The buy-to-let Budget headline you didn't see

The Autumn Budget contained more bad news for many buy-to-let investors which went largely unnoticed.

April 2018 will see the next step down in mortgage interest relief for investors in buy-to-let (BTL) residential properties. The amount of interest that can be offset against rental income drops from 75% to 50%, with a corresponding increase to 50% in the element that qualifies for a 20% tax credit.

If you pay tax at more than basic rate, that means more interest on which you effectively receive only 20% relief rather than 40% or 45%. It could also mean an increase in your gross income, which might trigger other undesirable tax consequences, such as a phasing down or out of your personal allowance.

The mortgage interest changes have encouraged BTL investors to buy new properties via specially-established companies, sometimes also transferring existing properties into the same company. Using a company can create a double capital gains tax charge – once in the company and a second time on the shareholder.

So far, however, the impact of this has been abated by the fact that corporate capital gains still benefit from indexation relief. That relief means only gains above inflation (measured on the more favourable Retail Prices Index – RPI) suffer corporation tax (currently 19%). As the example shows, even when inflation is relatively low, indexation can provide a real tax advantage.

The benefit of indexation relief

In February 2010, the Graham Property Company Ltd bought a flat for £200,000, including costs. Seven and a half years later the company sold the property for £257,000 (net of expenses) – a rise roughly in line with the performance of the Nationwide House Price Index. The RPI increase over the period was 25.3%, meaning the company had to pay corporation tax on a net gain of only:

£257, 000 – £200,000 x 1.253 = **£6,400**

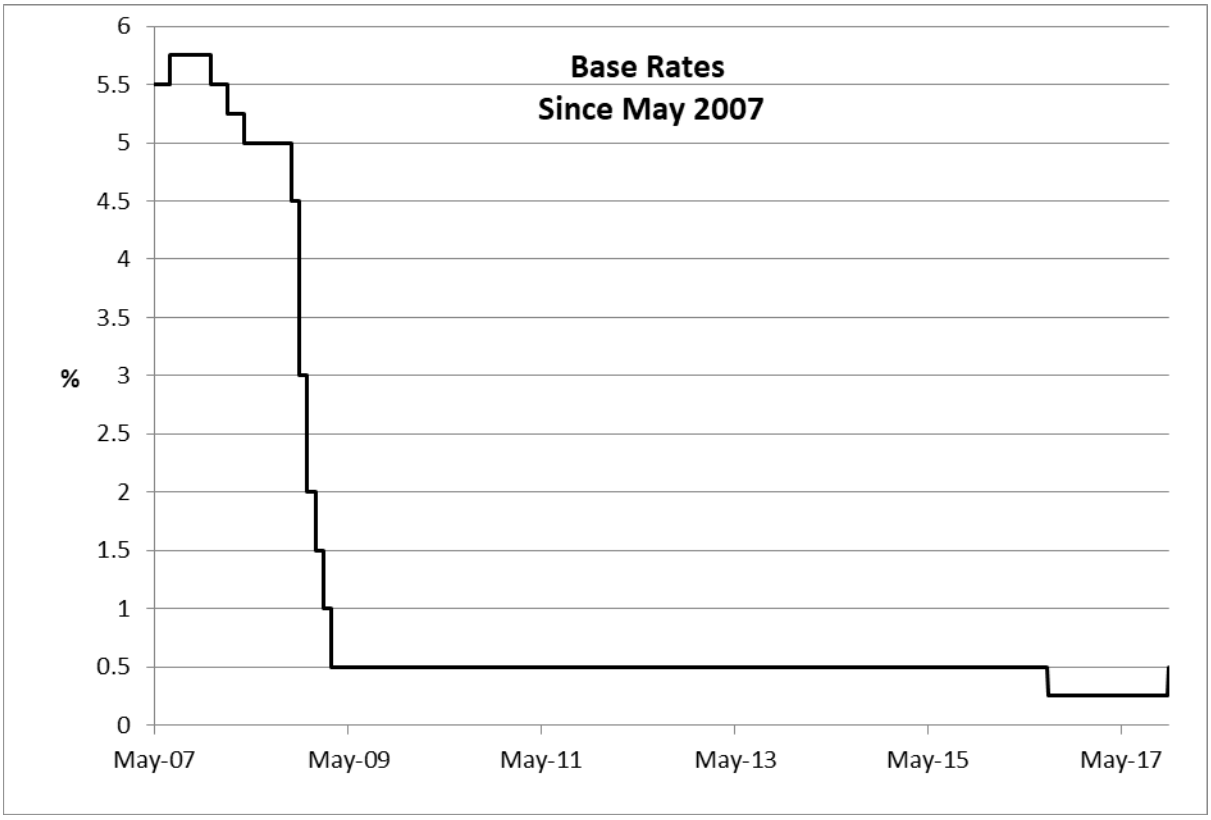
From January 2018, indexation will be frozen at the December 2017 level, exposing all *future* gains to tax. HMRC said in the policy paper on the change that "This measure has no impact on individuals or households as it only affects companies", but clearly individuals who have been driven to use companies for their BTL investment will be affected.

