

THE 2009 BUDGET BULLETIN

1. INTRODUCTION

As for last year we had “prior knowledge” of many, but by no means all, of the changes proposed through the Pre-Budget Report in October.

The challenging economic conditions necessitated further changes and the issues of greatest significance to the financial services sector are:

- The removal from 6 April 2011 of higher rate tax relief for pension contributions for those with income of £150,000 or more.
- The complex transitional provisions connected with the special allowance charge on pension contributions to prevent abuse in the intervening period.
- The introduction from 2010/11 of a 50% income tax rate (and 42.5% on dividends) for those with income of £150,000 or more.
- The reduction, from 2010/11 of personal allowances for those earning over £100,000.
- The increase of the trust tax rate to 50% and 42.5% for dividends – regardless of income levels.
- The increase of the annual ISA allowance to £10,200 from 2010/11 and from 6.10.09 for those 50 and over.
- The retention of small companies corporation tax at 21% for another year.

Our budget bulletin this year covers all of the main PBR proposed changes and all of the Budget changes and adjustments so that you will have our view of the latest position on what we believe to be the main areas of interest.

As ever, being aware of and able to effectively communicate relevant changes will be a powerful means of differentiation. The ability to identify opportunities to improve the financial position of individual, trustee and corporate clients will take the differentiation process to an even higher level.

We hope and trust that this year’s bulletin will help you to do just that.

YOUR GUIDE TO THE BUDGET BULLETIN

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The contents of this Budget Bulletin are based on the proposals put forward by the Chancellor in his Budget speech. These need to be approached with caution as the details may change during the passage of the Finance Bill through Parliament.

2. INCOME TAX

The two most important announcements made in connection with income tax were, from 2010/11

- (a) the introduction of a 50% rate of income tax
- (b) the removal of the personal allowance for persons with income in excess of £100,000

These changes are covered in 2.2 below.

2.1 PERSONAL ALLOWANCES AND TAX RATES IN 2009/10

2.1.1 PERSONAL ALLOWANCES (2009/10)

As announced in the Pre-Budget Report, allowances and thresholds for 2009/10 have generally been raised in line with inflation.

- The personal allowance is increased from £6,035 to £6,475. This represents an increase of inflation plus £130.
- An increase in the level of age allowance from £9,030 to £9,490 (for those aged 65 – 74) and from £9,180 to £9,640 (for those aged 75 and over). In 2010/11 the allowance for those aged 75 and over will increase to £10,000.
- The level of income that a person can enjoy before age allowance is cut back rises from £21,800 to £22,900.
- The married couple's allowance (MCA) for those aged 75 and over (provided at least one spouse was aged 65 or over before 6 April 2000) will increase to £6,965. The MCA for those aged 65 to 74 is not relevant for tax year 2009/10 and beyond as those eligible for this allowance in 2008/09 will attain age 75 at some time in tax year 2009/10 in which case they will qualify for the age 75 and over MCA.
- The universal MCA was, of course, withdrawn from 6 April 2000. In calculating the reduction in age allowance when income exceeds £22,900, the increased MCA is cut back to not less than £2,670 (the "minimum amount").
- Tax relief for maintenance payments will be available only where at least one party was 65 or over at 5 April 2000. The relief is increased to £2,670.
- Relief in respect of the MCA and maintenance payments continues to be given as a tax credit at the rate of 10%.

WHICH MEANS THAT ...

- Bearing in mind that a husband and wife each have their own personal allowance and their own starting and basic rate tax bands, more tax can be saved with planning.

Both personal allowances and starting/basic rate tax bands should, if possible, be used to the full, particularly where only one of the spouses is a higher rate taxpayer.

As well as a transfer of investments, considerable scope may exist for a business owner to employ his or her spouse and possibly then provide a pension for him/her. Care should be exercised to ensure that all payments made will be a deductible expense for the payer. The greater the remuneration, the greater the care!

- Age allowance applies separately to a husband and wife as does the total income limit of £22,900 above which the allowance reduces. By careful planning both spouses can possibly each qualify for a full age allowance. When investment income is in the “age allowance trap” it can suffer an effective rate of tax of 30% so reinvestment in non-income producing assets should be considered. Capital investment bonds, capital growth oriented unit trusts, OEICs and ISAs may be attractive as, (subject to guarding against “capital erosion”), “income” can be taken without loss of age allowance. With the capital investment bond, this will commonly be by use of the 5% annual withdrawal facility. In some cases, more than 5% can be taken (without an addition to total income which may impact on the age allowance) provided the first withdrawal is made in the second policy year.

Under current tax rules care should be exercised on final encashment of the bond or on part encashment over the cumulative unused 5% allowances as the entire chargeable event gain without top-slicing relief will count as income for age allowance purposes. However, careful advance planning can help to substantially reduce this problem.

In the case of unit trusts and OEICs, units or shares can be regularly encashed to make use of the annual capital gains tax exemption.

- In relation to trusts established by a parent for a minor unmarried child not in a civil partnership, where that child has a vested right to income, if the income exceeds £100 gross in a tax year it is automatically taxed on the parental settlor irrespective of whether the income is paid to or for the child’s benefit. However, scope exists for trusts for **grandchildren** where consideration should be given to investing in offshore distributor funds to obtain the benefit of gross dividends or distributions. If it is desired to achieve tax effective accumulation of income from UK investments held in a trust under which the grandchild has an interest in possession then, subject to investment considerations, it will be necessary to invest in areas that produce income other than UK dividend income. As well as interest from cash deposits, this will include income from corporate bonds and certain collectives whose income payments are treated as interest distributions rather than dividends.

2.1.2 RATES OF TAX (2009/10)

(i) THE STARTING RATE OF INCOME TAX

The starting rate of 10% for the tax year 2009/10 applies to the first £2,440 of taxable savings income (i.e. after allowances and reliefs).

If an individual's taxable non-savings income is more than £2,440 then the 10% savings rate will not apply. This is because in calculating tax, savings income "sits on top" of non-savings income. So if, for example, taxable non-savings income were £1,500 then £940 of savings income would benefit from the 10% rate.

(ii) THE BASIC RATE OF INCOME TAX

For 2009/10, the basic rate of income tax has been held at 20%. The higher rate threshold has been increased to £37,400. The basic rate of tax will apply to taxable income in the band £1 to £37,400 but subject to 2.1.1 above. The basic rate of tax is relevant to:-

- individual contributions to registered pension schemes which operate basic rate tax relief at source.
- charitable covenants and Gift Aid. For qualifying Gift Aid donations made before 6 April 2011 the Government will make an additional repayment to the charity so that the overall effect is that the 22% basic rate of tax (which applied up to 5 April 2008) still applies for repayment purposes.
- annual payments.

It should be noted that discretionary trusts and accumulation and maintenance trusts will, in general, qualify for a £1,000 standard rate tax band for tax year 2009/10.

WHICH MEANS THAT ...

By allocating income, and possibly gains, between spouses, particularly where the income is currently concentrated in the hands of one spouse and especially for those where one spouse pays income tax at a higher rate than the other, it is possible to save tax. This reallocation can be achieved by unconditionally transferring assets (including capital investment bonds to be encashed) from one spouse to the other. No capital gains tax liability or inheritance tax liability will arise on such transfers. Tax saved will mean that taxpayers are even better placed to invest in other investment products. There is no better time than the beginning of the tax year to implement "income splitting" plans.

Last year was meant to see the introduction of the controversial 'income-shifting' anti-avoidance rules. These would have affected both companies and partnerships and were designed to prevent business income being divided between the individuals (whether employees, shareholders or partners, related or not) in a way that does not reflect what HMRC regards as "commercial reality". However, in the 2008 Budget the Chancellor announced that legislation would not appear until this year's Finance Bill. By the November 2008 Pre-Budget Report the Chancellor had abandoned the 2009 legislation and instead decided to keep the issue 'under review'. There was no comment on the subject this time around.

(iii) THE HIGHER RATE THRESHOLD

The higher rate threshold has been raised to £37,400. Taxable income in excess of this will be taxed at 40% or 32.5% (UK dividend income).

Whilst there has been a healthy increase in the higher rate tax threshold this year, over the last 10 years or so the number of higher rate taxpayers has increased because the higher rate tax threshold has not increased in line with earnings. Higher rate taxpayers will still have a need to shelter income (particularly investment income) from tax. This will be even more the case in 2010/11 when people with high incomes will suffer income tax at 50% on taxable income above £150,000. At that time, the rate payable on UK dividend income will be 42.5% (see 2.3 below)

WHICH MEANS THAT ...

Where a person is or is likely to be a higher rate taxpayer, consideration should be given to:-

- Reducing taxable income by offsetting pension contributions against earned income.
- Individual savings accounts (ISAs).
- Investments which secure tax relief on investment, such as enterprise investment schemes and venture capital trusts.
- Capital growth oriented collectives.
- Life insurance investment bonds.

2.2 PERSONAL ALLOWANCES AND TAX RATES IN 2010/11

- It was announced that from 6 April 2010 that the rate of tax on taxable income in excess of £150,000 would be 50%. This brings forward and increases the 45% rate which had been proposed in the Pre-Budget Report to apply from 6 April 2011.
- From 6 April 2010, where an individual's "adjusted net income" exceeds £100,000 the level of the personal allowance will be reduced by £1 for each £2 over £100,000 until it reaches zero.

This potential reduction in the personal allowance is harsher than the previously proposed change in the Pre-Budget Report which would have resulted in a £1 for £2 cut off for gross income over £100,000 but restricted to the loss of half of the personal allowance. The remaining one-half of the personal allowance would have been reduced by £1 for every £2 of gross income above £140,000.

Adjusted net income is calculated in a series of steps. The starting point is "net income" which is the total of the individual's income subject to income tax less specified deductions, the most important of which are trading losses and payments made gross to pension schemes. This net income is then reduced by the grossed-up amount of the individual's Gift Aid contributions and the grossed-up amount of the individual's pension contributions which have received tax relief at source. The final step is to add back any relief for payments to trade unions or police organisations deducted in arriving at the individual's net income.

- In the Budget Note outlining these changes, mention is made of new powers to vary the income tax rates for the charges that apply to registered pension schemes (see section 13.4).
- From 6 April 2010 dividends received by individuals will be taxed as follows:

Basic rate taxpayer	10%
Higher rate taxpayer	32.5%
50% taxpayer	42.5%

WHICH MEANS THAT ...

Some thoughts follow on planning in light of the above changes particularly as the capital gains tax rate remains at 18%.

Many of these thoughts are a re-statement of tax planning that higher rate taxpayers should already be considering-but heightened by the additional “10%” on the higher rate of tax for those whose income may be over the £150,000 threshold next year.

- Consider investing for capital growth (taxed at 18% after the annual exemption) rather than income (taxed at 50%). Of course, tax should not be the sole determinant of investment planning strategy but a 10% increase in the income tax rate for wealthier taxpayers cannot be ignored.
- For those investors affected by the new rate, to the extent that investment returns arise predominantly from capital growth, the “Bonds v Collectives” balance would tip further in favour of collectives. Despite indexation allowance being available within the UK life fund, the tax payable by a 50% taxpayer on chargeable event gains realised under UK capital investment bonds would be 30% -up from 20%. And this rate will apply to gains that are already depleted by whatever the effective rate is on gains and income inside the UK life fund. Gains realised under offshore bonds would be assessed at the full rate of 50% with no tax credit – but with no ‘internal’ fund taxation.

A capital investment bond would, however, continue to represent a more tax attractive home for reinvested income as it currently does. Inside a UK bond, UK dividend income would bear no further tax and other income would be subject (broadly speaking) to a 20% tax rate at life fund level. There would be a 20% tax credit when a chargeable event gain was realised and, of course, tax effective withdrawals using the “5% rule” would be possible.

As well as the “5% rule” more attention will undoubtedly be focused on tax planning strategies to minimise the tax on taking benefits from the bond. Those who anticipate being able to exercise a strong element of control over their income at the time of any future bond encashment may be able to implement an attractive strategy of tax deferral during the period of accumulation followed by tax minimisation on withdrawal of benefits.

As is the case now, there will continue to be a number of issues to take into account in determining the most effective tax wrapper for a particular portfolio. The balance

between income and gains on the portfolio in question will, as it is now, be a particularly important one.

- The attraction of the tax free investment growth and income secured inside a registered pension scheme and an ISA will increase for people suffering 50% tax on income. And from 6 April 2010 the ISA annual contribution limit will be raised to £10,200 for investors of all ages, with the increase applying from 6 October 2009 for those aged 50 and over in tax year 2009/10.
- Where higher rate tax relief on pension contributions remains for an individual until 5 April 2011 (see section 13 for more detail) and assuming that, where appropriate, relief will be available at the new highest rate, then the immediate and continuing appeal of such contributions will be obvious. However, if the contribution is made when relief is secured at 40% but the emerging income is taxed at 50% then the tax attraction, while still strong (given the greater sum invested as a result of the tax relief and the tax freedom of the underlying fund) will be somewhat diminished. This will be even more so if the relief is limited to basic rate.
- There may be increased interest in the use of employee benefit trusts and family benefit trusts as a means of securing access to funds without immediate income tax or NIC cost. HMRC action will, however, need to be carefully monitored following the Sempra Metals case.
- Company owner/managers may well see merit in reinvesting into their business (rather than taking sums out by way of dividend or salary). The sums reinvested will have borne corporation tax only (possibly at the “held” small companies’ rate of 21%) instead of income tax, and if the value of the business is increased as a result of the reinvestment then up to £1 million of the gain eventually realised will, with the benefit of entrepreneurs’ relief, only be taxed at effectively 10% and at 18% for any gains over the lifetime capital gains limit of £1 million. Of course, despite the undoubted tax attraction of an effective 10% tax rate on capital gains of up to £1 million, there is an inherent risk in relying on one’s business as the SOLE source of future financial security...however tax attractive that strategy may be.
- Still on the company owner/managers theme, the dividend v salary decision would have been made even easier than it is now for those wishing to minimise the “outflow to the authorities” if the 50% rate only applied to earnings. However, it would appear that a comparable 42.5% rate would apply to dividends so that the dividend v salary choice would remain as it is now with the dividend having the (often overwhelming) advantage on tax/NIC grounds.
- A 50% tax rate may give greater incentive to those “affected” business owner/managers to “shift” income. Since the Government’s loss in the now famous “Arctic Systems” case we have been on notice that anti-avoidance measures would be introduced. We also knew that the anti-avoidance legislation that was “stalled” earlier last year could be incorporated into the 2009 Finance Act with the provisions taking effect from 6 April 2008. In the 2008 Pre-Budget Report it was announced that, while the Government was keeping this issue under review, it would not be bringing forward legislation in the Finance Bill 2009. No mention of “income shifting” has been made in this Budget.

The aim of these provisions, should they ever be introduced, will be to assess the “shifted income” (through salary, dividends or partner’s profit share) on the person making the main contribution to the business. It is expected that where the “shifted” payment can be justified (based on the receiving person’s contribution to the business) it will be fully effective with the income being assessed on the person who receives it and not attributed to the “shifter”.

- VCTs may look even more attractive given that dividend payments from them are tax free. The tax relief on input will not be affected by the new 50% rate. Of course, one must consider the risk element of such investments.
- Clearly there is little action that a taxpayer can take to secure their personal allowance if they enjoy sizeable earned income. However, for those with investment income which causes their gross income to be just over the £100,000 threshold, they could consider reinvesting into capital growth orientated investments or investments that produce tax-free income (e.g. ISAs). Clearly the investment risks need to be considered as do the CGT implications on reinvestment (although, of course, chargeable gains that exceed the annual exemption are now only taxed at a flat 18%).

