Putting your tax and financial affairs in order – a tax health checklist

TURCAN CONNELL
SOLICITORS AND ASSET MANAGERS

The end of the tax year signals certain activities that must be undertaken to comply with regulations, but it is also a very good time to take stock more generally of your overall affairs and to ensure that you are in good financial health.

At this time of the year, it is also opportune to check that you are paying the correct amount of tax and not losing out on any allowances or tax breaks for which you are eligible. In the current economic climate this is even more imperative, as we all look for ways of reducing our outgoings. To assist with this process, we have put together the following checklist which we hope you will find useful. Though this is not an exhaustive list of all the things you can do, it is a nevertheless a comprehensive starting point on the road to a clean bill of tax and financial health.

Savings and Investments

Individual Savings Accounts (ISAs): Research shows that millions of pounds are lost by taxpayers each year by not taking advantage of the full ISA allowance so you should always consider making use of your £7,200 tax free savings allowance – income and capital gains generated within an ISA are free from UK income tax and capital gains tax. You should note also that up to £3,600 of the allowance can be saved in cash with a single provider.

Venture Capital Investments: You can get 30% income tax relief on investments up to £200,000 per tax year in Venture Capital Trusts (VCTs). While growth prospects have in the past been good, these investments come with a corresponding level of risk which should be assessed carefully in light of current economic and investment market conditions. Income tax relief is also available at 20% on the cost, to a maximum of £500,000 per tax year, of subscribing for shares in private trading companies under the Enterprise Investment Scheme (EIS). Although EIS investments also enable the investor to defer capital gains tax in respect of other assets, serious consideration must be given to level of risk involved and professional advice should be taken before investing.

Investments – general advice: As the top rate of income tax is currently 40% (45% from 6 April 2011 on income above £150,000) compared with a flat capital gains tax rate of 18%, you should discuss with your investment adviser about switching to investments which generate capital rather than income. While investment values are low, diversification in this way may be possible without incurring capital gains tax.

Capital Gains Tax (CGT) allowance: This year individuals can realise up to £9,600 of capital gains free of tax. It is therefore sensible to carry out a review of investments and other assets and, where appropriate, consider realising any gains that might be available to use up any unused allowance. In the current climate it is to be expected that many investment portfolios will be showing losses rather than gains, and in some cases the losses will be significant. Consideration should be given where possible to realising capital losses to set against gains on other assets in the same period as effectively this provides tax relief on those losses. In addition, now may be a good time to diversify to reduce exposure on large shareholdings in any particular company. While ensuring that your 2008/09 annual allowance is fully used where possible, disposals should be timed carefully. For example, CGT on a 5 April 2009 disposal will be payable by 31 January 2010 whereas CGT on a 6 April 2009 disposal will be payable by 31 January 2011.

Married couples: Married couples should, if possible, optimise their combined CGT allowances as each spouse can realise annual capital gains of up to £9,600 free of tax. By transferring assets to a spouse prior to sale, a couple could achieve tax free capital gains of up to £19,200 and save CGT of up to £3,456. Anyone contemplating a large disposal should consider splitting it into two disposals immediately before and after the tax year end, allowing a 'doubling up' of the annual exemption.

It is also sensible for married couples to consider splitting income sources in a way which ensures that each spouse fully uses his/her personal income tax allowance and the basic rate tax band. Done correctly, this arrangement can produce significant tax savings. Although HM Revenue & Customs is keen to review certain income shifting practices, it has been confirmed that legislation to achieve this will be kept on hold for the time being. Married couples should review their income sharing arrangements while these arrangements are still possible.

Employment Tax

Company cars: Having a company car can create an annual taxable benefit as high as 35% of the car's value. Many executives are now choosing to receive additional salary in lieu of their company car. Where the employer also provides free fuel, this could further increase the employee's tax bill by up to £2,366. You should look carefully at the total tax cost of running a company car as there might be a better alternative.

