

Year end tax planning for individuals

By Doug Cowan

February and March are key months in which to consider tax planning to maximise the use of an individual's allowances, reliefs and exemptions for the current year. Some of these will be lost if not used before the tax year end in April.

Whilst it is as well to look at 2009/10 tax year, it is also an ideal time to put some planning in place for the 2010/11 tax year. This is more relevant this year, especially for those on higher incomes because we know that for them tax rates are set to increase, either directly or indirectly with effect from 6th April 2010. This means that prior action is needed for a person to optimise their tax position.

Income tax planning

Income tax rates are currently 10% (on certain investment income), 20% and 40%. Four key changes will take place from 6th April 2010:

- i. The standard personal allowance will be frozen at the 2009/10 rate (£6,475)
- ii. The threshold for the start of higher rate tax will be frozen at £37,400
- iii. A 50% tax charge will apply to taxable income that exceeds £150,000
- iv. People with income of more than £100,000 may find that they will lose some or all of their standard personal allowance.

The impact of (i) and (ii) will mean that even more people will fall into the higher rate tax charge. Anyone who was borderline for higher rate tax this year and who receives an increase in pay, will now find themselves in the higher rate tax net.

The impact of (iii) and (iv) means that people with income of more than £150,000 and £100,000 respectively will pay even more tax.

These tax increases can be

dealt with in a number of ways:

- *Independent taxation planning*
- *Utilising tax exemptions and allowances*
- *Tax efficient investment.*

Independent taxation planning

This has become more important following the Chancellors announcement that the top rate of income tax will increase to 50% for those earning £150,000 or more and the withdrawal of the standard personal allowance on income between £100,000 and £112,950. For such people who are married or have a registered civil partner, the tax savings available by diverting income into the lower income partner's name will be even more important. This is also true of the 40% tax payers. The appropriate type of planning to adopt will depend on the type of income a person enjoys, i.e. earned/business income or investment income. As stated earlier most strategies need a full tax year to deliver maximum effect, so this may serve as a reminder for planning in the coming year.

Utilising tax exemptions and allowances

Where possible, a couple should try to ensure that they both have pension plans to provide an income stream in retirement that will also use their personal allowances.

Clients should make maximum use of all personal allowances available to them and their family. A husband and wife each have their own personal allowance. This is particularly relevant where one spouse pays tax at a lower rate than the other. A non-working spouse with no investment income will be able to receive income of £6,475 for the tax year 2010/11 before he or she pays any tax.

With effect from 6th April 2010, a person whose income exceeds £100,000 will find that their personal allowance is cut back meaning that they may be paying a marginal rate of tax of up to 60% in the case of earned income.

Older married couples benefit from an increased age-related personal allowance. It may be advisable to transfer income producing assets between couples where one would otherwise exceed the age allowance limit of £22,900 (2009/2010 and 2010/11).

Tax efficient investment planning

With the rate of tax effectively increasing it is most important that people invest in the most tax efficient manner.

ISA

The ISA is still the main method of investing savings with freedom from income and capital gains tax. An individual can invest in any tax year from 6th April to 5th April using the following criteria:

- *Maximum annual contribution of £7,200, of which no more than £3,600 can be invested in cash. The balance can then be invested in stocks and shares. Alternatively the full amount of £7,200 can be invested in stocks and shares.*
- *Investors aged over 50 in this tax year can invest £10,200 of which £5,100 can be in cash or the full amount in stocks and shares.*
- *From 6th April 2010 the increased ISA investment limit applies to all qualifying individuals irrespective of age.*

- *Money invested in a cash ISA can be moved into a stocks and shares ISA but not from stocks and shares into cash.*
- *A child aged 16 or over can invest £3,600 in a cash ISA for this tax year or £5,100 in 2010/11*

So, for maximum efficiency for the tax year 2009/10 ISA investments need to be made by 5th April 2010 and for those aged 50 or more there is a one off opportunity to utilise the increased limit. If not used it will be lost.

Other tax efficient investments are dependent upon individual circumstances but include single premium investment bonds, enterprise investment schemes and venture capital trusts. These are not the only options open to investors and businesses alike but careful consideration needs to be given to any actions taken



Conclusion

Strategies for Tax Planning can be complex but if undertaken there is a potential for savings to be made. For example:

Owner/Directors of Private Limited Company

Where married couples run their business through a company it would be sensible to share salary/dividend payments evenly. In the run up to next year's tax increases, owner/directors should no doubt consider maximising the salary and dividends taken out of the business before 6 April 2010.

The Self Employed

The self employed have various options to delay the payment of income tax at 50%, for example; changing their tax year end to 31st March 2010 - if currently it is 30th April 2010 those earning £150,000 or more will be paying tax at 50% from 1st May 2010. By changing it to

31st March this increase is delayed by one year. For a sole trader, consideration should be given to splitting the profits with a partner, say a wife or civil partner thereby potentially reducing liability to the 50% tax bracket.

Earned Income £100,000+

From 6th April 2010, where earned income is more than £100,000 you will have to deal with the loss of the Personal Allowance against tax. Where this is the case you should look to reduce income either

by making a pension contribution or arranging for a salary sacrifice. This is particularly relevant to those earning between £100,000 and £112,500 as benefit is lost on a sliding scale reducing to nil for earnings in excess of £112,950.

There are other examples of tax savings and benefits for all our clients, but as each situation is individual professional advice should be taken and any solution tailored to their need.

For technical assistance and advice call:-

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