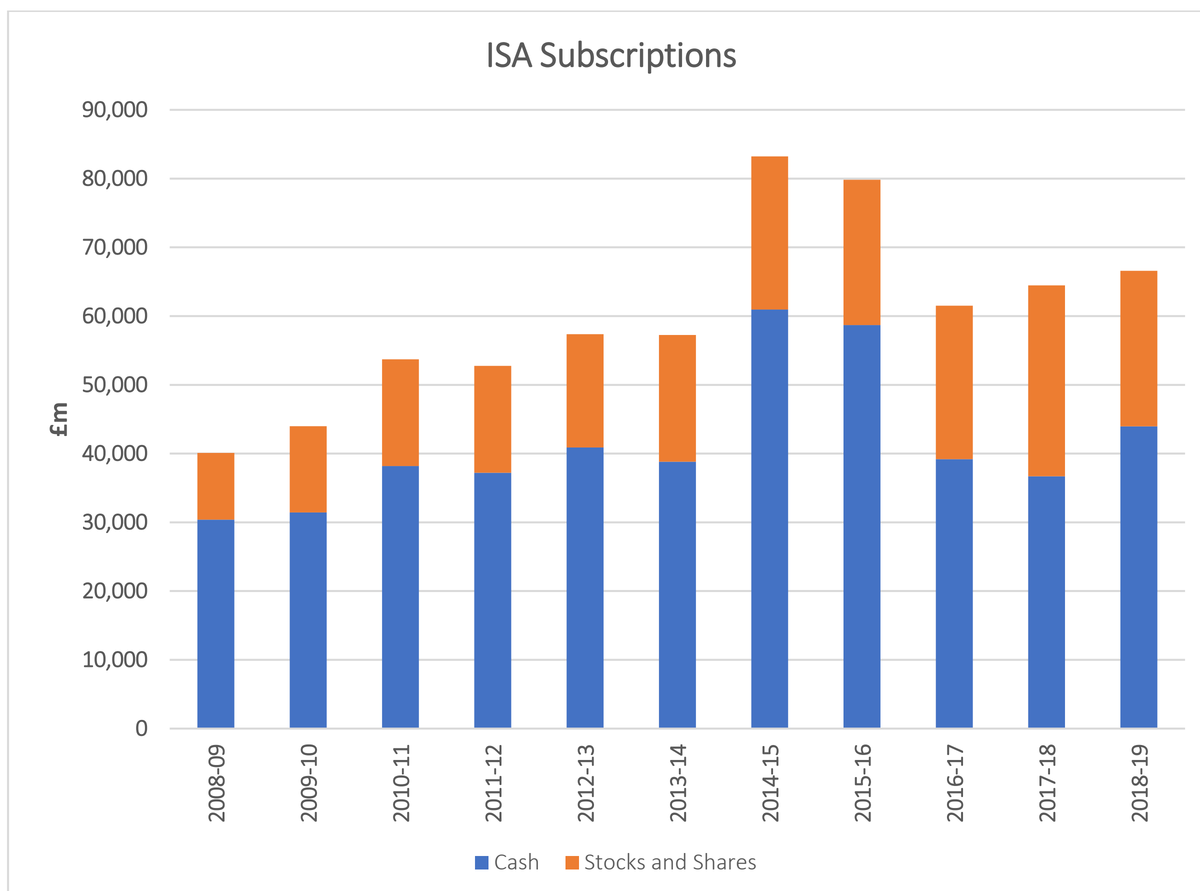
The Investment COACH

So much cash, so little interest…

The latest statistics on ISAs have emerged, showing nearly £270bn is held in cash.



Individual Savings Accounts (ISAs) reached their 20th birthday in April last year. Somewhat belatedly, HMRC has now issued ISA statistics up to April 2019. These reveal some surprising – and not so surprising – facts about ISAs:

- Overall ISA subscriptions in 2018/19 were almost a fifth lower than in 2014/15.
- Cash ISAs accounted for 46% of all the value held in ISAs as at April 2019, despite the ultra-low interest rates on offer.
- In 2018/19, 65% of all new ISA subscriptions were made to cash ISAs.
- In the three years to April 2019, the amount of cash held in ISAs was virtually unchanged, suggesting that subscriptions and interest were just about matched by withdrawals.
- Similarly, in the two years to April 2019, the total value of stocks and shares ISAs was down by 0.3%, also pointing to withdrawals matching investment returns plus fresh subscriptions.
- Lifetime ISAs have not been a great success, accounting for less than 1% of all ISA subscriptions in 2018/19.

There are two good reasons why ISAs have waned in popularity:

The personal savings allowance of up to £1,000, introduced in April 2016, combined with low interest rates means that many savers do not need a cash ISA to avoid paying tax on interest.

The dividend allowance, introduced alongside the personal savings allowance, exempts £2,000 of dividends from tax, so for many investors in share-based funds, an ISA offers no income tax savings.

But ISAs still have an important role to play in financial planning, particularly if your investment income already exceeds your available allowances or you regularly use your capital gains tax (GCT) annual exemption (£12,300 in 2020/21).

