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personal finance commentary and opinion

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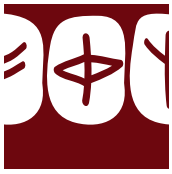

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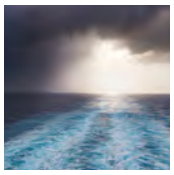

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If you have an idea for an article of something you would like us to investigate, please email the Holden & Partners Review team at:

info@holden-partners. co. uk

Welcome to the latest edition of H&P Review. Although we are only three months into 2016, it is shaping up to be both an eventful and unpredictable year.

Investment markets and economists have been acting strangely. By the end of 2015 market commentators were clamouring for an interest rate rise from the Federal Reserve, to restore confidence. Normally, the only reason to raise rates is if there is inflation in the economy and you want to eradicate it. The issue is that there was, and is, little inflation in the US or almost anywhere else, at the end of 2015. So, despite that, the markets got the rise that they wanted and… it helped lower economic activity, precisely as one would expect, which has had a decidedly negative impact on confidence.*

Traditionally January is a good month for equity markets, especially in the US, as new monies enter investment funds at a faster pace than is true for the rest of the year. 2016 has begun with a number of hangovers from 2015, which have meant the bears rather than the bulls have gained traction. The three main fears centre on China, oil and the risk of a global recession. Throw in a very unpredictable US election, a potential British exit from the EU, and economically speaking, 2016 becomes even more difficult to forecast.

It is true that the Chinese authorities' efforts to bring about an orderly economic slowdown remain a big source of concern and will do so for some time. However, the fears do seem to have subsided for now. Some commentators are predicting reduced growth of 4% a year over the next 10 years, which, although nowhere near previous levels, would certainly help bring about a sense of stability to the global economy.

Falling oil prices clearly cause a sense of unease in markets, however, if we are now seeing oil prices stabilise at a reasonable long-term level, the world economy should actually benefit. Nearly everything the consumer buys should become cheaper and this should stimulate spending on goods and services across the board.

So although negative sentiment currently prevails there are a few respected economic voices who think that the current state of the world economy is not quite as bad as others would suggest, with the positive effects of low resource prices being underestimated. Jeremy Grantham, the respected US investment manager suggests that both the US and global economies are likely to do significantly better this year than recent opinions predict, and that the U.S. has plenty of spare capacity to grow above its longer-term limits*. As always, time will tell.

In the latest edition of H&P Review Jack Rawcliffe looks at the implications of a UK exit from the EU, Stefani Rogers reviews the dividend tax regime, Amelia Sexton discusses the impact of the UN Paris agreement, Neil Sargeant looks at the latest round of proposed changes to pensions and Aram Kupelian considers how the new inheritance tax regime will work. Finally, Reece Biggadike evaluates end of tax year planning opportunities.

* Source: Mark Blyth Guardian 9th February
** Source: GMO Quarterly letter Q 42015

Steven Pyne
Financial Adviser
& Partner

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the rapidly reducing lifetime allowance

From 6 April 2016, the Lifetime Allowance (LTA) is reducing from £1.25M to £1.0M.

There is some respite in that this limit will be indexed in line with CPI from April 2018. Many of you will be familiar with the LTA and Fixed Protection. However, to summarise, while there is no limit on the total benefits you can accrue in your pensions, there is a LTA on the amount that you can benefit from without a tax charge. The LTA is tested whenever benefits are taken from a pension, at which point you use up a percentage of the LTA. This is known as a Benefit Crystallisation Event (BCE) and the following events trigger a test:

- receiving your pension from a defined benefit scheme
- entering drawdown
- purchasing a lifetime annuity
- taking lump sums
- reaching age 75
- death
- transferring to qualifying recognised overseas pension schemes.

Protecting your Lifetime Allowance: Fixed and Individual Protection

There have been a variety of protections available since the LTA was introduced in 2006. By registering for protection, an individual can mitigate, in part or in full, the potential LTA charge on large pension funds. If you already have Transitional, Fixed or Individual Protection in place, these will continue to apply, unless you have lost them by making additional pension contributions or accruing further benefits via a defined benefit scheme. You should be particularly cautious of Auto-Enrolment into any workplace schemes.

Anyone who does not have Primary, Enhanced or Fixed Protection 2012 or 2014 can apply for Fixed Protection 2016 (FP16) and / or Individual Protection 2016 (IP16).

- FP16: Protects the holder's LTA at £1.25M after 6 April 2014
- IP16: Available to those with funds valued at or above £1M as at 5 April 2016. Protects the value up to a maximum of £1.25M while allowing further contributions or benefit accrual

The application process differs this year in that there is no application deadline and no certificates will be issued. Instead, the member (or their authorised representative) will apply online and be provided with a protection reference number. This reference must be applied before any benefits are taken, to ensure the correct treatment. The online portal will not be available until July 2016, so if required urgently prior to drawing benefits, written applications to HMRC can be made.

