MOORE Kingston Smith

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BULLETIN

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FIXED INTEREST IN A DIFFERENT WORLD

World events in 2022 may have changed the investment landscape more than you realise.

At the start of 2022, the Bank of England base rate was 0.25%. Simultaneously, a ten-year government bond (gilt) offered a return for the following decade of about 1.1% a year.

On 23 March 2023, the Bank of England announced its eleventh consecutive rate increase, taking the base rate to 4.25% – the highest since 2008. At the same time, the return on the ten-year gilt was 2.5% higher than in January 2022, at 3.6%.

While the change in bank rates grabbed the media headlines, for investors the upward move in bond yields was the more significant event. For about 40 years until 2022, the yield on UK government bonds had largely moved in one direction – downwards. It was much the same picture in Europe and the US. Historically, bonds have constituted a crucial asset class for portfolios with a lower risk profile. Consequently, investors with a more conservative risk tolerance have predominantly experienced the impact of these market shifts.

The revival in bond yields has important consequences:

Bonds have become more attractive investments, particularly if you are seeking longer-term income.

There is now more potential for capital growth from investment in bonds. Partly, this is because scope for yields to fall (and thus bond prices to rise) now exists, whereas it had virtually disappeared with near-zero rates.

Bonds now have a potentially greater role in a diversified portfolio of investments. When yields were on the floor, there was no incentive to hold bonds in preference to equally low-yielding cash.

Higher bond yields mean better annuity rates, creating more retirement income options.

Furthermore, for clients maintaining substantial cash reserves, government bonds (gilts) could offer notable tax advantages compared to cash holdings. Interest accrued in deposit accounts is generally subject to taxation based on prevailing interest rates, which may diminish your returns by up to 45%. In contrast, the majority of returns generated by gilts are characterised as tax-exempt capital gains. There are many ways to gain access to the wide variety of bond investments. Advice is essential: while yield is important information, there are many other factors to consider.

Investments do not offer the same level of capital security as deposit accounts.

The value of your investment and the income from it 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.

THE BUDGET AND BEYOND: PREPARING FOR THE NEW TAX YEAR

The spring Budget, with its surprise proposed abolition of the lifetime allowance, brought the tax-planning landscape for 2023/24 into sharp focus.

Heading into the new tax year, the following key areas of change – and non-change – mean you should start your planning early.

INCOME TAX

The personal allowance and higher-rate threshold (outside Scotland) will be frozen until April 2028. The additional-rate threshold (and top-rate threshold in Scotland) will be reduced by nearly £25,000 to £125,140 for 2023/24. Not only will this mean you pay more tax as your income rises – even if it grows slower than inflation – but you may also move up a tax band.

DIVIDEND ALLOWANCE

The dividend allowance will halve from the current £2,000 to £1,000 in 2023/24 and then halve again to £500 in 2024/25 – a tenth of its original level. These reductions make it even more important to maximise your UK tax-free ISA allowances or look at different structures for your investments.

CAPITAL GAINS TAX

The annual exempt amount is on the same trajectory as the dividend allowance. It will fall from £12,300 in 2022/23 to £6,000 in 2023/24 and then to just £3,000 in 2024/25. The maximum corresponding amount for trusts will be half these figures. There are opportunities now to restructure your investments to mitigate this impact, and more active capital gains management can lead to significantly improved returns and flexibility.

PENSIONS

The Budget contained three significant changes to pension rules that take effect from 6 April 2023:

The lifetime allowance, which had been frozen at £1,073,100, will effectively be abolished. All the potential tax charges associated with it will disappear from 2023/24.

The annual allowance will increase by 50% to a maximum of £60,000 and to a minimum of £10,000 where taper rules apply. The same £10,000 figure will apply to the money purchase annual allowance, which is triggered when income is first drawn flexibly.

There will be a new monetary cap on the tax-free pension commencement lump sum of £268,275, unless you have earlier lump sum protection.

These reforms are designed to encourage high earners to stay in work and the retired to re-join the labour force. However, they have wider relevance and could mean your retirement planning strategy needs to be revised.

For more information on these changes, and potential impacts and opportunities, click here.

