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CHARTERED ACCOUNTANTS
& BUSINESS ADVISERS

Contents

Welcome 2

Tax
- Personal tax 3
- Capital gains tax 4
- Inheritance tax 5
- Business tax 6

VAT 7

Financial planning 8

Budget 2009

Practical tax planning strategies

financial support you can count on...

BUDGET UPDATE 2009

Welcome

"A mish mash of recycled announcements from a government skilled in raising false hopes and incompetent at delivering real help; or a package that will steer the UK through a credible and rigorous path to recovery?"

Once again we've gone beyond the brief case and focused on what you really want to hear: practical tax planning strategies that can help reduce your tax bill.

There are plenty of planning opportunities out there. Read on for some suggestions...

TAX

Personal tax

Income tax issues for individuals and trusts

From 2010 there will be an **Additional Rate of Income Tax** of 50% on income over £150,000. Personal allowances will be gradually removed for income over £100,000 so higher income individuals will see more tax to pay.

Do you have a **company car?** You should check whether it really is a benefit, because the tax charge can often be so high that it's not worthwhile. If you have free private fuel, it is nearly always worth changing your remuneration package to give this up, if possible. For 2009/10, the tax charge will stay the same as for 2008/09 with a generous low rate for very low emission cars of under 120g of CO_2 per km.

Venture Capital Trusts (VCTs) are investment companies that invest in small businesses. To encourage individuals to put money in them, investments qualify for tax relief at 30%, since April 2006. While VCT investments may well be very high risk, some have been set up to try to minimise any risk that does exist.

The **Enterprise Investment Scheme** allows investors to put money into unquoted trading companies and claim back 20% Income Tax relief, and also get Capital Gains Tax (CGT) exemption from the shares. You can invest up to £500,000 a year and get these reliefs.

If a couple consists of a higher-rate taxpayer and a basic-rate (or lower-rate) taxpayer, **moving investments from the higher-rate taxpayer** to the other still seems to work. But it does require a full transfer of ownership of the underlying assets. If the donor can still take the income in any way, an arrangement like this will not work.

If you leave money to a **charity** in your Will, the gift is free of Inheritance Tax (IHT). But, if you make the gift while you are alive (using Gift Aid), not only do you save the IHT but you also get Income Tax relief. If you want to, you can agree with HMRC that the Income Tax you save can be gifted to the charity too. Gifts while you are alive are more tax-efficient than waiting until you die.

Income from **overseas investments** (offshore bank accounts, overseas properties etc) is, and always has been, taxable in the UK, even if you never bring the income into the UK, unless you are foreign. Using offshore structures to save tax is usually a lot less effective than people assume. 2009 Budget changes ensure lots of offshore funds are taxed more or less the same way as if they were UK investments.

If you have a **foreign domicile** the rules changed from 6 April 2008 so that once you've been tax-resident in the UK for 7 tax years you are taxed on all your world-wide income and gains, unless you pay a £30,000 sum to opt out and avoid tax on offshore income not brought to the UK. If you've not been resident 7 tax years, you can benefit from this treatment automatically; and if your overseas income and gains left overseas are no more than £2,000, you can remain on the remittance basis. What counts as remittance of income to the UK includes a number of indirect ways value can be brought into the UK.

Being **non-resident** can save tax sometimes. Days of arrival and departure never used to count towards working out if you are resident. Since 2008/9, days of departure no longer count, but days of arrival will.

The tax return filing deadline is 31 January but paper returns need to be submitted three months earlier – by 31 October. There is a longer filing deadline if you submit your return electronically. We file almost all our clients' tax returns online. It's faster, reduces processing errors and sometimes allows tax refunds to be paid within days – and keeps the filing deadline of 31 January.

Capital gains tax for individuals and trusts

Individuals have a Capital Gains Tax (CGT) exemption of £10,000 for 2009/10.

Most capital gains, after the exemption, will be taxed at 18%. However Entrepreneurs' Relief may be available to reduce the tax rate to 10% on the first £1m of gains per individual (a lifetime limit) on sales of businesses. This relief is complicated and we recommend you seek advice.

If you have a large **share portfolio**, it is worth considering realising gains to use up the annual CGT allowance. If you want to buy the shares back again afterwards, you need to wait at least 30 days, or alternatively have them bought back in a different name – your spouse's, or through your ISA, for example.

A **property** which has been your home at some point in your ownership is likely to qualify for some CGT exemption, even if you have let it, or lived somewhere else at the same time. If you have two homes, you might need to elect which one counts as your main home, and there may be benefits in ensuring both properties count at some point. The rules on properties which have been your home at some time and let for some time are complicated, but we can advise on your expected tax bill in advance of a sale.

Selling your garden (as long as it is less than half a hectare) will normally be exempt from CGT. But if you sell your house before you sell your garden, then you lose the exemption completely.

