Personal Finance

Budget 2017 and your money

Round-up of the chancellor's measures on tax, investing and pensions

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Taxpayers were not expecting fiscal fireworks when Philip Hammond rose to the Commons despatch box on Wednesday to deliver his first (and last) Spring Budget (https://www.ft.com/topics/themes/UK_Budget).

In the event, the speech generated a huge amount of coverage — though not necessarily of the kind he would have relished.

"Rob the Builder: White Van Man battered by Budget"; "Spite Van Man"; and "Hammond's £2bn tax raid" were splashed over front pages on Thursday morning, as the rise in national insurance (http://next.ft.com/content/e273c41e-03e9-11e7-ace0-1ce02ef0def9)for the self-employed polarised opinion across the political spectrum

Billed as a move towards a “fairer” tax system, the measure was among a number of changes announced by the chancellor which have ramifications for investors, business owners and pension savers.

In the aftermath of the Budget, FT Money has analysed the figures to determine the winners and losers in Mr Hammond’s financial calculus.

Dividend allowance slashed

As well as the national insurance changes, the chancellor said he wanted to reduce the gap in the amount of tax paid by employed and self-employed people by slashing the tax-free dividend allowance (http://next.ft.com/content/c7f34d20-040d-11e7-ace0-1ce02ef0def9) from £5,000 to £2,000 from 2018.

The measure was designed to curb the ability of self-employed people to take advantage of this tax break by paying themselves in dividends, but it also affects investors holding shares outside individual savings accounts (Isas) or pension wrappers.

The government’s Budget document pointed out that it has recently increased the amount that investors can hold tax-free in an Isa to £20,000 (http://next.ft.com/content/38999538-ff5a-11e6-8d8e-a5e3738f9ae4) — a measure due to come into effect on April 6.

While experts were united on the increased importance of using tax-efficient wrappers such as Isas in light of the reduced dividend allowance, they were divided on the impact on investors.

Fidelity, the asset manager, says it will affect only “the wealthiest shareholders”, while Darius McDermott, managing director of Chelsea Financial, says it will only hit a small proportion of his clients.

“Around 80 per cent of our investors hold their money in Isas,” he says. “The question is — why would you hold your money outside an Isa if you didn’t have to? You wouldn't. This hits people who have used their Isa allowance."

However, the UK Shareholders' Association says the idea that the reduced allowance only affected very wealthy investors is "drivel".

"There will be all sorts of people who have money outside Isas," says Peter Parry, UKSA board member, who argues that older people saving for retirement would be worst hit.

"Fifty thousand pounds invested outside an Isa over a lifetime is not that much — the government wants people to save and it is wringing its hands over the cost of care," says Mr Parry. "These are people who have saved and done what the government wants."

This sentiment was echoed by EY, the global consultancy, which says the reduction in the allowance was a "bitter blow" to those saving for retirement.

The move is aimed at reducing tax losses. Before the changes announced this week, the Office for Budget Responsibility calculated that switching to a corporate form could save employed and self-employed individuals £3,300 and £700 a year respectively, if they had incomes of £30,000 a year.

But John Cullinane, tax policy director of the Chartered Institute of Taxation says the change will not remove the problem. "For example, for a basic-rate taxpayer, the impact of that change cannot exceed £225 a year, a fraction of the typical tax benefits of incorporation at such levels of income."

He adds that incorporation will also enable a self-employed entrepreneur to sidestep the chancellor's surprise national insurance (NICs) increases.

Bill Dodwell of Deloitte, professional services group, says: "The gap between being engaged through a company and being self-employed has narrowed, but both forms are still better than employment."

Top earners might, however, be an exception, in the wake of the recent rise in dividend tax rates. Someone earning at least £170,000 and taking dividends out of their company would pay more tax than if they were self-employed, he says.

Self-employed national insurance

The tax rises faced by millions of the self-employed are set to reduce — but not remove — the advantages of joining the fastest-growing part of the workforce, experts say.

About 2.5m self-employed people face a rise in national insurance contributions averaging £240 a week, with higher earners such as barristers and consultants bearing the brunt of the changes.

Podcast

FT Money Show (https://www.ft.com/content/709754ff-8731-468b-b2f1-1a61f29db5e7)

Presenter Lucy Warwick-Ching and guests discuss the 'slow and steady' Budget announcements and what they mean for your pocket.

(https://www.ft.com/content/709754ff-8731-468b-b2f1-1a61f29db5e7)

The Resolution Foundation calculates that a self-employed taxi driver with average earnings of £17,300 will be £20 a year worse off, while a self-employed management consultant with average earnings of £51,100 will be £620 worse off.