2.3 RENT A ROOM RELIEF

The threshold for tax exempt rents under the Rent a Room scheme for tax year 2009/2010 remains at £4,250.

2.4 TAX ON SAVINGS INCOME

The starting rate of 10% will apply to the first £2,440 of taxable savings income in appropriate circumstances - see section 2.1 for full details.

WHICH MEANS THAT ...

This is good news for those on lower incomes who qualify for the savings rate.

Non-taxpayers must reclaim any 20% tax deducted at source on savings income using HMRC form R40 unless they have certified for gross interest from a bank/building society account (form R85), or for a gross annuity (form R89). A 10% taxpayer will need to complete form R40 to reclaim overpaid tax.

2.5 DIVIDENDS FROM FOREIGN SHARES

See section 12.5 for full details.

2.6 TAX RECLAIM / TAX PAYABLE CHART (UK RESIDENT AND DOMICILED INVESTOR) 2009/2010

Source	Tax deducted at source?	Tax reclaim by non-taxpayer?	Tax reclaim by 10% taxpayer?	Tax payable by basic rate taxpayer?	Tax payable by higher rate taxpayer?
BUILDING SOCIETY/BANK INTEREST	YES 20% (R85)	YES 20% (R40)	YES 10% (R40)	NO	YES (40% WITH 20% TAX CREDIT)
NON-UK BUILDING SOCIETY/BANK INTEREST	NO	NO (NO NEED)	NO (NO NEED)	YES 20%	YES 40%
UK DIVIDENDS	NO (10% TAX CREDIT)	NO	NO	NO	YES (32.5% WITH 10% TAX CREDIT)
NON-UK DIVIDENDS	NO * (10% TAX CREDIT)	NO	NO	NO	YES * (32.5% WITH 10% TAX CREDIT)
GILT INTEREST	NO (IN MOST CASES)	NO (NO NEED)	NO (NO NEED)	YES 20%	YES 40%
TAXABLE ELEMENT OF ANNUITY	YES 20% (R89)	YES 20% (R40)	YES 20% (R40)	NO	YES (40% WITH 20% TAX CREDIT)
UK BOND GAINS	NO (BUT UP TO 20% SUFFERED IN FUND)	NO (NOT POSSIBLE)	NO (NOT POSSIBLE)	NO	YES 20%
NON-UK BOND GAINS	NO	NO (NO NEED)	NO (NO NEED)	YES 20%	YES 40%
OFFSHORE ROLL-UP FUNDS	NO	NO (NO NEED)	NO (NO NEED)	YES 20%	YES 40%
OFFSHORE DISTRIBUTOR FUNDS - DIVIDENDS	NO (10% TAX CREDIT)	NO	NO	NO	YES (32.5% WITH 10% TAX CREDIT)
OFFSHORE DISTRIBUTOR FUNDS – INTEREST DISTRIBUTIONS	NO	NO (NO NEED)	NO (NO NEED)	YES 20%	YES 40%

* For 2009/10 the 10% tax credit is not available in respect of a shareholding of at least 10% in a company in a non-qualifying territory.

3. NATIONAL INSURANCE

3.1 RATES

(A) 2009/10

The National Insurance rates and contribution limits announced in the Pre-Budget Report apply as follows for 2009/10:-

- The Employee's Primary Class 1 National Insurance rate is 11% on earnings between the Primary Threshold (£110 per week) and Upper Earnings Limit (£844 per week).
- Employees, in addition, pay 1% Primary Class 1 National Insurance on all earnings above the Upper Earnings Limit (£43,875 per annum).
- The Employer's Secondary Class 1 contribution rate on earnings above the Secondary Threshold (£110 per week) is 12.8%.
- The self-employed Class 4 rate on profits between the lower (£5,715 pa) and upper profits limit (£43,875 pa) is 8%.
- The self-employed Class 2 flat rate contribution is £2.40 per week.
- The self-employed, in addition, pay Class 4 contributions at a rate of 1% on all profits above the upper profits limit (£43,875).
- The Class 3 voluntary contribution rate is £12.05 per week.

(B) 2011/12

Changes, effective from 6 April 2011, already announced in the 2008 Pre-Budget Report are as follows:-

- From 2011/12, the NICs Primary Threshold will be broadly aligned with the basic personal allowance.
- From 2011/12, the main rate of Class 1 and Class 4 NICs will be increased by 0.5% to 11.5% and 8.5% respectively.
- From 2011/12, the Class 1 employer rate of NICs will be increased by 0.5% to 13.3%. The increased rate will also apply to Class 1A and Class 1B contributions.
- From 2011/12, the additional rate of Class 1 and Class 4 NICs will be increased by 0.5% to 1.5%.

WHICH MEANS THAT ...

The changes in the thresholds for 2009/10, and proposed future changes, should give advisers an incentive to visit their business clients to discuss effective methods of remuneration.

Those running their business through a company may well consider paying themselves dividends as opposed to salary. The main reason for this will, of course, be that dividends are not subject to National Insurance. The pros and cons of dividends and salary have been well rehearsed many times in the past and these should be revisited before any meetings are arranged with clients. This is covered in greater detail in section 14 - Remuneration strategies.

In addition, a review of the opportunities for payment of salary to working spouses could be beneficial. In any remuneration planning for a spouse it is important that payments, in order to be fully tax deductible, can be justified on the basis of work carried out.

Any planning carried out with a view to taking a spouse into partnership (where appropriate) or issuing shares to a spouse in order to pay dividends must be carefully discussed with professional advisers.

There may be an additional benefit to incorporation in the shape of the avoidance of the “unlimited” 1% Class 4 NICs on earnings over £43,875 that could be avoided on profits that accrue to a company. NICs could continue to be legitimately avoided, even if the money leaves the company, provided it is paid to the shareholders by way of dividend. Of course, before taking this important step (incorporating an unincorporated business), there are many other factors to be taken into account and professional advice is essential.

3.2 THE UPPER ACCRUAL POINT

The 2007 Budget announced a number of changes to the Upper Earnings Limit (UEL) for NI contribution purposes. The UEL was increased by £75 a week above normal indexation on 6 April 2008 and has been given a further above - indexation increase as at 6 April 2009 to £844 per week to align it with the threshold at which higher rate tax becomes payable, allowing for the single personal allowance.

Prior to tax year 2009/10 S2P benefit has accrued on individuals’ earnings between the Lower and Upper Earnings Limits. However, the Government has now capped the earnings for the provision of S2P benefits to an Upper Accrual Point, which will remain permanently fixed at £770 per week.

These changes introduce a sizeable increase in NI contributions.

4. CAPITAL GAINS TAX

Major changes in the taxation of capital gains for individuals and trustees took place from 6 April 2008. In this Budget the main change was the increase in the annual exemption. This is increased from £9,600 to £10,100 for individuals and personal representatives. For trustees the exemption increases from £4,800 to £ 5,050.

A change of less wide application was that removing transparency in respect of chargeable capital gains made by offshore funds that are not constituted as companies, unit trusts or partnerships. Such funds are understood to be mostly based on contractual relationships.

Some commentators predicted that the CGT rate, only recently reduced to 18%, might increase to 40% to help the Governments search for funds to reduce public sector debt. This fear has not been realised.

WHICH MEANS THAT ...

(i) Planning for individuals

- The annual CGT exemption has traditionally been an important weapon in an individual's CGT planning armoury. The value of it was somewhat diminished however with the reduction of the CGT rate to 18%. Each individual (in a family this means a separate annual CGT exemption for each spouse and each child) can realise gains each tax year within his/her annual CGT exemption tax free. The maximum saving from use of the allowance by an individual is £1,818.

A simple way for parents and grandparents to facilitate use of the annual exemption by children is for investments, such as growth-oriented unit trusts/OEICs, to be held on an absolute (or bare) trust or for the designated benefit of the child. In this way, the child's annual CGT exemption can be used to cover capital gains of the trust.

It needs to be borne in mind though that bare trusts offer little legal control to the investor should there be a desire to prevent the child from accessing funds on attaining the age of majority. This, in effect, is the price one pays for the ability to use the child beneficiary's annual CGT exemption.

Where greater control is required, a discretionary trust may be suitable. Abolition of the settlor-interested trust rules for CGT from 6 April 2008 means that a discretionary trust can be established for a minor child of the settlor with the trustees eligible for an annual CGT exemption (as opposed to the gains being assessed on the parental settlor) but this will generally be at half the level available to the bare trust ie. £5,050. Gains above the available exemption will be taxed at 18% in either case. The CGT 'price' to pay for discretion could thus be quantified at a maximum of £909 which many may find acceptable.

- Transfers between spouses living together continue to be treated as being made on a "no gain/no loss" basis. This means that as long as any transfer is outright and unconditional, a prior transfer from a spouse holding investments to a spouse with no

investments could effectively double the use of the family's annual exemption. The same rules apply to transfers between registered civil partners. Although these days it is harder to utilise the annual exemption through "bed and breakfast" transactions, "bed and spouse", "bed and ISA" and "bed and SIPP" arrangements can still work.

Special anti-avoidance rules exist to prevent CGT advantages arising on transfers between a husband and wife which have been made purely to take advantage of loss relief with neither party substantially changing their fiscal position.

(ii) Planning for trustees

Trustees will be entitled to an annual CGT exemption of £ 5,050 but where a settlor has created more than one trust, then this £ 5,050 is diluted by the number of trusts concerned, subject to a minimum exemption of £ 1,010. There are certain planning points that arise out of the use of the trustees' annual exemption, as follows:-

- If trustees wish to invest in ways in which they can effectively use the annual CGT exemption growth-oriented UK or offshore collective investments may be appropriate.
- In the case of larger trusts, if the trustees are likely to realise capital gains that exceed their annual exemption, the rate of CGT on such gains will normally be 18%. Where portfolio management without personal CGT risk is desired then a UK or (more likely) an offshore bond may be thought "tax suitable" to shelter gains that could arise simply through portfolio management. Of course, gains realised by the manager of the collective will be CGT free. Only realisation by the investor will give rise to the potential for personal taxation .

The choice of the most tax effective investment wrapper will be substantially portfolio dependant though and the overall effective rate of return on the investment (taking account of fund and trustee tax) will need to be taken into account in comparing investment wrappers. For other than bare trusts, the same factors as are relevant for higher rate taxpayers will need to be considered in making investment wrapper choices - see (iii) below.

(iii) Investment product wrapper choice

The abolition of taper relief and indexation relief and its replacement with the 18% flat rate has caused much rethinking on investment to take place. The introduction of a 50% income tax rate from 6 April 2010 will necessitate another review as a result of the consequent widening of the gap (for those investors with high incomes) between the taxation of income and capital gains.

In the financial services sector the debate over the most appropriate investment product wrapper for a particular portfolio is one that has been well aired.

As things stand currently,,(and as was always the case,) the choice of the most appropriate investment wrapper remains dependant on the circumstances of each case. At relatively lower levels of investment it is arguable that wrapper choice makes little tax difference.

However, it is clear that with more substantial sums the difference that product wrapper choice can make can be appreciable.

Key variables impacting on the decision are investment term, investor tax, the availability or otherwise of the CGT annual exemption, RPI, and the extent to which investment growth is driven by income (and what sort of income) or capital gains. In general, all other things being equal, one will find that where the investment growth is driven substantially by capital gain, collectives will look “tax best” and where there is high reinvested income, insurance products (bearing no internal tax on reinvested dividends) can look attractive – especially for higher rate taxpayers. As indicated above this conclusion will be even easier to arrive at in respect of those who will be caught by the higher rates of tax – especially the new 50% rate.

Offshore bonds look “tax good” for deferment but less appealing if fully encashed when the investor is a UK resident higher rate taxpayers – especially if the rate is 50%/

And of course, tax is not the only determinant of wrapper choice. Everything starts with portfolio choice. In the current environment there is high interest in income producing funds with income from interest on corporate and government bonds being particularly popular. The importance of reinvested dividends on equity funds has also been reinforced recently. In both cases the insurance structure will look more tax appealing to a higher rate taxpaying investor.

There is also administrative simplicity and appropriateness to hold in trust to consider though. Of course, collectives can be held in trust, it’s just that they may be a little more difficult to administer. How and when benefits are withdrawn is also a factor to take into account in choosing investment wrappers. Bonds (UK and offshore) offer the “5% tax deferred withdrawal” facility and collectives offer the use of the CGT annual exemption for tax free withdrawals of capital. And there’s the scope for “tax arbitrage” between married couples and registered civil partners. Assignment of a collective between these persons gives rise to no chargeable disposal for CGT. It will usually be designed to secure use of another CGT annual exemption to set against the gain made on the collective investment to be disposed of. With an 18% flat rate though, it will no longer be possible to access a lower CGT rate through “spousal assignment”.

Bonds, on the other hand, being insurance contracts can be assigned from anyone to anyone (provided the assignee can give a valid discharge), and lower tax rates can then be accessed and (for offshore bonds) even the personal allowance.

In conclusion then, what these changes tell us is that, more than ever, advice will be necessary when making decisions over the choice of investment wrapper – especially for the more substantial sums and tax will rarely be the only factor to take into account. We have touched on some of the “other” factors above. There is also the not unimportant issue of charges, reductions in yield and total expense rates to take into account.

When the penalty for getting the choice of wrapper wrong is so harsh – reflected in potentially significantly lower post tax returns – its worth taking some time over the choice and then documenting the “reasons why”.

And to the extent that there is uncertainty regarding the variables impacting on the choices, then the principle of “wrapper allocation” will be well worth considering to compliment a risk reducing investment strategy founded on asset allocation.

5. INHERITANCE TAX

5.1 NIL RATE BAND LEVEL

Increases in the nil rate band from 6 April 2008 until 2011 were announced in Budgets 2006 and 2007. For tax year 2009/10 the inheritance tax (IHT) nil rate band has been increased from £312,000 to £325,000. The threshold is to be increased to £350,000 in 2010/11. The Chancellor estimated that only 2% of estates will be subject to IHT in 2009/10 (compared with 5% in 2008/09).

WHICH MEANS THAT ...

For a person with assets of £325,000 or more the increase in the level of the nil rate band in 2009/10 will produce an increased IHT saving of £5,200. Coupled with the transferable nil rate band (see 5.3 below) for a married couple or registered civil partners this can mean that (at current levels of the nil rate band) up to £650,000 of the combined estate could pass free of the IHT.

5.2 EXTENSION OF AGRICULTURAL PROPERTY/WOODLAND RELIEF TO LAND IN THE EEA

The Finance Bill 2009 will introduce provisions to extend agricultural property relief and woodlands relief to property in the European Economic Area (EEA). Property that benefits from the extended IHT relief will also qualify for CGT hold-over relief. This will have effect for tax events on and after 22 April 2009. Furthermore, IHT due or paid on or after 23 April 2003 in relation to agricultural property located in an EEA state at the time of the chargeable event will become eligible for relief. The Finance Bill 2009 will provide that the earliest deadline for reclaiming overpayments on such property will be 21 April 2010.

Woodlands relief (WR)

Where conditions are met, WR allows IHT to be deferred on the value of timber or underwood until it is sold. Before 22 April 2009, WR could only apply in respect of land located in the United Kingdom. The Finance Bill 2009 will extend WR to property in other qualifying EEA states.

For deaths before 22 April 2009, property located within an EEA state will become eligible for WR. The time limit for obtaining WR is usually within two years of the date of death. The Finance Bill 2009 will provide that the earliest deadline for reclaiming overpayments on such property will be 21 April 2010.

CGT Hold-over relief

Hold over relief allows deferral of a CGT charge (on a gift or sale at undervalue of a business asset) until the asset is disposed of by the recipient. The Finance Bill 2009 will extend hold over relief to agricultural property in EEA states which has been farmed by a person other than the owner.