Transfers between spouses and civil partners (but not couples just living together) are exempt from CGT. When a couple separates, they can still transfer assets between them without tax charges during the year of separation (until the divorce is final), but not after. Getting the date of asset transfers right can make a big difference to any tax payable.

If you give assets away, you are still treated as if you sold them for CGT purposes, and it can mean you have tax to pay. In certain limited circumstances, you can make a holdover election so that you pass the tax problem over to the recipient of the gift, to be dealt with on a subsequent sale. Usually, this only applies to gifts of certain business assets, but most gifts to trusts will also qualify.

If you have a capital gain and you would like to defer paying the CGT, you can still "roll over" some of the gain by reinvesting in **Enterprise Investment Scheme (EIS) companies.** The added attraction of these investments is that they qualify for Inheritance Tax exemption after two years. This is in addition to the Income Tax and other CGT benefits referred to in the Income Tax section.

Inheritance Tax

The simplest trick to avoid paying Inheritance Tax (IHT) is still to **give assets away and then live seven years**. In practice, this means making sure that you make gifts as early in your life as possible.

Putting assets into **Trusts** not only gets them out of your estate, but also doesn't put the assets into the estates of your beneficiaries. Since 2006, the range of trusts qualifying for this special treatment has increased.

If you are entitled to income from a pre-1986 trust, the **value of the trust capital** could form part of your estate on death and thus could attract IHT at 40%. It might be worth considering whether to give up your interest in favour of the next generation to save IHT.

In the past we warned that **leaving everything to your surviving spouse** was tax-inefficient as the survivor would end up with more tax to pay in their estate. But now the survivor inherits any unused "nil-rate band" from the first one to die, so that this is not as much of a problem as it used to be. (The nil-rate band is £325,000 for 2009/10.) The rules are more complicated where one spouse is foreign-domiciled – you'd need to discuss it with us if this affects you.

Your home is likely to be your most valuable asset. There are anti-avoidance rules that make it difficult to give it away and then stay in it. It is possible to pass on some of the value, however, by means of an **equity release scheme** or something similar. Speak to **Critchleys Financial Planning** for more on this.

If your income is more than you need, then you may be building up your estate. If you can establish a **regular pattern of giving away surplus income**, however, those gifts would be outside your estate even if you don't survive seven years.

Certain investments are exempt from IHT. They include commercial woodlands, certain businesses, and (in some circumstances) farmland. By investing in these, you don't need to give assets away to save tax. You simply need to hold them for two years.

If you have cash you'd like to give away, but you need the income it generates while you are alive, there are certain financial products **(Discounted Gift Trusts)** that may be able to help you give away the capital while keeping the income. **Critchleys Financial Planning** can help you with this.

"Taper relief" reduces the tax on gifts if you die more than three years, but less than seven years, after making the gift. It isn't as generous as it sounds, because there's only tax on the gifts themselves if they exceed the nil-rate band. The main effect of most gifts is to use up some of the nil-rate band available to the estate, and taper relief does nothing to help that. The moral is clear: make gifts as early as possible so that you're more likely to survive seven years.

If someone dies with a will that is not tax-efficient, it is still possible to **rewrite the will** up to two years after the date of death to fix this. This involves a Deed of Variation. Don't rely on this though as it needs all beneficiaries to agree.

Your **pension fund** may well pay out a lump sum on your death. At the moment, the pension fund rules allow the whole fund to be outside your estate. By nominating a trust as the beneficiary on your death, you may be able to keep the proceeds outside the estate of your spouse, or other heirs.

Business tax

Is your business run through a company, or is it unincorporated (i.e. a partnership or sole trader)? **Getting the structure right** can save quite large amounts of tax. Talk to your usual Critchleys contact for advice.

If you have a **pension scheme for employees**, and the employees are contributing, you are missing a chance to save some National Insurance. It may be better to restructure the employees' remuneration so that you pay their contributions instead, and pay them less accordingly. It doesn't save any tax, but it saves National Insurance Contributions (NIC) on the amount of the contributions.

If you're going to **buy equipment** for your business anyway, getting it just before your year-end, rather than just after means you have the tax allowances a whole year earlier. Most businesses can write off the first £50,000 of expenditure straight away. For 2009/10, there are additional First Year Allowances if you spend more than that amount.

Companies that carry out **research & development** qualify for even higher allowances than for previous years. Small and medium-sized businesses can claim 175% of what they spend, while large businesses can claim 130%.

Splitting income between family members (making family members shareholders in the family company or partners in the family business) has worked as a way of moving income from higher-rate taxpayers to non-taxpayers. The plan was to introduce rules that stopped this working. It looks like these new rules have been put on hold. This may be particularly useful from 2010/11 when the new Additional Rate of Income Tax comes in.