The increase — which breached a manifesto commitment (http://next.ft.com/content/e8590bd6-03ef-11e7-ace0-1ce02ef0def9) — sparked fury from MPs, much of the press and many entrepreneurs, but it is only a small fraction of the tax gap between employees and the self-employed.

In his Budget speech, Philip Hammond said a self-employed person earning £32,000 would pay "significantly less than half as much" NICs as the £6,170 paid by an employee and his employer. He also drew attention to the "big pension boost" to the self-employed from the introduction of the new state pension and the 2018 abolition of Class 2 NICs for the self-employed.

Sir Steve Webb (https://www.ft.com/topics/people/Steve_Webb), policy director with the insurer Royal London says last April's changes to the state pension will "dwarf" the NICs rises. They would result in an extra £37,800 of income over a 20-year retirement, while the NICs changes would result in an extra bill of £7,720 over a 40-year working life for someone earning £25,000 a year.

The Institute for Fiscal Studies, the think-tank, calculates that the tax due on a job generating £40,000 in 2017-18 would be £12,146 for an employee, £8,713 for someone who was self-employed and £7,358 for an owner-manager. After the reforms, the tax bill for the self-employed would rise to £9,202 and for the owner-manager to £7,583.

But groups representing the self-employed are not impressed. Julia Kermode, chief executive of the Freelancer & Contractor Services Association, says: "I personally don't think it is relevant how significant the difference is because it will definitely will hit self-employed people."

Andy Chamberlain, deputy director of IPSE, a trade body representing freelancers, says: "If you put all these changes together, whatever model used for self-employment has become less attractive."

Pensions

One of the biggest surprises in the Budget was aimed at those looking to move their pensions abroad (http://next.ft.com/content/d56bc1b2-0408-11e7-aa5b-6bb07f5c8e12). For some, it could mean tax charges that wipe out a quarter of their funds.

Savers who have built UK pension pots face a 25 per cent tax charge on transfers made to qualifying recognised overseas pensions (Qrops) unless strict new criteria is met.

Advisers say the measure, which came into effect on Thursday, the day after the Budget, will have the greatest impact on those transferring their pensions to countries outside the European Economic Area (EEA).

Offshore pension transfers face 25% tax charge (http://next.ft.com/content/d56bc1b2-0408-11e7-aa5b-6bb07f5c8e12)

Non-doms given two-year window over mixed funds (http://next.ft.com/content/3614a276-0423-11e7-aa5b-6bb07f5c8e12)

“If the person moves to a country outside the EEA, the Qrops provider will also need to be based in that country or a 25 per cent tax charge will apply,” says Rachael Griffin, a financial planning expert with Old Mutual Wealth.

“This may create an issue as not all jurisdictions will have a Qrops provider that meets the qualifying criteria for HM Revenue & Customs.”

The policy is likely to “damp” Qrops transfers to low-tax jurisdictions outside the EEA, including Gibraltar and the Malta, which are popular with wealthy UK citizens, experts say.

The 25 per cent tax charge will not apply to people moving to a country within the EEA, provided the Qrops provider is also based in the EEA.

“The person and the Qrops provider do not need to be in the same country, they just both need to be within the EEA. So, potentially, the new rules will have a lesser impact on people within the EEA,” Ms Griffin says.

But should the person’s circumstances subsequently change within five years of the pension transfer, she adds, it will be necessary to reassess whether or not an overseas transfer charge applies.

The government also confirmed that it was to push ahead with a cut to the money purchase annual allowance (MPAA), which will restrict future pension saving for over-55s who have made the most of the pension freedoms.

The move to cut the MPAA from £10,000 to £4,000 (http://next.ft.com/content/c6b309d2-b192-11e6-a37c-f4a01f1b0fa1) from April 6 was announced in the Autumn Budget and was aimed at restricting opportunities for over-55s to recycle pensions tax relief. But it sparked widespread opposition in the pensions industry.

“We’re disappointed the chancellor is continuing with his proposals to cut the MPAA for those who have exercised pension freedoms,” says Kate Smith, head of pensions at Aegon, a pension provider.

“Only two years on, we’re already seeing the pension freedoms unravelled, based on no evidence that people are deliberately trying to abuse the pension tax system.”

“We expect few people will be aware of the risks they’re running by continuing to make pension contributions, once they’ve begun accessing their savings.”