In the past, the tax advantages of ISAs meant they were often regarded as buy-and-forget investments. If you have ISAs that fall into that category, blow the dust off them and take a look at how they are performing, or ask us to review them. Market-topping bonus interest rates and flavour-of-the-month funds can lose their attractions over the years.

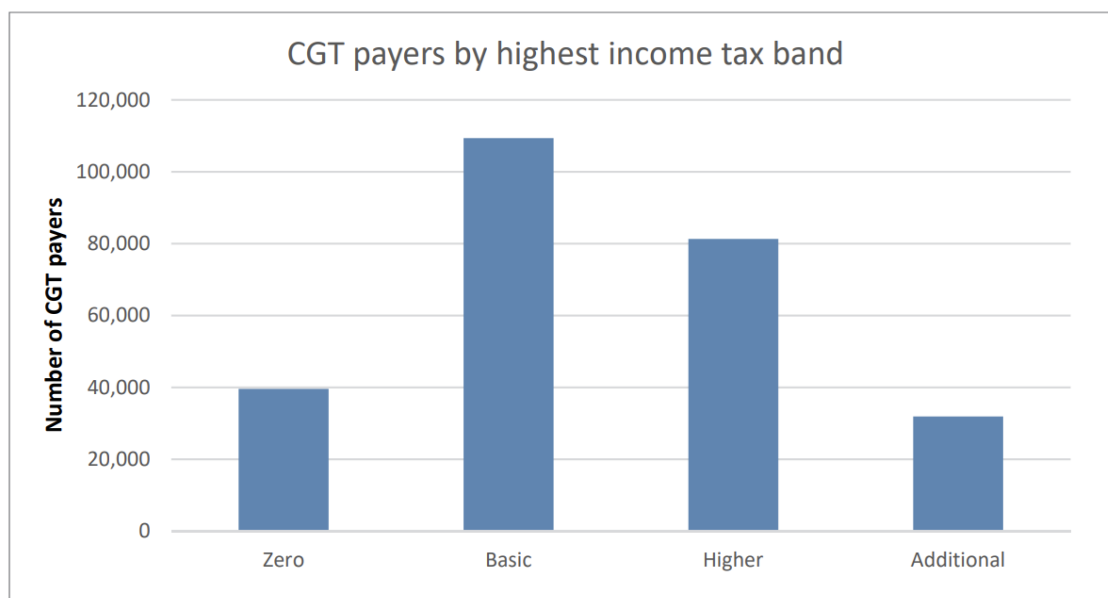
Capital gains tax comes under review

The Chancellor has asked the Office of Tax Simplification to review capital gains tax.

Within a week of giving his Summer Statement, the Chancellor wrote to the Office of Tax Simplification (OTS) asking it to "undertake a review of capital gains tax (CGT) and aspects of the taxation of chargeable gains in relation to individuals and smaller businesses". The request was unexpected and prompted some press speculation that Rishi Sunak was beginning his hunt for extra tax revenue after the unprecedented spending on Covid-19.

CGT is certainly an interesting place to start:

- The latest data from HMRC show that there were fewer than 300,000 CGT payers in 2017/18.
- Nearly two thirds of the tax raised in that year came from 3% of CGT payers who made gains of £1 million or more.
- Over half of the CGT payers either paid no income tax, or paid it only at the basic rate, as the graph below shows.



Source: HMRC Outturn data 2017/18[4]

The main reason why CGT payers are such a rare breed is the annual exemption. For 2020/21 this allows up to £12,300 of net gains to be realised before any tax becomes payable. Even then, the maximum tax rate is 20% (28% for residential property). At the last election, both the Labour Party and the Liberal Democrats called for gains to be taxed at full income tax rates and for the exemption to be cut to just £1,000 or abolished. The Conservative manifesto made no comment – CGT was not one of the taxes for which a rate freeze was promised.

Neither Mr Sunak nor the OTS has put any date on when the review might be published. However, the OTS has asked for all comments to be in by 12 October, so government proposals might emerge in the Autumn Budget, particularly if that Budget appears later in the year.

There is a precedent for changing CGT rates part way through a tax year – as then Chancellor George Osborne did in 2010. With this in mind, a wise precaution could be to review your portfolio and consider whether you wish to realise any gains in the next few months, while the current generous CGT regime is in place.

Summer stamp duty changes

The Chancellor's Summer Statement introduced temporary changes in stamp duty land tax on homes, which prompted similar – but not identical – changes in Scotland and Wales.

In his Statement on 8 July, the Chancellor raised the starting point for stamp duty land tax (SDLT) in England and Northern Ireland from £125,000 to £500,000 until 31 March 2021. Shortly afterwards, the Scottish government made a change to the nil rate band of its Land and Buildings Transaction Tax (LBTT), increasing it from £145,000 to £250,000. Last of the line was Wales, which adopted a slightly different tack, raising the nil rate band on land transaction tax (LTT) from £180,000 to £250,000, but only for main home purchases, but not for second homes or buy-to-let investments.

