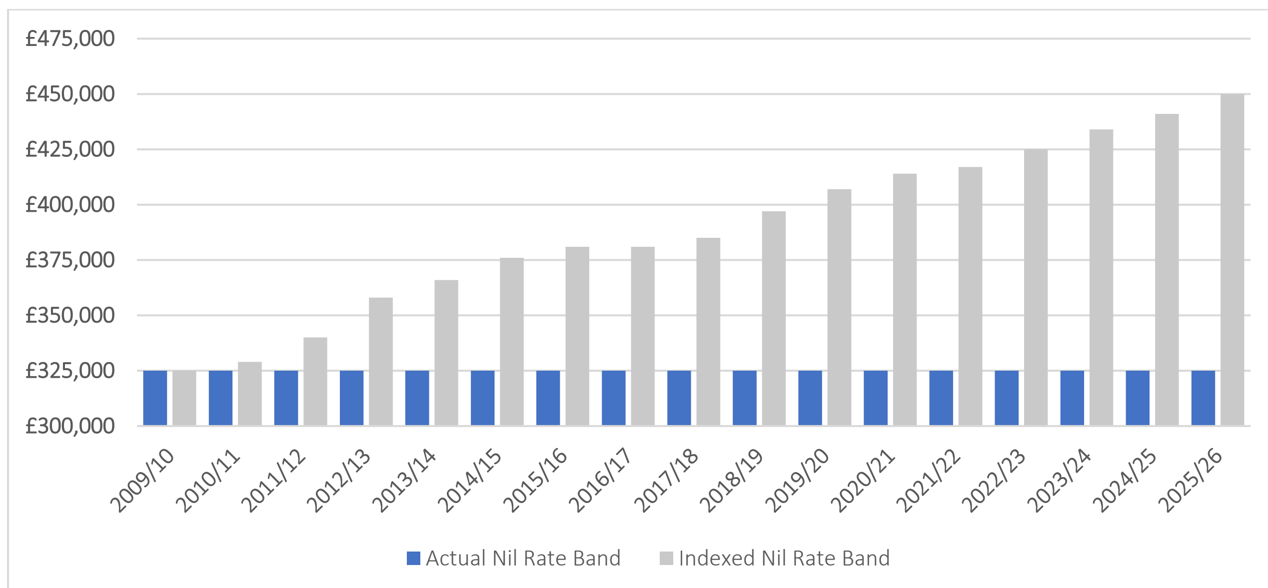
The twenty-year IHT freeze

The freeze on the inheritance tax (IHT) nil rate band will mean more tax from more estates.

The big freeze



In March 2006 the then Chancellor, Gordon Brown, announced that the IHT nil rate band for 2009/10 would be £325,000. Announcing the change over three years before it would happen was seen by some as a political tactic, kicking a contentious topic down the road. Little did anyone anticipate at the time that the figure of £325,000 would still apply two decades later. However, the announcement in the Spring 2021 Budget of a further freeze on the nil rate band means that it is now not due to change until at least 6 April 2026.

As the current Chancellor explained in his speech, albeit in the context of frozen income tax thresholds, "…this policy does remove the incremental benefit created had thresholds continued to increase with inflation". In the case of the nil rate band, that 'incremental benefit' is now no small number. If the figure Gordon Brown chose for 2009/10 had been increased in line with CPI inflation from 2010/11 onwards, as the graph shows, it would now be £417,000 – over 28% above its actual level.

The difference theoretically means up to an extra £36,800 in IHT at the standard rate of 40% in 2021/22. By 2025/26, the nil rate band would have been £450,000, based on the inflation assumptions made by the Office for Budget Responsibility.

