

Tax relief on pension contributions

A new set of rules were announced for tax relief on pension contributions for those receiving income of £150,000 or more in the Chancellor's 2009 Budget. In summary, as a result of the legislation there are two sets of regulations; those with immediate effect which came into force on 22nd April 2009, and those which will be introduced on 6th April 2011.

The 2011 regulations are yet to be announced in detail, but will restrict tax relief on pension contributions for people with income of £150,000 or more. Tax relief will be tapered for income between £150,000 and £180,000 so that at £180,000 it is restricted to basic rate tax relief; currently 20%.

Another unintended consequence of the recent Budget was that a number of people earning between £100,000 and £150,000 could potentially receive up to 60% tax relief by making sufficient pension contributions under the new

rules. This is based on the assumption that pension contributions come from gross income before the application of the personal allowance.

Once an individual's income exceeds £100,000, the personal allowance on which no tax is charged is reduced by £1 for every £2 of additional income. This means that the first £2 in this bracket has its own income tax charge of 40% (80p), plus it brings a further £1 into the taxable bracket – also charged at 40% (so another 40p). The total additional tax is therefore £1.20 – or 60%. This applies

until the personal allowance is exhausted; thereafter it reverts to 40% until the 50% rate kicks in at £150,000.

At the time of writing, only draft legislation was available which may be subject to change. This guideline is therefore based on our understanding of the draft legislation.

Whilst this new regime is still being finalised it is imperative that you seek advice from your usual UHY Hacker Young contact, or UHY Financial Planning specialist, on what is currently a constantly evolving subject.

VCTs and EISs for the higher rate taxpayer

Venture Capital Trusts (VCTs) and Enterprise Investment Schemes (EISs) are making increasingly compelling investments for those earning over £150k who are looking to save for the medium term, or build up a retirement pot in a tax efficient manner.

The increase in tax on income and pensions for those who earn over £150,000 means that VCTs and EISs can provide more tax efficient, albeit potentially riskier, investment opportunities.

VCT investments receive 30% upfront income tax relief (up to £200,000 per tax year), tax-free capital gains on the investment and tax-free dividends, provided you hold your investment for five years.

EIS investments provide 20% income tax relief (up to £500,000 per year),

100% capital gains tax deferral up to the amount of the investment, inheritance tax exemption after two years provided the investment is held at time of death, and tax-free capital growth.

Both VCTs and EISs are generally considered as higher risk investments. The Government provides tax relief to compensate investors for taking on this extra risk. Some VCT and EIS providers can reduce the investment risk and provide investments that are not correlated to the stockmarket.

The 2009 Budget has improved the flexibility of income tax relief from subscriptions in EIS qualifying shares, specifically when extending the period for carry back of relief.

While VCT and EIS products could provide a viable alternative for those likely to be affected by the new higher rate of income tax, they are not suitable for everybody. Please speak to your usual UHY Hacker Young partner or UHY Financial Planning specialist for further advice on the implications of switching to these investment products.

Income above £150,000 and pension contributions

Despite the highest rate of tax on income above £150,000 increasing to 50% and the personal allowance for those with income over £100,000 being reduced to nil, payment of personal pension contributions can still be an attractive option.

The definition of 'relevant earnings' for a high earner comes from the Finance Act 2009. In most cases, the maximum pension contribution rate is based on 'earned' income. To establish whether income is at or above £150,000 however, other items such as employment benefits, investment income and dividends are included.

This income limit also applies to the previous two tax years, so even if your income has not reached £150,000 this

tax year, but did in any of the tax years since 2007/2008, then you could be affected by these rules.

The calculation of income is as follows:

Total the following income:

- earnings from employment
- earnings from self-employment/ partnerships
- income from pensions in payment
- interest on savings
- dividend income
- rental income
- income received from a trust
- pension contributions paid under a net pay arrangement or salary sacrifice (not applicable if arranged before 22nd April 2009 and not increased).

Then deduct the following:

- trade and property loss relief
- gift aid
- relievable pension contributions

You will be left with your relevant income total.

It is important that you establish your relevant earnings and that pension contributions are appropriate for your personal circumstances. Even if you do not earn more than £150,000, other factors, such as those listed above, may push your income above this level. This will result in you being taxed at the higher 50% rate. It is imperative that you seek advice from your usual UHY Hacker Young contact, or UHY Financial Planning specialist in order to understand the complexities of this new regime.

Were you born between 1955 & 1960?

If you were born between 6th April 1955 and 5th April 1960 you have until the end of this tax year, April 2010, to decide whether to take the benefits from your pension/s, or to wait until after you turn 55. The reason for this deadline is that the minimum age from which you can take benefits from your pension/s is being increased on 6th April 2010 from 50 to 55.

If you were born on 5th April 1960 then you will be required to start taking your pension benefits by the end of that day (5th April 2010). What a way to celebrate your half century! If you miss this window you will be forced to wait another 5 years.

If you still plan to retire after 5th April 2010, but are under the age of 55, you will require other sources of income until your 55th birthday when you will have access to your pension.

Whether or not you are planning to retire soon, now is the time to make sure your pension arrangements are on track.

Savers and pensioners

The Chancellor has made two adjustments to help savers and pensioners who have been hit hard by the reductions in interest rates:

- The ISA savings limits are to be increased to £10,200, and £5,100 for the cash-only element of the ISA. These new limits come into effect on 6th April 2010 for most savers, but savers who are aged 50 or over on 6th October 2009 will be able to take advantage of the new limits from that date.
- The amount of capital disregarded when making a claim for pension credit, and certain other benefits, will be increased from £6,000 to £10,000 from November 2009.

For more information



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