take advantage of current tax rules for the rest of this tax year.

However, we fully accept that pre-emptive action could turn out to be the best option and, if you would like to consider that route, please let us know as soon as possible.

In the meantime, core actions to consider ahead of the budget, just in case there is a change which comes into effect at once and where there does not seem to be any significant potential downside or any reason to delay if funds are available are:

- Use your ISA allowance.
- Take advantage of any eligibility for higher rate tax relief on pension contributions.
- Consider realising capital gains on investments held outside a pension or ISA, to pay tax at current rates, given the high risk these will increase.

Important notes

Any opinions expressed on the merits or disadvantages of any options are intended as a general comment only and not as specific advice to the reader.

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