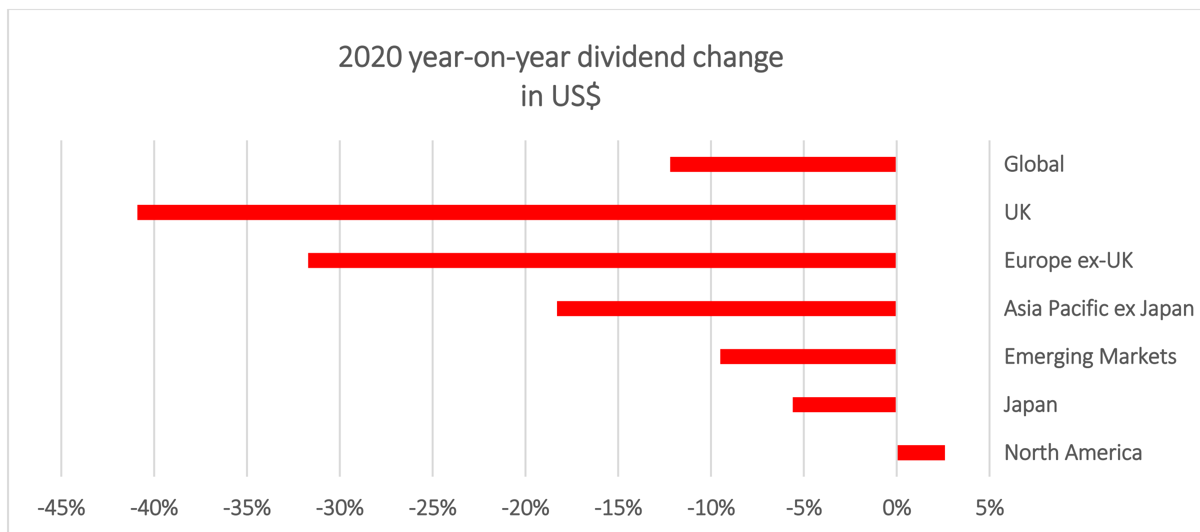
The residence nil rate band (£175,000) has also been frozen until April 2026. Before the Chancellor's announcement that he would be freezing the nil rate bands, there had been suggestions that Mr Sunak would introduce some reforms to IHT, drawing on two reports which were written by the

Office of Tax Simplification at the request of an earlier Chancellor. However, there was nothing in the Budget, although subsequently a relaxation in the requirements for IHT returns from 2022 was announced.

The unspoken message from the Chancellor is that he will continue to look to IHT to raise some much-needed revenue, making estate planning more important than ever.

Global dividends in 2020

A recent report showed that global dividend payments held up much better than those in the UK in 2020.



Source: Janus Henderson

For investors in UK shares and funds investing in UK companies, 2020 was a grim year when it came to dividends. The pandemic cast a long shadow over the pay outs to investors:

- Early on, the Bank of England effectively stopped all the major UK banks, including those mainly focused overseas, from paying dividends. The timing of the Bank's decision meant that the first dividends to disappear were final dividends, usually the largest of the year.
- Later, with oil prices having hit new lows, the UK 's two largest oil multinationals, Royal Dutch Shell and BP, both dramatically cut their quarterly dividends. The pair were in the top three of dividend payers by overall value between 2016 and 2019, so their decision hit many income funds hard.
- The economic uncertainty created by the pandemic encouraged many companies to cut or suspend dividends to preserve their cash holdings.
- More than a few companies took advantage of conditions to make cuts to dividend payments that had been looming for some time, but which had been sitting in the 'too difficult' tray.

The picture outside the UK was recently brought into focus in the latest edition of Janus Henderson's Global Dividend Index, which covered the final quarter of 2020 and the year as a whole. It showed that:

- Globally, between the second and fourth quarters of 2020, 12% of companies cancelled their dividends while 22% cut them. The corresponding figures for the UK were 32% and 23%. The much higher cancellation figure explains why the UK's relative performance looks so disappointing.

- The global sector with the largest overall dividends reductions, amounting to $70bn, was banking, which accounted for a third of total dividend reductions. This total was more than three times that of the next sector, oil and gas. Both sectors are major parts of the UK market.

The Global Dividend Index demonstrates that globally diversified investment can produce different returns from an investment portfolio focused on the UK, despite the UK's many multinational companies. By the end of 2020, the long-standing reign of 'UK All-Companies' as the largest investment fund sector had been ended by the 'Global' sector.

Should you incorporate?

The planned increase in corporation tax has changed some of the mathematics on incorporation.

The Budget announced a significant change to corporation tax from 2023:

- Small companies, with profits of up to £50,000, would continue to pay the tax at the current rate of 19%, subject to adjustments for associated companies and financial periods of other than 12 months.
- Large companies with profits of over £250,000 will pay corporation tax at a rate of 25%.
- For companies whose profits fall between £50,000 and £250,000 HMRC have said that there will be “marginal relief provisions”, which have now been set out in the Finance Bill. As under previous corporation tax regimes, the marginal relief is given by applying the lower rate up to the small companies limit and then applying a higher than standard marginal rate to profits above that threshold. With the new rates from 2023, the £200,000 band of profits above £50,000 will suffer a marginal tax rate of 26.5%.

