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editorial



The Chancellor announced in the April Budget that the higher rate of tax would increase to 50% in April 2010. There was a hope that this may not apply if there was a change in Government. However, the party conference season has destroyed

this hope as all parties now seem to be prepared to leave the 50% top rate in place at least in the medium term.

We have therefore focussed in this newsletter on possible ways of mitigating this higher level of tax. It should be noted, however, that there are suggestions that the Pre-Budget Report in late Autumn will introduce provisions designed to prevent such mitigation.

We shall have to see what the Chancellor has in mind, but many of these ideas are not new and amount to fairly standard planning which has been acceptable in the past.

We have also highlighted in this briefing the new offshore disclosure facilities. According to statements from HM Revenue & Customs this is the last time that such an 'amnesty' is to be offered so if you are still not disclosing in full any offshore income or gains now is the time to 'come clean'.

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gone phishing!



There are currently major tax related scams going around which entail emails being sent purporting to be from HM Revenue & Customs or the IRS.

The emails advise you that you are due a repayment of tax and ask you to fill in the form attached to the email to enable the repayment to be made directly into your bank account.

HM Revenue & Customs never correspond with taxpayers by email and the IRS do so only very rarely. These emails should be deleted on receipt without being opened.

Alternatively, you could forward these e-mails to us and we will pass them onto the HM Revenue & Customs' fraud section who are currently investigating these scams.

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the 50% rate of tax



The Chancellor announced in this year's Budget that the higher rate of income tax would be raised to 50% from April 2010. This rate will be applied to income over £150,000. These notes look at how the new rate will work and what possibilities

there are to mitigate its effects.

The new rate applies to **total** income in excess of £150,000. In addition the personal allowance, currently £6,475 is being withdrawn. The withdrawal is staggered, starting at income levels

of £100,000 and being fully withdrawn for income levels of broadly £113,000 and above.

There are a number of opportunities to minimise your tax rate depending upon your circumstances. Below we have looked at the opportunities for individuals, employed and self employed individuals including directors and partners and trustees. We have also looked at tax efficient investments. Pensions have become extremely complicated for the next two years due to the anti-forestalling provisions, so we have included a separate datasheet on this area.

employees and directors

dividends

Dividends might be brought forward to be paid in the current tax year, that is before 6 April 2010. With the benefit of the tax credit the effective rate of higher rate tax paid on a dividend currently represents 25% of the cash dividend received. With the introduction of the additional rate from 6 April next this will increase to 36.11%.

Where dividends are to be paid in respect of profits earned in the current tax year these should be paid before 6 April 2010 to benefit from the current lower marginal rate. Where available cash and distributable reserves permit, consideration might be given to the payment of interim dividends in the current tax year "on account" of next or future years' profit. In appropriate circumstances these dividends might be loaned back to the company by the recipient shareholders to assist the company's cash flow.

bonus payments

Similar considerations apply where discretionary bonuses are to be paid in respect of profits earned in the current tax year. Such bonuses should be paid before 6 April 2010 in order to secure that the bonus is taxed at the lower marginal rate in the current tax year.

Consideration might be given to accelerating bonus payments with respect to future years or making payments "on account" of such bonuses in the current tax year.

accelerated payments

It may, in appropriate circumstances, be possible to accelerate other contractual entitlements to employment income or benefit. Rights occurring under employee share participation arrangements might be vested in the current year, again with the

view of taxing the resulting income at a lower marginal rate.

share schemes

Employee share schemes which afford a capital return to employees on a sale of their employee shareholdings are made significantly more attractive with the rise in marginal rates of income tax. Share option schemes, such as the Enterprise Management Incentive (EMI) and the Company Share Ownership Plan (CSOP) afford employees the opportunity of receiving shares in their employer companies without income tax charge and with the potential to enjoy a capital return (taxed at CGT rates of currently 18%) on sale of the shareholdings acquired.

salary sacrifice

A successful salary sacrifice entails you, as an employee, giving up your right to receive salary in exchange for a non-cash benefit, most often a pension contribution. The use of a salary sacrifice in exchange for a non-taxable benefit would reduce the liability to tax at the 50% rate.

income splitting

In the Arctic Systems case HMRC challenged, under the settlement provisions, the situation where shares in a company are held by one spouse and all the value is added by that individual's spouse. An example would be where a wife owns shares in a company through which the husband conducts his business. The House of Lords held that the dividends would be treated as income of the spouse who owns the shares because it fell within an exemption for 'outright' gifts between spouses. HMRC have twice deferred introducing legislation to deal with this although it remains clear that they consider income splitting to be "unacceptable and unfair".