As if that were not enough, the proposed Stamp Duty Land Tax (SDLT) exemption for most first-time buyers outside Scotland will also hit BTL investors competing to purchase lower-priced property. On a typical £250,000 purchase, the first-time buyer will pay no SDLT, while the BTL investor faces an SDLT bill of £10,000, whether buying personally or via their company.

If you have the sense that the government is tilting the scales ever more against your BTL investment, then why not talk to us about other investments that are less heavily taxed?

The only way is up – after 3,773 days…

November marked the first rise in the Bank of England Base Rate in over ten years.



Source: Bank of England

At the start of November, the Bank of England raised its base rate for the first time since 5 July 2007. Just over a decade ago, the previous increase was 0.25%, from 5.5% to 5.75%. This time around the increase was the same, but represented a doubling in the base rate.

The move had been widely expected after several senior Bank officials dropped heavy hints that an increase was likely before the end of the year. In the run up to the announcement, the markets assumed a 0.5% rate as a done deal and focused on whether the rate increase would be "one and done" or the start of a series of rate rises.

The answer to that was given by the Bank's Governor, Mark Carney. He noted that money markets were forecasting two more rate rises over the next three years, a "gently rising path" consistent with inflation reaching target by the end of that period. In other words, the Bank currently expects base rate to reach the dizzy heights of 1% around early 2020.

If anything, news on inflation released less than a fortnight after the rate rise, pushed out the date of the next increase. Instead of rising above 3%, as widely expected, and thereby prompting an explanatory letter from Mr Carney to the Chancellor, CPI inflation remained unchanged.

The combination of 3% inflation and a 0.5% base rate is not good news if you hold cash on deposit: the gap between the two (plus any tax) is a measure of how fast buying power is being eroded. For alternative options, please talk to us.

The quiet NIC increases

The first Budget of 2017 in March hit a serious obstacle when the Chancellor attempted to raise national insurance contributions (NICs) for the self-employed. This time around he was subtler in his approach.

When Mr Hammond announced an increase to Class 4 NICs in the spring Budget, partly to offset the end of Class 2 contributions from April 2018, it nearly cost him his job. His backbenchers and the popular press rose up against this new imposition on white van man and his ilk. Within a week the Chancellor had backed down.

This autumn the government adopted different tactics. In a written statement issued three weeks before the Budget, the Exchequer Secretary to the Treasury announced that the proposed National Insurance Contributions Bill would be delayed until 2018, with the result that the abolition of Class 2 NICs (currently £2.85 a week) would be deferred for 12 months. The net effect may have been an increase in NICs for the self-employed, but there was barely a murmur in the press.

In his Budget, the chancellor added 10p a week to the Class 2 rate and raised the upper threshold for the full NICs rate for the self-employed (and employees) by £1,350. The net result is that in 2018/19 the self employed will pay *more* NICs than under the spring Budget plans if their income is less than £23,764 (but at least £8,424).

