TURCAN CONNELL
SOLICITORS AND ASSET MANAGERS

Briefing Note

Tax Year-End Planning 2010

As we approach the end of a tax year, it is a good time to take stock of your tax and financial affairs and to ensure that you are in good financial health.

As always at this time of the year, it is important to ensure that you are not paying more tax than you should or losing out on any available tax breaks. To assist you we have put together a few ideas.

Mitigating the 50% tax rate

From April 2010 certain individuals face the prospect of a 25% tax increase on taxable income above £150,000 as the rate of income tax payable on that 'slice' of taxable income increases from 40% to 50%. However, a number of steps to mitigate the impact of this increase could be taken which are noted below:

- Married couples might consider splitting income sources to make sure that each spouse fully uses his or her personal income tax allowance as well as the basic and 40% rate tax bands. Completed correctly, this exercise can produce significant tax savings and the planning is particularly relevant where either spouse is likely to come within the new 50% tax rate. 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 therefore review their income sharing arrangements while these arrangements are still possible.

- Income scheduled for receipt after 5 April 2010 should, where possible, be accelerated to the current tax year while the top rate of income tax is still 40%. This may be particularly appropriate in the case of bonus payments and dividends from private or family companies but could also affect those considering rearranging their investments.

- For owner-managed businesses' tax savings could be achieved by:

  - Splitting shareholdings and thus dividend income with a spouse or civil partner;
  - Setting up a family partnership with appropriate profit sharing ratios aimed at keeping family members' income within the critical thresholds; and/or
  - Incorporation or introducing corporate partners into family partnerships so that profits are taxed at the lower corporation tax rates.

- Investment bonds (either onshore or offshore) to defer income tax on investment gains. Investors can typically draw down an annual tax free sum of up to 5% of the capital invested in the bond. Income tax need not become payable on the bond until it is surrendered.

- Other income tax sheltering schemes such as venture capital investments can also be considered (these are detailed overleaf). While these schemes may involve investment risk, certain relatively low risk schemes providing attractive tax breaks are available.

- Individuals considering making charitable donations through Gift Aid may wish to do so as a priority before 5 April 2010. Although it is still possible for the individual to benefit from higher rate tax relief, it has been announced that this will be reviewed and in the future any benefit could be conferred only to the charity.

Savings and Investments

Individual Savings Accounts (ISAs): Research has shown that taxpayers are potentially losing out each year by not taking advantage of their full ISA allowance. It is recommended that you consider making full use of your tax free savings allowance of £7,200 for 2009/10 if you have not already done so. You should note also that up to £3,600 of the allowance can be saved in cash with a single provider. With effect from 6 October 2009, taxpayers who are aged 50 or over in the current tax year can invest up to £10,200 of which £5,100 can be held in cash.

Income and capital gains generated within an ISA are free from UK income tax and capital gains tax. From 6 April 2010 the annual ISA allowance increases to £10,200 for everyone.

Venture Capital Investments: You can take advantage of 30% income tax relief on investments of up to £200,000 per tax year in Venture Capital Trusts (VCTs). This is a highly specialist area of investment on which we can provide further advice.

Enterprise Investment Scheme: 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). EIS investments also enable the investor to defer capital gains tax in respect of other assets, but care should be taken as the flat 18% rate of capital gains tax could increase in years to come. EIS investment is a highly specialist area of investment on which we can provide further advice.

Capital Gains Tax (CGT) planning: In the 2009/10 tax year, individuals can realise up to £10,100 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. Many investment portfolios may still be showing losses rather than gains and, where they are significant, consideration should be given 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, it may be a good time to diversify your investments and reduce exposure on large shareholdings in any particular company. Market volatility experienced over the last few years would suggest that a healthy level of diversification is sensible, however, it should not be forgotten that an 18% level of capital gains tax is currently very low in the context of a top rate of 50% for income tax especially with the risk that the rate of CGT will increase in the future.

While ensuring that your 2009/10 annual allowance is fully used, disposals should be timed carefully. For example, CGT on a 5 April 2010 disposal will be payable by 31 January 2011 whereas CGT on a 6 April 2010 disposal will be payable by 31 January 2012.

Married couples should, if possible, optimise their combined CGT allowances as each spouse can realise annual capital gains of up to £10,100 free of tax. By transferring assets to a spouse prior to sale, a couple could achieve tax free capital gains of up to £20,200 and save CGT of up to £3,636. 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.

Investments – general advice: As the top rate of income tax is currently 40% (50% from 6 April 2010 on income above £150,000) compared with a flat capital gains tax rate of 18%, tax savings may be possible by 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. You should, however, discuss this with your investment adviser.

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 a 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, but of course a top rate of tax at 50% means that this needs to be considered carefully with your tax advisers.

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'. Where vested options are available at a profit, consideration should be given to exercising these before 6 April 2010 to limit the income exposure to 40%.

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 £245,000. Contribution for the current tax year must be made before 6 April 2010 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 (currently £1.75m) could be taxed on the excess at 55%. 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 have already protected their funds.

Drawing pensions early: Pension regulations change on 6 April 2010 and almost all pension schemes will raise the minimum retirement age from 50 to 55. Take advice immediately if you are between 50 and 55 on that date.

Salary Sacrifice: It is possible to benefit from enhanced employer pension contributions by exchanging salary – this offers immediate tax savings and reduces National Insurance contributions.

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 2010. 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 2008/09 exemption can still do so before 6 April 2010, otherwise it will be lost.

The small gifts exemption: This allows gifts of £250 each year to be given 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: This 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.

Turcan Connell is uniquely placed to advise those who are or may be affected by these important changes by drawing on our expertise across the disciplines of tax and financial planning and investment management. For advice and further information please contact your Client Care Partner or Bob Hair, Director of Financial Planning (Principal) or Ian McGowan, Director of Tax Services on 0131 228 8111.

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.

EDINBURGH LONDON GUERNSEY

Turcan Connell | Princes Exchange | 1 Earl Grey Street | Edinburgh EH3 9EE
Tel: 0131 228 8111 | email: enquiries@turcanconnell.com | www.turcanconnell.com

Turcan Connell is authorised and regulated by the Financial Services Authority for investment business.