Exceeding Lifetime Allowance

Any pension savings above the Lifetime Allowance are subject to the Lifetime Allowance charge. This continues to be levied as follows:

- 55% if the excess is taken as a lump sum
- 25% if the excess is taken as income. Income tax at your marginal rate will also be payable.

Key Considerations

- Value of benefits: The initial indicator will be whether the existing fund is approaching the reduced limit. However, your age or length of time to retirement should also be noted
- Age / time to retirement: The longer the timescale to draw benefits, the harder to predict the position and therefore the best option. A relatively small pot could increase substantially with tax efficient, compound growth over the course of, say, 15 to 20 years
- Risk profile: The level of potential investment returns will influence the future value of the pension
- Contributions: Are contributions being made by you / your employer. If so, is there an option to opt out, and if so, would the employer benefits be lost or paid in another way?

Each set of circumstances are different and the above factors are interlinked. The impact of the tapered annual allowance will exacerbate the issue for high earners. Accordingly, a discussion around the above factors and a personalised projection can help make an informed decision as to whether you will have LTA issues and, if so, how best to address these.

Neil Sargeant
Paraplanner

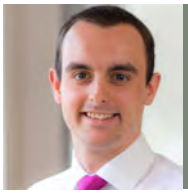

Bank of England data suggests that of the £17 trillion of global foreign direct investment (FDI) in 2013, a staggering 74% involved the EU in some capacity

sailing away?

Should the UK remain a member of the EU or not?

This is the question that will be put to the UK population on June 23rd and will determine the UK's continued membership of the twenty-eight-member union. In recent months numerous parties, spanning business groups, politicians and media outlets, have revealed which side of the divide they are on, validating their positions with a myriad of contrasting arguments. Given this conflicting backdrop, ordinary members of the public, the ultimate decision makers, could be forgiven for losing sight of the actual arguments for and against remaining a member. So, what are these arguments?

The arguments for the UK retaining its membership of the EU are predominantly economic and political in nature. From a trade perspective, membership simplifies rules on exporting to other EU countries, providing UK businesses smooth, relatively unrestricted access to over 505 million consumers, eight times the UK consumer pool. Such ease of access is important, given the fact that the EU is comfortably the UK's largest trading partner, accounting for £229 billion, or 44%, of all UK exports in 2014. UK consumers are beneficiaries of membership too, as not only does it provide far greater choice, but it ensures domestic companies are governed by the forces of competition, helping to maintain competitive pricing. Were the UK to leave the EU, trade with the continent would still be possible but it may be on more restricted terms, with the possible imposition of tariffs or other trade barriers. Trade agreements



Jack Rawcliffe
Investment Analyst

continued over

with each member country may also have to be negotiated, requiring UK firms to comply with multiple sets of regulations, as opposed to the single framework that prevails now.

Alongside the trade-related argument is investment. When treated as a single entity, the EU is the largest economy in the world, which inevitably attracts large investment flows. In fact, such is the EU's allure, Bank of England data suggests that of the £17 trillion of global foreign direct investment (FDI) in 2013, a staggering 74% involved the EU in some capacity. A little under £500 billion of this flowed through to the UK directly, contributing 46.5% of the UK's total FDI for that year, making the EU by far the UK's largest investment partner. These points imply that no longer being a member risks the UK becoming an isolated and marginalised voice when it comes to attracting future FDI, which may impact employment and somewhat suppress growth opportunities domestically.

Less FDI and fewer opportunities for growth could have the added consequence of businesses opting to allocate capital elsewhere or even relocate operations to what are perceived to be more attractive business environments.

Relinquishing membership of the EU would also have repercussions from a financial market standpoint. Credit rating agencies, such as Standard & Poor's, have already warned that they would likely cut the UK's much-cherished AAA credit rating, citing the 'economic implications' of the UK leaving. A rating downgrade would raise the cost of borrowing for the UK Government, at a time when public finances can ill afford it. Further, London's status as one of the world's leading financial centres may come under threat, as financial institutions with major operations, or even headquarters, in the city reconsider the status quo in a world where the UK stands alone. Obviously, this would have the potential to impact jobs and investment, affecting economic growth longer term.

Politically, membership grants the UK significant influence over the future direction of the EU. The UK currently enjoys the joint highest number of votes at the EU Council – the body that defines the overall political direction of constituent countries – allowing it to guide future policies to the benefit of the UK, its businesses, and its people. Withdrawing membership would mean the loss of this influence and no representation of British interests in Brussels, yet UK businesses would still be forced to abide by EU regulations when exporting to member countries.