individuals

equalisation of income tax between spouses

Since independent taxation was introduced, tax planning has included the equalisation of income. The object of the exercise being to ensure that both spouses utilise their personal allowances and lower rates of tax which is normally achieved by transferring cash or other assets between spouses to bring about equalisation. However beware of income splitting (see above). This is perhaps more significant following the introduction of the 50% rate of tax.

gift aid

Payments made to charities under the gift aid scheme reduce the tax payable at the higher rates of tax which after 5 April 2010 will be 50%. This will not affect the tax that can be claimed by the charity.

trustees

Trusts will also be affected by the increase in the higher rate of tax effective from 6 April 2010 as all of their income except dividends will be taxable at 50%. The dividend trust rate will be 42.5%. The individual beneficiaries' personal tax circumstances should be borne in mind when considering what can be done as this may affect the trustee's planning.

The terms of the trust will dictate what the trustees can do (assuming that they do not have an unused tax pool brought forward).

Perhaps the first thing the trustees may consider doing is to

make distributions before 6 April 2010 to beneficiaries. If a trust can still accumulate income and make capital payments then the trustees could consider making a distribution of income that is the maximum possible without incurring an additional tax liability. The balance could then be accumulated and distributed as capital.

Consideration could be given to giving beneficiaries an interest in possession in income (on a revocable basis in case of subsequent changes) which will, as well as benefitting beneficiaries, reduce tax compliance costs due to the simplified trust return.

self employed individuals and partners

incorporation

The introduction of the 50% additional rate means that the differential between the highest marginal rate of income tax (50%) and corporation tax (28%) will rise to 22% from 6 April next. This differential may be significantly greater where account is taken of the effect of national insurance contributions on employment and trading income and that the benefit of the small companies' rate of corporation tax may be available.

Unincorporated businesses might therefore consider the advantages of incorporation with a view to sheltering profits at lower rates of corporation tax. Clearly, incorporation has profound commercial consequences in terms of the ownership and management of a business and incorporation solely to enjoy the benefit of lower tax rate will generally be inappropriate.

change of year end

If you have an accounting year-end other than 5 April (or 31 March) then you could consider changing your year-end to

that date. The benefit of this would be that you are moving profits from the 50% rate of tax due next year to the current lower rate of 40%. The additional profits this year could be reduced by any overlap relief that is available for set off against the profits.

The downside to this is that you will be paying tax on the profits for the period from the end of your current accounting date to 5 April, less any overlap relief, a year earlier than you currently would do.

corporate partner

Partnerships for whom incorporation is inappropriate might consider introducing a corporate partner (or member in the case of an LLP) with the view of profits being sheltered at lower corporation tax rates. It is anticipated that the corporate partner or member would be owned by the partners and reflect their profit sharing arrangements. The corporate partner or member might provide other commercial facilities to the partnership with the view of extracting profit into the company tax regime.

investment

Notwithstanding the increase in income tax rates, capital gains tax rates are still at 18%. We do not know how long this will last but while it does it makes sense to try to utilise this rate where possible.

Firstly, it is worth re-stating the old adage that you should not let the tax tail wag the investment dog. The type of investment chosen should be based on your objectives and your attitude to investment risk. If you can then package the appropriate investment in a suitable tax wrapper, all well and good.

There are a number of tax wrappers that enable the generation of tax free or at least tax efficient income and these are summarised below.

Some investments are designed to produce capital growth rather than income. They can still be used by investors looking for income by putting together a portfolio of such investments maturing at regular intervals and treating the growth in value as income. Capital Gains are currently taxed at no more than 18%.

(i) ISAs

It is possible to invest up to £7,200 each tax year in ISAs (£10,200 from 6th April 2010 or from 6th October 2009 for the over 50s). Income and capital gains from ISAs are tax free. By making use of the allowances each year it is possible to build up a significant portfolio. Investment can be in cash and stocks and shares ISAs depending on how you want to invest and the amount of risk you want to take.

(ii) investment bonds

Investment bonds issued by insurance companies enable you to invest in a wide range of assets. The bonds are tax efficient in that the underlying funds are generally taxed at no more than 20% on income and gains. It is possible to withdraw up to 5% per annum of the original investment for up to 20 years with no further tax liability. Any withdrawals in excess of this will be liable to tax at your top rate less 20%. In the year of encashment there is a potential liability to higher rates of tax. Thus it is possible to defer higher rates of tax for 20 years or more and, by careful planning, the tax on final encashment can be reduced or avoided altogether.

These bonds can be arranged offshore and in this case the funds do not suffer tax but will not be able to recover any withholding tax (eg. on dividends). The same tax deferred 5% per annum regime applies. On final encashment, there is a potential liability to basic as well as higher rates of tax.

