



PKF

Accountants &
business advisers

Taxation

Private client update

Welcome to our private client newsletter, our regular way of keeping in touch with clients and friends of the firm. This edition is dominated by Finance Bill 2009 as it proceeds through Parliament, though there are other current issues to note.

Summer 2009

Budget Special

Commentary

No Chancellor can resist the temptation of leaving his mark on the tax system, and the twelve years of Labour Budgets under Gordon Brown (eleven Budget statements) and Alistair Darling (two Budgets) have added significantly to the complexity of tax legislation and administration in the UK. The UK courts and decisions from Europe have also played their part in making the UK's tax system one of the most complicated in the world. While many aspects of tax law might make sense in isolation, some impose pinch points and inconsistencies.

One example is the attraction of the dividend rate of tax compared to earned income; the tax saving is 15% at the moment for higher rate tax payers and from 6 April 2010 will, in essence, remain, dipping slightly for the highest earners, to 13.89%. Not everyone, however, is able to influence the level of dividend income they receive from year to year.

Another example is the divergence of income and capital gains tax (CGT) rates; at 18% the CGT rate (about the average within the EU) looks very attractive compared to higher income tax rates at 40%, 50%, and effective rates of 60%. Will we start to see individuals and trustees seeking to realise gains rather than income under the new regime?

High income individuals and their employers will, of course, need to consider a wide range of options for minimising the impact of the 50% tax rate and, looking further ahead, the increase in National Insurance Contributions scheduled for 2011/12. It is expected that creative use of share schemes and flexible benefit packages by employers will increase substantially, and individuals will seek advice from their Independent Financial Advisers on investment vehicles that effectively roll up income payments so that tax is deferred.

Individuals owning their own business will have the most options available to them and operating that business through a company may again become attractive for tax purposes.

Those who are able to bring forward profits or bonuses into 2009/2010 may also wish to explore that possibility. This is particularly relevant to self employed individuals whose accounting periods end on any date other than 31 March or 5 April. It is possible that anti-avoidance rules, similar to those for pensions as outlined below, may be introduced so it is vital that detailed advice is taken before plans are put in place.

Personal allowances from 6 April 2010

For individuals with total net incomes over £100,000 per annum, the personal allowance will be reduced by £1 for every £2 of net income over £100,000. Net income takes account of losses, pension payments and allowable contributions to charity. Although the level of personal allowance for 2010/11 has not yet been announced, the effect of this is likely to be that the basic personal allowance will be reduced to nil for net incomes over approximately £113,000 per year. Between £100,000 and £113,000 the gradual withdrawal of the personal allowance leads to a 60% effective tax rate.

50% tax band

From 6 April 2010, a 50% tax rate will apply to individuals with taxable non-dividend income above £150,000 per year (currently 40%) and a 42.5% dividend tax rate will apply (currently 32.5%). Taking into account dividend tax credits, this means that the effective tax rate on dividends received by higher rate taxpayers will increase from 25% to 36.11% of the net dividend.

Trust tax changes from 6 April 2010

The tax rate applicable to trusts for income in excess of the £1,000 basic rate band will be 50% and 42.5% for dividends. Note that the tax rate applicable to trusts applies where the trustees receive the income in their name, not where income is received directly by beneficiaries.

Pensions tax relief from 2011/12

The Government has stated that from 2011/12 onwards:

- individuals with total annual income of less than £150,000 will continue to be entitled to tax relief on pension contributions at their highest rate of tax (currently 40%)
- individuals with total annual income in excess of £180,000 will only be entitled to 20% tax relief on pension contributions
- individuals with total annual income between £150,000 and £180,000 will receive tax relief at between 40% and 20% – tapered away as their income increases.

Pensions tax relief – 22 April 2009 to 5 April 2011

In advance of 2011/2012, the Government has introduced transitional rules to prevent individuals benefiting from making substantial increases in their pension provision in 2009/10 and 2010/11.

These 'anti-forestalling' rules work by allowing individuals to claim full tax relief on their own contributions and then by clawing back relief given in excess of 20%. Unfortunately, the claw back 'Special Annual Allowance Charge' (SAAC) applies to all contributions made by **or for** an individual in a year. So, even if the individual does not make personal contributions on which tax relief could be claimed, if his or her employer increases contributions, the SAAC will be levied on the individual.

Only individuals with annual income in excess of £150,000 in a tax year (or either of the prior two tax years) will be subject to the SAAC. An individual's total income including interest, dividends, and trading income as well as earnings from employment (and salary foregone under a 'sacrifice' arrangement) will be counted towards this limit.

The charge will apply where the total contributions made by or for an individual in 2009/10 or 2010/11 exceed the normal ongoing pattern of pension contributions or £20,000, whichever is the greater. Individuals whose normal ongoing pattern of pension savings established in past years simply continues should not be affected.

