FLASH UPDATE

08 November 2024

NORTH CAPITAL

Budget Digest

A little over a week has now passed and we have digested the facts of October's Budget and, tried to position the immediate and longer-term impact to you.

The headline is that we will all pay more in taxes and consequently, objective-led wealth planning will help develop strategies to reduce your increased tax burden. Particularly for clients with large tax liabilities, be that income tax, Capital Gains Tax (CGT) and Inheritance Tax (IHT), your real wealth will be largely preserved by adopting tax-efficient planning.

We will avoid a full recap on all the changes introduced in this budget, and instead focus on CGT, IHT and Pensions.

Capital Gains Tax

Investors will breathe a sigh of relief as the CGT rise is far more benign than some of the speculations had suggested.

Effective from 30th October 2024, the basic rate of CGT will increase from 10% to 18% and the higher rate will increase from 20% to 24%. The latter increase also applies to trusts. Capital losses can still be offset against future gains. Loss relief (in particular, carry-forward losses from past tax years) is valuable planning tools, especially if CGT rates were to continue to rise.

We would always advocate using all available allowances as well as maximising your ISA subscriptions to benefit from tax-free growth. That said, for wealthy individuals, the annual personal CGT exemption of £3,000 p.a. and £20,000 ISA subscription is relatively insignificant in the greater scheme of the (tax) planning process, but nonetheless, an important discipline.

In the wider context, consideration should be given to tax-efficient investment vehicles such as Venture Capital Trusts (VCT) and Enterprise Investment Schemes (EIS) which offer a CGT exemption as well as income tax relief. Pensions and Investment Bonds also continue to offer CGT-free growth on the underlying assets.

The structure of the investment/underlying portfolio will determine whether CGT is applied on an arising basis (for segregated portfolios i.e. individual stocks/funds) versus portfolios held within an Open-Ended Investment Company (OEIC) or Unit Trust (UT) where gains and losses are incurred within the investment structure and a taxable event is only triggered on a sale.

There has been no change to the treatment of CGT on death, which means that an estate will be liable to inheritance tax but not CGT.

The rate payable on qualifying gains from the sale of business assets will increase from 10% to 14% from 5th April 2026 and the further increase to 18% from 6th April 2026. Very little planning can be undertaken to mitigate this increase other than to time the sale of assets within the relevant time periods.

Inheritance Tax

The IHT nil rate band and Residence nil rate band will remain at £325,000 and £175,000 respectively, and will now remain fixed at these levels for a further two years until 5th April 2030. A greater number of people will therefore be caught by IHT due to the growth of the assets in their estate.

Farmers and entrepreneurs are particularly impacted by the reclassification of assets that previously qualified for unlimited relief for IHT. Agricultural property and business property as well a forestry will now only benefit from limited relief following the introduction of a combined allowance of £1,000,000, above which an effective rate of 20% IHT will apply. This is scheduled to take effect from 1st April 2026.

The government will publish a technical consultation in early 2025, which will provide further insight into the proposal and inform the legislation, which will be included in a future Finance Bill.

The obvious questions will be how those affected will be able to fund a potentially substantial IHT liability without the necessary liquidity provisions. Planning considerations will likely focus on outright gifts to accelerate succession planning as well as insurance policies, subject to affordability. For any lifetime transfers, due consideration must be given to the potential CGT consequences. For business assets, clients will still be able to utilise holdover relief whereby the applicable CGT is deferred.

IHT planning is intrinsically linked with CGT considerations because of a transfer of legal ownership (to affect the reduction in the value of one's estate) or to create liquidity to fund an IHT strategy (by selling investment assets).

It may be worth discussing life insurance, discounted gift and loan trusts as well as investments into Business Property Relief qualifying assets (including EIS).

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Inheritance Tax

It is anticipated that from 6th April 2027 pension funds will form part of your estate for IHT. The tax will apply on the gross value of the pension immediately before death and can be paid by the scheme. It will be possible to avoid IHT on the first death if the pension funds pass to the surviving spouse.

Individuals should now reassess the suitability of future pension contributions. An alternative, for example could be a regular investment into EIS/VCT that also attract income tax relief by way of a tax reduction.

Where the withdrawal of tax-free cash (TFC) has been deferred, now would be the time to review this decision and consider the relative merits and drawbacks. TFC could also be used to fund your existing lifestyle or to make an outright gift.

It would also be sensible to review the nominated beneficiaries as passing the pension to a spouse may give more opportunity to remove the funds from the estate before the second death.

However, with changes not effective until 6th April 2026, we would err on the side of caution in making any decisions ahead of the response from the technical consultation paper, which is due on 22nd January 2025.

Bottom Line

The budget was busy and, in many ways, brutal. It is a reminder of the need for tailored and proactive financial planning to navigate the evolving tax landscape as well as safeguarding your wealth.

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