BUDGET 2009: CONTENTS AND CONSEQUENCES

Alistair Darling's second Budget had a feeling of déjà vu about it, rather like his first. Not only was it late – the latest Spring Budget since 1945 – but it was also even more heavily trailed than usual in the Pre-Budget Report (PBR) and last minute press leaks. With hindsight, it is clear that the Chancellor had already settled on a delayed Budget by last November. Hence his announcement of the income tax bands which are normally kept under wraps until the Budget proper.

UK and global economic conditions have worsened markedly since last November. Mr Darling's PBR projections for the economy to shrink by 0.75%-1.25% in 2009 looked optimistic as he announced them. They now are located at the fairytale end of the forecast spectrum. The revised figure for the performance of the UK economy– a *contraction* of 3.25%- 3.75% in 2009 followed by 1.25% growth in 2010 and 3.5% growth in 2011 – still looks on the rosy side. The IMF, for one, published gloomier predictions (-4.1% and -0.4%) on Budget Day. Two days later, National Statistics released figures showing that the economy had shrunk by 1.9% in the first quarter of 2009 alone. However, the Chancellor needed to keep his forecast on the relatively sunny side to avoid producing even larger deficits in his long-term forecasts.

The headline-grabbing moves in the Budget were the increases in tax for those with high incomes, both in terms of more tax and a reduction in the availability of tax relief on pension contributions. The attack on high earners appears more politically than financially targeted. Such are the deficits facing Mr Darling – £175bn this year and £173bn next year – that the extra £2.2bn revenue to be raised by these Budget measures in 2011/12 look little more than rounding errors.

In this Bulletin we look at the main changes that will affect individuals and businesses and examine some of the related planning issues. If any of this strikes a chord, you are strongly recommended to consult your financial adviser.

Contents

The contents of this Bulletin are based on the proposals put forward by the Chancellor in his Budget speech and explained in documents subsequently published by HMRC and the Treasury. All Budget proposals may be subject to change before the Finance Act is passed.

References to spouse, husband and wife and married couples include references to registered civil partners and civil partnerships.

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Personal Income Tax and National Insurance Contributions

The income tax and National Insurance contributions (NICs) changes confirmed for 2009/10 are:

- The 10% starting rate band, which caused so much controversy last year, has been increased to £2,440. As it continues to apply to savings income only, for most earners and pensioners it remains an irrelevance because it will be covered by earned and/or pension income.

- The basic rate of tax remains at 20%.

- The starting point for higher rate tax has risen by £2,600 (7.5%) to £37,400 of taxable income. The above-inflation increase is not all it seems because some of the tax saving will be clawed back as a result of changes to National Insurance contributions.

- The standard personal allowance has risen by 7.3% (to £6,475), while most other allowances have risen by 5% (see Appendix). Last year's post Budget £600 increase to the personal allowance has therefore been consolidated. However, the link between the personal allowance and starting point for NICs will be restored in 2011/12: for now NICs start at £5,715 a year (£110 a week), £760 below the personal allowance.

- The National Insurance upper earnings limit (UEL) for employees has increased by £74 a week (9.6%), increasing NICs for higher earners by up to about £350 a year. There is a corresponding adjustment for the self-employed, who face a maximum NICs increase of about £246 a year. The new UEL is designed to match the starting point for higher rate tax, once the personal allowance is taken into account (£6,475 + £37,400 = £43,875). In practice (see below), many higher-rate taxpaying employees will face 40% tax and 11% NICs on part of their income

- For 2009/10 there has also been a change in the rules for contracting out of the state second pension scheme (S2P), which affects some employee NICs. While the UEL has risen, the upper level of earnings which qualify for contracting out rebates has been fixed at £770 a week. This will mean:

    - If you are an employee contracted out via your employer's occupational pension scheme, you will pay full rate NICs (11%) on earnings between £770 and £844 a week rather than the reduced 9.4% contracted out rate.

- If you contract out using a personal pension, the amount of rebate paid into your plan will be based on earnings between £95 and £770 a week, even though the ceiling for full NICs runs up to £844 a week.

If you are not contracted out, the S2P benefit you accrue in 2009/10 will be based on earnings between £95 and £770 a week, ie. £74 a week below the full NICs threshold.

These changes mark the first stage of the reform of state pensions which will re-establish the link between basic state pension increases and the rise in average earnings and eventually see S2P become a flat rate pension.