Outside of Wales the tax cuts prompted several news stories about a boost to the buy-to-let market. There is no arguing that the costs of buying an investment property have dropped – by up to £15,000 in England and Northern Ireland. However, the extra 3% SDLT surcharge on the full price will continue in England and Northern Ireland, as will the corresponding 4% LBTT levy in Scotland.

The other tax changes which have been made to buy-to-let over recent years remain unaltered, meaning that:

- any personal mortgage borrowing cannot be offset against rent received but instead qualifies for a 20% tax credit; and
- any capital gains on sales not covered by the annual exemption are subject to rates of up to 28% and the tax must be paid within 30 days of completion.

In the English context it is also worth remembering that there is still an unfinished consultation on 'modernising the rental sector', including the possibility of removing the availability of assured shorthold tenancies (ASTs).

Another upshot of the tax changes was the suggestion that they had given buy-to-let investors, who directly own their property, a chance to move the property into a company, at a reduced cost, to increase tax-efficiency. This may be true in some instances, but any such transfer could result in one of the 30-day capital gains tax bills.

Buy-to-let investment has been on the government's hit list since 2016. If the stamp duty and land tax cuts tempt you to think about investing in this sector, make sure you take advice and understand *all* of the tax consequences before doing so.

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Inheritance disputes

More arguments about wills are reaching the High Court.

A recent report from the Ministry of Justice revealed that, last year in England and Wales, 188 cases involving contested wills were heard in the High Court, an increase of nearly 50% over the previous year. In practice that figure almost certainly understates quite how many disputes there are about wills and inheritances. The cost of going to court often encourages arguing parties to reach an agreement rather than see a slice of the estate – or their own funds – wasted on legal wrangling.

Challenges to wills can arise for a variety of reasons:

- A co-habiting partner may find that they have been left out of their late partner's will because it was not updated when the co-habitation began.
- Children from previous relationships may feel they have been unfavourably treated relative to others born later.
- An estranged child who is excluded from the will could attempt to make a claim for 'reasonable financial provision' under the Inheritance (Provision for Family and Dependants) Act 1975.
- Disappointed beneficiaries might argue that the deceased lacked the mental capacity to make a will or was subject to undue external pressure.
- The will may contain errors, a problem more likely to appear in DIY variants.

A common piece of advice is that if you think your will could be viewed as contentious for any reason, you should clearly set out the reasons for your decisions. Usually this would be done in a 'letter of wishes' that sits beside the will but is not itself a legal document. In an ideal world you would also explain your choice to the person(s) involved during your lifetime, but such discussions can be highly emotive, making them difficult or impossible.

The Covid-19 pandemic prompted a sudden interest in will writing and estate planning at a time when doing either was logistically problematic due to social distancing. It may also have resulted in some homemade wills that will reach the courts in years to come.

On 25 July the Ministry of Justice announced it would be amending the law in England and Wales to allow remote witnessing of wills by video link for a period of two years, with a retrospective start date of 31 January 2020. Wills made in Scotland are already able to be witnesses via video. Will writing and estate planning are best done with expert advice in an unrushed manner. But, as Covid-19 presented an unwelcome reminder, it does need to be done.

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Dividends fall by over 50%

Dividends paid by UK companies dropped dramatically in the second quarter of the year.

The impact of the Covid-19 pandemic on dividend payments has been highlighted by recent research from Link Asset Services, one of the leading UK company registrars. It looked at the dividend payments from UK listed companies in the second quarter of the year and found that:

- Total dividend payments, both regular and one-off special payments, fell by 57.2% compared with the same quarter in 2019. If special dividends are excluded – and there were very few – regular dividend payments fell by 50.2%.
- 176 companies cancelled their dividends and 30 more cut them. In total that represented three quarters of the payers in an 'ordinary' second quarter.
- Among the 100 largest companies, dividend pay outs fell by 45%, but in the next tranche of more UK-focused 'mid-cap' companies, the drop was 76%.

To some degree, the second quarter of 2020 represented the perfect storm. This is when the big banks (Barclays, HSBC, Lloyds, NatWest (formerly RBS) and Standard & Chartered) usually pay their final dividends. This year, none of them made a payment, following direction from the Bank of England on preserving capital. Those five alone accounted for half of the decline in regular dividends over the quarter. April to June was also the period in which the dramatic dividend cut from Royal Dutch Shell took effect. For each of the last five years from 2015 to 2019, Shell has been the company which has paid out the largest amount in dividends, but its June 2020 quarterly dividend payment was around one third that of March.

Looking ahead to the rest of the year, Link predicts that, at best, the drop in total annual dividend payments will be 39% for regular dividends and 45% for all dividends; the worst case scenarios are 43% and 49% respectively. For 2021, the report suggests that there could be a rebound of 'as much as 29%' in dividends.

Inevitably the dividend cuts will work their way through to the payments made by UK equity income funds. Some will be harder hit than others, particularly those that relied on banks to boost portfolio income. The income funds for the 'new normal' are likely to look different from their predecessors. For our view of the income funds to consider now, please contact us.