If you are a higher rate taxpaying employee, then typically your NIC bill will rise by about £104 a year, cancelling out almost a third of your income tax savings from the increased personal allowance and higher rate threshold, as the example below shows.

Income tax savings NICked?

	2017/18 **£**		**2018/19** **£**	
Gross Earnings	50,000		50,000	
Income tax @ 20%		6,700		6,900
Income tax @ 40%		2,000		1,460
Total income tax	(8,700)		(8,360)	
NICs @ 12%		4,420		4,551
NICs @ 2%		100		73
Total NICs	(4,520)		(4,624)	
Net Income	**36,780**		**37,016**	

NICs are an income tax in all but name. In some circumstances, such as salary sacrifice for pension contributions, this can be turned to your advantage. To find out more, please talk to us.

Venture capital schemes and the Budget

The Autumn Budget included a raft of measures focused on venture capital schemes.

The writing was always on the wall after a Treasury consultation issued in August posed the leading question, "Are there areas where the cost effectiveness of current tax reliefs could be improved, for example reducing lower risk 'capital preservation' investments in the venture capital schemes?"

The Autumn Budget gave the expected answer 'yes' by revealing a new "risk to capital" condition. Broadly speaking, this will require venture capital trusts (VCTs), enterprise investment schemes (EISs) and seed enterprise investment scheme (SEISs) to invest only in companies where "there is significant risk of loss of capital". The new rule will apply from when the Finance Bill 2017-18 receives Royal Assent, probably in early spring 2018. Full details are awaited, but it appears that all existing schemes will be affected if new investments are made.

This is an area that the Treasury has visited may times over the years, with the latest example a ban on investment in any form of energy generation activity, which took effect from the start of 2016/17.

If you did not invest in venture capital schemes before the Budget, your choice may be limited now as many schemes raised the funds they were seeking before 22 November. However, there are still some schemes open and new schemes may appear as we near the tax year end. Careful selection will be more important than ever, given the new constraints on investment managers. For more information and an update on availability, please call us.

Fancy your chances at 1 in 24,500…?

National Savings & Investments have increased their interest rates – and boosted a chance of winning.

National Savings & Investments (NS&I) beat many of its banking competitors by announcing a 0.25% increase in its variable rate products. These took effect from 1 December and are shown in the table below for taxable products open to new investment:

Product	Old rate	New rate
Direct ISA	0.75% tax-free/AER	1.00% tax-free/AER
Direct Saver	0.70% gross/AER	0.95% gross/AER
Income Bonds	0.75% gross/AER	1.00% gross/AER
Investment A/C	0.45% gross/AER	0.70% gross/AER
Junior ISA	2.00% gross/AER	2.25% gross/AER

None of the non-ISA rates are especially competitive. For example, at the time of writing the best instant access rates were around 1.3%. The Direct ISA is nearer the top of the league tables, although the recently launched Junior ISA lags behind.

The Premium Bond prize fund interest rate was also boosted by 0.25%, from 1.15% to 1.40%. NS&I used the increased prize fund to improve the odds of winning a monthly prize from 30,000:1 to 24,500:1. The mix of prizes was not changed: 90% of the prize fund will continue to be paid in prizes of £100 or less. According to NS&I this will mean that in December 2017, 982 out of every 1,000 Premium Bond prize winners will receive the near-ubiquitous £25 prize.

That skew towards £25 prizes is indicative of the fact that, for complex statistical reasons, the averagely lucky Premium Bond owner will 'earn' less than 1.4% prize fund rate. The averagely lucky owner's shortfall is made up by the handful of big prize winners who receive considerably more than 1.4%.

NS&I does offer Treasury-backed security for your money, but this is a guarantee that you pay for in terms of generally lower returns. Before you put £50,000 into Premium Bonds hoping for £700 a year tax-free, do make sure you talk to us about your other options.