Allowing for the tax and NIC changes, in cash terms, the winners are generally those earning £43, 875 or more, as they gain the full benefit of the increased higher rate threshold. The full results are demonstrated in the table below:

Earnings	**2008/09**		**2009/10**		**Overall Budget Benefit***
£	**Income Tax £**	**NICs £**	**Income Tax £**	**NICs £**	**£**
10,000	793	502	705	471	+ 119
15,000	1,793	1,052	1,705	1,021	+ 119
20,000	2,793	1,602	2,705	1,571	+ 119
25,000	3,793	2,152	3,705	2,121	+ 119
30,000	4,793	2,702	4,705	2,671	+ 119
35,000	5,793	3,252	5,705	3,221	+ 119
40,000	6,793	3,802	6,705	3,771	+ 119
45,000	8,626	3,856	7,930	4,209	+ 343
50,000	10,626	3,906	9,930	4,259	+ 343

** Based on an employee under age 65 with a single personal allowance who is contracted in to the State Second Pension. Tax credits are ignored.*

For 2010/11 onwards the Chancellor announced two changes to the proposals he originally put forward in the Pre-Budget Report (PBR) last November. Both will increase income to the Exchequer:

- *Personal allowances:* Personal allowances will now be phased out at the rate of £1 for each £2 of income in excess of £100,000. The definition of income is, broadly speaking, gross taxable income less specified deductions, such as pension contributions and Gift Aid payments.

  The result of this reform will be that from 2010/11 the band of income between £100,000 and £112,950 will suffer a marginal tax rate of up to 60%, assuming that the personal allowance is unchanged next tax year.

The PBR had suggested that the allowance would be phased out in two stages, with half phased out at £100,000+ and the other half phased out after £140,000.

- *Additional higher rate of tax:* For 2010/11 there will be a new higher rate of tax of 50% (42.5% for dividends) on taxable income over £150,000. The same 50%/42.5% tax rates will also apply to trusts from 2010/11. The original proposal had been for a 45% top tax rate to be introduced from 2011/12.

The Chancellor announced in the PBR that from 2011/12 all NIC rates will rise by 0.5%. Thus someone with earnings of over £150,000 in that tax year will only retain £48.50 out of each £100 of earnings above £150,000.

Tax credits

Tax credits generally rose by 5%, in line with inflation to September 2008. However, the most widely claimed credit, the family element of Child Tax Credit, once again remains at £545, the level at which it was first set for 2003/04. There was also a freezing of the childcare payments and the income threshold (£6,420) above which credits start to be withdrawn, other than for people claiming only Child Tax Credit.

Company Cars

The company car benefit scales remain unchanged for 2009/10. The next adjustment will take place in 2010/11, when there will be a 5g/km decrease to 130g/km for the lower threshold (15% for petrol). This will be followed in 2011/12 by a further threshold reduction to 125g/km and the abolition of all the current scale-rate reductions for alternatively-fuelled cars (eg LPG), other than for electric-only vehicles.

The multiplier for calculating car fuel benefit in 2009/10 was left at £16,900, in spite of the substantial falls in petrol and diesel prices over the last year. According to the AA, the average UK price in April 2008 was 108.1p a litre for petrol and 117.4p for diesel.

Residence and domicile

A number of mostly technical changes were announced to the new non-domicile tax rules introduced from 2008/09. The most significant of these was the removal of the requirement for all individuals employed in the UK to file a self-assessment tax return if they have also received income from overseas employment in the same tax year.

For 2008/09 and subsequent tax years there will be no requirement to file a return where:

- overseas employment income is less than £10,000;
  and
- overseas bank interest is less than £100 in any tax year;
  and
- all of the income is subject to a foreign tax.

Furnished holiday lets

In a surprise move, hidden deep in the Budget documentation, the Chancellor announced that the furnished holiday lettings legislation would be repealed from 2010/11. A clue to why this move was made can be found in the fact that for 2009/10, the rules will be extended to include qualifying lettings in the EEA.

Offshore disclosure – round two

HMRC will operate a new disclosure opportunity that will run until March 2010. If you hold an offshore account, this will give you an opportunity to disclose (and pay) any unpaid tax or duties. Details of penalty charges have yet to be confirmed.

A number of offshore centres have recently signed new exchange of information treaties with the UK, which HMRC probably hopes will encourage some reconsideration by those who ignored the original offshore disclosure window in the first half of 2007.

Planning Points

Taking advantage of the new 40% tax and full NICs thresholds

The increase in the upper earnings limit now means that if you are entitled only to the personal allowance, in 2009/10 you will pay full NICs on earnings from £5,715 a year up to the starting point for higher rate tax (£43,875).

If you are an employee with any taxable fringe benefits, such as a company car or private health insurance, the way that PAYE operates means you could be in the position where an extra £1 of earnings is subject both to 40% tax *and* to 11% NICs – a total marginal rate of 51%. The flip side of this is that exchanging that £1 of earnings for an employer pension contribution through a salary sacrifice would effectively mean you benefited from 51% combined tax and NIC relief.

