

Preparing for a 50% top tax rate

The lowest rate of income tax, 10%, was removed for most individuals in 2008. Nowadays it applies only to a small slice of savings income and to those people on the lowest incomes. For most, the 2009/10 tax rates are 20% and 40%, the latter having been the top rate since 1988.

From April 2010 a new top rate of income tax is being proposed: **50% on income over £150,000 and 42.5%** (up from 32.5%) **where the top slice of income is dividends.**

In addition, from April 2011 those earning more than £150,000 a year may lose higher rate tax relief on their pension contributions. New rules have been introduced to stop those who might hope to use the time before then to increase

premiums or contributions to make the most of 40% relief this year and 50% relief in 2010/11.

These changes serve to emphasise the importance of proper financial planning. We can advise on strategies to minimise taxes and maximise the strength of your business and long-term financial health through:

making the most of tax breaks for you and your business

planning to extract profits from your business tax-efficiently

making the most of tax-advantaged savings (including pensions)

reducing the inheritance tax due on your estate.

Tax and financial planning are essential parts of managing your business and your personal finances.

Talk to us now for advice on making the most of the opportunities available to you and your business this year.

Year-round planning

The end of the tax or business accounting year is a key time to focus on tax and financial planning, but you should also try and think about these issues throughout the rest of the year.

Many of the strategies outlined in this guide need not wait until the end of the year, though in some cases timing is critical.

While opinions vary as to the likely rate of the UK's recovery from the recession, by preparing and updating a forecast of income and outgoings you can identify times when money may be short and plan for them. We can help you with this.



In this guide

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Tax-efficient ways of extracting profit

There are numerous ways of extracting profit from your company, each of which has its own implications for the tax you pay, and for the company itself.

Most of the strategies below relate to limited companies. Company cars and vans are discussed in *Reducing the Cost of Business Motoring* on page 4.

Corporation tax is due on a company's profits, while personal income tax generally applies to what is drawn out of the company by means of a salary, bonus, or other form of remuneration.

Dividend versus salary/bonus

The question of whether it is better to take a salary/bonus or a dividend can be a difficult one and the issue requires careful consideration. A dividend is paid free of national insurance contributions, which would typically cost 13.8%, whilst salary/bonuses can carry up to 23.8% in combined employer and employee contributions. However, salary/bonuses are generally tax deductible to the company, whereas dividends are not, so the choice is not always straightforward. Paying a dividend can create a considerable saving. 5 April 2010 is the last date for paying a 2009/10 dividend, and any higher rate tax on that dividend will not be due until 31 January 2011. For those whose income could exceed £150,000 in 2010/11, thus attracting the new 42.5% rate of tax on dividend income, thought needs to be given to accelerating dividends into 2009/10.

Alternative options

You may also want to consider alternative means of extracting profit, which might include the following:

Tax-free allowances

Tax-free allowances, such as mileage payments, apply when you drive your own car or van on business journeys. The statutory rates are 40p a mile for the first 10,000 miles and 25p a mile above this. If you use

your motorbike the rate is 24p a mile, and you can even claim 20p a mile for using your bicycle!

Childcare

Parents of young children may be entitled to tax and national insurance-free childcare vouchers, including the provision of vouchers of up to £55 a week, provided by their employer. Whether both parents are employees of the same or different employers, the exemption is effectively doubled. The costs are usually deductible to the employer. (Your children also have their own personal allowances capital gains tax (CGT) exemptions and tax rate bands, so depending on your circumstances, it may be possible to take advantage of these allowances to help maximise family income and wealth.)

Pensions

Employer pension contributions can be a tax-efficient means of extracting profit from your company, as long as an individual's overall remuneration package remains commercially justifiable. The costs are usually deductible to the employer and tax and national insurance-free to the employee.

Care may be needed if the anti-forestalling provisions will affect you (see below for further details).

Property

Where property which is owned by you is used by the company for business purposes, such as an office building or car park, you are entitled to receive a rent, which can be anything up to the market value, if you wish. The rent is usually deductible to the employer. You must declare this on your Tax Return and pay income tax, but a range of costs connected with the property can be offset. On the other hand, receiving rent may mean a bigger capital gains tax bill if/when you come to sell the property, so care needs to be taken to weigh up the pros and cons.

We can advise you on the most appropriate options for extracting profits from your business.

Maximising your retirement income

The gap between the amount of money that people are saving, and the amount they need to ensure a comfortable retirement, is a perennial problem. It is important to act now to help maximise your income in retirement, including making the most of the available tax breaks.

Investing in a pension scheme, whether a company or a personal scheme, allows you to enjoy tax breaks on your pension savings. There are tax reliefs as you invest and a tax-free regime for your savings. Your employer may also be able to contribute and obtain tax relief.

Scheme managers can provide pension forecasts to help you judge whether you are saving enough, and what additional savings you might have to make in order to generate the income you will need in retirement.

Pension contributions based on 2009/10 earnings must be paid by 5 April 2010. Tax relief is available on annual contributions limited to the greater of £3,600 (gross) or the amount of the UK relevant earnings, but subject also to the annual allowance, and special annual allowance for those with annual income over £150,000 (see below).

