

Thankful for Small Mercies

A few small grains of comfort can be gleaned from the our first Budget of 2010:

Capital gains tax has been held at 18% - an anomalously low level which should encourage both individual investors and trustees to spring-clean their portfolios.

Pension contributions can be used to avoid the reduction in personal allowances affecting those earning more than £100,000 p.a. However, for those earning in excess of £130,000 there are further tax consequences.

ISA contribution limits will be raised in line with inflation from the new level of £10,200 as from April 2011.

The ISA tax breaks, which include freedom from capital gains tax and the ability to draw a tax-free income, make these the natural complement to pension provision. Another benefit is that investment returns need not be included in tax returns.

The comparison between the returns from a fund which is held within an ISA and one held outside are startling. It has been calculated that if a higher-rate taxpayer had accumulated £50,000 in a Corporate Bond fund, he or she would be £14,000 worse off if the fund had been held outside an ISA than within - an 83% lower return!

Financial Housekeeping

Regardless of current tax rates, investors will benefit from adopting a few commonsense measures:

- Protect against inflation, possibly by holding low-risk index-linked gilts. These are not subject to capital gains tax, so a gross return of 5% is a 5% net gain, though it should be noted that this includes the interest, which is taxable. Index-linked National Savings certificates may also be worth considering.
- When deciding what to invest in tax-wrappers such as ISAs and pension funds, give priority to higher-yielding investments which would otherwise suffer most tax.
- Make full use of the annual capital gains tax allowance by transferring assets between spouses or civil partners.

- Use single premium investment bonds to defer income to later years, when taxable income may be lower.
- Repay debts in preference to investing when the return from the investment may be lower than the cost of servicing the debt.
- Maintain sufficient liquid cash to meet foreseeable needs.

Pensions for Ex-Pats

A survey by the Foreign and Commonwealth Office suggests that four out of ten people approaching retirement are considering moving abroad. But what effect would this have on pension benefits which had accrued in the UK?

There has always been the facility to transfer UK pension benefits overseas, but until 2006 this was a complex process requiring individual consideration for each scheme and often a translation of the rules of the receiving scheme.

Now, for those who have left the UK permanently or are planning to do so, and those who are UK resident but non-domiciled, much simpler arrangements are available, known as Qualifying Recognised Overseas Pension Schemes ('QROPS').

QROPS are overseas schemes to which UK pension savings can be transferred, subject to the receiving scheme having applied for and been granted recognition by the UK Revenue and having pledged its future co-operation.

HM Revenue & Customs maintain a list of QROPS, and any transfer to one of the listed schemes must be notified to HMRC by the administrator of the UK scheme from which the transfer is proposed

Technically, transfers involve crystallising the UK fund and calculating whether the value exceeds the standard lifetime allowance (£1.8m in 2010/11) above which UK pensions are subject to a tax charge. If the fund does exceed this value, the transfer to QROPS will only avoid the tax charge if a primary or enhanced protection certificate is in place.

One of the conditions of recognition is that QROPS must report to HMRC all payments of benefits made within five years after the transfer, and the pension holder will be subject to UK tax on any payments which would have been regarded as unauthorised under the UK rules.



After five years, the reporting obligation ceases and the way in which the funds can be invested and payments made and the tax payable will all be subject to the rules of the QROPS and the pension legislation of the local jurisdiction.

However, HMRC is on the look-out for abuse of QROPS. In October 2009 it issued a statement to the effect that if a QROPS were to invest UK-sourced transfer monies in residential property even after the five years had expired, this would need to be reported to HMRC and would give rise to an unauthorised payment charge on the member.

QROPS schemes have varying requirements. For example, some occupational QROPS require proof of employment, whereas individual schemes may only have a residency test. QROPS are complicated, and advice is essential.

Thought for the Day

"Compound interest is the eighth wonder of the world. He who understands it earns it. He who doesn't pays it".

Albert Einstein

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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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