The 51% 'Tax' Rate

In 2009/10 Bill earns £43,500 a year and has a company car with a taxable value of £3,000. He is contracted into the state second pension. His net allowances are £3,475 (£6,475 - £3,000), giving him a PAYE tax code of 347L. His income is subject to tax and NICs as follows:

Band of earned income	Tax %	NICs %	Total %
£0 - £3,475	0%	0%	0
£3,475 - £5,715	20%*	0%	20
£ 5,715 - £40,875	20%	11%	31
£40,875 - £43,500	40%	11%	51

* *The 10% starting rate only applies to savings income*

Thus on his top £2,625 of earnings Bill will be paying 40% income tax plus 11% NICs – a total of 51%. If he sacrifices that £2,000 of gross salary in favour of an employer pension contribution, he will effectively get 51% total relief, so the £2,000 pension contribution will only cost him £980 in reduced net income.

The widening age allowance trap

Your entitlement to age allowance depends upon your total income if you are 65 or over by 5 April 2010. You receive the full allowance provided your total income does not exceed £22,900. Above that level your allowance entitlement is reduced by £1 for each £2 of income, although the allowance cannot be reduced below the standard personal allowance. With basic rate at 20% in 2009/10, the age allowance reduction means that at the margin you could be a 30% taxpayer, paying tax on £2 of income plus a further £1 because of the lost allowance.

A similar rule applies to the husband if you and/or your spouse were born before 6 April 1935 and are therefore eligible for the married couple's age allowance. However, the relief given by this allowance is at a rate of only 10%, so the effective tax loss is at a rate of 25%. Not surprisingly, the married couple's allowance is reduced only *after* all the personal age allowance is lost.

The sharp increase in age allowances over recent years means that bands in which the 25% and 30% tax rates could apply are now surprisingly wide. For a single person aged under 75, the 30% band now stretches from £22,900 to £28,930, while for the husband of a married couple aged 75 or over, the two bands extend from £22,900 to £37,820.

If you are 65 or over and have a total income above £22,900, you may be able to regain some or all of your age allowance, and thus save tax, by rearranging your investments. This need not mean reducing your spendable income – the key is to reduce your *taxable* income. There are variety of ways in which a suitable reduction can be achieved, including the use of ISAs and investment bonds.

Turning tax credit claw back to your advantage

While you may think of tax credit as relevant only for the lower paid, many higher rate taxpayers are eligible for an element of tax credit. Usually this is the family element of Child Tax Credit, worth up to £10.50 a week (£21.00 for a child under age 1), but there may be additional credits, eg the childcare element of Working Tax Credit, which can be worth up to £240 a week.

The calculation of tax credit entitlements is complex, but if you are a higher rate taxpayer there are two important rules to watch:

- The family element of Child Tax Credit is clawed back at 6.67% of family income (broadly taxable income) over £50,000 or, if greater, the level at which all other tax credits are extinguished.

- Tax credits, other than the family element of Child Tax Credit, are clawed back at a rate of 39% in 2009/10.

The combined effect of higher rate tax and tax credit claw back can therefore be 46.67% or 79%. In other words, an extra £1 of taxable income could mean you lose 40p in tax and 39p in tax credit, leaving a net 21p.

The reverse is also true: £1 less of taxable income could imply only 21p less net income. So, for example, if you reduce your taxable income by making a pension contribution, you may be securing £1 of retirement benefit at an effective cost of 21p.

Think ahead to 2010/11

Next tax year will see the arrival of the new 50% top tax rate and phasing out of personal allowances if you have income exceeding £100,000. To minimise the impact of these changes, now is the time to consider:

- Whether to rearrange investment holdings so that dividend and interest income flows to the lower taxpaying spouse. In theory, a married couple need not worry about the 50% tax rate until their total joint income exceeds £300,000.

- Bringing forward payments of bonuses or, if you are a company owner, dividends to the current tax year, when the maximum tax rate is 40% (32.5% for dividends).

- Closing interest-paying accounts shortly before 6 April 2010, so that interest is crystallised (and taxable) in 2009/10.

- Before 6 April 2010, realising any chargeable event gains on life policies that you intend to encash some time in the next couple of years.

Capital Gains Tax

The reform of capital gains tax (CGT), which took effect from 6 April 2008, now looks to have been somewhat academic, given the falls in investment values since then. With UK share prices still languishing at levels last seen in 2003, there are few gains around on which to pay 18% flat rate CGT.