Hold over relief will also become available in respect of disposals of agricultural property located in a qualifying EEA state in the past. The time limit for claiming hold over relief is five years from 31 January following the tax year to which the claim relates. Claims to relief in respect of the tax year 2003/04 can therefore be made until 31 January 2010.

Legislation in Finance Act 2008 has already reduced the time limits for hold over relief claims to four years from 1 April 2010. Claims in respect of 2004/05 and 2005/06 will therefore need to be made by this date.

5.3 TRANSFERABLE NIL RATE BAND

The Finance Act 2008 introduced legislation to allow a claim to be made on the death of the survivor to transfer any unused **nil rate band** on the death of the first of a couple to die to the estate of their surviving spouse or civil partner who dies on or after 9 October 2007.

The new provisions, known as the transferable nil rate band (TNRB), apply to anyone who dies on or after 9 October 2007, regardless of when their spouse died (including deaths before 1986 when IHT was introduced).

WHICH MEANS THAT ...

Following the introduction of the TNRB, many couples with combined assets of up to twice the nil rate band (£650,000 currently), especially those whose main asset is their home, will no longer need, or be interested in, IHT planning. This is not to say that there will be no further use of “first death” nil rate band planning for couples. Some may still see this as valuable [eg those who believe that the value of the assets in question will increase at a rate faster than the expected increase in the nil rate band or where the surviving spouse has already inherited (from an earlier marriage) a 100% multiplier of the nil rate band.]

And even where the TNRB is to be used, the use of an Immediate Post-Death Interest Trust (IPDI), with the immediate life interest being given to the surviving spouse, can ensure that there is certainly over the final destination of the trust assets.

Section 5.4.(2) below gives further consideration of inheritance tax planning for those who wish to pursue it either during lifetime or through the Will on the first death.

5.4 IHT PLANNING

Although the Chancellor estimates that only about 2% of estates will pay inheritance tax in 2009/10, the number of families concerned about the impact of IHT is considerable.

With the nil rate band increasing to £325,000 for tax year 2009/10, and asset values having reduced, now is a good time to consider lifetime gifts for those people who are worried about inheritance tax. In practice, of course, the feasibility of this is likely to depend on the capital and income needs of the would-be donor. The reduction in asset values may have increased these needs. Another challenge to consider is that if we have a change of government the impact of IHT may be reduced. This needs to be carefully borne in mind with any planning that is being carried out now.

As things stand a number of opportunities for mitigating IHT still exist and so, for those who wish to plan, it is important to make maximum use of the current rules for those who believe that they will still have a liability to IHT which they will want to do something about.

In very brief terms the main advantages of the current inheritance tax regime are as follows:-

- a new nil rate band is, in effect, available every 7 years
- the potentially exempt transfer rules remain on the statute book but, in general, only apply to outright gifts and certain gifts to absolute trusts and trusts for the disabled.
- a 100% maximum level of business property relief and agricultural property relief is available, subject to satisfying the appropriate conditions
- planning using deeds of variation can still take place – although the “retrospective” use of the nil rate band in this way is likely to be less well used following the introduction of the transferable nil rate band
- lump sum inheritance tax schemes (eg. discounted gift trusts (DGTs) and loan trusts) that avoid the gift with reservation rules and the rules on pre-owned assets can still be implemented with beneficial results
- there are advantageous rules for excluded property trusts for non-UK domiciliaries who may become UK domiciled or deemed domiciled in the future.

(1) Lifetime gifts

The nil rate band has been increased as indicated above. Individuals who have a potential inheritance tax liability may well be inclined to use their nil rate band sooner rather than later. This will get growth out of the estate and open up the chance of being able to use a fresh nil rate band after 7 years. This means making lifetime gifts.

The 2006 reform of trust taxation severely reduced the scope for making PETs in that lifetime gifts to interest in possession trusts and A&M trusts no longer qualify for PET treatment. Of course, those who are happy to make an outright gift or a gift to an absolute trust will still benefit from the PET treatment ie. that there will be no IHT at all, regardless of the size of the gift, if the donor survives the gift by 7 years. Even if death occurs within 7 years, provided the donor survives for at least 3 years taper relief will apply to reduce any tax charge. Anybody contemplating making substantial lifetime gifts in order to save IHT should sensibly consider doing so whilst PET treatment is available.

Where the potential donor prefers to maintain an element of control over the asset being gifted, this can be achieved by making a gift to a trust. As long as the donor's nil rate band is not exceeded, there will be no immediate IHT to pay. And remember that between them, a husband and wife/civil partners who had not made previous gifts could still transfer £650,000 in this way. Indeed this would increase to £662,000 if they hadn't previously used their £3,000 annual exemptions.

The choice of trust will naturally have to be considered and since 2006 discretionary trusts have become more popular. Remember though that although most trusts (other than bare trusts) are now subject to the same IHT and CGT regime, income tax consequences differ considerably in that they are generally more straightforward for interest in possession trusts. Proper advice should be sought when making any gift to a trust.

Life assurance can be effected to cover any potential IHT liability on the death of the donor within 7 years. Careful consideration needs to be given to the CGT implications of making gifts and the CGT cost of making a gift balanced against the potential IHT saving. However, CGT hold-over relief is now available on gifts to most types of trust.

Detailed consideration of insurance-based plans can be found in (5) below.

(2) Will planning

The introduction of the transferable NRB (see above) means that many couples will be content with passing their entire estate to the survivor on the first death as it will no longer, in most cases, mean the loss of one NRB. However, it is undoubtedly the case that the predictions that nil band trusts will become obsolete have been exaggerated.

The following circumstances give examples of situations when a first death discretionary Will trust may be appropriate:-

- (i) The partners may each be in a second marriage and each of the couple may wish to benefit his/her children from a former marriage on the first death or it may just be that each of the couple does not want the survivor to have complete legal and beneficial control of the assets following first death. Whilst this could technically be achieved using a life interest trust in the Will – known as an immediate post-death interest trust, (with income payable to the surviving spouse and capital held for the children from the first marriage), that route lacks flexibility especially if there is an intention to make capital payments to the widow/widower by way of interest-free loans.
- (ii) There may be a desire to avoid assets being available to the local authority in the event of the survivor going into care. By leaving assets to a trust on the first death those assets will not count as part of the surviving spouse's resources for the purposes of the local authority charge. Indeed, the split ownership of certain assets between a trust and surviving spouse may reduce the value of the assets in the hands of the surviving spouse- for example in the case of a private residence.
- (iii) It may be desired to avoid children inheriting assets outright. By passing assets to them via a trust it will mean that they are protected from the claims of creditors and ex-spouses.
- (iv) Further IHT savings could be secured by the trustees of the Will trust making loans to the surviving spouse if and when funds are needed which create debts and so reduce the taxable estate of the survivor on his/her subsequent death. Here, one would need to identify whether the surviving spouse had previously made lifetime gifts to the deceased because in those circumstances there could be a restriction on the ability to deduct the loans from the survivor's taxable estate. (see section 103(1) Finance Act 1986).

- (v) Where a person has remarried after his/her former spouse has died without using his/her nil rate band, the surviving spouse may have a nil rate band of, currently, up to £650,000 available on his/her death first. Clearly, it would be important to utilise this because otherwise up to £325,000 of the nil rate band could be lost on the survivor's death.
- (vi) It may be felt that investments made subject to the Will trust on the first death will increase in value at a greater rate than the increase in the nil rate band.

Also, even if a discretionary Will trust does come into existence on the first death and, after the first death, this is not required there would, within 2 years of death, be scope to appoint absolutely out of that discretionary trust and achieve the same IHT results as if the asset had passed directly under the Will (see below).

Planning after the first death

In cases where the first of a couple has already died then, clearly, if there was a trust in the Will this will now have come into effect. If the surviving spouse feels that he or she would have had a better inheritance tax position by having available the whole of the nil rate band of the first to die, and the trust is a discretionary trust, the trustees can within 2 years of its creation (on the first death) make an absolute and irrevocable appointment in favour of the surviving spouse. Under section 144 IHT Act 1984 this will mean that such an appointment will be treated for IHT purposes as if the asset was left under the Will directly to the spouse on the first death. This will mean that the assets would be treated as passing directly to the surviving spouse on the first death and so the spouse exemption would apply and all of the nil rate band of the deceased would be freed up for use on the second death.

Three other points arise out of this:-

- (i) An outright appointment should not be made within 3 months of the deceased's death because in those circumstances section 144 will not apply.
- (ii) If it was still desired to use a trust (to control the destination of assets after the survivor's death) yet secure ongoing entitlement to the whole of the deceased's nil rate band, an interest in possession trust could be used. Technically this would be treated as an IPDI (immediate post-death interest) trust and would secure the spouse exemption.
- (iii) As ever, all the tax implications of the appointment would need to be considered – including capital gains tax.

Married couples alive now both with Will trust clauses

In cases where married couples have already made Wills which use the nil rate band on the first death, and both are still alive, it will make sense to consider whether the nil rate band clause is still valid. If they decide, for whatever reason, that it isn't they should:-

- (a) consider amending their Wills now – if they are certain that none of the circumstances described above apply; or

- (b) make sure they can rely on section 144 IHT Act 1984 and appoint benefits within 2 years of the first death to the surviving spouse. This will mean that the nil rate band of the first to die can then be used by the survivor.

(3) Pilot trusts

Given that IHT calculations for trusts generally depend on the value of the gift, the occasion when the trust is created and the subsequent value of the trust property, it will often be advantageous to have more than one trust created on different occasions. For this reason “pilot trusts” have become more popular since 2006.

A pilot trust is a trust set up with a nominal gift (but there must be a transfer of some property to the trustees) with the intention of subsequently adding to it. Such trusts can currently be particularly useful to avoid the related property provisions when it is intended to create more than one trust on death. By having a number of unrelated pilot trusts set up on different days during lifetime it is, under current legislation and case law, in effect possible to use the available nil rate band on death to “seed them” but with each trust being entitled, in effect, to its own nil rate band.

(4) Deeds of variation

Under current legislation, within two years of a person’s death, it may be possible for the beneficiary(ies) of a gift under a Will (or on an intestacy) to vary the destination of the gift. Such a variation can, depending on the circumstances, save IHT.

In the past this provision has been successfully used to establish a nil rate band discretionary trust under the Will of the first spouse to die, when he or she has left all of his/her estate to the surviving spouse.

In these circumstances, if there was a variation in a Will that creates a discretionary nil rate band trust, in the light of the availability of a transferable nil rate band (see above) this will to a greater or lesser extent mean that there will be a loss in the proportion of the transferable nil rate band available on the second death.

But what if a variation has already been made to use the nil rate band and one is still within the two year period since the testator died? Can another variation on that same property be made to rectify the problem and so reinstate the whole of the transferable nil rate band? Well, in these circumstances, aside from needing to obtain the consent of all the beneficiaries affected by the variation, this “double variation” will not work because an instrument will not fall within section 142 IHT Act 1984 if it further redirects any item that has already been redirected by an earlier instrument. However, as explained above, an appointment in favour of the surviving spouse within 2 years will have the result of effectively reinstating the transferable NRB

(5) Lump sum inheritance tax plans

Retention of the right to income and/or capital by the donor (or settlor) of a gift will normally mean that the gift with reservation (GWR) provisions will neutralise any IHT benefit of a gift. If the GWR provisions are avoided, then the POAT (pre-owned assets tax) charge is likely to bite. Certain lump sum inheritance tax plans, usually based on capital investment

bonds, seek to overcome both of these problems and, so far and despite the number of provisions introduced to combat IHT planning, have not been neutralised.

These plans, of which there are a number, will often enable an investor to establish a trust and enjoy some form of “income” (normally in the form of capital payments), possibly provide a level of access to capital and provide some control and flexibility via a trust. Ignoring annuity/life assurance (back to back) arrangements, there are two primary forms of lump sum inheritance tax plan, both based on the combination of a trust and a capital investment bond:-

- (a) The gift and loan (or “loan only”) scheme – a gift is made to a trust (or a trust declared with no gift) and an interest-free loan, repayable on demand, made to the trustees. The trustees invest in a capital investment bond. “Income” is enjoyed in the form of tax free loan repayments financed by the trustees making annual 5% part surrenders from the bond. The investment growth is outside the investor’s taxable estate and free of IHT. HMRC has confirmed to the ABI that this type of arrangement remains effective for IHT and is not caught by the gift with reservation rules and the POAT charges.
- (b) A discounted gift plan – a bond is made subject to a trust where “income rights” in the form of payments of capital are held for the absolute benefit of the settlor (funded by withdrawals from the underlying bond) with the remaining part of the investment held either on a bare trust or a discretionary trust for family. Part of the initial investment (the discounted gift) is either a PET (if the trust is a bare trust) or a chargeable lifetime transfer. In the latter case it is important to ensure that the chargeable transfer does not cause the settlor to exceed his IHT nil rate band or a 20% IHT charge will arise on the excess. As with the loan plans in (a) above, HMRC has confirmed that, in general, the gift with reservation and POAT charges will not apply to this type of plan.

There is little doubt of the appeal that lump inheritance tax schemes hold for people who have investment capital and wish to plan to reduce inheritance tax but wish to retain some access to “income” or capital.

The question of which type of scheme is most appropriate will depend on all the personal and financial circumstances of an investor – not least the age of the investor and the flexibility he or she requires over the future rights to “income”/capital. In larger cases it may well be appropriate for a combination of plans and trust types to be effected in order to achieve the balance between access, “income”, IHT effectiveness and flexibility that any particular client requires.

For those who are concerned that the need for IHT planning may be diminished under a future Conservative government and who wish to make a substantial gift but retain access to the funds given, there may be more of a temptation to use loan trusts as opposed to discounted gift trusts. This is because loan trusts give more flexible access to the whole of the original capital invested and so, if circumstances change, the donor can recoup all of the initial investment.

(6) Business/agricultural property relief

Currently most business and agricultural assets qualify for 100% relief, subject to certain conditions being satisfied, which effectively removes the assets from the inheritance tax net.

Therefore making lifetime gifts will not reduce any potential liability and will generally only be made if it is desired to pass assets to the next generation who are involved in the business.

On the other hand, holdings of shares in non-listed companies where the donor is not personally involved may offer significant planning opportunities – remember these also qualify for 100% BPR after two years of ownership. Care needs however to be exercised in connection with the definition of “listed” for the purposes of IHT business property.

(7) Excluded property trusts

Where a person, who is non-UK domiciled (for inheritance tax purposes), establishes a (normally discretionary) trust and that trust invests in non-UK situs property or UK authorised unit trusts or OEIC funds, under current law the trust will be outside the IHT net forever – even if the settlor later becomes UK domiciled for IHT purposes. This is what is known as an excluded property trust and the trust will not be subject to IHT even if the settlor is a potential beneficiary.

While sweeping changes have been introduced to the taxation of income and gains of the non-domiciled UK residents, (and these clearly need to be taken into account) the rules on excluded property and IHT treatment of excluded property trusts are not changing and so this presents a continuing opportunity.

6. CORPORATION TAX

6.1 RATES OF CORPORATION TAX

The rates of corporation tax for the financial year starting 1 April 2009 are as follows:

- The small companies' rate of corporation tax is maintained at 21% and applies where a company has profits of up to £300,000.
- The main rate of corporation tax is maintained at 28% and applies to profits of a company of more than £1,500,000.
- Between £300,001 and £1,500,000 marginal rate relief applies. This operates to increase the overall rate of tax on the profits to somewhere between the small companies' rate of 21% and the main rate of 28%. Profits in excess of £300,000 will effectively bear tax at the marginal rate of 29.75%.

WHICH MEANS THAT ...

Subject to a company having a corporation tax liability, the structure and form of effective corporate tax reducing strategies can continue to be relevant. In particular, contributions to registered pension schemes (covered in section 13 of this bulletin) can be particularly effective.