The current tax regime encourages rewarding employees (especially of quickly growing businesses) with **share options** in the company they work for. For start-ups short of cash, offering some sort of stake in the business (and in future proceeds when the company is sold) helps recruit key staff.

Trading companies can **sell shares in subsidiary companies** and won't have to pay any tax on the gains at all, as long as they remain trading after the sale. That usually means that the proceeds of the sale need to be reinvested in the business.

Want to know more?
Call Gerry Jackson on 01865 261100 or email gjackson@critchleys.co.uk

VAT

The Chancellor has confirmed that the standard rate of VAT **will revert to 17.5% on 31 December 2009.** There will be legislation to prevent certain "forestalling", particularly between connected parties - i.e artificially securing the 15% rate by pre-invoicing for goods or services delivered after 1 January 2010.

Looking forward, we think that the standard rate of VAT will probably **rise again next year** to help balance the public books. (After the next General Election?)

The 1 January 2010 is also the effective date for some technical changes relating to the way cross-border trade is dealt with for VAT. This means that **all businesses** will need to make some changes to their invoicing systems in time for 1 January but those involved in cross-border trade in services may have to make significant changes.

Two other measures came into force from 1 April, both relevant to the need to ensure that your VAT records and returns are correct, tempting as it may be to cut back on administration in these challenging times.

New penalties came into force on 1 April 2009, with a maximum rate of 100%. Penalty rates will be assessed according to HMRC's assessment of a taxpayer's conduct and whether a taxpayer has made an unprompted disclosure. No penalty will be levied if the error is disclosed and occurs despite a taxpayer taking "reasonable care".

From 1 April 2010, the time limit for both assessments and claims is increased from three years to four years. There will be transitional arrangements from 1 April 2009 - claims and assessments will generally be able to go back to prescribed accounting periods ending on or after 1 April 2006. This will remain the case until 1 April 2010, when the four-year time limit will apply. This will allow the time limit to move gradually from three to four years.

Finally, a message for the current economic climate. **Remember that VAT impacts on a business' cashflow**. Look at tax points, bad debt relief, and, if turnover is less than £1.35 million, the Cash Accounting Scheme. On purchases, ensure that VAT is recovered as early as possible. If you are not Cash Accounting, do you wait until invoices are paid before claiming the VAT? How much VAT does this lock up?

Want to know more?
Call Steve Chamberlain on 01865 261100 or email schamberlain@critchleys.co.uk

Financial Planning

If you invest into **Individual Savings Accounts**, the Government has now announced that the annual ISA investment limit will rise to £10,200, of which £5,100 can be saved in cash. These higher limits will be introduced for those aged 50 for tax year 2009-10, with the first deposits being available from 6 October 2009. The higher limits will then apply to everyone from 6 April 2010.

The Government has now announced that from April 2011 **tax relief on pension contributions** will be restricted for those with incomes over £150,000. From that level of income the value of pensions tax relief will be tapered down until it is 20 per cent for those on incomes over £180,000. The Government is also to introduce legislation to prevent those individuals taking advantage of the higher rates pre 2011.

Protected rights- these are pension funds built up under a registered pension scheme by an individual being contracted out of either the State Second Pension (S2P) or its predecessor, the State Earnings Related Pension Scheme (SERPS).

As part of the Government's reform of state pension benefits, there are some important changes to the state second pension (S2P) and contracting-out which took effect on 6 April 2009. Previously, people built up S2P benefits on earnings between the lower and upper earnings limit, £4,680 and £40,040 in 2008/09. From 6 April, the upper accrual point (UAP) replaced the UEL as the higher threshold for earning S2P. Although the UEL, the upper limit for paying national insurance contributions, will rise to £43,888 from April, the UAP will remain frozen at £40,040.

This means that people who earn above £40,040 and contract-out via a personal pension will pay extra national insurance contributions, yet see no increase in the rebate paid into their pension scheme. Remember the Government has also committed to abolishing contracting-out, through defined contribution schemes, probably from 2012.

Safeguarded Rights - Before 6 April 2009, any contracted-out rights awarded to an ex-partner under a pension sharing order following a divorce settlement became safeguarded rights. Two aspects of the safeguarded rights rules in particular frustrated clients, namely that:

- retirement benefits could not be paid from safeguarded rights before age 60, and
- no tax free lump sum could be paid from safeguarded rights funds.

The Government has now abolished the safeguarded rights rules from April 2009 which means that contracted-out rights awarded as part of a pension sharing order on divorce are now treated in exactly the same way as other shared rights. So they can now:

- be paid from the same normal minimum pension age of 50 (increasing to 55 from 6 April 2010),
- provide the usual 25% tax free lump sum, and
- be held in the same pension arrangement as other shared pension rights.

Want to know more?
Call Jason McGuigan on 01865 261100 or email jmcguigan@critchleys-fp.co.uk