This year the Chancellor has done the bare minimum to capital gains tax, increasing the annual exemption for individual investors by £500 to £10,100.

Planning Points

18% is better than 20%, 40% or 50%

Unless you are one of those lucky few who are able to benefit from the 10% savings rate band, 18% is the lowest tax rate that you will pay on your investment returns. It looks even better if you consider that in 2010/11, the highest rate of tax (on taxable incomes over £150,000) will be 50%.

Although the tax tail should never wag the investment dog, there is now a stronger case for favouring growth over income when setting your investment goals. There are many anti-avoidance rules which prevent income being transformed into capital gains, but it remains the case that some financial product structures provide income returns while others produce capital gains even though the underlying investments are the same. Selecting the right structure could therefore halve your tax bill.

Use your annual exemption

Would you waste a tax exemption worth up to £1,818 a year?

That is what your full annual capital gains tax exemption is worth in terms of tax saving. As far as possible it is important to use the exemption each year (and for your spouse/partner to do the same) because, if unused, it cannot be carried forward.

If you do not systematically use your annual exemption, you are more likely to reach a point where some of your gains are subject to tax, especially now taper relief has disappeared. Unfortunately you cannot simply crystallise a gain by selling and then repurchasing an investment - so called bed-and-breakfasting. However, there are other ways of achieving similar results:

- *Bed-and-ISA* You can sell an investment, eg shares in an open-ended investment company, and buy it back immediately within an ISA. For 2009/10 the maximum ISA investment is currently £7,200, but the limit will rise to £10,200 from 6 October 2009 if you were born before 6 April 1960.

- *Bed-and-SIPP* This is a similar process to bed-and-ISA, but the cash realised is used to make a contribution to a self-invested personal pension (SIPP). The reinvestment is then made within the SIPP. This approach has the added benefit of income tax relief on the contribution and may also offer a higher reinvestment ceiling than an ISA, depending on your earned income and other pension contributions. However, if you have income of £150,000 or over, the new rules on pension tax relief must be borne in mind (see below).

- *Bed-and spouse* You can sell an investment and your spouse can buy the same investment without falling foul of the rules against bed-and-breakfasting. However, you cannot sell your investment to your spouse – the two transactions must be separate.

Keeping down your CGT bill

There is a variety of tactics that can be used to limit your exposure to capital gains tax, including:

- Maximise the use of ISAs, where there is no capital gains tax. Do not forget that from 6 April 2008, all existing PEPs became stocks and shares ISAs.

- Use funds of funds rather than individual fund holdings. Fund changes made *within* a fund of funds do not create any immediate gain for the investor. This is one of the reasons why private client portfolio managers have increasingly adopted fund of funds instead of individual portfolios.

- Share your gains. Transfers between spouses living together are on a no gain/no loss basis, so if your spouse has not fully used their annual capital gains tax exemption and you have, together you could save tax.

- Take advantage of venture capital trusts (VCTs) and enterprise investment schemes (EISs). These are high risk investments, but they are generally free of capital gains tax.

Replace 40% CGT with 18% CGT

If you paid CGT at a rate of more than 18% on gains made in 2006/07 or 2007/08, you could consider using an EIS investment now to claw back the tax you have paid and bring the gains into the 18% tax world.

An investment in an EIS allows you to claim reinvestment relief for any capital gain (*before* taper relief) that you have made in the previous three years. This allows you to reclaim any tax you have paid on the gain or defer tax that is due. When you sell the EIS shares, the gain you have reinvested is crystallised and becomes chargeable, but at *current* tax rates. So you might be able to turn a former 40% tax liability into an immediate tax repayment and an 18% deferred tax liability. The maximum amount of EIS investment that qualifies for income tax relief is £500,000 in 2009/10, but there is no limit to investment where the claim is only for CGT reinvestment relief.

Mind your losses

In current market conditions, the rules on the treatment of capital losses are arguably more important than those which apply to capital gains. These contain a trap which could mean your losses are wasted if you realise losses and gains in the same tax year. The example below highlights the situation.

A Wasted Loss?

In December 2008 Jill finally decided to sell her RBS shares, having watched their value evaporate over the previous year. What had originally cost her £10,000 was eventually worth just £1,000 – a £9,000 loss.

Three months later, in late March 2009, Jill had thoughts about selling another long-term shareholding (in Astra Zeneca), which would realise a profit of £5,000.

- If Jill had sold her Astra Zeneca shares before 6 April 2009, the RBS loss would have been set against the gain, leaving £4,000 of loss to be carried forward to 2009/10 and beyond.
- If Jill had sold her Astra Zeneca shares on or after 6 April 2009, ie in the 2009/10 tax year, the calculation would be rather different. The RBS loss would now be a carried forward loss. Such losses are only used *after* the annual exemption is exhausted. So in 2009/10 the Astra Zeneca gain would be set against Jill's annual exemption. If Jill does not make further gains of over £5,100 in 2009/10, she will then be able to carry forward the whole £9,000 RBS loss to future tax years.