Separately, the government also revealed this week that it had raised nearly five times (http://next.ft.com/content/aa48c1c0-0411-11e7-aa5b-6bb07f5c8e12) as much tax revenue from the pension freedoms as it had expected, after over-55s cashed in more of their pensions at a faster rate than anticipated.

While the Treasury had estimated an extra £300m in tax in the 2015-16 tax year as a result of the pension freedoms, it ended up raising £1.5bn.

The £1.1bn it now expects to raise this tax year is itself almost double the initial £600m estimate.

“These figures raise interesting questions about how people are using pension freedoms,” says Vince Smith-Hughes, retirement expert at Prudential.

“It is clear from this data that the tax taken from pension freedoms is considerably higher than originally expected — this having been caused by larger withdrawals — including in some cases all of the fund being withdrawn in one go.”

Philip Hammond © AFP

Other measures

● **Making tax digital review:** Consultation announced on the design aspects of the tax administration system (http://next.ft.com/content/1cac7c94-f435-11e6-95ee-f14e55513608)including interest and penalties, with the aim of adopting a consistent approach across taxes. Businesses with a turnover of less than £83,000 will have an extra year before the "making tax digital" reforms come in.

● **Tax avoidance:** **New penalties (http://next.ft.com/content/ee3d13ac-0413-11e7-ace0-1ce02ef0def9)**for people who facilitate tax avoidance as part of a drive to "enhance the fairness of the tax system". The government announced there would be "tough" penalties for professional enablers of tax avoidance ploys that were later defeated in court.

● **Mobile phones:** Consumers will face higher costs for using mobile devices (http://next.ft.com/content/ee3d13ac-0413-11e7-ace0-1ce02ef0def9)outside the EU, after the Treasury imposed 20 per cent value added tax on roaming telecoms services. Flagged in the Autumn Statement.

● **NS&I Savings bond**: Mr Hammond confirmed that the National Savings & Investments bond (http://next.ft.com/content/e273c41e-03e9-11e7-ace0-1ce02ef0def9) will be available from the autumn, and will pay 2.2 per cent on deposits up to £3,000.

● **Personal allowances:** In 2017-18, the personal income tax allowance for England, Wales and Northern Ireland rises to £11,500 (and the allowance will reach £12,500 by the 2019-20 tax year). The higher-rate threshold will increase to £45,000.

● **Rent-a-room relief:** A consultation will be held on proposals to redesign rent-a-room relief to ensure it is better targeted to support affordable longer-term lettings. No timescale for the consultation set.

● **Taxation of benefits in kind**: The government is to publish a call for evidence on exemptions and valuation methodology for the income tax and employer national insurance contribution treatment of benefits in kind.

● **Parental benefits for self-employed**: The government will consider whether there is a case for greater parity in parental benefits between the employed and self-employed. Currently, the self-employed qualify for maternity allowance at the flat rate of £139.58 (or 90 per cent of their earnings if lower) for 39 weeks during maternity. Employees receive the same amount in statutory maternity pay for the last 33 weeks, but during the first six weeks, they qualify for 90 per cent of their pay as SMP.

● **Childcare:** The tax-free childcare (TFC) policy (http://next.ft.com/content/8e123f26-faad-11e6-bd4e-68d53499ed71), which provides parents with children under the age of 12 with up to £2,000 a year per child to help towards childcare costs, will be rolled out from April 2017. The government also confirmed that parents with children who are three and four years old will see their free childcare entitlement increase from 15 hours to 30 hours a week from September 2017.

● **Non-dom rules**: Extension of the rules governing non-doms bringing overseas (http://next.ft.com/content/3614a276-0423-11e7-aa5b-6bb07f5c8e12) monies to the UK could see more cash flow into the country. There will be a two-year respite on the rules on repatriating mixed funds, comprising more than one type of income or capital.

• **Sin taxes:** No increases in alcohol or tobacco duties (http://next.ft.com/content/0b0dfdde-03fb-11e7-aa5b-6bb07f5c8e12) on top of those previously announced. Tobacco will rise by 2 per cent above retail price index (RPI), and duty on beer, cider, wine and spirits will increase in line with RPI. Fuel duty frozen for a further year.

• **Consumer protection:** Plans were announced to end the cycle of "subscription traps", where people sign up for a paid-for service without meaning to, such as when a paid subscription starts automatically after a free trial has ended. New measures to be considered in a green paper in the summer.

• **Return to work fund**: £5m to support people returning to work after a career break.

Reporting team: James Pickford, Aime Williams, Josephine Cumbo, Vanessa Houlder and Lucy Warwick-Ching

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