Whilst the arguments for EU membership are valid, there are, unquestionably, arguments against.

The first, quite simply, is cost. It costs a considerable amount of money to be an EU member. Figures from the Office for Budget Responsibility (OBR) show that in the 2014/15 financial year, the UK's contribution to the EU budget was £10.4 billion. Forecasts for 2015/16 suggest this figure will increase 8.65% to £11.3 billion. Put into context, this latter figure is 34% higher than the £8.425 billion budget awarded to the Department for Transport, or, put another way, more than the budgets of the Department for Work and Pensions, Department for Culture, Media, and Sport, and the Foreign and Commonwealth Office combined, with £1.44 billion to spare. It is little wonder, therefore, that some question the continued viability of the UK maintaining EU membership and whether or not this represents value for money, especially at a time of strained public finances.

A further argument against continued membership is legislation, centred on the view that EU directives hinder UK companies. In the financial arena, Brussels' aim to impose a tax on financial transactions is viewed by some as unfairly penalising London, Europe's de facto financial capital, to the detriment of the UK economy. In other sectors, many UK businesses have complained of onerous and costly-to-follow EU legislation, inhibiting growth and forcing prices to rise for the end consumer. In total, analysis by British economist Tim Congdon suggests EU regulations cost the UK 5–6% of GDP per year, which could be recaptured were the UK to leave.

Immigration is an additional point to consider. While it is widely acknowledged that migrants from the EU enrich the UK economy, some commentators believe that their number has grown too great and that membership renders the UK powerless to control its borders, placing unsustainable burdens on some local communities and impacting the job opportunities for British people. A related concern is that 'benefit tourism' has flourished, the idea that, due to the EU's founding principle of the free movement of people between member states, EU citizens are coming to the UK to exploit the welfare system, whether it be use of the NHS or some other government-funded benefit.

Indisputably, then, there are strong arguments both for and against the UK being a member of the EU. Economic and political aspects underpin the argument for, while cost, legislation, and immigration support the argument against. It remains to be seen how the UK public will ultimately perceive these arguments and what significance they attach to them, but what is for certain is that the debate will be passionately contested by both sides in the run up to the referendum.

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pension annual allowance taper from 2016/17

The current Pension Annual Allowance for 2015/16 is £40,000 and this will continue for 2016/17, albeit with new restrictions for high-earners. From 6 April 2016, the annual allowance (AA) will be tapered for high-income individuals.

These are individuals who have 'adjusted income' of more than £150,000 and 'threshold income' of more than £110,000. These two checks are carried out in sequence to determine whether any reduction in AA applies.

Adjusted income

Adjusted income is tested first and this is broadly equal to all gross taxable income plus the total pension input (including employer contributions) less any personal pension contributions in the tax year. If this exceeds £150,000 then a check will also need to be made against threshold income.

Threshold income

Threshold income is then tested if the adjusted income limit is breached, and is equal to an individual's total income less personal pension contributions that qualify for tax relief at source. Threshold income will also include any salary sacrifice arrangements that started on or after 9th July 2015.

The two layers of testing intend to prevent those with a one-off spike in adjusted income, for example due to a large Defined Benefit pension accrual, being penalised.

Reduced allowance and tax impact

Those exceeding the adjusted income and threshold income levels, will lose £1 of the AA for every £2 of adjusted income above £150,000. This is subject to a minimum Annual Allowance of £10,000 for those with adjusted income in excess of £210,000.

The worst case scenario for those falling foul of the taper would be a tax bill of £13,500 (based on a £30,000 reduction in AA, at 45% marginal rate).

The tapered AA will need to be reviewed and recalculated annually as it is dependent on earnings and pension contributions in each tax year.

Carry forward

You will still be able to carry forward unused allowances to use in a tax year where the standard AA has been reduced. But the available carry forward from a tax year, where the annual allowance has been reduced by the taper, will be the balance of the tapered amount.

Key considerations

If you think you may be affected by the tapered AA, you should consider maximising your pension contribution in 2015/16, before the restrictions apply. You should also liaise with your employer to establish whether alternative remuneration is an option if you are forced to reduce your pension accrual with them.

A discussion and a personalised calculation can help make an informed decision on whether you will have taper issues and, if so, how best to address these.

Neil Sargeant
Paraplanner

tax planning opportunities

The run-up to the tax year end on 5 April 2016 is the perfect time to consider tax planning opportunities.