Inheritance Tax

Inheritance tax has dropped out of the headlines in recent times. The introduction of the transferable nil rate band in October 2007 took some of the political sting out of the tax. Falling house prices – the Halifax index for March 2009 is now down 21.2% from its August 2007 peak – have also helped lower the tax's profile.

The nil rate band has increased to £325,000 in 2009/10, a move that was legislated for in 2006 by Gordon Brown.

The Chancellor announced that the availability of agricultural property relief and woodlands relief would be extended to agricultural property and woodlands situated in the European Economic Area. This change is effective from 22 April 2009, and earlier in certain circumstances.

Planning Points

Time to review your estate planning

The introduction of the transferable nil rate band 18 months ago has made inheritance tax planning considerably simpler for many married couples. It is now no longer necessary to ensure that your nil rate band is used on first death to minimise IHT liabilities. This reform can result in significantly reduced IHT bills for widows (and widowers), even if their spouse died many years ago.

Not everybody has benefited from the reform. If you had already planned (and had the resources) to use the nil rate band on first death, you are no better off as the result of the introduction of transferability. If you are not married, you cannot benefit, other than as a widow/widower.

If you have not reviewed your estate planning and Wills in response to nil rate band transferability, you should do so now. It may be that no change needs to be made to your existing arrangements but, as ever with estate planning, it is better to be safe than sorry. Even though a revised plan may not reduce your IHT bill, it could simplify estate administration by, for example, removing the need to include a complex trust in your Will.

Regular and out of income

There are three yearly exemptions which are available for IHT planning:

- *The £3,000 annual exemption.* Any unused part of this exemption can be carried forward one tax year, but it must then be used *after* the £3,000 exemption for that year. So, for example, if you made a gift of £1,000 covered by the annual exemption in 2008/09, you can makes gifts totalling £5,000 covered by the annual exemption in 2009/10.

- *The £250 small gifts exemption.* You can make as many outright gifts of up to £250 per tax year as you wish free of IHT, provided that the recipient does not also receive any part of your £3,000 annual exemption.

- *The normal expenditure exemption.* Any gift that you make is exempt from IHT if:

    - it forms part of your normal expenditure; and

    - taking one year with another it is made out of income; and

    - it leaves you with sufficient income to maintain your usual standard of living.

The normal expenditure exemption is often forgotten. You may be making regular gifts which you think are covered by the £3,000 exemption, but which could actually count under normal expenditure, leaving your £3,000 exemption unused. For example, if you pay premiums for a life policy held under trust, such payments frequently satisfy all the conditions to be treated as normal expenditure, leaving the £3,000 exemption available for other gifts.

Turn low values to your advantage

The value of most investments today is substantially lower than twelve months ago. For instance the FTSE 100 index closed on Budget Day at 4018.2. At the start of April 2008 it was 5702.1.

There is one way to turn depressed investment values to your advantage, and that is by making lifetime gifts of some of those investments now. This has three main advantages:

- The value of the gift will be based on the depressed value, so any potential IHT liability is correspondingly reduced.

- While the gift will usually count as a disposal for capital gains tax purposes, the gain will be that much less (if any).

- Any subsequent growth in value of the investment is outside of your estate and, at worst, subject to 18% capital gains tax, rather than 40% IHT as part of your estate.

Footnote The same logic suggests that if you think investments will recover, now is the time to place fresh investments into trust for your children and grandchildren.

Investments

The Chancellor announced a number of changes on investment taxation, most of which had been subject to widespread consultation.

Individual Savings Accounts (ISAs)

The most important change on the investment front was the revision of the ISA limits, which had been hinted at by the Prime Minister in March. However, the proposed revision is not as straightforward as it might be:

- Until 5 October 2009, the 2009/10 ISA investment limit is £7,200, of which £3,600 may be invested in the cash component.

- From 6 October 2009, the 2009/10 limit will rise to £10,200 (of which £5,100 may be in cash), but you can only take advantage of this if you are aged 50 or over by the end of the tax year (ie. born before 6 April 1960).

- From 6 April 2010, the start of the new tax year, the age 50 restriction will disappear and the new higher limits will apply for all eligible investors.

Given that the original ISA investment ceiling was £7,000 in April 1999, the new limit is higher than it would have been if it had been adjusted each year in line with inflation (which would have made it about £9,300).

