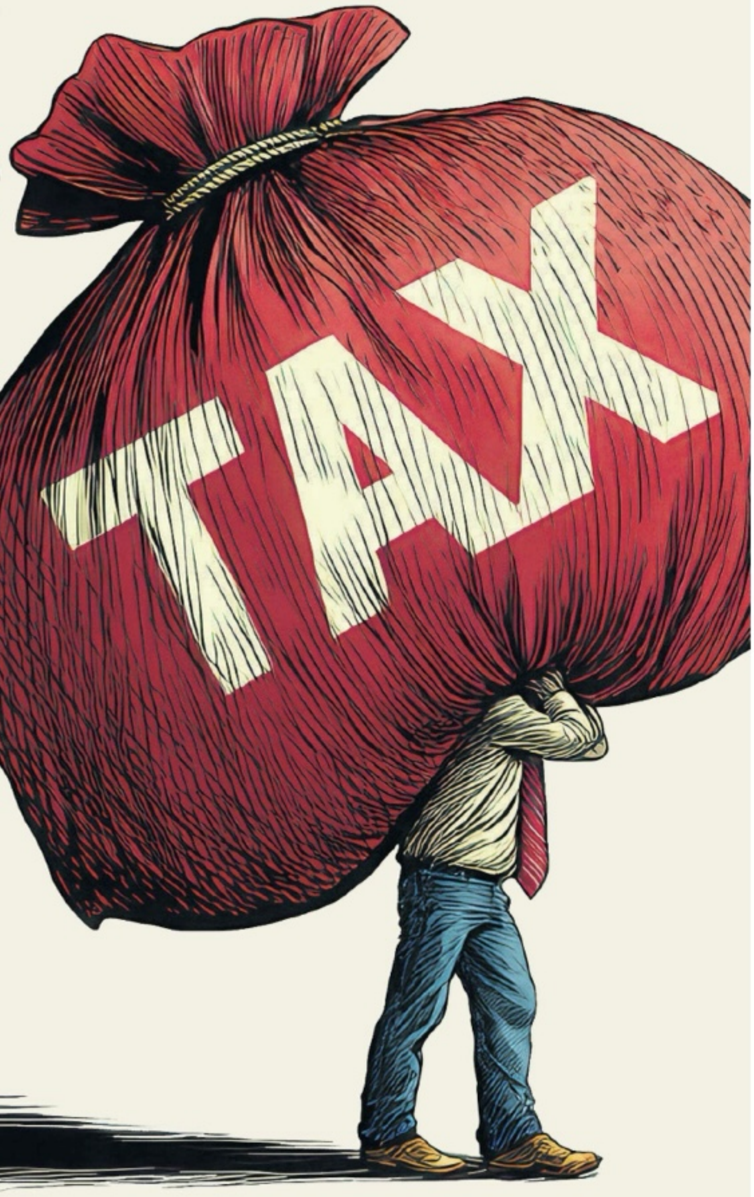
Budget Special

Money

AS THE COUNTDOWN BEGINS...

How to escape yet another big squeeze



The budget on November 26 is likely to be bad news for already hard-pushed taxpayers. Here's **Imogen Tew**'s guide to easing some of the pain

When Rachel Reeves stood up in the Commons last October to deliver her maiden budget as chancellor, she admitted that she had made some "very difficult decisions on tax" to restore stability to the public finances.

Then came a barrage of tax increases for employers, second-home owners and investors, while the chancellor laid the ground work for making pension savings liable to inheritance tax.

That tax-raising budget came not long after the Conservatives had been voted out of government, having started a deep freeze on tax thresholds that, combined with rising prices and wages, has meant millions more of us paying higher rates of tax.

Fast-forward nearly a year and the country is bracing itself for another bruising budget. Reeves's second budget will be on Wednesday, November 26, and she said this week that had "more to do".

With another, far larger, multibillion-pound black hole reportedly in the nation's finances — and Torsten Bell, the pensions minister and former head of the left-wing think tank the Resolution Foundation, now at the helm of budget preparations — it seems certain that considerable tax rises are coming. Before the election Labour pledged to not raise income tax national insurance or VAT for "working people", but it may be running out of wriggle room.

Any increases will come on top of what is already the highest tax burden since the Second World War.

