

YEAR END TAX PLANNING

When investment returns are low it is more important than ever to ensure that full advantage is taken of the opportunities which exist to minimise tax.

Married Couples

Married couples and registered civil partners can reduce the amount of income tax they pay by switching investments to whichever partner pays tax at the lower rate and by utilising both personal allowances.

Transfers must be outright and unconditional. A non-working spouse will be able to receive income of £6,035 for the tax year 2008/9 and £6,475 for 2009/10 before paying any tax.

Older couples enjoy an increased age-related personal allowance in respect of income up to a maximum which has been set at £22,900 p.a. for (2009/10). So this is another trigger point for equalising income and needs to be borne in mind when considering the funding of couples' individual pension plans.

Pensions

5 April 2009 is the deadline for making an election to HM Revenue & Customs for the protection from tax of pension funds accrued prior to the introduction in 2006 of limits on the size of funds entitled to favourable tax treatment.

Most people requiring this protection will already have made the necessary election, but some may have based their calculations on the assumption that the Government would pursue its original intention progressively to increase the Lifetime Allowance, and may need to reconsider their position now that this allowance has been frozen at £1.8m for the five tax years up to 2015/16.

ISAs

The appeal of ISAs is based on their freedom from both income tax and capital gains tax plus the absence of any restrictions on withdrawals.

There are two forms of ISA – cash ISAs and stocks and shares ISAs – but the rules have been changed to permit cash ISAs to be switched into stocks and shares ISAs (but not *vice versa*).

The annual contribution limit is £7,200, of which no more than half (£3,600) can be invested in a cash ISA.

Any excess over this amount can be invested in a stocks and shares ISA. Most ISAs are in fact invested in Unit Trusts and OEICs rather than directly into stocks and shares.

Children over the age of 16 are permitted to invest up to £3,600 in cash ISAs.

Capital Gains Tax

In 2008/9, both husband and wife (and civil partners) are able to realise gains up to £9,600 without liability to tax, and any excess is taxed at 18%. So transfers of chargeable assets between spouses could double the annual exemption.

Consideration might be given to realising losses on investments to offset against taxable gains; and losses which are carried forward can be offset to the extent that they reduce gains in the current year to £9,600, with any excess being carried forward. However, transferring an asset with a loss to a spouse who owns assets on which a taxable gain is to be realised could result in anti-avoidance rules being triggered.

If a disposal is being considered which would give rise to a taxable gain, it might be sensible to spread the disposal over two tax years. Alternatively, if the gain cannot be spread or is very large, delaying the disposal until after 5 April 2009 will result in the payment of tax being deferred until 31 January 2011.

Bare Trusts For Children

If a parent establishes a bare trust for a minor unmarried child, all capital gains within the trust will be taxed on the child beneficiary and will benefit from the child's own exemption (£9,600 in 2008/9). However, if income of over £100 p.a. is generated by the trust assets, this income will be taxed as if it were the parent's income.

A potential disadvantage of a bare trust is that the trust capital can be claimed by the child beneficiary on attaining the age of 18 (16 in Scotland).

Discretionary Trusts

Discretionary trusts give settlors a greater degree of control than bare trusts and could provide income tax benefits.

Gross income up to £1,000 p.a. is taxed at the standard rate, and income in excess of this figure is taxed at the rate applicable to trusts, currently 40% on savings income and 32.5 on dividends



The rate of tax on dividends is set to rise in 2011/12.

However, beneficiaries of savings income distributed by trustees can recover from HMRC the difference between the tax paid by the trustees and their own tax rate, so non-taxpayers are able to reclaim the tax in full. Income derived from dividends is treated less favourably, being subject to an effective charge of 20% for non-taxpayers.

It is therefore important to give consideration to tax when selecting investments for a discretionary trust.

Life Policies In Trust

One of the simplest and most effective means of providing cash on death to meet Inheritance Tax liabilities is to write a life insurance policy under trust. In the case of a married couple this should be on a joint lives, last survivor, basis. The premiums on the policy will invariably be exempt from Inheritance Tax on the basis that they fall within either the £3,000 annual exemption or the exemption for normal expenditure out of income; and the proceeds will fall outside the estate of the life insured.

Topping-up State Pensions

The period for which National Insurance contributions will need to have been paid in order to secure a full State pension will reduce in April 2010 to 30 years.

Where an NI record is not sufficient to obtain a full State pension 'added years' can be purchased. However the cost of making up any shortfall will increase significantly from 6 April 2009.

Therefore, people expecting to retire before April 2010 with a shortfall may benefit from making a top-up payment before 6 April 2009. The first step is to obtain a benefits forecast from The Pension Service (0845 300 0168).

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No responsibility can be accepted for the accuracy of the information in this newsletter and no action should be taken in reliance on it without advice. Please remember that past performance is not necessarily a guide to future returns. The value of units and the income from them may fall, as well as rise. Investors may not get back the amount originally invested

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