Overseas dividends

Last year's Budget made changes to the treatment of overseas dividends received by individuals. This briefly opened up a loophole which would have allowed investors to earn interest free of basic rate tax. However, the Treasury spotted their error – after the press had highlighted it – and inserted an appropriate anti-avoidance clause into the Finance Bill 2008. In 2009, the Chancellor revisited the issue.

From 22 April 2009, individual shareholders with 10% or more shareholdings in a non-UK resident company will generally receive the same treatment as investors with smaller holdings, i.e. dividends from the foreign company will be deemed to be accompanied by a non-payable 10% tax credit. The foreign company must be resident in a country which has a double taxation agreement with the UK, with a non-discrimination article

Offshore funds

This Budget has made a sensible change to the treatment of offshore fund distributions which its predecessor attempted, but failed, to do.

For income payments from offshore funds made to individuals on or after 22 April 2009:

- If the fund is an equity fund, then the distribution will be accompanied by a 10% non-payable tax credit. If you are a basic rate taxpayer, you will therefore have no further tax liability. If you are a higher rate taxpayer, your additional tax liability will be 25% of the dividend you receive.

- If the fund is not an equity fund, the distribution is classed as an interest payment with no attached tax credit. A fund in not an equity fund if it holds more than 60% of its assets in interest bearing securities, cash deposits and similar investments.

Before these changes, all distributions from offshore funds were treated as dividends, but with no attaching tax credit. The reforms therefore *reduce* the amount of tax you will have to pay on equity fund dividends, but increase tax payable on non-equity fund income. The overall effect is to bring tax on offshore fund income payment largely into line with that of their onshore counterparts. If you are looking for income, the Chancellor's reworking of the 2008 Budget reform makes high yielding offshore equity funds, including exchange traded funds, more attractive.

UK authorised funds

UK authorised investment funds will be able to opt to become tax elected funds (TEFs) from 1 September 2009, if they satisfy certain conditions. A TEF will have to divide its income distributions to investors into two parts:

- A dividend, covering UK dividend payments received by the fund, which will be accompanied by the usual 10% non-payable tax credit; and

- A non-dividend distribution which represents all other income and is taxable as interest. For individual investors this will be paid with 20% reclaimable tax deducted.

The reform will make little difference to taxpaying investors, but will make certain types of fund, such as funds which hold equities and bonds or funds invested in foreign equities, more attractive if you are a non-taxpayer or investing via ISAs or pension arrangements.

Venture Capital Trusts and Enterprise Investment Schemes

The 2006 and 2007 Budgets were both bad news for venture capital trusts (VCTs) and Enterprise Investment Schemes (EISs), as they placed tighter constraints on the companies eligible for investment and, for VCTs, reduced the level of tax relief. The net result has been that new VCT investments fell from £780m in 2005/06 to £230m in 2007/08 and probably to even less in 2008/09. At a time when the issue of financing business is high on the political agenda, there were hopes that the Chancellor would do something to boost the attraction of EISs and VCTs.

In the event, there were a number of minor technical changes, but no increase in the rates of tax relief. For the EIS the Budget revised the backdating rules so that it is now also possible to backdate the whole of an EIS investment into the previous tax year for income tax purposes. Previously only up to half of the investment (with a cap of £50,000) could be backdated. The requirement that any backdated investment must be made by 5 October in the tax year has also been removed.

Planning Points

ISAs

Since 6 April 2008 it has been possible to transfer the cash component of an ISA, including anything from a former TESSA, into the stocks and shares component. When this option was first announced, it was widely viewed as a rather pointless facility, as for most investors the value of the income tax saving from the cash component was greater than any tax savings offered by the stocks and shares component.

However, the world has changed since this switch facility first became available. Back then, base rate was 5.25%, so that interest on the cash component of an ISA could be a meaningful amount. With base rate now just 0.5%, many existing cash ISAs are paying 1% or less.

If you are looking for income from your ISA, a switch from cash to the stocks and shares component now has much more appeal. For example, an investment in a corporate bond fund could produce 6% or more tax-free income. The quid pro quo for the immediate extra income is that you lose the capital security of the cash ISA and your new higher income will not rise if base rates climb and could fall. Before making the switch – which is irreversible – you should always take independent advice.

Offshore funds

The changes to offshore fund taxation have largely removed the income tax advantage of holding offshore rather than onshore fixed interest funds, but given a new tax advantage to offshore equity funds. In some instances it may now be preferable to hold overseas equities via offshore rather than onshore funds.

If you have funds which invest in overseas equities or offshore fixed interest funds, you should review your holdings in the light of these tax changes.

