

Newsletter

Spring 2011



Welcome to the latest edition of our new regular financial newsletter. We hope you find it of interest. If you know someone else who would also appreciate a copy, please just send us their email and we'll add them to the mailing list.

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Budget Day

It is now less than one month until Budget day and it will be interesting to see how George Osborne reacts to the continuing economic weakness. And less than two weeks after the Budget is the end of the tax year.

There will be many changes – especially in the pensions arena – and you would be prudent to make sure that you have taking the appropriate action before that date.

The June 2010 Budget and its March predecessor both impact on the checklist for year-end planning for this tax year. Indeed the changes announced in both budgets will take a few years to work through the system

This newsletter highlights action that could be taken to achieve the best financial outcome; We hope you find it of interest.

Pensions

Contributions

The old rule used to be that a pension contribution made by 5 April would save you income tax for the year. In 2010/11 that remains the general case, but the principle has been complicated because the maximum contribution has been reduced to £50,000 with effect from 6 April 2011.

The lowered annual allowance will replace the current much higher annual allowance. And if you try to pay in much higher amounts before then, there are rules to restrict your tax relief if you are a high earner.

Contracting Out

If you are contracted out of the State Second Pension (S2P) via a personal pension, now is the time to decide whether you wish to stay in this situation.

The option to contract out in this way (and via a money purchase occupational scheme) will disappear from 2012/13.

Successive governments have reduced the financial benefit of personal pension contracting out to zero for most people, although it can still be the right decision – for now – in a limited number of cases. It might be time to review your position.

This year's limit will rise to £10,680 (£5,340 in cash)



The impact of IHT will increase in the coming years



Individual Savings Accounts (ISAs)

ISA contribution limits will be index-linked from 2011/12, so this year's limit of £10,200 (£5,100 in cash) will rise to £10,680 (£5,340 in cash) on 6 April.

With short-term interest rates still at historically low levels, the tax benefits of a cash ISA are relatively modest. Variable rates of around 3% are on offer for new savings, but these rates almost invariably contain a large bonus element which falls away after a fixed period, typically 12 months.

If you arranged a cash ISA a year or more ago, it is worth checking what interest rate your ISA is now earning - it could be 0.5% or even less.

If you live on the interest, you might want to consider a transfer to a stocks and shares ISA invested in income-producing funds. You would lose the security of a capital deposit, but your income potential could increase significantly.

Inheritance Tax (IHT)

Before last year's General Election there was the possibility that the IHT nil rate band would rise to £1 million.

The Coalition Agreement put an end to any such hope, with George Osborne not changing his predecessor's plan to freeze the nil rate band at the 2009/10 level of £325,000 through to 5 April 2015. He confirmed this by stating that it would not change during the course of this parliament.

This means that if your total assets – house, contents, property and investments – amount to more than £325,000 there will be IHT of 40% to pay. For a married couple, they each get the benefit of a nil rate band.

With inflation still close to 5% and unlikely to fall in the short term, the five year freeze means that the impact of IHT will increase in the coming years.

Capital Gains Tax (CGT)

Capital gains tax underwent a metamorphosis in the June 2010 Budget. The flat rate of 18% disappeared from 23 June 2010 and capital gains once again became taxable as the top slice of your income.

That is, it is added after everything else has been added up to determine which rate of CGT you should pay.

For gains falling into the higher (40%) or additional (50%) rate bands, the tax rate applied is 28%, while other taxpayers face an 18% rate.

While the rate applied is determined by when the gain is realised in 2010/11, losses are not time sensitive and can be set against any gains made in the tax year.

Fortunately, the annual capital gains tax exemption was unchanged: it remained at £10,200.

The menu of tax breaks is attractive



Venture Capital Trusts (VCTs) and Enterprise Investment Schemes (EIS's)

The continued attack on pension contribution tax relief means that attention is increasingly focused on VCTs and EISs.

Neither offers full income tax relief, but the menu of tax breaks is attractive compared to other types of investment

The EIS capital gains tax reinvestment relief is now more valuable, given the increased rate of CGT.

VCTs and EISs are both very high risk investments in fledgling companies and should only form a small part of a well diversified investment portfolio.

The high risk involved is the main reason why the Government is prepared to offer such generous tax reliefs.