It will also be necessary to take full account of the relevant corporate tax rates in determining the best way to take funds from the business i.e. by salary or dividends or pension contributions. This is covered in section 14 - remuneration strategies.

For companies where the profit is in excess of £300,000, any strategy (such as making a deductible employer contribution to a registered pension scheme or incurring expenditure qualifying for 100% capital allowances) to reduce profit in excess of £300,000 will result in an effective corporation tax saving of 29.75%. So, for example, if a company with profits of, say, £350,000 made a £50,000 allowable pension contribution its corporation tax bill would fall by £14,875 making the net cost of the contribution £35,125.

In all pension planning for those members whose income exceeds £150,000 due account needs to be taken of the potential for a special allowance charge (see section 13 for more detail).

6.2 PERSONAL TAX ACCOUNTABILITY OF SENIOR ACCOUNTING OFFICERS

An additional burden is to be placed on senior accounting officers of large companies and large groups of companies that will make them personally responsible for the accounts lodged by the company.

Legislation will be introduced in the Finance Bill 2009 to require:

- senior accounting officers of such companies to take reasonable steps to establish and monitor accounting systems within their companies that are adequate for the purposes of accurate tax reporting;
- senior accounting officers of such companies to certify annually that the accounting systems in operation are adequate for the purposes of accurate tax reporting or to specify the nature of any inadequacies and confirm that those inadequacies have been notified to the company auditors; and
- such companies to notify HM Revenue & Customs (HMRC) of the identity of the senior accounting officer.

Both the senior accounting officer and the company will suffer penalties for a careless or deliberate failure to meet the obligations set out above, and for the giving of a carelessly or deliberately incorrect certificate or notification.

6.3 FOREIGN DIVIDENDS

Foreign dividends and other distributions received are currently chargeable to corporation tax, with credit given for any foreign tax withheld from a dividend and (for shareholdings of 10 per cent or more) for foreign tax charged on the profits out of which the dividend is paid (underlying tax). Currently UK distributions received are generally exempt from corporation tax.

New legislation will be introduced which will treat foreign and UK distributions in the same way. Distributions will generally be exempt if they fall into an exempt class and anti-avoidance provisions do not apply. The vast majority of distributions are expected to be exempt from corporation tax. In addition to the changes announced in the 2008 Pre-Budget Report, exemption for dividends or other distributions arising from holdings of ten per cent or more will be extended to all companies.

These changes will apply to distributions received after 30 June 2009.

7. CAPITAL ALLOWANCES

Most of the changes being made to capital allowances from April 2008 were announced before this Budget, some as far back as Budget 2007. The first thing to note from the outset is that from 1 April 2009 most assets will fall into one of two pools, the general plant and machinery pool or the special rate plant and machinery pool.

7.1 ANNUAL INVESTMENT ALLOWANCE ON PLANT & MACHINERY

In April 2008 a new annual investment allowance (AIA) giving 100% tax relief for the first £50,000 of a business's expenditure on most plant and machinery each year was introduced.

The AIA is available to:

- any individual carrying on a qualifying activity (this includes trades, professions, vocations, ordinary property businesses and individuals having an employment or office);
- any partnership consisting only of individuals; and
- any company (subject to certain limitations).

Where businesses spend more than £50,000 in any chargeable period, any additional expenditure will be dealt with in the normal capital allowances regime, entering either the special rate or main pool, where it will attract WDAs at the appropriate rate.

The AIA complements and does not replace any of the existing 100 per cent first-year allowance (FYA) schemes. Similarly, expenditure that qualifies for 100 per cent allowances under separate capital allowances codes (for example, Research & Development Allowances or Business Premises Renovation Allowances) will be unaffected by the introduction of the AIA.

7.2 EXPENDITURE IN EXCESS OF AIA - "TEMPORARY FIRST YEAR ALLOWANCE"

A temporary 40 per cent (rather than 20%) first-year allowance (FYA) will apply for expenditure on general plant and machinery that exceeds the AIA. That is expenditure on plant and machinery that would normally be allocated to the main capital allowance pool.

The 40% rate will apply to any expenditure made between 1 April 2009 and 31 March 2010 for companies and 6 April 2009 and 5 April 2010. This will apply to annual expenditure in excess of the Annual Investment Allowance.

As announced last year, the main rate of writing-down allowances for new and unrelieved expenditure on general plant and machinery (including cars) allocated to a pool will be reduced from 25 per cent to 20 per cent.

7.3 THE SPECIAL RATE POOL

From 1 April 2008 (corporation tax) or 6 April 2008 (income tax) a new special rate pool was introduced. With effect from those dates, expenditure on long-life assets, thermal insulation and integral features are allocated to the new special rate pool and the rate of writing down allowance applicable to that pool will be 10 per cent per annum on a reducing balance basis.

7.4 INDUSTRIAL BUILDINGS ALLOWANCE, AGRICULTURAL BUILDINGS ALLOWANCE AND ENTERPRISE ZONES.

Industrial and agricultural buildings allowances ended in April 2009.

The withdrawal of the 100% enterprise zone allowance will have effect on and after 1 April 2011, for businesses within the charge to corporation tax, and 6 April 2011 for businesses within the charge to income tax. The withdrawal will not be subject to the phasing out that will apply to the other two allowances.

7.5 LONG-LIFE ASSETS

The rate of writing down allowances on long-life assets is now 10% (previously 6%). Any unrelieved expenditure in the long-life asset class pool will, for chargeable periods starting on or after the operative date, be allocated to a new, 10 per cent “special rate” pool. Long-life asset pools ceased to exist for all accounting periods starting on or after 1 April 2008 for businesses charged to corporation tax and 6 April 2008 for other businesses. There will be transitional provisions where a business’s chargeable period spans the dates given above.

7.6 NATURAL GAS, BIOGAS AND HYDROGEN REFUELLING EQUIPMENT

The 100 per cent FYA for expenditure incurred on natural gas and hydrogen refuelling equipment, due to end on 31 March 2008, was extended to 31 March 2013. Its scope has also been extended to include refuelling equipment for biogas.

7.7 EXPENDITURE ON CARS

There are special capital allowances rules for cars. While expenditure on cars costing less than £12,000 is allocated to the main capital allowances pool, expenditure on cars costing over £12,000 is required to be accounted for separately from other assets with each car placed in a single asset pool. Writing down allowances are calculated in the normal way (at 20 per cent) for cars in a single asset pool but they are then restricted to an annual amount of £3,000.

The special rules that restrict the amount of capital allowances for cars costing more than £12,000 will be replaced by new rules. Qualifying expenditure incurred on cars on or after 1 or 6 April 2009 will be allocated to one of the two general plant and machinery pools depending on the car’s CO₂ emissions. Expenditure on cars with CO₂ emissions exceeding 160g/km will be dealt with in the special rate pool and attract WDA at 10 per cent. Expenditure on cars with CO₂ emissions of 160g/km or less will be added to the main rate pool and attract WDA at 20 per cent per annum. Expenditure incurred before April 2009 will

continue to be subject to the old “expensive” car rules for a transitional period of around five years.

7.8 FIRST-YEAR TAX CREDITS

From 1 April 2008 loss-making companies will be able to surrender losses attributable to 100 per cent first-year allowances (enhanced capital allowances) on designated energy-saving or environmentally-beneficial plant and machinery in exchange for a cash payment (a first-year tax credit) from Government provided the loss cannot otherwise be relieved.

A company will receive a first-year tax credit of 19 per cent of the loss surrendered, although this is subject to an upper limit. The upper limit of the tax credit will be the greater of:

- the total of the company’s PAYE and National Insurance Contributions (NICs) liabilities for the period for which the loss is surrendered; and
- £250,000.

7.9 ENERGY EFFICIENT AND WATER SAVING (ENVIRONMENTALLY-BENEFICIAL) TECHNOLOGIES

Currently two schemes exist that give 100 per cent FYAs for expenditure on certain energy-saving and water technologies. The schemes are aimed at businesses investing in designated technologies that reduce energy consumption, save water or improve water quality. It was announced in the Budget that the Government intends to increase the list of technologies that are covered by the schemes.

The qualifying technologies are published in the Lists: the Energy Technology Criteria List and Water Technology Criteria List. Every year these lists are reviewed by the Department of Energy and Climate Change (DECC) and the Department for Environment, Food and Rural Affairs (Defra) respectively, to ensure that the qualifying technologies, and the criteria that technologies must meet if they are to qualify for the relief, are still relevant.

Following this year’s review, the energy efficient scheme list will be revised to include one new technology (uninterruptible power supplies) and two new sub-technologies (air to water heat pumps and close control air conditioning systems). Three existing sub-technologies (air source: single duct and packaged double duct heat pumps, ground source: brine to air heat pumps and water source: packaged heat pumps) will be removed.

WHICH MEANS THAT ...

Capital allowances continue to be an important feature of tax life for businesses. Of course, as for any expenditure, businesses should consider carefully the commercial appropriateness of any investment. As ever, the tax tail should never be allowed to wag the dog - however attractive the tail is! Advisers must be fully aware of the capital allowance system so that they can properly advise their business clients on the tax impact of various items of expenditure.

Especially at a time when businesses may be “cash constrained” there may well be “competition” for available expenditure say between making a pension contribution and

purchasing capital equipment. While tax is important it should never be the determinant. Especially with interest rates at their current low levels some businesses with occupational schemes may consider the merits of trying to secure “the best of both worlds” through a deductible pension contribution and (subject to satisfying the usual conditions) loan back to make the purchase of capital equipment qualifying for 100% Annual Investment Allowance or Temporary 40% First Year Allowance. Of course, before making such a decision all of the implications, commercial and tax must be carefully weighed up.

8. LIFE POLICYHOLDER/LIFE COMPANY TAXATION

8.1 LIFE POLICYHOLDER TAXATION

8.1.1 Tax avoidance using life policies

Targeted anti-avoidance legislation will be introduced in Finance Bill 2009 to counter certain tax schemes which involve the use of offshore life policies to secure a claim for income tax loss relief.

Draft legislation, published on 1 April, proposes an amendment to section 152 Income Tax Act 2007 (ITA). Section 152 provides for loss relief against “miscellaneous income”. For this purpose miscellaneous income includes offshore income gains (ie. gains arising on the disposal of units/shares in offshore non-distributor funds).

Miscellaneous income also includes chargeable event gains arising under policies which fall within section 531(3) Income Tax (Trading and Other Income) Act 2005 (ITTOIA). Such policies are those for which no basic rate tax relief is available on a chargeable event gain because the underlying investment fund has not suffered tax at a rate of at least 20%. These section 531(3) policies are:-

- (i) Those forming part of the tax exempt business of a friendly society.
- (ii) Offshore policies (ie. policies issued by a non-UK resident life company) other than those which are qualifying policies.
- (iii) Annuities paid from a fund which has not been subject to corporation tax.
- (iv) An offshore capital redemption policy.

Where instead of a chargeable event gain, a loss arises on such policies then under section 152 ITA the loss can be set against miscellaneous income in general.

From the explanatory note that accompanies the draft legislation it would seem that losses generated from offshore life policies have been used to avoid tax on offshore income gains.

To prevent what is seen by HMRC as abuse, gains from section 531(3) ITTOIA policies will no longer fall within section 152 ITA with the result that any losses generated by such policies will not be available to support a claim for loss relief against miscellaneous income.

The legislation will apply to all losses arising on or after 6 April 2009. In addition, losses claimed for in previous years which would not be relievable under the new proposed legislation cannot be used after 5 April 2009.

Policies affected are those issued on or after 1 April 2009, and pre-1 April 2009 policies which are varied on or after that date so as to increase the benefits. Also affected are pre-1 April 2009 policies which, on or after 1 April 2009, are assigned to the person claiming relief or used as security for a debt of the person claiming relief

Apparently it is the view of HMRC that such losses have never been relieviable but the proposed legislation has been introduced to put the matter beyond doubt.

It is important to note that this change will not impact on deficiency (loss) relief whereby, broadly, a loss arising on a final chargeable event (such as death giving rise to the payment of benefits or full surrender) can be offset against income subject to higher rate tax to secure 20% tax relief. The amount of loss that can be offset in this way is restricted to the amount of any chargeable event gains that have previously arisen under the policy. The purpose of this relief is to relieve gains that may previously have suffered income tax and not to provide relief for investment losses.

8.2 LIFE COMPANY TAXATION

8.2.1 Simplification

Legislation is be introduced in Finance Bill 2009 to

- Clarify the law relating to the tax treatment of amounts introduced by shareholders into the long term insurance fund (LTIF) of a life insurance company.
- Restrict the Case I deduction for amounts allocated to policyholders in certain exceptional circumstances.
- Clarify the transitional rules governing relief for repayments of contingent loans taxed under section 83ZA of the Finance Act (FA) 1989.
- Amend the rules governing the calculation of the 'floor' for gross roll-up business investment return to ensure consistent treatment of foreign business assets.
- Change the anti-avoidance rules relating to value shifting to ensure that they will not apply when a reduction in value arises as a result of a transfer of long-term insurance business between companies in the same group.

These changes are largely effective from 22 April 2009.

9. TAX AVOIDANCE

As has become a feature of recent Budgets the Chancellor announced a series of anti-avoidance measures.

As might be expected, the measures apply to some complex transactions. Set down below are the areas affected, with a reference to the relevant Budget Note if further information is required.

•	Sale of Lessor Companies	BN 12
•	Financial Arrangements	32
•	Plant and Machinery Leasing	33
•	Foreign Exchange Losses	35
•	Transfers of Income Streams	36
•	Disguised Interest	37
•	Interest Relief (see our bulletin of 27.03.09)	38
•	Manufactured Interest	39
•	REITS – Artificial Restructuring	41
•	Life Insurance Policies	57
•	Employment Income	58
•	Double Taxation Relief	60 & 61
•	Publishing the Names of Deliberate Tax Defaulters	63

10. STAMP DUTY LAND TAX / STAMP DUTY

10.1 TEMPORARY INCREASE IN THRESHOLDS

In September 2008 the Chancellor announced a “holiday” from stamp duty land tax (SDLT), which exempted from SDLT any acquisitions of residential property for not more than £175,000. The measure applied to acquisitions between 3 September 2008 and 2 September 2009 inclusive.

The Chancellor has announced that regulations will be introduced to confirm that the starting threshold for SDLT on residential property will increase from £125,000 to £175,000 on transactions made between 22 April 2009 and 31 December 2009 inclusive. After that date the SDLT threshold for residential property will revert to £125,000.

Individuals who are purchasing residential property between 22 April 2009 and 31 December 2009 will therefore not pay SDLT where the chargeable consideration for the property is no more than £175,000.

It should be noted that for these purposes, the effective date is normally the date of completion, not the date of exchange of contracts. However, the effective date may be earlier than the date of completion if the contract is substantially performed, for example, if the purchaser takes possession or pays the purchase price in advance of completion.

10.2 TREATMENT OF SHARED OWNERSHIP

Legislation will be introduced in Finance Bill 2009 to:

- extend favourable stamp duty land tax (SDLT) treatment to purchasers under shared ownership schemes operated by profit-making Registered Providers of Social Housing, where the scheme is assisted by public subsidy;
- extend the SDLT relief for purchases by Registered Social Landlords (RSLs) to profit-making Registered Providers of Social Housing where the purchase is assisted by public subsidy; and
- simplify the SDLT treatment of purchasers under rent to shared ownership (“Rent to HomeBuy”) schemes.

This will benefit individuals who are:

- seeking affordable housing, and are purchasing housing under a rent to shared ownership scheme;
- seeking affordable housing under a shared ownership scheme operated by a profit-making Registered Provider of Social Housing, where the scheme is assisted by public subsidy; and

- Registered Providers of Social Housing who receive assistance from public subsidy.