Business Tax

There were no major changes to corporation tax that took effect from 1 April 2009. The mainstream rate of corporation tax will remain at 28% for the next financial year, while the small companies' rate is set to rise to 22% in 2010. However, there were useful temporary changes to business tax.

Trading losses

The Budget increased the timeframe of the PBR proposals to extend the carry back of losses for companies and unincorporated businesses. A trade loss may now be carried back for a period of three years, rather than just to the immediately preceding year. Only a maximum of £50,000 may be carried back beyond the immediately preceding year, and then only when profits for that year have been offset in full. These rules apply for company accounting periods ending between 24 November 2008 and 23 November 2010 and for tax years 2008/09 and 2009/10 for unincorporated businesses.

Capital allowances

There were two important revisions to capital allowances:

- *Cars:* A new capital allowance structure based on CO_2 emission levels now applies for cars. For newly acquired cars with emissions of more than 110 g/km up to 160 g/km, there is a 20% writing down allowance, with no cash ceiling. For higher emission cars, the writing down rate is 10%. Cars with emissions of 110g/km or less qualify for 100% first year allowances.

  As a consequence, the special rules that restrict the amount of car lease rental payments that can be deducted for tax purposes have been changed. The restriction is now a flat rate disallowance of 15% of relevant payments and this only applies to cars with CO_2 emissions exceeding 160g/km.

- *New first-year allowance:* There is a temporary first-year allowance of 40% for most investment in plant and machinery for one year only from 1 April 2009 for companies and 6 April 2009 for unincorporated businesses. This allowance will apply where investment exceeds the £50,000 100% annual investment allowance and represents a doubling of the standard 20% writing down allowance.

Income-shifting

The controversial subject of 'income-shifting' received a brief mention, with a reminder that the government is keeping the matter 'under review'.

Planning Points

Dividends or Salary... or Pension Contribution?

Still Worth It

Brian has £50,000 of gross profits in his company which he wishes to draw, either as bonus or dividend. Assuming the company pays corporation tax at the 2009 small companies' rate of 21% and Brian is already a higher rate taxpayer, with annual earnings in excess of £43,875, his choice can be summarised thus:

	Bonus **£**	**Dividend** **£**
Marginal gross profit	50,000	50,000
Corporation tax @ 21%	N/A	(10,500)
Dividend	N/A	39,500
Employer's National Insurance contributions (NICs) £44,326 @ 12.8%	(5,674)	N/A
Gross bonus	44,326	N/A
Brian's NICs £44,326 @ 1%	(443)	N/A
Income tax	(17,730)	(9,875)*
Net benefit to Brian	**26,153**	**29,625**

** after allowing for 10% tax credit*

The benefit of the dividend route is due to the savings in NICs; more tax (corporation tax and income tax) is payable under the dividend route.

The changes to the NICs and the new higher rate threshold have altered slightly the mathematics of the choice between dividends and salary. Nevertheless, if you are in a position to choose between the two and not caught by the IR35 personal company rules, a dividend remains the more efficient choice, as the example below shows.

A point worth noting is that the 50% tax rate and phasing out of personal allowances, both due from 2010/11, suggest that you might want to bring forward dividend payments into this tax year where the necessary funds are available.

Watch your Capital Allowances

The introduction of a 100% annual investment allowance for the first £50,000 of new investment in plant and machinery from April 2008 and the temporary 40% first-year allowance for one year from April 2009 have made the timing of such investment more important for businesses. From April 2010 anything in excess of £50,000 will generally attract only a 20% writing down allowance, so the timing of a major investment needs to be considered carefully.

Past experience of high first year allowances suggests there is a trap to be wary of: investing purely for the tax relief. When 100% allowances were universally available in the 1970s, there were many stories of businesses which bought new equipment that was not needed, simply to save tax. Some of the more apocryphal stories tell of farmers with barns full of combine harvesters gathering dust.

Today's lower limits and much-reduced corporation tax rates should mean unnecessary investments will be rarer. However, as with any investment, tax is a factor, but should not be the driving consideration.

Pensions

The focus for new pension legislation in the last few years has been the development of personal accounts and the reform of state pensions. The simplified tax regime introduced from 6 April 2006 had been bedding down quietly, with minor adjustments regularly made in each Finance Act.

However, the relative peace in the land of pension tax has now been completely shattered. The first rumblings were heard in the 2008 Pre-Budget Report. This contained an announcement of a freezing of the lifetime allowance and the annual allowance at their 2010/11 levels for the following five years. Most experts had been expecting inflation-plus-a-little rises.

The Budget proper brought the earthquake of restrictions to higher rate income tax relief for contributions. In the week before the Budget there had been assorted leaks that something would happen to higher rate relief, but nobody predicted anything as complex as what finally arrived.