Of concern to some is the notional tax rate of 60%; this is due to the loss of the personal allowance when total income exceeds £100,000. Rather than earning less, the solution is to make a personal contribution to a pension or, alternatively, sacrifice part of your income – you need to do this before it has been received – to reduce your taxable income below £100,000 (and by default, the tax you pay). With personal contributions to pensions, basic rate income tax is granted at source, though you should also claim any marginal rate liability through your self-assessment return.

Salary or bonus sacrifice has the effect of reducing both your income and National Insurance (NI) contributions at source, so you receive immediate benefit without the need to claim back any tax relief. Employers are increasingly assisting employees who wish to do this, which has the effect of increasing the employee's net income. For the employer, the contribution can be treated as a trading expense, as well as reducing employer NI costs. In addition some employers will rebate part of the Employer NI saving to add to the pension. Salary sacrifice needs to be established in the correct manner to ensure HMRC accept it as a bona fide sacrifice, otherwise they will deduct tax and NI on the sacrifice.

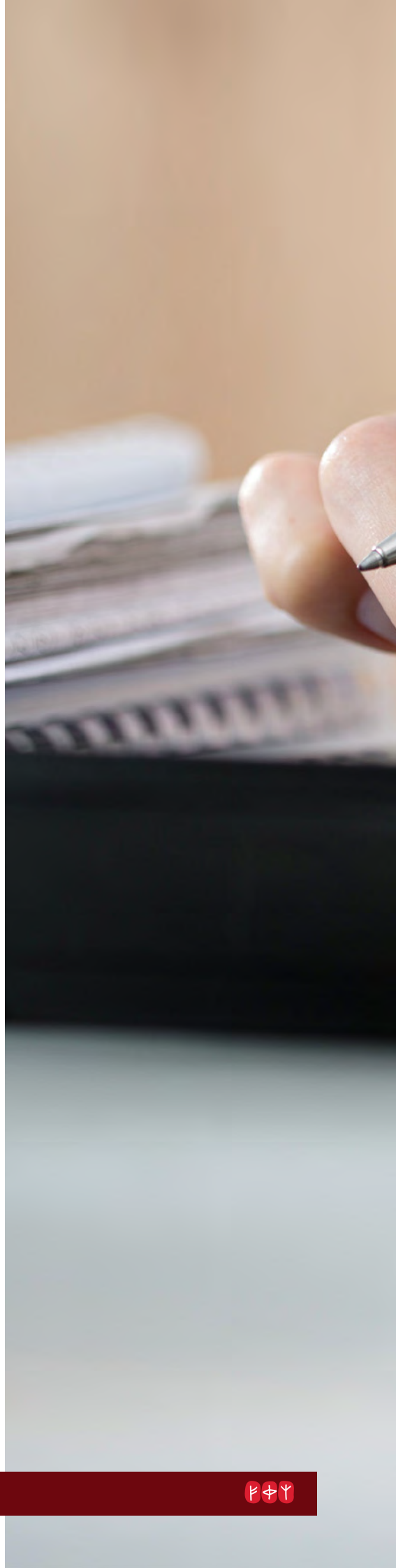
Pension contributions remain an attractive means of tax efficient long-term saving. Current rules allow you to contribute 100% of earned income, up to a limit of £40,000, per annum. However, up to £190,000 can be paid into a pension, through the use of carry forward of unused relief for up to three previous tax years, assuming you have not already used this allowance in those previous years. Care needs to be taken with on-going contributions, in particular where you are a member of a defined benefit scheme, such as that offered by the NHS, where the annual "input amount" – the notional value of each year's pension increase – can exceed the Annual Allowance (AA) and lead to an additional tax charge.

Significant changes to pensions were announced in the summer budget which will have an impact on how much you can contribute to pensions from the next tax year.

Those affected are individuals whose 'adjusted income' in the 2016/17 tax year, and later tax years, exceeds £150,000. 'Adjusted income' means the individual's income after adding back any employer pension contributions. This is to prevent individuals from avoiding the restriction by exchanging salary for employer pension contributions. New anti-avoidance rules will apply, so that any salary sacrifice set up on or after 9 July 2015 will be added back to income for the purpose of the £150,000 income test. Car allowance etc. will also be included.

Note: 'Income' is not explicitly defined in the announcements, and it could well include investment income, e.g. dividends, rent, interest, etc., in addition to income from employment or self-employment.

For those individuals affected, the AA will be reduced by £1 for every £2 that the 'adjusted income' exceeds £150,000, up to a reduction of £30,000 and therefore an effective maximum contribution of £10,000 per annum.



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The solution (to a notional tax rate of 60%) is to make a personal contribution to a pension or, alternatively, sacrifice part of your income

The existing rules that allow unused AA to be carried forward will continue to be available, but the amount available will be based on the unused reduced AA.