The new anti-forestalling rules

In the 2009 Budget, the Government announced its intention to restrict tax relief on pension savings with effect from 6 April 2011 for people with taxable income of £150,000 or more. The relief will be tapered down until it reaches the basic rate of 20%.

Anti-forestalling legislation has been introduced to prevent those potentially affected from seeking to circumvent this change by increasing their pension savings in excess of their normal regular pattern, prior to the restriction taking effect.

For those with income of £150,000 or more in 2009/10 (or either of the previous two years) the new anti-forestalling rules mean that typically the amount which can be invested in pensions is capped at the pattern of investment already set at 22 April 2009. Those with regular pension savings may be able to invest at those levels and obtain tax relief at 40% this year, perhaps with scope to increase the level of investment to £20,000 per annum. Those paying irregular premiums may invest up to the greater of their average pension savings in 2006/07, 2007/08 and 2008/09 or £20,000, up to a maximum of £30,000. Note that the rules applying for 2009/10 and 2010/11 may also mean that a tax charge can arise for employees on employer pension contributions – talk to us about the new anti-forestalling provisions before acting.

We can help you with all aspects of financial planning, including compiling a forecast of your spending needs, post-retirement. Please call us for further advice and assistance.



The inheritance tax legacy

With increases in the inheritance tax (IHT) threshold failing to keep up with the speed of house price growth over the last 15-20 years, even in the current economic climate people have continued to find that the value of their home has taken them over the threshold.

IHT is currently payable at 40% on assets exceeding £325,000 (2009/10), so if you own your own home and have some savings and other assets such as shares and securities, your estate could be liable. Early planning is therefore essential in order to minimise your liability to IHT. Your IHT planning strategies may include the following:

Making use of reliefs

There are a number of IHT reliefs available – perhaps most importantly relief on business and agricultural property, which effectively takes most of such property outside the IHT net. As always, there are detailed conditions, including a two-year minimum holding period, but business property will generally attract 100% or 50% relief.

Exempt transfers

Transfers of assets between two spouses are generally exempt from IHT, regardless of whether they are made during a person's lifetime or on their death. In addition, the transferable nil-rate band may be transferable between spouses. This means that if the bulk of one spouse's estate passes on death to the survivor, the proportion of the nil-rate band unused on the first death goes to increase the total nil-rate band on the second death.

Other exempt transfers include:

small gifts (not exceeding £250 per tax year) to any number of individuals

annual transfers not exceeding £3,000 (any unused amount may be carried forward to enhance the following year's exemption)

certain gifts in consideration of marriage or civil partnership

normal expenditure out of income

gifts to charities

Lifetime gifts

Introducing a programme of lifetime gifts can also significantly reduce the IHT liability on your estate. This has the advantage of allowing you to witness the benefits they bring to your family members, while also escaping IHT as long as you survive the gift by seven years and no longer continue to benefit from the gift yourself. A discount can also apply where lifetime gifts were made between three and seven years before death (note that the discount applies not to the gift but to the tax on the gift).

Utilising trusts

Trusts can be used to help maintain a degree of control over the assets being gifted, for example in the case of younger recipients. Life assurance policies can be written into trust in order that the proceeds will not form part of the estate on your death. Talk to us about using trusts to suit your planning needs.

Through a course of lifetime planning and action, you can reduce your liability to IHT – contact us to find out more about strategies that could work for you.

Reducing the cost of business motoring

Over recent years, the cost of motoring has increased significantly, partly as a result of regular increases in fuel prices. Despite this, the company car remains an important part of the remuneration package for many employees.

However, tax and national insurance costs could mean that your company car may not be the most tax-efficient option for either the employer or the employee. There is also a fuel benefit charge where fuel for private use is provided with the car.

For some, an employer provided van may be a viable alternative to a company car – the maximum tax charge is £1,200 plus up to £200 for fuel!

The company car or van benefit is subject to a Class 1A national insurance charge of 12.8% payable by the employer.

It may also be time to review the company car policy completely, as it may be more beneficial to pay employees for business mileage in their own vehicles, at the statutory mileage rates.

We can help you to weigh up the relative costs and benefits of each option and decide on the best course of action for your business.

My Year End Checklist!

- Plan to minimise the tax take, including VAT and capital gains tax
- Make sure I avoid overvaluing stock and work in progress
- Talk to my accountant about ways to extract profits from my business at the smallest tax cost
- Consider ways of improving cash collection
- Review my pension arrangements
- Find out how the timing of dividends and bonuses could reduce or defer tax
- Make the most of my 2009/10 ISA allowance
- Find out the impact of accelerating disposals into the current financial year or deferring them into the next
- Claim capital allowances for expenditure on business equipment
- Make sure I am offering tax-efficient staff remuneration packages
- Put in place a tax-efficient gifting strategy
- Review my estate plan
- Send my business and personal records to my accountant in good time
- Contact my accountant regarding these and any other issues relating to my business, tax and personal financial situation.

We are here to help:

Make good use of us! This guide is merely a starting-point, designed to help you identify areas that might have a significant impact on your tax planning.

Please keep us informed of your plans and consult us early for help in taking advantage of tax-saving opportunities and tax-efficient investments. We are always pleased to discuss matters with you and advise in any way we can.



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