Company share option schemes: In the current economic climate, many share schemes may not provide the benefits that might previously have been expected. Nonetheless, scheme members should remember to check the vesting period for exercising share options where these are not 'under water'.

If gains arising on the exercise of options are taxed under PAYE, the employee must reimburse the employer for the PAYE within 90 days of the exercise date. Failure to do so will mean the PAYE paid by the employer is treated as a taxable benefit in kind, in effect creating a tax on tax! If option gains are not taxed under PAYE, exercising them immediately after the start of the new tax year will give an extra year before the tax needs to be paid. However, this planning requires careful consideration of the impact on any tax payments to account that might be payable.

Retirement Planning

Stakeholder pensions: These are available to carers, children, students and others with no earned income. Basic rate tax relief is added automatically to the contribution, meaning the annual contribution limit of £3,600 only costs £2,880.

Pension contributions: Individuals can now contribute up to 100% of their relevant earnings to their pension fund, subject to the annual allowance which is currently £235,000. Contribution for the current tax year must be made **before 6 April 2009** as there is no 'carry back' facility which previously allowed contributions to be made up to 31 January following the tax year of claim.

Pensions for children: You can also fund pensions for your adult children on up to 100% of their earnings. This facility can provide a useful home for any planned gifts and a good start for the next generation's pension funding.

Pension simplification/Lifetime allowance: Following extensive changes to the pension funding rules from 6 April 2006, pension funds valued in excess of the lifetime allowance of £1.65m could be taxed on the excess at 55%. There are ways in which the value of the fund can be protected against this tax charge but only by submitting appropriate forms to HM Revenue & Customs **before 6 April 2009**. Clients with funds near to, or over, the lifetime allowance should take advice as they might not be able to make further pension contributions if they wish to protect their funds.

Tax Payments and Payments on Account

Tax payments on account for the current tax year should be reviewed to keep these to a minimum especially where income is in decline. It may be possible to reduce the amount payable by 31 July 2009 and, where relevant, it is not too late to revise 31 January payments and recover any excess tax already paid. For those in business, you should ensure that trading losses are claimed against other income to minimise tax payable. In some cases losses can be set against income of an earlier tax year to recover tax already paid.

Estate Planning and Inheritance Tax

Annual exemption: Making annual gifts can reduce the value of an individual's estate for Inheritance Tax (IHT) purposes. Each year individuals can gift assets up to a value of £3,000 free of IHT. Spouses each have their own exemption. Individuals who have not used their 2007/08 exemption can still do so before 6 April 2009, otherwise it will be lost.

The small gifts exemption allows gifts of £250 each year to individual beneficiaries free of IHT, but this exemption cannot be used in addition to the annual exemption in respect of gifts to the same beneficiary.

The normal expenditure out of income exemption enables regular gifts to be made out of income entirely free of IHT without the need to satisfy the seven year survival period, provided they do not reduce the donor's standard of living. There is no limit on the number or value of gifts that can be made out of income, but strict compliance with HM Revenue & Customs rules is essential and anyone considering using this relief is recommended to take advice.

Gifts which do not qualify for these exemptions may also be made IHT-free subject to surviving the gift by seven years. In these circumstances it may be sensible planning to gift assets in the current climate while valuations are low.

Wills and Powers of Attorney: It is 'good housekeeping' to make sure that your Will is brought up to date and where appropriate you should consider putting Powers of Attorney in place.

Information provided in this document and any opinions expressed are for general use and not personal to your circumstances, nor are they intended to provide specific legal or financial advice. If you are unsure as to the suitability of any investment you should seek professional advice. All information provided is based on our understanding of current legislation which is subject to change. Taxation is based on individual circumstances and is subject to change. The value of investments and the income derived from them may fall as well as rise and you may not get back the full amount you invest. Past performance is not a guide to future performance. Turcan Connell is authorised and regulated by the Financial Services Authority.