

# “A new dawn for financial planning?”

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**William Pratt, Director of Paradigm Norton, shares his view on how the new coalition government may impact upon financial planners.**



**What will the new coalition government mean for financial planners?  
All will be revealed on 22nd June (or will it?)**

Even before the general election result was known, it was clear that the parlous state of the UK economy and the size of our budget deficit was likely to result in a whole load of pain coming our way, whoever managed to grab the keys to Number 10. With the budget date now set for 22<sup>nd</sup> June, the “two for the price of one” coalition government we now have could prove to be a rare bargain.

Sadly, our erstwhile chancellor, Alistair Darling, failed to adhere to the golden rule of long term financial planning; spend less than you earn. It's therefore now down to George Osborne to reverse that. Simplistically, he has two levers at his disposal; spend less and earn more. Clearly the situation calls for both.

On the expenditure side, we already know where £6.2bn will be saved from, and the autumn Comprehensive Spending Review will identify many more spending cuts I'm sure. On the income side, other than selling the family silver (there's no gold left, Gordon already sold that), George Osborne must look to the tax system to generate a higher income. This means the unassuming British electorate attracted to the political rhetoric that promised “the restoration of economic stability” will soon find that was a euphemism for “you lot are going to have to cough up to get us out of this mess.”

The UK tax system is split between cash cows and under performers. According to the Institute of Fiscal Studies, 46.6% of the Treasury's income comes from Income Tax and National Insurance (~£254bn). A further 15.1% (~£82.6bn) comes from VAT (figures based on 2008-09 tax year).

In contrast, Capital Gains Tax only provides 0.9% of the Treasury's income, with Inheritance Tax only producing 0.6%. Together they generate a pitiful £8bn. Even Corporation Tax only manages 8.2% (~£44.9bn).

So is George Osborne a farmer or a school master? Does he milk his cash cows further knowing a couple of percentage points here and there on income tax and VAT will make a huge difference to the Treasury's coffers, or does he discipline his under achievers and make CGT and IHT work harder and do better?

Alistair Darling chose the agricultural route; targeting National Insurance (aka "The Jobs Tax") and making those nasty rich people pay 50% income tax whilst taking away their higher rate tax relief on pension contributions.

The scorn poured on the jobs tax by David Cameron suggests the new government might leave the cash cows be and look to the underperformers to take the strain. Certainly CGT has been most in the headlines with the coalition document promising to tax "non-business capital gains at rates similar or close to those applied to income, with generous exemptions for entrepreneurial business activities." (The term "generous" could well be relative!).

With CGT only contributing £4.9bn to the Treasury in 2008-09, clearly a big hike is going to be needed to make it contribute significantly more. "Hear, hear" cry the Liberals. "Hiss, boo" cry the Tories. The newly-weds are having their first tiff, and now there is talk of indexation and taper relief being applied to soften the blow. Before you know it, we'll have the system we only got rid of . . . oh yeah, 2 years ago! At least it won't cost much for HMRC to change their software; Tax Comp 07/08 v 3.2 should still work!

But the sheer size of the structural deficit means surely the cash cows have to produce more too. With National Insurance surely a U-turn too far at such an early stage of the new government, VAT is rumoured to be head of the queue. The Liberals also had as part of their manifesto the removal of higher rate tax relief on all pension contributions, which would be an increase in Income Tax receipts by the back door; the new government's first stealth tax perhaps?

So what does all this mean for financial planners? Clearly none of us really know the detail of what will change, and there are real dangers in trying to give advice based on what we think *might* happen. Encouraging clients earning less than £130,000 to make as big a pension contribution as possible "whilst they can", or systematically rebasing the cost of every client portfolio could result in unhappy clients at best, or compensation claims at worst if we allow ourselves to get swept along with the tide of hearsay and speculation which does not then materialise.

For sure, we'll have clients who want to consider doing both these things and more in anticipation of what might be round the corner. Our job, as ever, is to keep our heads when all around us are losing theirs, and talk each client through the pros and cons on a case by case basis to make a considered and balanced judgement (oh and don't be afraid to use "insistent client" procedures to cover yourself if a client is determined to act pre-emptively in a way you think unnecessary or unwise).

But will all become clear on 22<sup>nd</sup> June? History would tell us, probably not. Changes to tax legislation and the Law of Unintended Consequences are like peas in a pod. One only has to look at recent pension changes to see that. Pension Simplification didn't last long before Pension Mystification was announced from April 2011. The law of unintended consequences then resulted in Pension Incomprehension as we grapple with the complicated anti-avoidance rules that span the 2009/10 and 2010/11 tax years.

The general consensus is that the new government will try and get all the bad news out early in the parliament so that we've all forgotten about it, forgiven them, and vote for them again in five years

time. With so little time to prepare the emergency budget, it is inevitable that the Pre Budget Report in the autumn and the budget next March will contain swathes of new legislation to further reduce the deficit and to tackle the unintended consequences that will surely follow from the preparation of such a potentially radical and comprehensive budget by 22<sup>nd</sup> June.

So as financial planners, we will need to not only guide our clients through the uncertainty of the next couple of weeks, but also brace ourselves and prepare our clients for the prospect of further changes over the next year. Good quality financial planning will therefore be more valuable than ever, as we encourage our clients to stay focussed on their long term goals and objectives and not be swayed and unduly distracted by noise and hyperbole.

For sure, the changes on 22<sup>nd</sup> June and subsequently will require us to be nimble and on our toes to respond appropriately to the challenges and opportunities that new tax legislation will bring for our clients. But as ever, if we can give advice based on the long terms goals and objectives of our clients first and foremost, and not based narrowly on tax legislation per se, we will continue to give our clients the most important outcome of all; peace of mind over their finances whatever the short term changes and challenges.

William Pratt  
Director, Paradigm Norton Financial Planning

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