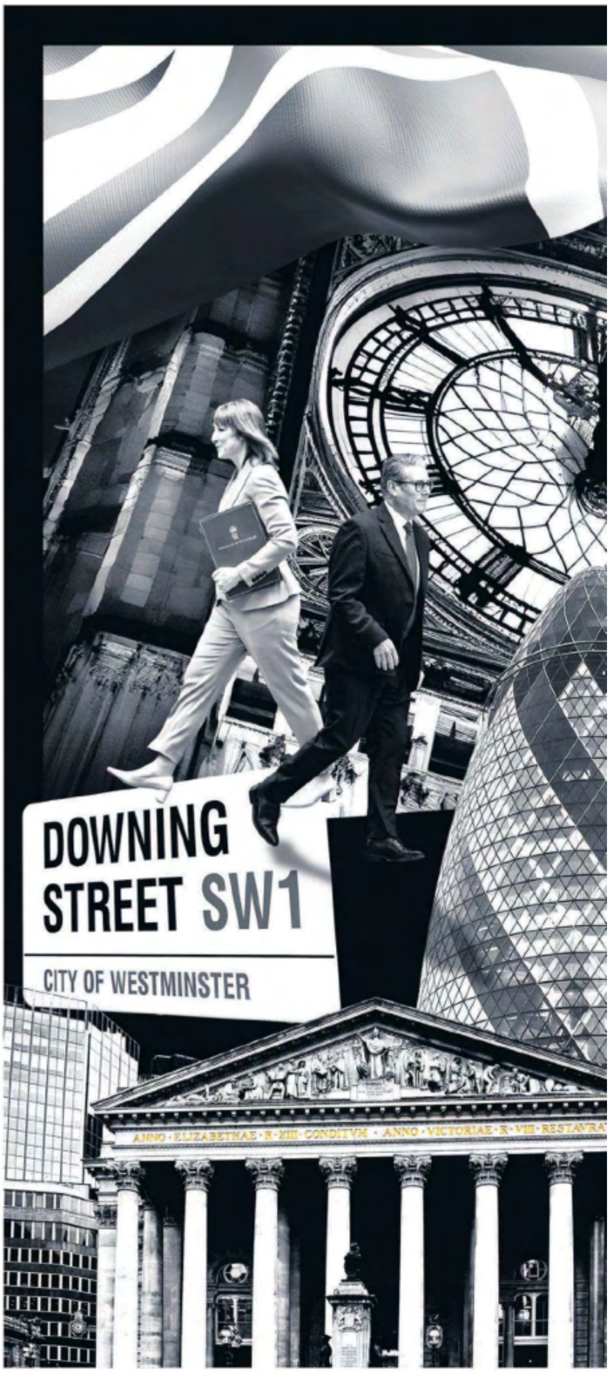
Critics have called for the government to rein in spending rather than increase taxes. But it may have to do both. With government borrowing costs at their highest level in 27 years, this is not a situation that the chancellor can borrow her way out of.

So, the countdown to November begins, with savers, workers and pensioners up and down the country wondering what the budget will mean for them — and what they can do to prepare for it.

Here, in our Budget Special, Money examines what is potentially in the chancellor's crosshairs, and how you could protect some of your wealth from Britain's relentless squeeze.

See pages 56-57

What to expect from the budget — and what you should do now



There are five main areas that the chancellor can target as she attempts to balance the nation's books. **Imogen Tew** looks at the potential damage

Your home

With about £5.7 trillion of wealth locked up in property, it's unsurprising that the chancellor is thought to be eyeing up ways to further tax your home.

Reports suggest that Reeves could impose capital gains tax (CGT) on sales of high-value main homes. This could hit homeowners with huge bills. If the high-value threshold was set at £1.5 million, for example, then higher-rate taxpayers selling with a gain of about £830,000 would get a CGT bill of about £200,000.

"The biggest fear for people is a tax on their homes," said Daniel Austin from the property finance company ASK Partners. "High-end homeowners are particularly worried about CGT changes or new levies."

Other property tax suggestions have included a new yearly levy on homes worth more than £500,000, or replacing stamp duty with an annual property tax. Nimesh Shah from the tax firm Blick Rothenberg said property wealth was an easy target. He said: "You need somewhere to live, so there's little you can do quickly. Some of our more mobile clients will sell their UK properties, preferring to rent when in the country and have wealth elsewhere."

If you are already selling, it could be worth pushing to complete before November so that you still get the capital gains tax exemption. Another option would be to transfer property to family members before the budget, although this involves legal and financial complexity, especially if mortgages are involved.

Tim Stovold from the accountancy firm Moore Kingston Smith said families could consider such moves if there are more hints of government plans, but warned against hasty action. "Transferring properties or sharing ownership adds significant complication," he said.

Advisers urge against rash moves based solely on speculation — only act to beat the budget deadline if you had already planned to make a move.

Your pension

Pensions rarely escape attention at budget time. Last year Reeves ruled that from 2027 pension pots would form part of estates for inheritance tax, and could be taxed at up to 40 per cent, depending on who you leave them to.

There are now fears that the beloved tax-free lump sum, which allows you to take 25 per cent of your pension tax-free (up to £268,275), could be reduced or even scrapped.

Rebecca Penny, a financial adviser from Norwich, said: "People are concerned that careful financial planning over many years will now be disrupted. We aren't talking about flash holidays and new cars, it's more about paying off the mortgage."

Such rumours, coupled with the inheritance tax threat to pensions, has prompted many to take their tax-free lump sums now and give them away. Again, this is only sensible in certain cases. Aysha Marley from the tax firm RSM said that some who took their tax-free lump sum before last year's budget tried to "reverse" their decision afterwards when they realised that the chancellor had not changed the rules.