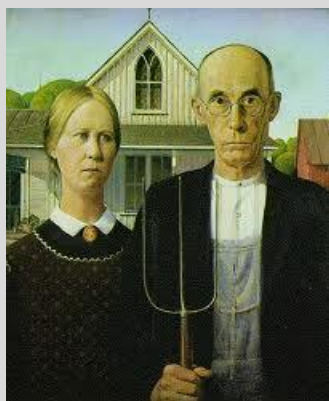
National Insurance Contributions

From 6 April 2011, all of the main rates of national insurance contributions (NICs) will rise by 1%; the primary (employee's) Class 1 rate will be 12%, the secondary (employer's) Class 1 rate will be 13.8% and the self-employed Class 4 rate will be 9%. The additional employee and self-employed NIC rates, applicable on earnings above £42,475 in 2011/12, both double to 2% from 6 April.

There will be increased starting thresholds for all NICs, mainly aimed at reducing the impact of the higher rates on low earners.

If you are employed and have the option of receiving a bonus or other earnings before 6 April 2011 rather than on or after that date, it could be worth accelerating the payment to avoid a higher NIC bill for you and your employer. However, be careful that the extra income does not push you into a higher tax band.

If you are self-employed, your scope to sidestep higher NICs is more limited. Provided that your business year-end is before 6 April, you may be able to bring forward profits or defer allowable expenditure to boost your 2010/11 earnings.



Employ your spouse

BUSINESS SECTION

Employ your spouse!

The general thrust of last June's Budget was to increase taxes; the rise in VAT and higher national insurance contributions from April 2011 being prime examples.

However, the June Budget was not all tax hikes. At the lower end of the income scale are two important tax reductions will take effect from 6 April 2011:

1. The personal allowance will rise by £1,000 to £7,475.
2. The starting point for employee national insurance contributions (NICs) will rise from £110 a week to £139 a week. For the self-employed, Class 4 contributions will start at profits of £7,225 rather than the current £5,715.

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business if you are able to do so. The employment must be genuine and the rate of pay justifiable; HMRC will take a dim view of an hour's tea making or filing being worth £140 a week.

Here is an example:

Jack is a self-employed designer, with earnings of around £70,000 a year. He decides to employ his wife, Jill, to run his office on a part-time basis.

Jill's pay in 2011/12 is £135 a week (£7,020 a year), just below the threshold at which Jack would have to start paying employer's NICs. Jill has only £450 of other income, so remains a non-taxpayer.

The overall result is extra net income for the couple of nearly £2,950 in the year:

	Jack's Loss	Jill's Gain
	£	£
<i>Earnings</i>	<i>7,020</i>	<i>7,020</i>
<i>NICs (2%/0%)</i>	<i>(140)</i>	<i>Nil</i>
<i>Income tax (40%/0%)</i>	<i><u>(2,808)</u></i>	<i><u>Nil</u></i>
<i>Total</i>	<i><u>4,072</u></i>	<i><u>7,020</u></i>

The immediate financial benefits of such an arrangement can be significant, as the example shows. There are also potential long-term benefits:

- Although neither Jack, as employer, nor Jill pay any NICs
Jill will accrue entitlement to basic state pension and State Second Pension (S2P). With only 30 qualifying years now needed for a full basic state pension, for many people with career breaks each year's employment has become more valuable. Each year's employment could earn Jill as much as £5 a week in state pension entitlement.
- Jack could add to Jill's state pension benefits by setting up and contributing to a pension arrangement for her. This would normally reduce his taxable (and NIC-able) profits further, so each £1 of contribution would only cost him 58p.

If you could employ your spouse/partner but currently do not, consider whether to do so. If they are already in your employ, you may want to increase their pay for 2011/12 to reflect the new tax and NIC thresholds.

Company cars cost more

If you have a company car, the tax you pay on it is likely to increase yet again this April.

The same is likely to happen again in 2012, when the special rates for low emission cars are substantially revised.



At present cars with emissions of between 76g/km and 120g/km have a taxable benefit of 10% of their list price (13% for diesel cars). By 2012/13, the 10%/13% rate will only apply if emissions are between 76g/km and 99g/km.

So if you are due to replace your company cars soon, make sure you know how much tax it will cost you by 2012.

Choose the wrong set of wheels and you could see your company car tax jump up by a half!

The company car tax reforms are yet another stealth revenue-raising measure. As a fringe benefit, the company car has lost much of its appeal.

The information regarding taxation is based on our understanding of current legislation, which may be altered and depends on the individual financial circumstances of the investor.

Past performance is not a guide for the future. The value of units can fall as well as rise. If an investment is surrendered in the early years, the surrender value may be less than the original investment. Currency fluctuations can also affect performance.

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