The tax year 2015/16 has been split into two mini tax years. The first part is from 6th April to 8th July and this is called the pre-alignment tax year. The AA for this part is £80,000 (plus any carry forward from the three previous tax years).

The second mini tax year runs from 9th July to 5th April 2016 and is known as the post-alignment tax year. This mini tax year has a nil AA but has the ability to use carry forward from the prealignment year of up to £40,000

Individuals with large pensions should note that the LTA will reduce from £1.25 million to £1.00 million from 6 April 2016.

Do not forget your annual Capital Gains Tax (CGT) exemption, currently £11,100 in 2015/16. Where you have assets that are not held in a tax privileged environment, for example directly held shares or unit trusts, realised gains of more than £11,100 in any one tax year are subject to CGT at either 18% or 28%. A process of controlled use of the allowance to rebase your investments would improve your tax position in the longer term. If you have realised any capital loss during 2015/16, you should ensure that the loss is stated on your tax return. The loss can be allocated against gains realised in the year, any losses that are not set against gains in that year, can be carried forward indefinitely to be set against capital gains in future tax years.

Make sure you fully use your tax efficient Individual Savings Account (ISA) allowance. For those that have yet to pay the maximum into your ISAs, you can invest up to £15,240.

This means that married couples, for example, could put up to £30,480 between them into ISAs this tax year (before 5 April) and a further £30,480 from 6 April. Junior ISAs can be used to provide long-term savings for a child's future. You can save up to £4,080 per child.

Meanwhile, the Help to Buy ISA offers unique incentives to those looking to buy their first home. If you're saving for your first home, you can deposit up to £200 a month in a Help to Buy ISA (plus an additional initial deposit of £1,000), with the government topping up these savings by 25%, up to a maximum bonus of £3,000. You can use Help to Buy ISA savings to buy a home worth up to £250,000, or £450,000 in London. Individuals cannot hold both a Help to Buy ISA and a Cash ISA. Only one ISA can be held in a tax year.

For those who perhaps do not want to, or are unable to, consider contributing to a pension, we are now entering the season for new Enterprise Investment Scheme (EIS) and Venture Capital Trust (VCT) offerings, so if you have already maximised your ISAs by contributing £15,240 before April, the ability to receive 30% relief on your investment may be attractive.

If you are married and do not own assets in some form of joint ownership, it may be advantageous, for tax purposes, to transfer to joint ownership. Consider transferring savings and investments to your spouse if they pay a lower rate of tax.

Meanwhile, the Marriage Allowance means that in this tax year up to £1,060 of an individual's personal allowance may be transferred by eligible spouses or civil partners to their husband, wife or civil partner, providing neither of them pays tax at the higher rate. This can reduce the tax burden by £212.

For those that donate to charity, the gift aid scheme is for gifts of money to charities by individuals who pay UK tax. Charitable donations are regarded as having basic rate tax (20%) deducted but if you are in the higher income tax bracket, you can claim the difference between this and the higher rate through your tax return.

Reece Biggadike
Financial Adviser

dividend revolution

With the aim of updating what George Osborne calls an 'arcane' and 'complex' dividend tax regime, a substantial overhaul of the way dividends are taxed is due to be introduced on the 6th April 2016.

This change is predicted to generate more than £2bn during 2016/17, making it one of the largest revenue-raisers in last year's Summer Budget. From this, it's easy to see that these changes are likely to impact a significant number of individuals in receipt of dividend income.

Stefani Rogers
Financial Adviser

Before we look at the new method of taxing dividends, we thought it would be worth reviewing the existing regime.

Present Regime

Currently, dividends paid by companies to individuals are notionally 'grossed up' by 10% before being taxed, i.e. 'net' dividends (the value which is paid into your account) are multiplied by 10/9 to produce a 'gross' dividend. For example, a dividend of £90 is grossed up to £100, and it is this higher amount which is taxed at either 10% (basic rate tax payers), 32.5% (higher rate tax payers) or 37.5% (additional rate tax payers).

The difference between the net and gross dividend (the 'tax credit') is subsequently subtracted from the liability. As a result, the net effective liability on dividend income equates to:

Basic rate: 0%
Higher Rate: 25%
Additional Rate: 30.5%

New Regime

Under the new system, the grossing up of dividends will cease, the tax credit will be abolished and a new tax free dividend allowance of £5,000 will introduced. Dividends will continue to be eligible for the personal allowance for income tax (£11,000 in the 2015/16 tax year). Therefore, if you have £16,000 of dividend income (and no salary), no tax will be payable.