Furnished holiday lets – urgent action may be required before 31 July 2009

Until 5 April 2010, certain holiday lets in the European Economic Area (EEA) will be treated as a trade for UK tax purposes under the Furnished Holiday Letting (FHL) rules. The let property should have all the following characteristics:

- the property must be situated in the EEA (previously only UK properties benefited from this tax treatment)
- the business must be carried on with a view to a profit
- the property must be available for letting as holiday accommodation to the public for at least 140 days during the relevant 12 month period
- the property must be let as holiday accommodation to members of the public for at least 70 days during the relevant 12 month period, and
- not more than 155 days may fall into periods where the property is occupied by the same tenant for a period exceeding 31 days.

If a loss occurs in the trade, then that loss may be set against the taxpayer's other income (including UK

source income) in the year to 5 April 2010. Such loss relief must normally be claimed within one year and 10 months after the relevant tax year but, by concession, HMRC will allow claims for 2006/07 to be made by 31 July 2009 so, where appropriate, you will have to act quickly. A similar claim for 2007/08 can be made by amending your return by 31 January 2010 and claims can be made on your returns for 2008/09 and 2009/10.

Claims for some of the other tax reliefs available on FHLs all have five year and 10 months time limits, so if you have owned such a let property at any time since 6 April 2003 it may be worth investigating your tax position in detail. In some circumstances, the asset can qualify for 100% inheritance tax (IHT) business property relief, making it easy to pass such an asset to members of the family. For example, if

you let a serviced skiing chalet on short term lets, a transfer of the property may currently qualify for business property relief.

After 6 April 2010, the FHL rules will be abolished for both UK and overseas property and all income and capital gains tax advantages will cease. For example, any income loss arising thereafter will be treated as a loss on foreign property income and relievable only against future income from overseas property, apart from any capital allowance element which may be treated as a UK loss.

Apart from the changes for furnished holiday lettings, inheritance tax relief for agricultural property and woodlands are now to be extended to land owned by UK residents in other countries in the EEA with effect from 22 April 2009.

All change for UK resident non-domiciliaries

The 2008/2009 tax return for UK resident non-domiciliaries comes with a few changes:-

- All UK resident non-domiciliaries claiming the remittance basis will lose their personal allowances and annual exemption for capital gains tax purposes if they have more than £2,000 of unremitted income and/or gains in the tax year.
- Those who wish to claim the remittance basis who have been resident in the UK for at least seven out of the last nine tax years must make a payment of £30,000 tax and nominate an overseas source of income or gains to 'frank' the £30,000 payment.
- Care must be taken with gifts to immediate family members; some of these may constitute a taxable remittance for the donor.
- Take care to avoid remittances from 'mixed funds'. The tax rules from 6 April 2008 clearly set out the order in which funds from such accounts are characterised when they are remitted to the UK, generally in a way that yields the maximum amount of tax.

Falling asset prices....a gift for IHT planning

For quite some time now, many families have been worried about the potential exposure to IHT on their death. Rising stock and property values caused concern as to the tax liabilities that would arise on death. For lifetime planning, a similar concern arose where assets were gifted or placed into a trust wrapper and the donee did not survive the seven

years necessary for the gift to fall out of account. However, with recent falls in property and share values, now might be a good time to consider gifts to family members or into other structures. Such a 'transfer of value' may now come with much lower IHT and capital gains tax costs, or no cost at all.

HMRC's new High Net Worth Unit

We attended the launch of HMRC's High Net Worth Unit in April. After disbanding its Complex Tax Returns department, the new unit is now tasked with dealing with the affairs of the wealthiest 5,000

taxpayers in the UK. If you would like to read our summary of the points made by HMRC at the presentation, please email privateclienttax@uk.pkf.com.

Upcoming tax dates for your diary

- Late July 2009** – Royal Assent is expected, when the 2009 Finance Bill becomes law
- 31 July 2009** – deadline for making loss claims on furnished holiday lettings for 2006/07
- 31 July 2009** – date of second payment on account of income tax for the 2008/2009 tax year
- 31 October 2009** – last date for those who wish to send in a paper tax return for 2008/09 to HMRC
- 31 January 2010** – due date of electronically filed tax returns for 2008/09 and payment of tax due

PKF in the news in 2009

- February** – PKF warns overseas holiday home owners of a potential double tax whammy on selling, from falling prices and the falling pound – *Sunday Times*
- March** – Ask the experts, PKF solves readers' tax problems – *Mail on Sunday*
- April** – PKF warns of 'potentially misleading' new HMRC guidance for the non-domiciled – *Accountancy Age*
- Matt Coward joins Nicky Clark and Andy Verity on air to give an expenses masterclass - *BBC Radio 5 Live's Wake up to Money*
- Budget coverage – online blogging and answering viewers' and readers' questions - *Sky News and The Guardian*
- May** – 'U R L8 & U O HMRC £s!' - PKF responds to news that HMRC will contact some taxpayers by text message - *Mail on Sunday*

If you have any questions on these issues or any other tax matters please get in touch with your usual PKF contact or email privateclienttax@uk.pkf.com

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