A new type of shared ownership scheme, “Rent to HomeBuy”, helps individuals to purchase homes using shared ownership schemes by allowing them initially to occupy the property under an Assured Shorthold Tenancy, to allow them to save for a deposit. Under current rules, the SDLT treatment of these schemes can be complex, the Finance Bill 2009 will therefore simplify the SDLT rules for these schemes.

11. TRUST TAXATION

In the Pre-Budget report in November 2008, the Chancellor announced that the trust tax rate would increase to 45% with effect from 6 April 2011. In his Budget the Chancellor not only increased the tax rate that will apply to trusts but also brought forward the date of implementation to 6 April 2010.

With effect from 6 April 2010, the 40% trust rate will increase to 50% (with the dividend rate increasing to 42.5% from 32.5%). This is a serious increase for trustees and, unlike the 50%/42.5% rates for individuals, it is not restricted to income that exceeds £150,000.

WHICH MEANS THAT...

For settlor-interested trusts, if the settlor is not a higher rate or 50% taxpayer he/she will be able to recover the overpaid tax. This means there will be occasions where a higher rate (ie. 40%) taxpayer will be entitled to reclaim the excess 10% tax.

For all other discretionary trusts there will be at least a 25% increase in tax on trust income although it should be remembered that such trusts will, in general, qualify for the £1,000 standard rate tax band for tax year 2009/10. Action that the trustees could take to reduce exposure to the new higher rate tax could include the following:-

- Subject to considering important investment suitability and risk they could consider reinvesting in capital growth orientated assets with a view to reducing taxable income and replacing it with assets that will produce capital gains. The use of the trustees' annual exemption with an 18% CGT rate on excess gains will be more appealing than the new income tax rates. It should of course be borne in mind that the trustees' annual CGT exemption may be diluted where the settler has created more than one trust.
- Life insurance investment bonds could look more tax attractive as trustee investments to the extent that the chosen investment portfolio produces income. Inside a UK bond dividends will be reinvested tax-free and other income will, broadly speaking, be taxed at 20%. There will be no tax inside an offshore bond. The tax rates on encashment (for the settlor or trustees as appropriate) will, however, rise to 30% and 50% respectively. The usual strategies to minimise tax on withdrawing benefits will be appropriate and, in particular, the potential to assign policies "in specie" (and tax free) to potentially lower rate taxpaying beneficiaries before encashment occurs.
- Where the trust has non-taxpaying or 10%/basic rate taxpaying beneficiaries and the trust has income, it could make good tax sense for the trustees to make income distributions in order to enable that beneficiary to recover some of the higher rate tax suffered by the trustees. It should not be forgotten however that a beneficiary cannot recover the 10% tax credit on dividend income paid to the trust even though the payment to him/her from the trust is classified as income from a trust.

12. SAVINGS AND INVESTMENTS

12.1 OVERVIEW

Managing one's investments (incorporating appropriate asset allocation) to produce acceptable returns, whilst managing risk, takes absolute priority in portfolio planning. However, maximising the tax efficiency to minimise tax on investments can substantially add to the bottom line.

We cover pensions and life assurance policies elsewhere in this bulletin but in this section we will look at

- ISAs
- The Child Trust Fund
- Venture Capital Trusts and Enterprise Investment Schemes
- Offshore funds

Changes were proposed to all of these.

12.2 ISAs

(i) Individual Savings Accounts (ISAs)

The ISA is still the main non-pensions method of investing savings with freedom from income tax and capital gains tax. From 6 April 2009 the annual contribution limit is maintained at £7,200, with the maximum contribution to a cash ISA being £3,600. From 6 October 2009 the maximum contribution for those aged 50 and over is raised to £10,200 (for the 2009/10 tax year), with the maximum contribution in cash being £5,100.

From 6 April 2010 the new limits will apply to all ISA investors.

COMMENT

This substantial increase in the investment limit (for older investors first), while valuable to all, will be particularly welcome for those who will be adversely affected by the removal of higher rate tax relief on pension contributions and those who will pay the higher 50% rate of tax on income.

The value of the tax freedom on income delivered by the ISA will effectively increase for prospective 50% taxpayers.

The ISA/pension comparison was one that was valid even for 20% and 40% taxpayers, it is even more so for those who will pay 50% tax on income - especially where they will receive only basic rate relief on their pension contributions.

The appeal of making a contribution attracting 20% relief but paying tax on income at (possibly) 40%/50% will be questionable. This is especially so where the investor can secure tax free growth and income in the ISA.

It is thus thought that the combination of the increasing of the ISA input limit together with the introduction of the 50% tax rate and limitation of pensions tax relief to basic rate for certain high earners will serve to give the ISA market a significant boost.

12.3. CHILD TRUST FUND

Every eligible child born on or after 1 September 2002 has a Child Trust Fund account. Family and friends can contribute up to £1,200 into the account each year.

In this Budget, it is proposed that the Government will make payments of £100 per year into the Child Trust Fund accounts of all disabled children. Severely disabled children (those who receive the High Care element of Disability Living Allowance) will receive £200 per year. These payments will not count towards the £1,200 yearly contribution limit.

COMMENT

Where amounts in excess of the Government - provided CTF payments (at whatever level) are to be committed to child's savings, contributors requiring more control over when the funds invested are released may find a separate discretionary trust with suitable underlying investments more appropriate.

Of course, thought should also be given to appropriate tax exempt friendly society plans.

12.4 VENTURE CAPITAL SCHEMES

Proposals have been made that will affect:-

- investors receiving tax relief under the Enterprise Investment Scheme (EIS), Corporate Venturing Scheme (CVS) and the Venture Capital Trust (VCT) scheme;
- companies attracting investment under those schemes;
- Venture Capital Trusts; and
- EIS Investment Funds.

For EIS, the measure proposed:-

- relaxes the time limits concerning the employment of money invested;
- removes the link to other shares of the same class issued at the same time as qualifying shares;
- extends the period for carry back of relief and allows the full amount subscribed (subject to the overriding limit) to be carried back; and
- corrects an anomaly regarding the capital gains position for investors in the event of a share for share exchange.

For CVS and VCT, the measure relaxes the time limits concerning the employment of money by companies receiving investment.

The measure in respect of the employment of money will have effect for EIS and CVS investments made on or after 22 April 2009. The removal of the link to other shares issued at the same time will apply to shares issued on or after 22 April 2009 and the correction of the capital gains anomaly to new holdings issued on or after 22 April 2009. In relation to the carry back of relief it will apply to the tax year 2009-10 and subsequent years. For VCT schemes the changes will apply to investments made out of funds raised by VCTs on or after 22 April 2009.

The background to these changes is as follows:

- (i) The EIS currently requires that 80 per cent of the money raised by the issue of shares be employed for the purposes of a qualifying activity within 12 months of the issue of the shares or, if later, of the commencement of a qualifying activity. The balance is required to be employed within a further 12 months. The Finance Bill 2009 will replace these rules with a single requirement that all of the money raised by the issue of shares be wholly employed within two years of the issue of shares or, if later, within two years of the commencement of a qualifying activity.
- (ii) In addition, the investee company is currently required to use money raised from the issue of other shares on the same day and of the same class as the EIS shares within the same time limits. This link is being removed and there will be no restriction on the use of money raised by the issue of non-EIS shares.
- (iii) Currently an investor may carry back income tax relief to the previous year by claiming that qualifying shares are treated as having been issued in the previous year. This is restricted to shares issued before 6 October and subject to a limit of half of the subscriptions in that period, up to an overall limit of £50,000 subscribed. The Finance Bill 2009 will remove these restrictions. The total investment that can be taken into account for the purposes of calculating income tax relief for any particular year will remain subject to a limit, currently £500,000 subscribed.
- (iv) It is currently possible that a charge to capital gains tax can occur on a share for share exchange where such a gain would not normally be charged. The Finance Bill 2009 removes the rules that prevent the normal share for share exchange capital gains tax rules from applying to the gain on the disposal of shares when all deferral relief has been recovered. Now on the occasion of a qualifying (under sections 135 and 136 of the Taxation of Chargeable Gains Act 1992) share for share exchange, any deferral relief given will be recovered as before but no gain or loss will be brought into charge in respect of the disposal of the shares that form the subject of the exchange.
- (v) The CVS and VCT schemes currently require that 80 per cent of the money received by the investee companies must be wholly employed for the purposes of the relevant trade within 12 months and the balance within a further 12 months. The Finance Bill 2009 will replace these rules with a single requirement that all the money raised must be wholly employed within two years, or, if later, within two years of the commencement of the qualifying activity.

12.5 PERSONAL DIVIDENDS FROM OFFSHORE COMPANIES AND OFFSHORE FUNDS

Important changes have been proposed to the taxation of dividends paid from offshore companies and funds.

For the purposes of this bulletin we will separately consider dividends from:

- Offshore companies (which aren't offshore funds/collectives) and
- Offshore funds.

(i) Personal dividends from offshore companies (non funds)

When dividends from *UK resident companies* are charged to tax, shareholders are entitled to a non-payable tax credit of one ninth of the distribution under the provisions of section 397(1) of the Income Tax (Trading and Other Income) Act 2005 (ITTOIA). Because tax is charged on the gross dividend received, including the tax credit, this lowers the effective rate on these dividends at the personal level to 0 per cent for basic rate taxpayers and 25 per cent for higher rate taxpayers.

Section 397A of ITTOIA, introduced by the Finance Act 2008, extended the non-payable tax credit of one ninth of the distribution to individuals in receipt of dividends from non-UK resident companies, if they own less than a 10 per cent shareholding in the distributing non-UK resident company regardless of the territory in which the company is resident provided the company is not an offshore fund.

Legislation in Finance Bill 2009 will amend section 397A of ITTOIA to extend further eligibility for the non-payable tax credit to individuals in receipt of dividends from non-UK resident companies where the individual owns a 10 per cent or greater shareholding in the distributing non-UK resident company. The tax credit will however only be available if the source country is a "qualifying territory". A territory is a "qualifying territory" if there is a double taxation agreement with the UK, with a non-discrimination article. Regulations will permit HM Treasury to vary the list of qualifying and non-qualifying territories. Luxembourg and Ireland, are for example, qualifying territories.

The legislation will include anti-avoidance measures, including a targeted anti-avoidance rule, to counter the use of conduit structures designed to secure the tax credit for dividend income originating other than in a qualifying territory, to ensure that these new rules are not subject to abuse.

This relaxation does not apply exactly as stated to offshore funds.

The new rules for *offshore funds paying dividends* are covered in section (ii) below.

(ii) Personal dividends from offshore funds

Legislation has been proposed which substantially aligns the categorisation and taxation of dividend paying offshore funds with that of UK funds in relation to the extent to which the fund is invested in equities and debt (interest producing) investments.

Currently all distributions from offshore funds are received and taxed as dividends. The “UK” concept of an “interest distribution” does not exist for offshore funds.

Since 6 April 2008, individual shareholders with shareholdings of less than 10 per cent in non-UK resident companies (see (i) above) have been entitled to a non-payable dividend tax credit. This tax credit resulted in tax freedom for non and basic rate taxpayers on such “interest-fuelled” dividends and a 22.5% rate for higher rate taxpayers (32.5% - 10%).

However, the tax credit was withdrawn for offshore funds as some collective investment schemes were seeking to exploit the extension by locating their cash or bond fund ranges offshore, with the intention of securing tax advantages by paying dividends funded by non taxed interest which carried a 10% tax credit. So, as things stand, before the latest proposed amendments, distributions made as dividends from offshore funds received by individual UK resident shareholders are currently taxed at rates of 10 per cent for basic rate and 32.5 per cent for higher rate taxpayers regardless of the nature of the investments underlying the fund. Where the distributions are from non-corporate offshore funds they may be taxable at different rates depending on the type of fund and (in some cases) the nature of the fund income.

Legislation in Finance Bill 2009 will amend section 397A of the Income Tax (Trading and Other Income) Act 2005 to extend further eligibility for the non-payable tax credit to individuals in receipt of dividends from non-UK resident companies *including offshore funds that are companies*.

However, where the offshore fund holds more than 60 per cent of its assets in interest-bearing (or economically similar) form, any distribution will be treated in the hands of the UK individual investor as a payment of yearly interest. This will mean that no tax credit will be available and the tax rates applying will be those applying to interest.

This mirrors the current treatment of UK corporate investors with holdings in similar funds (in the UK or offshore) and also means that UK individuals will pay tax on interest-like distributions at the same rate as tax is borne by individual investors on interest distributions received from UK authorised funds. This change is proposed to take place from 22 April 2009.

This change will not affect the taxation of UK investors in offshore funds which are transparent for the purposes of tax on income as in such cases the investor is taxed on their share of the underlying fund income according to the type of income received and not on the distribution made.

12.6 DEFINITIONS OF OFFSHORE FUNDS

Under current legislation, the definition of an investment in an offshore fund is based upon the regulatory definition of ‘collective investment scheme’ as set out in the Financial Services and Markets Act 2000, with modifications for tax purposes.

The new definition of an offshore fund uses a characteristics based approach which has been the subject of detailed consultation with the funds industry as set out in the relevant HM Treasury documents. There are also exceptions specified in the legislation to ensure that fixed share capital arrangements that do not mimic open-ended arrangements will remain outside

the definition. This includes specific provisions for continuation votes and capital only arrangements.

12.7 TAX ELECTED FUNDS

Under current rules, UK Authorised Investment Funds (AIFs) are normally chargeable to corporation tax on taxable income at a special rate of 20 per cent.

That will remain the case under the new regime, but UK AIFs that meet certain conditions will be able to elect to be treated as a tax elected fund (TEF). TEFs will be required to make two types of distribution of the income they receive - a dividend and a non dividend (interest) distribution. UK dividend income will remain non taxable in the fund and will be distributed as a dividend. For all other income that is distributed as a non-dividend (interest) distribution, the fund will receive a tax deduction up to the same amount. The new regime will be introduced by secondary legislation.

UK investors are treated as receiving UK dividend income (including the non payable dividend tax credit) and a payment of yearly interest.

12.8 CHARGEABLE GAINS AND OFFSHORE FUNDS

UK investors are most familiar with offshore funds constituted as companies or trusts. Some funds are, however, created by contractual arrangement. These are currently treated as “transparent” for the purpose of capital gains tax with gains made by the fund being assessed on the investor.

Legislation will be introduced in Finance Bill 2009 to provide similar treatment to that given by section 99 of the Taxation of Chargeable Gains Act 1992 for investments in unit trusts to investments in other types of offshore fund which are not companies, unit trusts or partnerships.

The effect of this change will be that an interest in a transparent offshore fund will be an asset for the purpose of calculating capital gains tax on chargeable gains (as is already the case for shares in a company or units in a unit trust). Investors will no longer be required to consider disposals of the underlying assets for calculating capital gains tax on chargeable gains.

The Government will also discuss with industry how to make similar changes to the tax treatment of chargeable gains for investors subject to corporation tax.

There will be no effect on interests in tax transparent foreign partnerships which will continue to be treated as transparent for both income and gains in the same way as United Kingdom partnerships.

13. PENSIONS

13.1 RESTRICTING TAX RELIEF FOR HIGH INCOME INDIVIDUALS

The Government intends from 6 April 2011 to restrict tax relief for individuals with an annual income of £150,000 or more. Relief will be tapered away so that for those earning over £180,000 relief will be worth 20 per cent, the same as for a basic rate taxpayer. Details of how this tapering will work have not yet been made available.

In order to avoid individuals increasing their regular pension contributions prior to 6 April 2011 to forestall the above new rule, the Government is introducing new rules to apply from 22 April 2009 to restrict higher rate tax relief on pension contributions for individuals between 22 April 2009 and 5 April 2011 inclusive ie. from the date of the Budget until the new rules take effect.