Dividends above the allowance(s) will be taxed at the following rates:

Basic rate: 7.5%
Higher rate: 32.5%
Additional rate: 38.1%

Going back to our previous example of a £90 net dividend, under the new regime, both the notional grossing up and netting down will be abolished. You will continue to receive a £90 dividend and the level of dividend you receive will not change.

How will this affect investors?

For those receiving dividends from ISAs and pension funds, the dividends received will remain tax free. If the dividends you receive from a taxable portfolio are below £5,000 per annum the income received will also be tax free.

However, if dividends are drawn (outside of a tax efficient wrapper) above the dividend allowance, tax will be payable. We explain the tax situation in a few examples below. Please note that we are assuming that all dividends are drawn from an investment outside of an ISA or pension:

EXAMPLE ONE
Salary £18,000
Dividends £22,000

- The £18,000 salary takes up the entire personal allowance of £11,100.
- The first £5,000 of dividends is included within the dividend allowance.
- As a basic rate tax payer, the next £17,000 of dividends is taxed at 7.5% (basic rate).

This is calculated as follows:

Salary	£18,000
Less personal allowance	-£11,100
Salary subject to income tax	£7,000
Dividends	£22,000
Less Dividend Allowance	-£5,000
Taxable dividends	£17,000
Dividends taxed at 7.5%	£1,275

In this example, you will pay £1,275 more in dividend tax in 2016/17 then you would in 2015/16.

(continued over)

The majority of small business owners will be worse off following the changes. (But) there are several ways in which you can minimise the negative impact of these changes.

EXAMPLE TWO
Salary £42,000
Dividends £9,000

- The £42,000 salary takes up the entire personal allowance of £11,100.
- The first £5,000 of dividends is included within the dividend allowance.
- As a higher rate tax payer, the next £4,000 of dividends is taxed at 32.5% (higher rate).

This is calculated as follows:

Salary	£42,000
Less personal allowance	-£11,100
Salary subject to income tax	£31,000
Dividends	£9,000
Less Dividend Allowance	-£5,000
Taxable dividends	£4,000
Dividends taxed at 32.5%	£1,300

In this example, you will pay £1,300 more in dividend tax in 2016/17 then you would in 2015/16.

How will the changes affect small business owners?

The current dividend tax regime was created more than 40 years ago when corporation tax was 50%. With Corporation Tax currently at 20% and reducing to 19% in April 2017, the Government are of the opinion that many people now set up limited companies simply to save tax. It's therefore not surprising that the majority of small business owners will be worse off following the changes.

Over the years, individuals have taken a combination of both salary and dividends to reduce their overall tax and National Insurance liability. From April 2016, although taking a higher level of dividends can still be a better option, this tax gap is closing and it is therefore important that you speak with your tax adviser to establish the most tax efficient route for you.

Salary £8,060
Dividends £60,000

For business owners, £8,060 is the most tax-efficient salary to pay yourself in the 2015/16 tax year.

- £8,060 salary is included within the personal allowance of £11,100.
- The first £2,940 of dividends is included within the personal allowance (£11,000 - £8,060).
- The next £5,000 of dividends is included within the dividend allowance.
- The next £27,000 of dividends are taxed at 7.5% (basic rate).
- The remaining £28,000 of dividends are taxed at 32.5% (higher rate).

The calculation is as follows:

Salary	£8,060
Less personal allowance	-£11,100
Remaining personal allowance	£2,940*
Dividends	£60,000
Remaining personal allowance	-£2,940*
Less Dividend Allowance	-£5,000
Taxable dividends	£52,060
£27,000 taxed @ 7.5% (basic rate)	£2,025
£28,000 taxed @ 32.5% (higher rate)	£9,100

In this example, you will pay circa £4,000 more in dividend tax in 2016/17 than in 2015/16.

EXAMPLE THREE

Whilst some individuals may benefit from the changes (such as higher and additional rate tax payers with dividend income of £5,000 or less); many will pay more dividend tax. There are several ways in which you can minimise the negative impact of these changes:

- Utilise your ISA and SIPP allowances each tax year: dividends received from these accounts will continue to be tax free;
- Maximise your annual tax-free dividend allowance of £5,000 each tax year. Married couples should spread their taxable portfolios between themselves to make full use of this allowance.
- Use the new personal savings allowance for interest. From April 2016, the first £1,000 of interest income (£500 for higher rate tax payers) will be tax free.
- Contribute into a pension to increase the basic rate tax band.
- For those investors who are willing to accept a higher level of risk with their investments, consider investing in VCTs to generate tax-free dividends.

history is here

climate change negotiations get the green light, but what is the impact for investors?

With all the media furore surrounding the 21st Conference of the Parties in Paris, it is easy to lose sight of the specifics of the agreement and their immediate impact.

