

PRIVATE CLIENTS

Dealing with the 50 per cent tax rate

With the end of the tax year approaching, and the new higher rates of tax applying from 6 April 2010, now is the time to make sure you are minimising your future tax costs

It has been well publicised that where an individual has income over £150,000 they will pay tax on the excess at substantially increased rates: dividends received will be taxed at an effective rate of 36.11 per cent and all other income at 50 per cent. In addition, where income falls between £100,000 and £112,950 there will be an effective rate of tax of 61 per cent. Below are ten basic planning strategies to consider.

Maximising all allowances and reliefs - are you and your family members all fully utilising your annual tax allowances?

Income tax

Each individual has a personal tax free allowance of £6,475 and lower rate tax bands:

| | Dividends | Other income |
|----------------|---------------|---------------|
| up to £37,400 | 10 per cent | 20 per cent * |
| up to £150,000 | 32.5 per cent | 40 per cent |

* Assuming non-savings income exceeds £2,440

Individual Savings Accounts (ISAs) - annual allowances use them or lose them

ISA's can be held by any UK resident over 16 years of age.

The annual allowances for the current year are:

| Age | Cash only | or | Investment |
|------------|-----------|----|------------|
| 16 to 18 | £3,600 | | n/a |
| Under 50 | £3,600 | | £7,200 |
| 50 or over | £5,100 | | £10,200 |

The over 50 amounts above will apply to all age groups in 2010/2011.

Capital gains tax

The annual capital gains annual exemption is £10,100.

There is a level of uncertainty whether the current low rate of capital gains tax of 18 per cent will continue indefinitely. Where substantial amounts are involved or a sale is envisaged in the near future you may want to consider accelerating the disposal of an asset before the end of this tax year. Please let us know as soon as possible if this may be of interest to you.

EIS and VCT investments provide both income tax and capital gains tax benefits. However, these are considered to be higher risk investments.

Advancement of income to pre 6 April 2010 - can you draw income now which will be taxed at 40 per cent?

Examples include:

- Employers advancing bonus or salary payments.
- Companies voting and paying special dividends.
- Closure of an account or disposal of an investment.
- If you are over 50 consider increasing your pension drawdown.
- Trustees may consider increasing income distributions.

The cash flow disadvantages of paying tax sooner has to be weighed against the ten per cent income tax saving.



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What can you do after 5 April 2010? Longer term planning.

Defer income

You may be able to waive rights to income in the short term in the hope you will pay lower rates of tax later.

Examples include:

- Waiving rights to income such as salary and dividends.
- Certain life insurance products have for some time effectively both deferred and reduced income tax whilst allowing a five per cent withdrawal of the original capital per year tax-free.

Convert income into capital

You could consider investing your funds in capital-growth rather than income producing assets, although this would have to be considered as part of your overall investment strategy. A number of products are now out in the market which should enable you to do this.

In a corporate context a sale or liquidation rather than dividends could be beneficial.

Employers may look to incentivise and reward employees by using shares or options.

Review your family arrangements and business structure - have a health check to ensure that assets are held in the most appropriate manner.

Depending on your circumstances, you may wish to gift the whole or just a share of an income producing asset to a family member. This type of planning can be effective not only for income but also capital gains and inheritance tax savings.

In order to ensure any gift is effective for tax purposes, it must be an outright gift. However, it is still possible to maintain a level of control over the asset if you use a Trust or Family Partnership.

Where an existing business is held via a company or a partnership a reorganisation may result in year on year tax savings on both distributed and retained profits.

Trusts - Are you a trustee or a beneficiary?

The 50 per cent tax rate will also apply to all the income of discretionary and accumulation and maintenance trusts (after taking into account the modest £1,000 standard rate band).

Where the trustees have a historic tax pool of undistributed income thought should be given to making tax efficient income distributions prior to 6 April 2010.

If sizeable income distributions are to be made to beneficiaries the creation of a revocable interest in possession should be considered. This will result in the income being taxed at lower rates in the hands of the trustees and can result in a higher net receipt for the beneficiary where the trustees have received dividend income.

Expatriation - the most drastic 50 per cent planning involves you leaving the UK.

Whilst this can be hard to achieve from a tax perspective we can advise on the steps you need to take if this is a practical solution for you.

Pensions - there are a number of pension changes which affect the amounts you are able to contribute tax effectively to pensions and the timing of withdrawals of pension benefits.

Depending on your personal circumstances it may be still tax efficient to make or increase your current pension contributions. The rules which came into effect from 22 April 2009 are complex and it is essential that you get advice before you change any existing pension payments.

Were you born between 7 April 1955 and 5 April 1960? If so, you should be aware that from 6 April 2010, the earliest age at which benefits can be normally taken from pension arrangements rises from 50 to 55. This means that if you are planning to take all or some of your pension benefits, and will be over 50 but under 55 on 6 April 2010, then you will have to wait until your 55th birthday before doing so.

Whilst a number of the ideas above are relatively straightforward it is important that they are implemented carefully to be effective for tax purposes.

Also, when undertaking tax planning ideas, any investment or disposal must be considered in light of your overall investment strategy and you should take investment advice before taking any action.

This list is by no means exhaustive if you are interested in putting some planning in place or have any queries, please speak to your usual BDO advisor or

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