The Finance Bill 2009 will introduce a new and additional special annual allowance and an associated tax charge. The special annual allowance charge sets an upper limit on the amount of additional pension savings for which full relief at the higher rates of tax will be available. This is set as £20,000 for tax years 2009/10 and 2010/11. Above this level the additional pension savings will be subject to a tax charge which will have the effect of restricting the tax relief to basic rate. For tax year 2009/10 the tax charge will be 20%. The tax charge has not yet been set for tax year 2010/11 but is likely to be 30% to tie in with the new 50% tax band in 2010/11. This new charge will not apply to any normal ongoing regular pension savings that were already in place before 22 April 2009 provided there has been no change to the pattern of those contributions or the way in which the benefits are accrued.

This new charge will only apply to people with incomes of £150,000 or more, who on or after 22 April 2009, change:

- Their normal pattern of regular pension contributions; or
- The normal way in which their benefits are accrued;

And where their total pension contributions/benefits accrued exceed £20,000 a year.

When assessing whether an individual's income is in excess of £150,000, his income will be assessed for the tax year in question (ie. 2009/10) and the two immediately preceding tax years and if his income exceeded £150,000 in any one of these tax years he will be deemed to be covered by these provisions.

The definition of income will embrace an individual's total income for the tax year, including unearned income less any normal deductions for relief (e.g trading losses), including pension contributions but only up to a maximum of £20,000. Gift aid contributions can also be deducted. It will also include any remuneration that has been sacrificed by the individual in return for the payment of an employer pension contribution or increased pension benefits, where the salary sacrifice took place on or after 22 April 2009.

Regular pension contributions are defined as the contributions being paid quarterly or more regularly. The normal pattern of such contributions would not be regarded as being changed

where they are determined as a fixed percentage of salary or where they are paid as an amount that will contractually increase by a fixed percentage each year. It is interesting to note that contributions paid annually would not be regarded as regular contributions.

Regular pension accrual applies where the member is accruing benefits under a final salary scheme and there is no change in the rate of accrual (e.g from N/60ths to N/45ths).

When assessing the £20,000 limit this will apply to all contributions paid to money purchase schemes in respect of a member on or after 22 April 2009 irrespective of whether the contribution has been paid by the member, his employer or a third party. When assessing this limit for a member of a defined benefit scheme the normal ten times multiplier will be applied to the increase in the member's pension benefits under the scheme on or after 22 April 2009 in respect of the tax year concerned.

This special annual allowance charge will be assessed in respect of pension savings accrued between 22 April 2009 and 5 April 2010 for tax year 2009/10 and on a tax year basis for each subsequent tax year. The tax charge will be collected via an individual's self assessment tax return.

Where an individual is subject to an annual allowance charge as well as the special annual allowance charge, the amount chargeable to the special annual allowance charge will be reduced by the excess over the existing annual allowance to avoid a double tax charge.

Where an individual is subject to the new special annual allowance charge he may be able to seek a refund of his personal contributions. This will be subject to the scheme rules permitting such a refund and the scheme administrator agreeing to the refund. The refund would not be made until the tax year following the tax year in which the contributions were paid. For example where a refund was made in tax year 2010/11 in respect of personal contributions paid in tax year 2009/10 this would be subject to a tax charge of 40%.

The Disclosure of Tax Avoidance Schemes (DOTAS) regime will be amended. The Descriptions Regulations (SI 2006/1543) will be amended to include a new description: arrangements where one of the main benefits of an individual entering the arrangement might be expected to be that the individual will not be subject to the special annual adjustment charge, which charge they would have been subject to had they not entered into those arrangements.

It is interesting to note that the expected tax recovery by HMRC in respect of this change in tax years 2009/10 and 2010/11 before the main change commences is zero. While a need can be seen for this transitional anti avoidance provision it drives a further nail in the coffin of pensions simplification and ranks in complexity with the ASP and IHT changes, the recycling of tax-free cash rules and the treatment of pension term assurance contributions. In all these cases highly complex rules have been imposed which are many miles from the initial pensions simplification concept.

13.2 LIFETIME ALLOWANCE/ANNUAL ALLOWANCE

The standard lifetime allowance and the annual allowance have been increased in tax year 2009/10 to the already legislated levels of £1.75 million and £245,000 respectively.

The Chancellor proposed in the November Pre-Budget Report that the standard lifetime allowance and the annual allowance would remain at their levels in tax year 2010/11 of £1.8 million and £255,000 respectively for the following five tax years (i.e. up to and including the tax year 2015/16).

When the new regime started in 2006, the Treasury announced the levels of the standard lifetime allowance and the annual allowance for the 5 tax years ending in 2010/11. While these allowances increased in each tax year, there was no guarantee that they would be uprated subsequently as this would be subject to the discretion of the Treasury when it reviewed the limits for the next 5 tax years.

The freezing of the standard lifetime allowance (SLA) will not only affect those individuals whose retirement funds are likely to exceed that level but will also affect benefits that are either based on a percentage of the SLA (e.g. the trivial commutation limit) or that increase in line with the SLA (e.g. protected pre A-Day cash). HMRC have indicated that other benefits based on the SLA will also be restricted by the freezing of the SLA limit unless a separate announcement is made in respect of them.

It is particularly interesting to see the potential impact on a member's scheme specific protected cash of the freezing of the SLA. For a member in such circumstances their cash is determined as the aggregate of two calculations:

1. The first element is based on increasing their protected cash as at 5 April 2006 in line with changes in the SLA up to the date benefits are drawn. The cap on the SLA will restrict this element of the cash calculation where benefits are drawn in tax years 2011/12 to 2015/16.
2. The second part of the calculation potentially provides further cash, using the ALSA formula, of 25% of the difference between the value of the member's pension rights when the cash is taken and the value of his pension rights as at 5 April 2006 increased in line with changes in the SLA up to the date benefits are drawn. In this case the cap on the SLA will increase the likelihood of an additional cash sum as any increase in the member's actual fund value above the capped revalued fund (ie. fund value as at 5 April 2006 increased in line with SLA) is available as extra PCLS.

The freezing of the SLA may also inhibit pension contributions/accrual for those individuals whose present benefits are close to but do not currently exceed the SLA. These individuals may well have made an assumption that the SLA would be increased each year by the Treasury. They may now be worried that the Treasury may extend the freezing of the SLA beyond tax year 2015/16, which could result in their benefits exceeding the SLA.

The freeze may also encourage a delay in contributions until close to retirement: as current market conditions have demonstrated, fund values can move significantly in a short period.

13.3 STATE BENEFITS

The Basic State Pension has been increased in line with the increase in the RPI to £95.25 per week (single person) and £152.30 per week (married couple) from April 2009. In addition a one off £60 payment was made to all pensioners early in 2009. This had the effect of bringing forward the increase in the Basic State Pension to January 2009.

A 4.8% increase has been made in the minimum income guarantee element of the pension credit from April 2009 raising this to £130.00 per week for a single person and £198.45 per week for a married couple.

The government will increase the capital disregard in the calculation of pension credit from £6,000 to £10,000 from November 2009.

The government has committed to pay Winter Fuel Payments of £200 for households with someone aged over 60, and £300 with someone over 80, for the lifetime of this Parliament. The Budget 2009 announces an additional payment this winter, worth £100 for households with someone aged over 80 and £50 for households with someone aged over 60. This will increase this winter's payments to £400 for households with someone aged over 80 and £250 for households with someone aged over 60.

As announced in October 2008, the Government changed the Class 3 voluntary national insurance contribution rules to allow those reaching state pension age between 6 April 2008 and 5 April 2015 with 20 qualifying national insurance years to purchase up to six additional years from 1975-76 on top of the normal six year catch up period. The package is intended to be cost neutral overall and the Class 3 rate has therefore risen accordingly from £8.10 a week to £12.05 a week from April 2009.

13.4 TAX AND NATIONAL INSURANCE

The payment of pension contributions by salary sacrifice will be encouraged by several NIC and tax changes now in train, although consideration will also need to be given to the new restrictions on tax relief for higher income individuals (see section 1 above):

1. The £3,835 increase in the upper earnings limit (UEL) for national insurance contributions from April 2009, which now aligns the UEL with the rate at which people start to pay higher rate income tax (i.e. from £43,875);
2. The reduction in the personal allowance for individuals with gross income of over £100,000 from April 2010;
3. The introduction of a 50% tax rate for individuals with income of £150,000 or more from April 2010; and
4. The 0.5% increase in NIC rates for both employer and employees from April 2011.

However, individuals who already have large pension benefits may be loathe to increase their contributions if they fear that this will result in their aggregate benefits exceeding the SLA (see our comment in 2. above).

The introduction of the new 50% tax band in 2010/11 means that the government will consider consequential changes to the pension tax charges (e.g annual allowance and lifetime allowance charges and the unauthorised payment charges). Details of any revisions to the tax rates will be included in the 2009 Pre Budget Report.

13.5 TAXATION OF FAS PAYMENTS

In December 2007 the government announced a major set of improvements to benefits payable by the Financial Assistance Scheme (FAS). These included the ability to make lump sum (i.e. tax-free cash) payments. The government is now including legislation in the Finance Bill 2009 to allow payments made by the FAS to have broadly the same tax treatment as if they had been made from a registered scheme. This is to ensure that a member of the FAS is not subject to unauthorised payment charges when receiving a lump sum. This legislation will apply to all such payments made by the FAS, including any made prior to the legislation being passed.

13.6 TAX AND THE FSCS

Legislation will be introduced in Finance Bill 2009 to provide powers to make regulations to ensure that in the circumstance where the Financial Services Compensation Scheme (FSCS) assists an insurance company, there will be broadly the same tax treatment for the resulting payments or transfers as if the FSCS had not intervened.

The FSCS assistance can include transferring an individual's rights to another insurer or paying compensation to the individual. Tax rules would apply differently because the FSCS is not a registered pension scheme. This measure will ensure that the individual will not be disadvantaged because of FSCS involvement.

14. REMUNERATION STRATEGIES FOR SHAREHOLDING DIRECTORS

14.1 DIVIDENDS V SALARY

The variables that have an impact on the relative attraction of dividends and salary as a means of extracting benefits from a company for a shareholding director are

- (i) the NIC rate (personal and corporate)
- (ii) Personal tax rates
- (iii) the corporate tax rates

While the bands and thresholds for income tax and NIC have changed (as they do every year) they have not for corporation tax.

Determining the so called “remuneration strategy” for shareholding directors is an area where a financial adviser can add significant value - especially when working together with the client’s accountant. The increase in the burden of NICs as a result of the raising of the upper earnings limit for 2009/10, the increase in the rates of employer and employee NIC scheduled for 2011/12 and the planned increase in income tax rates for high earners give an opportunity to focus on appropriate remuneration strategies for working owner managers of private limited companies.

Comparisons of the relative merits of dividend -v- salary are summarised below. It seems that the risk of the settlements legislation being applied to payments to a “non-contributing” shareholding spouse has subsided following HMRC’s announcement that they are not introducing the planned income shifting legislation in the 2009 Finance Bill.

Especially towards the company year end, shareholding directors will value information and guidance on how best to extract funds from their business. For most, day-to-day income will be taken by way of salary (although regular interim dividends are possible). So in the majority of cases the dividend/salary debate is concerned with the extraction of profits over and above regular payments.

For example, assuming that a company pays corporation tax at the small companies’ rate of 21% and wishes to use £10,000 for the benefit of a shareholding director who is a 40% taxpayer and earning above the employee’s upper earnings limit (£43,875), the following will be the position in respect of both dividends and salary for tax year 2009/10.

Dividend

Company:

Pre-tax profit	£10,000
CT @ 21%	£ 2,100
Net to distribute	<u>£ 7,900 (1)</u>

- (1) Because the dividend is not deductible the corporate tax liability for the company remains at 21% ie. £2,100, so £7,900 is available for distribution.

Shareholding director:

Director receives		£7,900
Grossed up by 10% (net dividend x 0.111)	£ 878	
Taxable	<u>£8,778(1)</u>	
Tax @ 32.5%	£2,853 (2)	
Less tax credit	£ 878	
Net tax to pay		<u>£1,975 (3)</u>
Net dividend		£5,925 (4)(5)
Effective rate of tax		40.75%

- (1) The dividend is £7,900 grossed up by 10% (tax credit) to £8,778. This is simply done by multiplying the net dividend by 1.111.
- (2) The rate of tax payable on the gross dividend by a higher rate taxpayer is 32.5%.
- (3) Tax of £878 is already deemed to have been paid via the tax credit and so the balance tax liability is £1,975.
- (4) The director is left with a net dividend of £5,925. The dividend has therefore suffered an effective rate of tax of 40.75%.
- (5) A “short cut” to arriving at the additional tax payable on the dividend is to multiply the net dividend by 25%. The result will be £1,975.

Salary

Company		
	£	
Salary	8,865 (1)	
Employer’s NIC	1,135	
	<u>10,000</u>	all deductible
Director		
Salary	8,865	
Higher rate tax	3,546 (2)	
NIC	89	
Net received		<u>5,230 (3)</u>
Effective rate of tax		47.7%

- (1) Where the £10,000 is paid by way of salary, the whole amount is deductible. However out of the £10,000, employer's National Insurance of 12.8% is payable (again deductible).

So taking account of £1,135 employer's National Insurance, £8,865 is available as a bonus.

- (2) The director will suffer 40% higher rate tax and the 1% NIC charge via the PAYE system on the salary and this liability equals £3,635.
- (3) The director is left with £5,230 net in his hands. The £10,000 available in the company has effectively suffered tax at 47.7%.

In these circumstances therefore, purely on tax grounds alone (and there are other factors to consider), the dividend will look most attractive and, in all cases, payment of a dividend will on tax grounds be preferable to paying a salary.

For a basic rate taxpayer the choice of dividend over salary for money that is to be extracted from the company for expenditure is even easier. Here, the fact that not only employer's but also employee's NICs will be due is a significant financial reason for seriously considering payment by way of dividend rather than salary as the difference in the effective rate of deduction is bigger than for a higher rate taxpayer.

This is best illustrated by an example that shows the effective rates of deduction (ie. combined income tax and National Insurance) borne by both higher and basic rate taxpayers receiving dividends from companies paying respectively the small companies', main and marginal rates of tax.

The assumptions used are as follows:-

- (i) £10,000 available to the company pre tax.
(ii) 12.8% employer NICs payable in all salary examples.
(iii) 11% employee NICs payable on salary only by 20% taxpayers.
(iv) 1% employee NICs payable on salary over (£43,875 only by 40% taxpayers).

		NET DIV £	ERD*	NET SAL £	ERD*	BEST OPTION? DIVS OR SALARY
(a) 21% Taxpaying Company						
(i)	20% personal tax rate	7,900	21%	6,117	38.83%	DIV
(ii)	40% personal tax rate	5,925	40.75%	5,230	47.7%	DIV
(b) 28% Taxpaying Company						
(i)	20% personal tax rate	7,200	28%	6,117	38.83%	DIV

(ii)	40% personal tax rate	5,400	46%	5,230	47.7%	DIV
(c) 29.75% Taxpaying Company						
(i)	20% personal tax rate	7,025	29.75%	6,117	38.83%	DIV
(ii)	40% personal tax rate	5,268	47.32%	5,230	47.7%	DIV

* **ERD** = effective rate of deduction.

Despite the immediate attraction of dividends, in many cases (though there are obviously exceptions) it is essential that any taxpayer, in deciding how to extract funds from his company, makes the decision being fully aware of all the facts, including the impact that choosing dividends over salary can have on pension provision.

For non-taxpayers dividends will be positively disadvantageous as they will be unable to reclaim the tax credit.