There is no doubting the importance of negotiations that, if failed, may have sounded the death knell for UN multilateralism and collective global efforts to tackle climate change, but the agreement itself is merely a stepping stone in limiting global warming to a manageable level. The physical effects of climate change, including extreme weather patterns, are increasingly prevalent. The agreement has not saved the planet, nor will it solve many of the problems that are associated with carbon emissions, not on its own at least. But it has set in motion something significant, something that could have a fundamental impact on the way companies in the fossil-fuel, environmental, and renewable energy sectors operate: a change in sentiment.

For the first time, it seems that there is unparalleled political recognition of the risk that climate change now poses and its effect on the global economy. So, is 'history' really here and if so, what does it mean for investors?

Participants in global financial markets have long been aware of the danger that global warming presents to the environment, but these considerations have not always featured prominently enough in investment decision-making.

Perhaps the culture of short-termism in asset management and focus on annual, or even quarterly, portfolio returns has obscured the importance of the longer-term threats to economic prosperity. It's easy to understand why; leading commentators in the scientific world are not predicting the severest environmental effects until 2050, and with an investment horizon of several years or less in many cases, what is the urgency for the majority of investors?

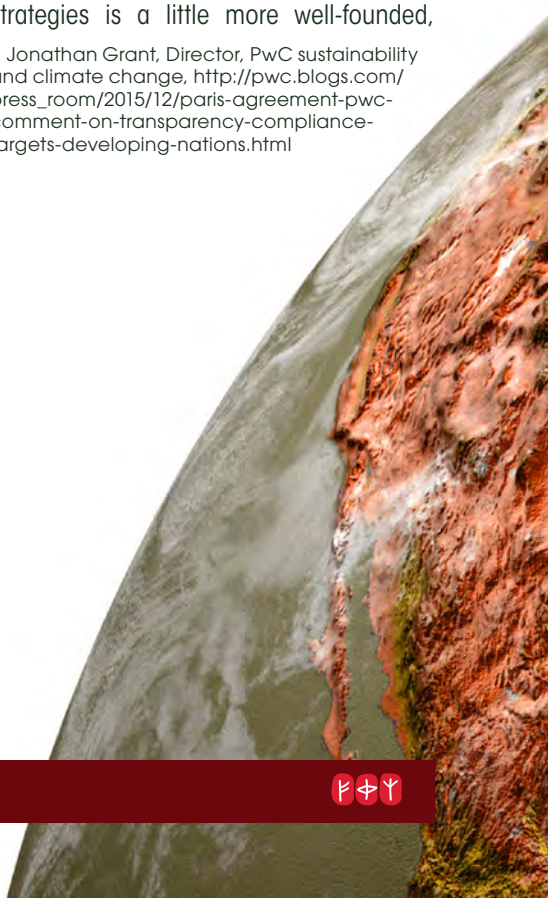
The incoherence of government policy on the issue has not helped, particularly in the UK where the Conservative Party have repeatedly vacillated between support and discouragement of clean energy alternatives, cutting subsidies under the guise of preventing a rise in consumer energy bills several times in the past year. Many investors are gaining a greater understanding of the implications of economic adjustment to climate change (or absence of) on portfolio returns, but bringing this rationale for investment into the mainstream requires coordinated action from governments, businesses, and financial institutions to put the economy on a solid path to a low-carbon future, and encourage investors to adjust their views on the most appropriate ways to allocate capital.

The Paris agreement is an important milestone in tackling these concerns. It achieves a number of objectives, albeit in a drastically different manner to that of the Kyoto Protocol, signed 18 years earlier. In essence, it does not legally require countries to cut emissions at all; the long-term greenhouse gas reduction target, formally adopted by the World's nations in somewhat vague language, is an aspirational goal to keep global temperature increases to 'well below' 2°C, and perhaps even to as little as 1.5 °C, not an obligatory pledge. Whilst this may seem completely nonsensical, and has led some environmentalists and academics to question the agreement's impact and even criticise its execution, there is good reason for this approach.

The failure of the Kyoto Protocol demonstrated the impracticalities of compelling national governments to meet sharp emission cuts that they did not necessarily want to follow, with the deal quickly losing momentum as it passed through the US Senate. The Paris negotiations therefore changed tack, allowing nation states to formulate their own reduction targets, and implementing a legally-binding process to review and report on efforts to achieve them, obliging countries to consider whether to strengthen policies every five years. In this respect, the agreement adds well-needed structure and momentum to initiatives that are already under way across the globe to limit global warming to a reasonable level. The negotiations may have incorporated a certain element of 'constructive ambiguity'[1] but the importance of this development should not be understated: it is the mechanism by which countries will be pressurised to deliver, and hopefully increase, their voluntary emissions targets over time; it is a signal that they are willing to do more than ever before to tackle the grave risks emanating from climate change.