CORPORATION TAX

From 1 April 2023, the main corporation tax rate for companies with profits of at least £250,000 will rise from 19% to 25%. For companies with up to £50,000 profits, the 19% rate will continue to apply. For companies with profits in the £50,000–£250,000 band, the first £50,000 of profits will also be taxed at 19%, with the excess subject to an effective rate of 26.5%. These new tax bands will discourage directors from extracting corporate profits through dividends. Pension contributions have become more attractive, following the Budget allowance changes, and other tax-advantaged investments will continue to play an important role.

If you have been left financially dizzy after Mr Hunt's one-two punch of autumn statement and spring Budget, please talk to us about a tax planning review.

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The value of your investment and the income from it 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 with your overall attitude to risk and financial circumstances.

Occupational pension schemes are regulated by The Pensions Regulator.

CAUGHT IN THE UNMARRIED TRAP?

Being frank about your finances is important in any relationship. But cohabiting couples in particular, who do not have the same legal protections as those who are married or in civil partnerships, need to know where they stand should one of them die or the relationship break down.

A recent report noted that 46% of people wrongly assume cohabitees are in a 'common law' marriage. This concept doesn't in fact exist in UK law. The government recently rejected calls to boost legal rights for cohabiting couples, although unmarried people are now entitled to claim bereavement benefits should their partner die.

This change still means cohabiting partners do not inherit assets tax-free if their partner dies – unless the estate is under £325,000 and left to them in a will – and may not inherit anything at all if there is no will. They may also not be in line to receive funds from pensions or life insurance policies. Couples who have children together or co-own their home need to plan their finances carefully.

Surprisingly, research by Scottish Widows found that only half (52%) of unmarried adults in a relationship knew whether or not their partner had a life insurance policy.

Starting a discussion involving the four steps below should ensure partners have some protection in place, whatever the future holds.

- Check property ownership: Ensure you know whether your property is owned as a 'joint tenancy' or 'tenancy in common' and whether the arrangement will meet your needs if one of you dies.
- Write a will: These can be individual or 'mirror wills' for couples, setting out who inherits assets or looks after any children in the event of one or both partners dying.
- Nominate your partner as a beneficiary on your pension or life insurance policy: This generally involves completing one form, often online.
- Consider life insurance: Protect your loved ones by guaranteeing the availability of funds to settle outstanding debts, compensate for lost income or address potential inheritance tax liabilities.

The Financial Conduct Authority does not regulate will writing and some forms of estate planning.

Life assurance plans typically have no cash in value at any time and cover will cease at the end of term. If premiums stop, then cover will lapse.

TESTAMENTARY FREEDOM AND ADMINISTERING AN ESTATE IN THE UK AND CROWN DEPENDENCIES – AN OVERVIEW

In many countries and in particular in civil law jurisdictions in Central or South America, Central or Eastern Europe and East Asia, a prescribed portion of one's estate must pass to a spouse or descendants on death. In the UK, this is commonly referred to as 'forced heirship rules'.

Our legal team specialises in the administration of estates in England and Wales and has contacts throughout the crown dependencies who can help you to administer an estate in any of these jurisdictions. Read more **here** for an overview on testamentary freedom and administering an estate.

CAN YOU MEET THE RISING COST OF RETIREMENT?

The recent rise in living costs means many people will now have to save a lot more to ensure financial independence later in life.

The Pensions and Lifetime Savings Association (PLSA) estimates pensioners now need a minimum income of £12,800 to cover basics in retirement — up 18% in the past year.

THE COST OF A MORE COMFORTABLE RETIREMENT

Those wanting more than just the basics should be targeting an income of £23,300 a year to enjoy a 'moderate' standard of living, with £37,300 (or £54,500 for a couple) for a 'comfortable' retirement, according to the PLSA. To generate this kind of income in retirement, a couple sharing costs would need to save around £328,000, on top of two full state pensions.

BUILD IN FLEXIBILITY

It isn't just higher bills that might derail your retirement plans. Recent reports suggest the government is actively considering increasing the state pension age (SPA) again.

The SPA of 66 is due to rise to 67 by 2028. But the government is considering raising it to 68 by 2035, potentially affecting millions born in the 1970s who will either have to save more to make up this shortfall or work for a year longer.