At present, from a tax viewpoint, it can be better to run a business via a company rather than on a self-employed basis. This is mainly because a company will allow the bulk of earnings to be received as dividends, thereby avoiding national insurance contributions (NICs). While this approach will still work for businesses with profits that would attract only the 19% small companies’ rate, it is a different picture for higher profits, as the example below shows.

Higher corporation tax rate bites

Phil’s business generates £100,000 of profit. If he has no other income, the tax situation as self-employed or as a company now and in 2023/24 is:

	Self-employed	**Company 2021/22**	**Company 2023/24**
Gross profit	£100,000	£100,000	£100,000
Salary	N/A	£8,840	£8,840
Taxable profit	£100,000	£ 91,160	£ 91,160
Corporation tax		(£17,320)	(£20,407)
Dividend		£73,840	£70,753
Income tax	(£27,432)	(£13,211)	(£12,207)
NICs	(£ 4,816)		
Net income	**67,752**	**£69,469**	**£67,386**

If Phil decides to incorporate, then the tax savings will turn into a tax loss after two years.

The decision on business structure should never be made based on tax alone as there are many other factors involved. However, the deferred tax changes announced in the Budget may tip the scales for some. As ever, advice based on your personal – and business – circumstances is essential.

ESG comes into its own

Three letters, ESG, have become a major driving force in investment decisions.

ESG – environmental, social and governance – considerations are playing an ever-increasing role in investment decisions. What used to be classed as ethical investment, socially responsible investment (SRI) and green investment have now to some extent merged under the ESG banner. The table below gives a taste of the broad range of ESG investment considerations.

Environmental	Social	Governance
Carbon emissions	Employee treatment	Workforce diversity
Forest destruction	Child labour	Board diversity
Pollution	Slave labour	Executive remuneration
Waste management	Human rights	Political influencing
Resource use	Workplace health & safety	Tax policy

In 2020, the popularity of ESG funds among the UK investing public grew dramatically, perhaps at least in part a response to the pandemic. The Investment Association's (IA) 'Responsible Investments' category saw net retail sales more than treble to £10bn, almost a third of all 2020 sales and equal to the 2019 total for net retail sales. The IA 2020 statistics also show that over the year the value of funds in the category increased by two thirds, to £45.7 billion.

The latest figures from the IA show that were ESG funds to be classed as a fund sector, they would represent the eighth largest of the IA's 38 fund sectors. However, they are not a unique sector as there are ESG funds to be found covering nearly all investment areas.

Across these areas ESG funds also take different routes to implementing the ESG approach. It is common for fund managers to rely on external ESG rating bodies, which do not always agree with each other. As is always the case with investing in funds, it is best to take advice on what is under the bonnet rather than relying on the marketing badge outside.

If you'd like more information around ESG investment, please get in touch.

The Investment COACH

Tax Day 2021

The Spring Budget on 3 March was not the end of the taxing story.

The run up to the March Budget was accompanied by much press speculation about changes to capital gains tax (CGT), inheritance tax (IHT) and pension tax relief. The first two had been the subject of reports from the Office of Tax Simplification (OTS) while the Treasury has issued a consultation paper on the third. When Budget Day arrived, the trio received almost no mention from the Chancellor.

Attention then turned to 'Tax Day' – 23 March – when the Treasury had promised to publish a raft of documents that in earlier years would have come out alongside the Budget. The delay was designed to allow for more transparency and scrutiny by tax professionals. Once again, there was disappointment at what was missing. However, some indications of the direction of travel emerged from more than 30 sets of consultation papers, calls for evidence, summaries of responses and other documents issued on 23 March:

- ***Inheritance tax*** From 1 January 2022, IHT tax return procedures will be simplified so that "over 90% of non-taxpaying estates" will no longer have to complete IHT forms when probate or confirmation is required. If you have ever been involved in completing such paperwork, you will appreciate how much time this will save many executors.
- ***Holiday lets*** It has become increasingly common to classify holiday lets as being subject to business rates, often with the consequence that Small Business Rates Relief meant no rates were payable. This loophole is to be closed, with account taken of the actual number of days a property is rented when determining the rate bill.
- ***Timely payments*** One of the features of tax policy in recent years has been an acceleration of when tax becomes payable – the recent changes to CGT on residential property were a classic example. Under the heading of 'timely payments', the Treasury is beginning "…to explore the opportunities and challenges of more frequent payment of income tax within Income Tax Self Assessment, and of corporation tax for small companies, based on in-year information".

The absence of any major announcements on CGT, IHT and pensions could mean these will appear in the autumn Budget, leaving a window of planning opportunities until then.