(iii) unit and investment trusts

Dividends from unit and investment trusts are treated in the same way as dividends from shares – in other words there is a credit to cover the basic rate tax liability but, if you are a 50% tax payer, the dividend will be taxed at the additional rate of 42.5%. However, there are some opportunities for avoiding tax on income.

Split capital investment trusts attracted a poor press some years ago because of the closely inter-related structure of some trusts and their failure to perform. However, the theory of these trusts is sound and those trusts structured to generate no income but capital gains could benefit from a renaissance.

Trusts investing in overseas equities do not generate much by way of dividends, focusing on capital growth instead. Unit and Investment Trusts are a good way of investing in overseas stock markets.

(iv) zero coupon bonds

A zero-coupon bond is a fixed interest investment or debt security bought at a price lower than its face value, with the face value being repaid at the time of maturity. It does not make periodic interest payments, or have so-called “coupons,” hence the term zero-coupon bond. Investors earn a return from the compounded interest all paid at maturity plus the difference between the discounted price of the bond and its par (or redemption) value. Examples of zero-coupon bonds include U.S. Treasury bills and U.S. savings bonds.

(v) national savings

Many National Savings products (but not all) provide tax free returns. Examples are Premium Bonds, Fixed and Index-Linked Savings Certificates. Furthermore they offer high levels of security. However, generally the returns are poor – the prize fund for premium bonds is currently only 1% and Savings Certificates offer a maximum return of 1.9% per annum over 5 years.

Having said that, if we are in for another bout of high inflation, Index Linked Certificates offering inflation plus 1% per annum tax free could be attractive.

(vi) pensions

The attached datasheet from haysmacintyre Financial Planning gives detailed advice on the planning opportunities and the anti-forestalling provisions.

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new disclosure opportunity (NDO)



HM Revenue & Customs (HMRC) have applied for permission to serve disclosure notices on more than 300 Financial Institutions in the UK. The disclosure notice will require the Institution to furnish HMRC with details of all offshore accounts in

existence in the last 6 years where the account holders have registered an address in the UK.

The prospect of obtaining this information has prompted HMRC to introduce the NDO. Under the NDO people who make a complete and accurate disclosure, between 1 September 2009 and 12 March 2010 (see timetable below), of any unpaid tax arising as a result of offshore assets will be able to settle their tax liabilities at a favourable (10%) penalty rate. Failure to take advantage of this opportunity may result in a higher penalty on subsequent discovery of the unpaid tax and in extreme cases may result in prosecution.

If you were written to by HMRC under the previous offshore disclosure facility (ODF) (that ran from April to November 2007) about offshore income but did not take advantage of the ODF but now wish to make a disclosure, you will be subject to a less favourable penalty of 20%.

timetable

The timetable for the NDO is as follows:

- 1 September 2009 – earliest date for notification by paper, the closing date is 30 November 2009.
- 1 September 2009 – earliest date for disclosure by paper, the closing date is 31 January 2010.
- 1 October 2009 – earliest date for online notification, the closing date is 30 November 2009.
- 1 October 2009 – earliest date of online disclosure, the closing date is 12 March 2010.

HM Revenue & Customs have also reached agreement with the Lichtenstein authorities and a separate disclosure applies to those with accounts and funds in Lichtenstein. As this disclosure will only cover 10 years unlike the 20 years of the NDO there would be an advantage in disclosing under this note if you have undisclosed Lichtenstein income or gains.

If you have any questions or wish to make a disclosure then please contact your usual engagement partner or a member of the tax team.

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VAT increase from 1 January 2010



Last year's surprise reduction in VAT to 15% was always intended to be temporary. As a result we all know about (and this time can actually prepare for) the increase back to 17.5% from 1 January 2010.

Invoices for work already performed dated before the increase should charge VAT at 15%. Invoices can be issued on account charging VAT at the lower rate providing payment is not deferred by more than six months.

Prepayments less than £100,000 can secure VAT at 15% even where the invoice is subsequently issued in January assuming the services or product is not artificially split into a number of payments below this limit.

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future events

2009/2010 Training courses for trustees of charities:

- understanding charity accounts 17 November 2009
- what every new trustee should know 24 November 2009
- managing cash and investments 12 January 2010
- charity law update 19 January 2010
- good governance 26 January 2010
- charities and their property 10 February 2010
- charities and their people 23 February 2010

• annual conference for independent schools: 03 February 2010

For further information on these events please contact
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www.haysmacintyre.com

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A list of partners' names is available for inspection at Fairfax House, 15 Fulwood Place, London WC1V 6AY.

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