Saving sufficient sums can seem like an uphill task – particularly if the goalposts keep moving. But reviewing plans regularly and building in some flexibility is increasingly important. Identifying potential shortfalls at an earlier stage means savers are in a better position to plug any gaps over the longer term and secure a more comfortable retirement.

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WHERE IS YOUR MONEY GOING?

Inflation is everywhere but your experience of it may not match the figures in the headlines.

In 2022, four main measures of inflation published by the (ONS) ranged from 9.2% to 13.4%, with the most used, the consumer prices index (CPI), registering at 10.5%.

A breakdown of the 2022 inflation rate into each of the dozen categories which make up the CPI shows the highest rate of inflation was in the category including electricity (up 65.4%) and gas (up 128.9%).

The ONS, which reviews the contents of the CPI 'shopping basket' each coming year, gave electricity and gas a combined 2022 weighting of 3.6% of overall household expenditure. That low percentage reflects the timing of world events: the basket weightings were set before the Ukraine situation.

If you are retired or work from home, utility bills will impact your finances more than if your employer provides a warm working environment. Similarly, lower earners are likely to spend more of their income on the essentials, like home heating and food (the second highest inflation category in 2022).

The Bank of England forecasts CPI inflation should drop to 'around 4%' by the end of 2023. However, as 2022 proved, forecasts from even the most respected sources are not the same as outcomes.

The CPI in December 2022 was 17.6% higher than in January 2020. After such a spike, a review of your personal finances to see whether any adjustments are needed makes good sense. For example, funding plans for school/university fees, potential inheritance tax liabilities or even that retirement world cruise may now be inadequate. Remember, just because the future rate of inflation looks set to drop does not mean the cumulative damage caused by past inflation will disappear.

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READ HERE:

CASH MANAGEMENT STRATEGIES DURING UNCERTAIN TIMES – A GUIDE FOR BUSINESS OWNERS

DIGITALLY DEFERRED

HMRC's plans for digital tax have been delayed...again.

In December 2015, HMRC published 'Making Tax Digital' (MTD), a paper in which it said: "By 2020, businesses and individual taxpayers will be able to register, file, pay and update their information at any time of the day or night, and at any point in the year, to suit them. For the vast majority, there will be no need to fill in an annual tax return."

It has not quite worked out that way.

Almost exactly seven years after the original MTD paper was published, a House of Commons written statement revealed that the introduction of the MTD regime for the self-employed and landlords, requiring income and expense data to be submitted online quarterly, would be deferred for at least two years:

For those with a gross income of over £50,000 a year, MTD will now become mandatory from April 2026.

Those with gross income of over £30,000 a year will join MTD from April 2027.

PLANS FOR LOWER EARNERS NOT YET REVEALED

What will happen to the self-employed and landlords with income of £30,000 or less is unclear – the government has promised a review. General partnerships have similarly been told their start date has been deferred from April 2025 "to a later [unspecified] date".

It seems certain that MTD for income tax will eventually happen but, at least for now, it remains confined to VAT.

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DO YOU HAVE A NATIONAL INSURANCE GAP?

An important pension deadline has been extended.

In 2013, as part of the launch of the new state pension, the government announced that, until 5 April 2023, people could fill in gaps in their national insurance contribution (NIC) record between April 2006 and April 2016. The offer was potentially valuable because under the new pension regime, a ten-year minimum of NICs (including any NIC credits) are needed for any state pension entitlement. In theory, for someone with a nine-year NIC record, filling in just a single year's gap – typically at a current cost of £824.20 – means the difference between no state pension and one of just over £3,000 a year.

In early 2023, this opportunity belatedly gained the national press coverage it deserved, resulting in HMRC and the Department for Work and Pensions being swamped with enquiries. The government has responded by extending the deadline to 31 July.

More information can be found **here.**

If you think this could affect you, do not wait any longer to act.

READ HERE:

BOLSTER YOUR STATE PENSION ENTITLEMENT: EXTENDED 31 JULY DEADLINE

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CONTACT US

Call:
+44 (0)20 4582 1000

Or email:
privateclient@mks.co.uk

Offices in:
City (London), Heathrow, Redhill, Romford, St Albans, West End (London)

MOORE Kingston Smith

www.mks.co.uk

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