It should be noted that the position for salary/bonus will worsen in 2011/12 if the proposed increase 0.5% in the rate of employer/employee's NICs take effect. However the increase in income tax to 50% (salary) or 42.5% (dividend) from 6 April 2010 will be neutral for these purposes.

14.2 PENSION CONTRIBUTIONS

Where the object of "extraction" of funds from the company is for the individual director/shareholder to make an investment then the option of a direct employer contribution into a registered pension scheme should be considered. This will facilitate maximum investment to provide for the director's future financial security with no NIC/income tax depletion. Account will need to be taken of the implications of any contribution for the individual's Annual Allowance and Lifetime Allowance. It should be noted that any tax relief on an employer contribution is now determined under the "wholly and exclusively for the purposes of the trade" provisions and this is now considered. For those whose income exceeds £150,000 consideration will need to be given to the new additional special annual allowance charge (see Section 13.1 for more detail).

And by way of a reminder... deductibility of employer pension contributions - HMRC guidance

Since 6 April 2006 ("A-Day") the clarity on the availability of tax relief on employer contributions has been removed.

Tax relief is available on unlimited contributions paid to a registered pension scheme provided they meet the general rules on allowable deductions (ie. under Case I of Schedule D) other than the rule disallowing capital expenditure. This means they must pass the "wholly and exclusively" for the purposes of the trade test.

HMRC has issued guidance in its Business Income Manual (BIM) which seeks to clarify the position regarding the availability of relief on employer contributions.

In this HMRC confirms that tax relief on employer contributions (including contributions by a former employer) to a registered pension scheme is given in accordance with the normal tax rules for the deductibility of the expenses of a trade or profession, except that

- contributions are not treated as capital payments for tax purposes
- the timing of the deduction for a contribution does not follow its accounting treatment. Relief on a pension contribution will only be allowed in the accounting period in which it is paid and not the period it is recognised in the accounts.

HMRC has indicated that “it will be relatively rare in the context of pension contributions to have to consider whether there is a non-trade purpose for the employer’s decision to make the contribution.” This means that in the vast majority of cases an employer pension contribution will be tax relievable although in certain cases, particularly in the case of controlling directors and relatives, and contributions paid where a company is winding up, the position needs to be considered more closely.

When assessing whether an employer contribution for a controlling director, or close friend or relative of such a director is allowable under the “wholly and exclusively” rules it is important to consider:

- Whether the level of the remuneration package is excessive for the value of the work undertaken by that individual for the employer. In assessing the overall remuneration package this should take account of all aspects, and not simply the employer pension contribution. BIM 46035 indicates that *“on occasion an employer may make an increased pension contribution on the basis that a scheme is under funded. It is important when comparing contributions between periods to consider the full facts, including the history of remuneration and contributions, before challenging a deduction based solely on annual comparatives. It should be borne in mind that the significant increase in qualifying limits with effect from 6 April 2006 will in itself facilitate and encourage an increase in contributions over earlier periods”*. General guidance on deductions for remuneration paid to close relatives of directors can be found at BIM47105 and BIM47106.

Where the remuneration package paid to the controlling director (or close relative/friend of that director) is comparable with that paid to unconnected employees performing duties of similar value it will be accepted that the employer pension contributions are paid “wholly and exclusively” for the purposes of the trade. Where there are no employees whose duties are genuinely comparable HMRC has indicated that the guidance set out in BIM 47105 should be followed.

BIM 47106 indicates that *“controlling directors are often the driving force behind the company. Where the controlling director is also the person whose work generates the company’s income then the level of the remuneration package is a commercial decision and it is unlikely that there will be a non-business purpose for the level of the remuneration package. It should be noted that remuneration does not include entitlement to dividends etc arising in the capacity of shareholder”*.

When considering that action should be taken regarding an excessive remuneration package for a director, or an employee who is a close relative or friend of a controlling director, BIM 47106 states as follows.

“If the amounts involved and the facts established indicate that a remuneration package is demonstrably in excess of what is commercially reasonable, then there may be other avenues to consider in addition to the question of whether an element of the payment is other than wholly and exclusively for the purposes of the trade. In particular it may also be appropriate to consider whether the settlements legislation might apply or if payment is in fact part of the controlling director’s remuneration or the proprietor’s drawings rather than the market rate remuneration of the relative/friend employee”.

If a payment or part of a payment to a relative or close friend of a director appears not to form part of their remuneration, to the extent to which it appears to exceed what is reasonably commercial, then HMRC argue it may actually be part of the director’s own remuneration. Therefore although the payment may be ‘wholly and exclusively’ for the purposes of the trade, it will in the following circumstances be taxable on the director rather than the employee if:

- the spouse or close relative is simply acting as a conduit for the director (in which case it may be taxable as earnings of the director), or
- the payment is made to a relative or a member of the director’s family or household (in which case it may be taxable on the director under the benefits legislation)

If there is any doubt about the deductibility of a pension contribution, it will be best to seek professional advice.

15. EMPLOYEE BENEFITS

15.1 COMPANY CARS AND VANS

Cars

Where a car is made available for an employee's private use a taxable benefit arises. Since April 2002 the taxable benefit has been calculated by applying a percentage to the list price of the car. The percentage is related to the CO₂ emissions of the car and ranges from 15% to 35% (in 1% increments) for a petrol car. Diesel cars that do not meet Euro IV emissions standards attract a 3% supplement on the petrol percentages (capped at 35%). Cars that run on alternative fuels attract discounts to the petrol percentage. The CO₂ emissions qualifying for the minimum 15% charge on a petrol car are as follows:

- 2008/09 135 grams per kilometre of CO₂
- 2009/10 135 grams per kilometre of CO₂
- 2010/11 130 grams per kilometre of CO₂

A number of changes to car benefit taxation will apply from 6 April 2011

- the upper limit of £80,000, that currently applies to the list price on which the tax charge is based, will be removed.
- the lower threshold CO₂ emissions figure (130g/km for 2010-11) will be reduced by 5g/km to 125g/km;
- the "appropriate percentage" applicable to electrically propelled cars first registered from 1998 onwards will be reduced from 15 per cent to 9 per cent. This is the effect of withdrawing the 6 per cent relief that is currently available. Also, the provisions relating to electrically powered cars first registered before 1998 will be removed as there are no cars to which they can apply; and
- the reductions currently given for electric/petrol hybrid cars and cars propelled by bi-fuels, road fuel gas and bioethanol will be abolished. The discount given for Euro IV standard diesel cars registered before 1 January 2006 will also be abolished.

Car fuel

An additional taxable benefit arises if the employee receives free fuel for the company car for their private use. Since April 2003 the fuel benefit charge has been calculated by applying the company car tax appropriate percentage to a set figure. The figure for 2009/10 is £16,900.

Cars that are capable of running on alternative fuel such as liquefied petroleum gas (LPG), compressed natural gas (CNG) or battery-propelled cars, currently enjoy a discount from the equivalent company car percentage.

WHICH MEANS THAT ...

Where a company car is to be provided the charge on the employee can be substantially reduced if a “qualifying low emissions car” (QUALEC) or an electronically propelled car then rates of 10% and 9% respectively of the list price of the car may make the tax cost acceptable.

15.2 LIVING ACCOMMODATION

Where an employee is provided with accommodation there is a tax charge on the benefit to the employee of that accommodation. Where rent is paid by the person at whose cost the accommodation is provided the charge is based on the actual rent paid (less any amount made good by the employee), where that is more than the annual value. However, some arrangements are being entered into that involve upfront payments, which are described as a lease premium, and payment of a very small rent in order to try to avoid paying tax.

The legislation will ensure that where a lease premium is paid for a lease of 10 years or less, the same tax treatment will follow as if the lease premium were actual rent paid. The taxable amount in any tax year will be treated as the amount of the lease premium spread over the duration of the lease plus the amount of any rent paid by the person at whose cost the accommodation is provided less any amount made good by the employee.

The new rules will apply to leases entered into or extended on or after 22 April 2009.

16. DOMICILE AND THE REMITTANCE BASIS OF TAXATION

The major changes to the remittance basis of taxation announced in the 2007 Pre-Budget Report and subsequently passed into legislation have been operational for a full 12 months now and in this year's Budget some further minor changes are proposed.

Broadly speaking, the remittance basis of taxation results in only gains and income brought into the UK (there is a wide definition of remittance for this purpose) being subject to tax. However, the 2008 rules provide that, broadly speaking and subject to some exceptions, an individual who has been UK resident for at least seven out of the last ten tax years (including the year in question) will need to pay a remittance basis charge of £30,000 to access the remittance basis for a tax year.

Following detailed consultation with external stakeholders, Finance Bill 2009 will introduce further minor changes to these rules. These are designed to make the rules simpler to operate in practice and to ensure the legislation effectively delivers its policy objectives.

The changes which apply to individuals with small amounts of overseas employment income, individuals with less than £2,000 of unremitted foreign income and gains for a tax year, individuals with no UK tax liability and no remittances in a tax year, exempt property and Gift Aid donations will have effect on and after 6 April 2008. The remaining changes will have effect on and after 22 April 2009.

So what are the proposed changes? BN55 states the following.

(i) Individuals with small amounts of foreign employment income

Individuals employed in the UK are currently required to file a Self Assessment tax return if they have also received income from overseas employment in the same tax year. This is the case even where there is little or no tax to pay in the UK because the overseas employment income has already been subject to tax in the other country.

This obligation to file a return will be removed with effect from 6 April 2008 where such individuals have overseas employment income of less than £10,000 and overseas bank interest of less than £100 in any tax year, all of which is subject to a foreign tax.

(ii) Exempt Assets

There are currently a number of exemptions which allow an individual using the remittance basis to bring property into the UK which has been purchased from relevant foreign income (broadly speaking income from overseas investments and savings) without triggering a liability to UK tax.

The scope of these exemptions will be extended with effect from 6 April 2008 to include property purchased out of foreign employment income and foreign chargeable gains as well as relevant foreign income.

(iii) Application of the Remittance Basis Without a Formal Claim

In most cases, individuals who wish to use the remittance basis of taxation are required to make a formal claim to do so through the Self Assessment process. However, no such claim is required where an individual has unremitted foreign income and gains of less than £2,000 in any tax year. In such cases it is assumed that the individual has chosen to use the remittance basis.

Following representations that the current rules are not clear on this point, the legislation will be amended to put beyond doubt that a claim will not be required in these circumstances. The effect will be that the individual will be treated as having used the remittance basis unless they notify HM Revenue & Customs (HMRC) that they wish to be taxed under the arising basis. This will apply from 6 April 2008.

The situations where a claim will not be required will also be extended to cover cases where an individual has total UK income or gains of no more than £100 which has been taxed in the UK, provided they make no remittances to the UK in that tax year. This extension will also come into effect from 6 April 2008.

(iv) The Remittance Basis and the Settlements Legislation

The new remittance regime includes transitional provisions which prevent certain income which arises before 6 April 2008 from being taxed as a remittance if it is brought to the UK on or after that date. These provisions will be extended to ensure that they operate as intended in their application to individuals who are taxed under the settlements legislation in Chapter 5 of Part 5 of the Income Tax (Trading and Other Income) Act 2005.

Legislation will also be introduced to clarify the interaction between the remittance basis regime and the tax rules which apply to settlements which are settlor-interested.

The first of these changes will have effect from 6 April 2008 and the second will come into force on 22 April 2009.

(v) Gift Aid donations

The Gift Aid provisions in Chapter 2 of Part 8 of the Income Tax Act 2007 (ITA) allow charities to claim tax relief on any gifts of money from individuals, provided the donor has paid sufficient UK income and capital gains tax in the tax year in which the donation was made. In situations where the donor pays tax on the remittance basis, and is required to pay the £30,000 Remittance Basis Charge under section 809H of ITA, it was always the intention to treat the £30,000 in the same way as other types of income tax or capital gains for the purposes of Gift Aid. Finance Bill 2009 will amend the remittance basis rules to ensure that tax relief under Gift Aid is available in such circumstances.

This change will have effect from 6 April 2008.

(vi) Anti-avoidance provisions

Section 809M of ITA defines ‘relevant person’ for the purposes of the remittance basis and includes participators in a close company as defined by reference to sections 414 and 415 of the Income and Corporation Taxes Act 1988.

However, the term ‘participator’ is not itself defined and it is not made explicit that references to a close company includes subsidiaries of companies. The legislation will be amended, with effect from 22 April 2009, to clarify the scope of the terms ‘participator’ and ‘close company’ and remove the potential for abuse.

Section 809Z5 of ITA applies in circumstances where property is purchased out of overseas income and gains and forms part of a larger set, such as a series of linked artworks or a stamp collection, and only individual items are brought into the UK. This statutory rule is intended to apply more widely when determining the value of such items for the remittance basis.

To remove any uncertainty, and to remove the potential for abuse the legislation will be amended to make clear that the rule currently in section 809Z5 applies in all cases where individual items from a larger set are purchased out of overseas income and gains and brought into the UK. This change will have effect from 22 April 2009.

Draft legislation and explanatory notes covering these anti-avoidance provisions have been published today on the HM Revenue & Customs website.

(vii) Not ordinarily resident employees and HMRC Statement of Practice 1/09

On 18 March 2009, HMRC issued a Statement of Practice 1/09 which sets out how they will treat transfers made from an offshore account which contains only the income relating to a single employment contract, and how earnings should be apportioned between UK and non-UK employment where an employee is taxed on the remittance basis. This replaced the earlier Statement of Practice 5/84 which was withdrawn with effect from 6 April 2009.

The Government will legislate Statement of Practice 1/09 in Finance Bill 2010, to allow for a period of consultation with external stakeholders on the most effective way of doing so.

WHICH MEANS THAT ...

In considering planning opportunities for UK resident non-domiciled investors advisers should keep in mind the continuing legitimate means of deferring taxation on income and gains through offshore bonds and the capital gains tax planning opportunities through some offshore trusts.

APPENDIX – TAX FACTS AND FIGURES AND NICs

MAIN INCOME TAX ALLOWANCES AND RELIEFS

	2008/09	2009/10
	£	£
Personal allowance – standard	6,035	6,475
- Age 65 – 74	9,030	9,490
- Age 75 and over	9,180	9,640
Married couple's allowance (MCA) – minimum amount	2,540 (B)	2,670 (B)
- Age 65 - 74	6,535 (C)	N/A
- Age 75 and over	6,625 (C)	6,965 (C)
Age-related allowances reduced if total income exceeds (D)	21,800	22,900
Maintenance to former spouse for all orders provided one party was aged 65 or over before 6 April 2000	2,540 (A)	2,670 (A)
Tax-free employment termination lump sum limit	30,000	30,000

- (A) Relief at 10%.
 (B) Minimum amount of MCA applies for age allowance purposes only.
 (C) Relief available at 10% only if at least one of the couple was born before 6 April 1935.
 (D) For 2009/10 the reduction is £1 for every £2 additional income over £22,900 [£21,800 for 2008/09]. Standard allowance(s) **only** are available if total income exceeds:-

	2008/09	2009/10
	£	£
Taxpayer aged 65 - 74 [personal allowance]	27,790	28,930
Taxpayer aged 65 - 74 [married couple's allowance]	35,780	N/A
Taxpayer aged 75 and over [personal allowance]	28,090	29,230
Taxpayer aged 75 and over [married couple's allowance]	36,260	37,820

INCOME TAX RATES

	2008/09	2009/10
	£	£
Starting rate on savings income - 10% *	1-2,320 *	1-2,440*
Basic rate – 20% [20%]	1-34,800	1 - 37,400
Tax on first £34,800 [£37,400]	6,960**	7,480**
Higher rate - 40%	Over 34,800	Over 37,400
Discretionary and accumulation trusts (except dividends) ***	40%	40%
Discretionary and accumulation trusts (dividends) ***	32.5%	32.5%
Income other than dividends for a basic rate taxpayer	20%	20%
Ordinary rate on dividends (basic rate taxpayer)	10%	10%
Upper rate on dividends (higher rate taxpayer)	32.5 %	32.5%

* Only applies if total taxable non-savings income is less than £2,440, otherwise 20%.