£60k

The maximum you can pay into a pension each year and get full tax relief

Other rumoured changes include limiting income tax relief on pension contributions to 20 per cent (which would hurt higher and additional-rate taxpayers, who get 40 or 45 per cent relief) and making pension contributions made through salary sacrifice liable for national insurance.

Stovold suggests paying in as much to your pension as possible before the budget to benefit from full tax relief, if you can afford to. You can pay in up to £60,000 a year (or 100 per cent of your salary, whichever is lower) and get full tax relief, and carry forward unused allowances for three years.

Your savings

While there has been much talk of the government creating a wealth tax, it is more likely that wealth will be targeted through changes to the tax rates on capital gains and dividends.

In the last budget CGT rates went from 10 per cent to 18 per cent for basic-rate taxpayers and from 20 to 24 per cent for higher-rate taxpayers and some suspect that the higher rate could be go up further to 30 per cent.

Dividend tax rates could be increased to match income tax rates, rising from 8.75 per cent to 20 per cent for basic-rate taxpayers, from 33.75 per cent to 40 per cent for higher-rate payers and from 39.35 per cent to 45 per cent for top-rate taxpayers.

The easiest way to protect your money from dividend tax and capital gains tax is to ensure that you use all your allowances. You can pay £20,000 into an Isa every year and all growth and income earned from cash and investments held within that Isa is tax-free. Another £60,000 can go into a pension, tax-free. You can earn £500 a year in dividends tax-free outside an Isa and £3,000 a year in capital gains, tax-free.

Scott Gallacher from the financial planning firm Rowley Turton said: "My advice would be to take advantage of all types of allowances in advance of the budget if you can. I can't imagine that the budget will give much for anyone to cheer about."

Cash savers are unlikely to see any change to the personal savings allowance (the amount of interest you can earn each year tax-free), which has been stuck at £1,000 a year for basic-rate taxpayers and £500 for higher-rate taxpayers since it was introduced in 2016. Additional-rate taxpayers get no allowance. Again, maximising your Isa allowance is the best way to protect your wealth.

Your income

Income tax thresholds have not changed since April 2021 and have been frozen until at least 2028, adding billions to the Treasury coffers — the Office for Budget Responsibility estimates that it will raise more than £38 billion in the 2029-30 tax year. Many believe Reeves will extend the freeze.

Laura Ripley from the West Midlands financial planning firm BRI Wealth Management said: "It's the most likely outcome; although not a headline rise, this fiscal drag gradually pushes more people into higher tax bands as wages increase, reducing real disposable income."

If a bump in wages is going to push you over a tax cliff-edge (whether that's over the £50,270 higher-rate income tax threshold, the £100,000 point at which you start to lose your tax-free personal income allowance or the £125,140 additional-rate tax threshold), you could consider paying more into your pension to keep your income below the limit.

If your income is from buy-to-let properties or investments, you may be concerned by speculation that national insurance payments could be charged on rental and investment income. National insurance is levied at 8 per cent on income between £12,570 and £50,270 and 2 per cent on income above this.

Austin said: "For landlords, reviewing ownership structures is essential. It is now generally more efficient to hold buy-to-let property through a company because then you pay corporation tax on profits, rather than income tax and potentially national insurance on rental income, and can offset expenses. In many cases selling properties and lowering debt levels is advisable."

Your legacy

Regardless of what happens in November, your inheritance tax liability is likely to grow. The Office for Budget Responsibility (OBR) expects that by 2030 some 10 per cent of estates will be subject to

ILLUSTRATION BY PAUL BROOKBANKS

> If you are planning to give away a large sum, do it before the budget and keep detailed records

inheritance tax — double the proportion affected today — because of pension changes and frozen thresholds.

And this could go even higher after the budget. Anything you give away throughout your life is tax-free if you live for seven years after making the gift, but there are reports that this could be subject to a lifetime limit. The chancellor is also said to be looking at abolishing taper relief, which reduces the rate of inheritance tax payable on gifts made at least three years before death.

Alex Shields from the wealth manager The Private Office said he had had a flurry of worried messages from clients about the potential changes. "Everyone uses gifting as a way to minimise inheritance tax, so it is something the government could easily target," he said. "The fact that it is unlimited means that you can give away millions of pounds completely tax-free seven years before you die."

One way to cover an inheritance tax bill for your beneficiaries is to take out something called whole of life insurance, according to Alice Haine from the wealth manager Evelyn Partners.

If you are married or in a civil partnership, then opt for a "joint life, second death" policy, which covers you both but only pays out on the second death. This is because anything left to a spouse or civil partner is inheritance tax-free, so they will not have to pay anything if you die first. Haine said: "Take out the policy, have it written into trust so that the payout does not form part of your estate for inheritance tax purposes and your beneficiaries can use the proceeds to promptly settle the tax bill."

And if you are planning to give away a large sum or valuable item, then do it before the budget and keep a detailed record.

Shields said: "With all of this, whether it be Isa allowances, pension contributions or giving money or assets to your family, if you are planning to do something and it won't harm your finances, then why not do it before the budget? Get it done — the tax regime is only going to get more punitive."