The signal this sends to investors is one of certainty. Now that a commitment to limit global warming is in place, the belief that the world's governments are going to stay the course on their stated environmental strategies is a little more well-founded,

1 Jonathan Grant, Director, PwC sustainability and climate change, http://pwc.blogs.com/press_room/2015/12/paris-agreement-pwc-comment-on-transparency-compliance-targets-developing-nations.html



providing a favourable backdrop for investment in low-carbon sources of power. For those investors who were not already convinced by the long-term prospects for renewable energy generation, the agreement confirms the transition away from the fossil fuel era. For those that were, it underpins momentum in the growing development of the industry. This shift was reflected in market movements that occurred in the immediate aftermath of the agreement's announcement: the MAC Global Solar Energy Index surged 4.5 percent, whilst shares in a number of coal producers, such as Peabody Energy, declined dramatically[2]. Commodity market movements can be extremely fickle, but the early fluctuations seem to be a reflection of the change in sentiment that is now set in motion.

2 http://uk.reuters.com/article/us-climatechange-summit-stocks-idUKKBN0TX22A20151214

And this trend is unlikely to be short-lived. The fact that national policies will have to be reviewed every five years, provides the means to extend the scale of the current targets. The International Energy Agency, for example, estimates that over $16 trillion will be invested in renewables and energy efficiency over the next 15 years[3]. Indeed, in order to limit global warming to less than 2°C, most countries will have to make radical changes, and quickly – the voluntary targets proposed in Paris set the world on the path to 2.7°C of warming, far short of what is required. The initiatives that are now in place provide a framework for progression, and assurance that nation states are working together towards a common goal, but make no mistake: the Paris deal is just the start of the heavy lifting.

3 http://www.whebgroup.com/cop-21-did-it-change-the-world/

Sustainable investors are able to take advantage of a more certain environment, but it is how nations develop and implement their regional targets from here that will ultimately determine how successful the fight against climate change will be.

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nil rate band boost for homeowners

In the summer budget, George Osborne introduced a new main residence nil-rate band (MRNRB) for Inheritance Tax (IHT) purposes. This was with the intention of reducing the number of estates liable to IHT, which has been steadily increasing for many years.

Current rules: existing Nil Rate Band (NRB)

Currently, individuals can leave an estate valued up to the NRB (£325,000) free from IHT to their beneficiaries. Anything in excess of this amount will be subject to IHT at 40%.

Where an individual leaves everything to their husband, wife or civil partner, their estate will be exempt from IHT. It is also possible for married couples and civil partners to transfer their unused nil rate band to the surviving spouse, thereby enabling them to pass on assets valued up to £650,000.

New rules: MRNRB

An MRNRB will be introduced from April 2017, which will allow couples to pass up to £850,000 of their assets, including the family home, to their direct descendants free of tax.

The MRNRB will be phased in as follows:

- **£100,000 in 2017/18**
- **£125,000 in 2018/19**
- **£150,000 in 2019/20**
- **£175,000 in 2020/21**

It will then increase in line with Consumer Prices Index (CPI) from 2021 to 2022 onwards.

The outcome is that by 2020/21, each individual will have a NRB of £325,000, plus an additional allowance of £175,000, provided that their estate includes a property worth at least £175,000.

A point to note is that for estates with a net value of £2m, the MRNRB will be subject to a tapered withdrawal. For every £2 of value over £2M, £1 will be deducted from the MRNRB from 2017.

The 'family home' can be nominated if there is more than one in the estate with no requirement that the property is occupied as a residence throughout the ownership period. 'Direct descendants' has been defined as children, step-children, adopted and foster children, and grand-children.

Downsizing relief

This all sounds positive and means the burden of IHT will be reduced for some families. However it has been observed that people may be deterred from downsizing their properties, as it is no longer tax efficient.

Therefore, from 8 July 2015, the MRNRB will also apply to estates where homes have been downsized or converted to cash. In this instance, the MRNRB will still be available provided:

- The individual died on or before 6 April 2017
- The property disposed of was owned by an individual, and it would have qualified for the MRNRB had the individual retained it
- A less valuable property, or other assets of an equivalent value if the property has been disposed of, are in the deceased's estate
- A less valuable property and any other assets of an equivalent value are inherited by the individual's direct descendants.

As long as the disposal of the property occurred after 8 July 2015, there is no time limit on the period in which the downsizing or disposal took place.

These changes may have an impact on the best way to pass on your assets, and it is therefore important to review your estate planning strategy regularly, so you can pass on your accumulated wealth to your beneficiaries' estate in the most tax efficient way.

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