** Assumed 10% band not available in 2008/09 and 2009/10. £6,728 and £7,236 respectively if full 10% band is available.

*** Up to the first £1,000 of gross income is generally taxed at the standard rate, ie. 10% or 20% as appropriate.

CAR AND CAR FUEL BENEFITS

The charge is based on a percentage of the car's "price". "Price" for this purpose is

1. The list price at the time the car was first registered plus the price of extras.
2. Where the "price" exceeds £80,000, the "price" used is restricted to £80,000.

For cars first registered before 1 January 1998, the percentage of the "price" charged is based on engine size.

Engine size (cc)	Percentage of car's "price" charged to tax
0 – 1,400	15
1,401 – 2,000	22
2,001 and more	32

For cars first registered after 31 December 1997 the charge, based on the car's "price", is graduated according to the level of the car's approved CO₂ emissions.

For cars with an approved CO₂ emission figure.

CO ₂ emissions in grams per kilometre (g/km)	Percentage of car's "price" charged to tax
2008/09 and 2009/2010	
120 or less	10*
121-139	15*
140-144	16*
145-149	17*
150-154	18*
155-159	19*
160-164	20*
165-169	21*
170-174	22*
180-184	24*
185-189	25*
190-194	26*
195-199	27*
200-204	28*
205-209	29*
210-214	30*
215-219	31*
220-224	32*
225-229	33**
230-234	34***
235-239	35****
240+	35****

Notes

- (1) * Diesel supplement = + 3%
 ** Diesel supplement = + 2%
 *** Diesel supplement = + 1%
 **** No diesel supplement - maximum charge of 35% already applies.
- (2) The exact CO₂ emissions figure should be rounded down to the nearest 5 g/km for levels of 125g/km or more.

For cars with no approved CO₂ emissions figure, the charge is based on engine size.

Engine size (cc)	Percentage of car's "price" charged to tax
0 – 1,400	15
1,401 – 2,000	25
2,001 and more	35

There is a 3% supplement for diesel subject to the maximum charge of 35%.

CAR FUEL BENEFITS

For cars with an approved CO₂ emission figure, the benefit is based on a flat amount of £16,900 for 2009/10 (unchanged from 2008/09). To calculate the amount of the benefit the percentage figure in the above car benefits table (that is 10% to 35%) is multiplied by £16,900. The percentage figures allow for a diesel fuel surcharge. For example, a petrol car emitting 165 g/km in 2009/10 would give rise to a petrol benefit of 21% of £16,900 = £3,549.

VALUE ADDED TAX

From	1 April 2008	1 Dec 2008	1 May 2009	1 Jan 2010
Standard rate	17.5%	15%	15%	17.5%
Annual turnover limit for registration	£67,000	£67,000	£68,000	£16,800

INHERITANCE TAX

	Cumulative chargeable transfers [gross]				% tax rate on death
	2007/08	2008/09	2009/10	2010/11	
	£	£	£	£	
Nil rate band	0 – 300,000	0 – 312,000	0 – 325,000	0 – 350,000	0
Excess	No limit	No limit	No limit	No limit	40

CAPITAL GAINS TAX

MAIN EXEMPTIONS & RELIEFS

	2008/09	2009/10
	£	£
Annual exemption	9,600*	10,100 *

* Reduced by 50% for most trusts.

	2008/09 and 2009/10
Principal private residence exemption	No limit
Chattels exemption	£6,000
	2001/02 to 2003/04
Retirement relief: Age 50 or over, or retiring on ill-health grounds under age 50	
2001/02 100% exempt	First £100,000 of gains
50% relief on	Next £300,000 of gains
2002/03 100% exempt	First £50,000 of gains
50% relief on	Next £150,000 of gains
2003/04 100% exempt	Nil
50% relief on	Nil
	2008/09 and 2009/10
Entrepreneurs' relief : tax due on 5/9ths of the qualifying gains to give an effective rate of 10%	First £1 million of cumulative lifetime qualifying gains

RATES OF TAX

Individuals: 18% [2008/09 - 18%]

Trusts and personal representatives: 18% [2008/09 - 18%]

TAPERING CHARGEABLE GAINS – RELIEF WITHDRAWN FOR DISPOSALS TAKING PLACE AFTER 5 APRIL 2008

Gains on business assets		Gains on non-business assets	
Number of complete years after 5.4.98 for which asset held	Percentage of gain chargeable	Number of complete years after 5.4.98 for which asset held *	Percentage of gain chargeable
<i>(i) Disposals before 6.4.2002</i>		<i>All disposals</i>	
0	100	0	100
1	87.5	1	100
2	75	2	100
3	50	3	95
4 or more	25	4	90
		5	85
<i>(ii) Disposals after 5.4.2002</i>		6	80
0	100	7	75
1	50	8	70
2 or more	25	9	65
		10 or more	60

* Assets held on 16 March 1998 qualify for a bonus year of ownership.

CORPORATION TAX

	Year ending 31 March	
	2009	2010
Main rate	28%	28%
Small companies' rate	21%	21%
Small companies' limit	£300,000	£300,000
Upper marginal level	£1,500,000	£1,500,000
Effective marginal rate	29.75%	29.75%

TAX PRIVILEGED INVESTMENTS (MAXIMUM INVESTMENT)

	2008/09 £	2009/10 £
ISA		
<ul style="list-style-type: none"> ▪ Overall per tax year ▪ For those aged 50 and over in 2009/10 	7,200 7,200	7,200 10,200*
Maximum in		
- Cash	3,600	3,600
For those aged 50 and over in 2009/10	3,600	5,100*
- Stocks and shares and life insurance	7,200	7,200
For those aged 50 and over in 2009/10	7,200	10,200*
Maximum in cash for 16 and 17 year olds	3,600	3,600
ENTERPRISE INVESTMENT SCHEME (20% income tax relief)	500,000**	500,000**
Carry back to previous tax year for an investment made before 6 October - lower of amount shown and 50% of the investment	50,000	No restrictions apply
VENTURE CAPITAL TRUST (30% income tax relief)	200,000	200,000

* From 6 October 2009

** No limit for CGT reinvestment relief.

PENSIONS

	2008/09	2009/10	2010/11-2015/16
Lifetime allowance*	£1,650,000	£1,750,000	£1,800,000
Annual allowance	£235,000	£245,000	£255,000
Lifetime allowance charge:			
Excess drawn as cash	55% of excess		
Excess drawn as income	25% of excess		
Annual allowance charge	40% of excess		
Max. pension commencement lump sum*	25% of pension benefit value		
Max. relievable personal contribution	100% relevant UK earnings <i>or</i> £3,600 if greater		

* May be increased under transitional protection provisions

FAMILY TAX CREDITS

The main features of the tax credits are:

1. Child tax credit

- Eligibility is assessed on household income.
- The claimant must be responsible for one or more children aged 16 or under, or at least one child under age 20 and in full-time non-advanced education.
- The family element of the tax credit is £545 per annum and is doubled in the first year of a child's life.
- The child element is £2,235 per annum for each child.
- The disabled child element is £2,670 per annum (where relevant).
- HMRC will pay the CTC to the main carer for the child.

2. Working tax credit

- The claimant, or one of the joint claimants, must be in qualifying remunerative work.
- The amount of WTC will be based on circumstances which are primarily the number of hours worked and the income of the claimant (or joint income for a couple).
- The age and working hours conditions are not straightforward. Generally, the minimum weekly working requirement will be:
 - a) 16 hours for families with children and workers with a disability. The claimant can be aged 16 or over.
 - b) 30 hours for workers with no children and no disability. The claimant has to be aged 25 or over.
- The basic element of the tax credit is £1,890 per annum.
- The couple or lone parent element is £1,860 per annum.
- A 30 hour element of £775 per annum is payable where the claimant or one of the claimants works at least 30 hours a week (couples with children may aggregate their hours for this purpose).
- A disabled worker element of £2,530 per annum or more is available where the claimant, or his or her partner, has a disability.
- There is 50-plus element and a childcare element.

- For employees, payment will normally be made by their employer with their wages (except the childcare element which is paid direct to the main carer). For the self-employed, payment is made directly by HMRC.

3. Calculating the credits

It is necessary first to total the various elements available to arrive at the maximum available amount of tax credits before any reduction on account of income. All elements can be reduced at the rate of 39% (ie. 39p per £1 of income), except the family element of CTC which is reduced at a rate of 6.67%.

NATIONAL INSURANCE CONTRIBUTIONS FOR TAX YEAR 2009/10

Definitions

Lower Earnings Limit (LEL) the minimum level of earnings at which an employee will qualify for a State Second Pension (S2P). This is also the lower level of earnings which will be used in determining any NI Rebate.

For tax year 2009/10 the Lower Earnings Limit is £95 per week (£4,940 per year).

Upper Accrual Point (UAP) the upper level of earnings on which an employee's S2P entitlement is based (or on which any NI Rebate is determined). For tax year 2009/10 and subsequent tax years the Upper Accrual Point is fixed at £770 per week (£40,040 per year).

NI Rebate the Rebate of employer's and employee's National Insurance contributions that is available where an employee is contracted out of S2P. This is based on the employee's earnings between the Lower Earnings Limit (LEL) and Upper Accrual Point (UAP).

The Rebate will vary depending on the type of pensions vehicle used to contract out of S2P. Where this is a final salary occupational scheme this will be 3.7% (employer) and 1.6% (employee) in respect of the employee's earnings between the LEL and UAP.

Where this is a money purchase occupational scheme or contracted out money purchase stakeholder pension scheme the Rebate will be 1.4% (employer) and 1.6% (employee) in respect of the employee's earnings between the LEL and UAP. The aggregate Rebate will be determined on an age related basis (varying from 3.0% to 7.4%) and any further Rebate due (i.e. over and above the amounts mentioned earlier in this paragraph) will be paid by the HMRC NICO to the scheme after the end of the tax year.

Where this is a personal pension or stakeholder scheme National Insurance contributions will be paid at the contracted in rate and the Rebate, which will be determined on an age related basis, will be paid directly to the member's personal pension by the HMRC NICO after the end of the tax year to which it relates.

The Rebates will also vary in accordance with an individual's earnings, in each of the following bands:

<u>Band</u>	<u>Age related Rebate</u>
1 (£4,940 - £13,900)	9.4% - 14.8%
2 (£13,900 - £31,800)	2.35% - 3.7%
3 (£31,800 - £40,040)	4.7% - 7.4%

Primary Threshold

the level of earnings at which employees start to pay Class 1 National Insurance contributions.

For tax year 2009/10 this is £110 per week (£5,715 per year).

Secondary Threshold

the level of an employee's earnings at which the employer starts to pay Class 1 National Insurance contributions.

For tax year 2009/10 this is £110 per week (£5,715 per year).

Upper Earnings Limit (UEL)

the upper level of earnings on which an employee will pay full rate Class 1 National Insurance contributions. The reduced 1% NI contributions will apply to earnings above this level. For tax year 2009/10 this is £844 per week (£43,875 per year).

Employees - Class 1

Contracted in

Nil on first £110 per week (i.e. up to Primary Threshold)
11% of £110.01 per week to £844 per week.

1% on earnings above £844 per week.

Contracted out

Nil on first £110 per week (i.e. up to Primary Threshold)
9.4% of £110.01 per week to £770 per week
11% of £770.01 per week to £844 per week
1% on earnings above £844 per week.

The employee's NI Rebate is still payable in respect of the employee's earnings between the LEL and UAP including those in excess of the LEL and up to and including the Primary Threshold. In the first instance, the Rebate reduces the National Insurance contributions payable by the employee. However, where the National Insurance contribution payable by the employee is reduced to nil, the excess Rebate will be available for the employer to set against his overall National Insurance contribution bill. Please see examples after the table for how this works.

Married Women and Widows

4.85% of £110.01 to £844 per week.

Reduced Rate

1% on earnings above £844 per week.

Employer - Class 1 Contributions

<u>Weekly Earnings</u>	<u>Contracted In</u>	<u>Contracted Out</u>	
		COSR	COMP**
	%	%	%
On first £110	Nil	Nil	Nil
£110.01-£770	12.8	9.1	11.4
£770.01 - £844	12.8	12.8	12.8
Over £844	12.8	12.8	12.8

Although the reduced level of National Insurance contributions only applies to the employee's earnings in the band between the Secondary Threshold (£110 per week) and the UAP (£770 per week), the NI Rebate is still available in respect of the employee's earnings between the LEL and UAP, including those earnings between the LEL (£95 per week) and the Secondary Threshold (£110 per week). Employers are able to reduce their overall National Insurance contributions liability to reflect the Rebate applicable to the employer's contributions on the employee's earnings between £95 per week and £110 per week.

** Where a COMP (Contracted Out Money Purchase Occupational Scheme) is involved the Rebate is determined on an age related basis and any additional Rebate due over and above that shown above will be payable by HMRC NICO to the scheme after the end of the tax year. This will also apply to a Contracted Out Money Purchase Stakeholder Pension Scheme (COMPSHP).

COSR is a Contracted Out Salary Related Occupational Scheme.

Self-Employed

Class 2
(lower profits limit) £2.40 per week flat rate.
(applicable where profits are less than £5,075 per annum)

Class 4
8% of profits between £5,715 p.a. and £43,875 p.a.

1% on profits above £43,875 p.a.

Voluntary Contributions

Class 3
£12.05 per week

Examples of Class 1 NI Contributions for Employees Contracted Out Under Occupational Schemes

1. David Lovell earns £150 per week. He is contracted out of S2P under a final salary occupational scheme. David's weekly National Insurance contributions are as follows:

Up to £110 per week - Nil

£110 per week to £150 per week - $9.4\% \times £40 = \underline{£3.76 \text{ per week}}$.

However this is reduced by the employee Rebate (1.6%) payable on earnings between the LEL (£95 per week) and the Primary Threshold (£110 per week).

i.e. $£15 \times 1.6\% = \underline{£0.24 \text{ per week}}$.

David's revised NI liability is £3.52 per week (i.e. $£3.76 - £0.24$).

His employer's weekly National Insurance contributions are:

Up to £110 per week - Nil

£110 per week to £150 per week - $9.1\% \times £40 = \underline{£3.64 \text{ per week}}$

However, this is reduced by the employer Rebate (3.7%) payable on earnings between the LEL (£95 per week) and the Secondary Threshold (£110 per week) - i.e. $£15 \times 3.7\% = \underline{£0.55 \text{ per week}}$.

The employer's revised NI liability is £3.09 per week ($£3.64 - £0.55$)

2. Jane Redfearn earns £100 per week. She is contracted out of S2P under a final salary occupational scheme.

Jane pays no National Insurance contributions as her earnings are below the Primary Threshold.

However, the employee Rebate is available in respect of Jane's earnings between the LEL (£95 per week) and £100 per week. (i.e. $1.6\% \times £5 = \underline{£0.08 \text{ per week}}$).

As Jane is not paying any National Insurance contributions the £0.08 will be used to reduce the employer's overall National Insurance contribution liability.

Her employer will pay no National Insurance contributions in respect of Jane as her earnings are below the Secondary Threshold. However, the employer's Rebate is still available in respect of Jane's earnings between the LEL (£95 per week) and £100 per week. (i.e. $3.7\% \times £5 = \underline{£0.18}$). This will be available to reduce the employer's overall National Insurance contribution liability.