The Chancellor plans to restrict the value of tax relief on *all* pension contributions (including those made by employers) from 2011/12 for those with income of £150,000 or more. This will be achieved by tapering relief down from that income threshold to 20% for those with income over £180,000. Thus nobody will be able to obtain pension contribution tax relief at the new 50% tax rate from 2011/12.

The 2011/12 starting date is justified by 'the importance of consulting on this measure'. However, the Chancellor has found no need to consult on a raft of complex 'anti-forestalling' measures, designed to limit the opportunity to make large pension contributions before 2011/12. These measures, which will last for just two years, will only affect you if:

- Your **'relevant income'** is £150,000 or over in the current tax year or either of the two preceding tax years;
  and
- You increase your **'normal regular ongoing pension savings'**
  and
- Your **'total pension savings'** during a tax year exceed £20,000 (the special annual allowance).

'Relevant income' is defined as your total income less normal deductions and reliefs (eg trading losses) and Gift Aid, but with any deduction for pension contributions limited to a maximum of £20,000.

‘Normal regular ongoing contributions’ to a pension arrangement are:

For money purchase schemes, such as personal pensions

- The total annual amount of your contributions to the arrangement, provided that the contributions were made at least quarterly before 22 April 2009;
  plus
- Any increase in your regular contribution that was agreed before 22 April 2009.

  For an individual pension arrangement, such as a personal pension, a ‘normal regular ongoing contribution’ must be made to the existing (pre-22 April 2009) arrangement. If you keep the total level of your total regular contributions the same, but pay them to different arrangements, then such contributions are not ‘normal regular ongoing contributions’.

For defined benefit arrangements i.e. final salary pension schemes

- All your pension savings (which are measured by reference to the change in value of your accrued benefits from one tax year’s end to the next). This is subject to the proviso that the way your benefits are calculated under the scheme rules does not change on or after 22 April 2009, except in certain limited circumstances.

The money purchase scheme requirement that contributions are made quarterly or more frequently means that no account is taken of annual payments or one-off lump sums, even though this is the typical method of paying contributions by high earners.

‘Total pension savings’ are all of your pension savings (from whatever source) that receive UK tax relief, including employer contributions. The pension savings value placed on your benefit accrual under a final salary scheme is 10 times the increase in pension plus any increase in a separate cash lump sum. For example, an extra £5,000 pension accrual is deemed to be £50,000 of pension savings.

If you are caught by the ‘anti-forestalling’ rules, then:

- You will receive full tax relief on your ‘normal regular ongoing contributions’;
  but
- Any *additional* pension contributions (from whatever source) or the value of any *additional* benefit accrual will effectively be restricted to basic rate to the extent that your ‘total pension savings’ exceed £20,000 in the tax year.

Relief is restricted by the application of a special annual allowance charge (at 20% in 2009/10) to the additional contribution. This will be collected via your self assessment return.

HMRC recognises that these new rules may result in pension contributions being made inadvertently. The Finance Bill therefore will include legislation that allows individual (not employer) non-regular contributions to personal pensions and AVC arrangements that attract a special annual allowance charge to be refunded, subject to scheme consent. The refund, which can only be made after the end of the tax year to which it relates, will be subject to a 40% deduction made by the scheme. As a result, any special annual allowance charge already declared on a tax return would have to be amended.

The forestalling rules include a crop of anti-avoidance measures, some of which are very broadly defined. Any 'scheme' to exchange salary for pension contribution is likely to be ineffective.

The Special Annual Allowance Charge in Practice

High income, no special annual allowance charge
Ann has gross income of £158,000 in 2009/10 and made an individual pension contribution of £10,000, to which her employer added another £15,000. Her gross income in earlier years was under £150,000. Although her gross income exceeds the £150,000 threshold in 2009/10, her 'relevant income' is under £150,000 after deduction of her £10,000 pension contribution, so Ann is not subject to the special annual allowance tax charge.

High income, special annual allowance charge
David has 'relevant income' of £170,000 in 2009/10 and has a self-invested personal pension to which total pension contributions of £50,000 were made by himself and his employer. The contributions were David's regular monthly contribution of £2,000 (as in previous years) and a single employer payment of £26,000. David's income exceeds the £150,000 threshold and his 'total pension savings' are more than the £20,000 special annual allowance. His 'normal regular ongoing contributions' of £24,000 are not subject to the special annual allowance charge. However, the additional employer contribution of £26,000 will be subject to a special annual allowance tax charge of £5,200 (£26,000 x 20%). David will pay this via his 2009/10 self assessment tax return on 31 January 2011.

High income, special annual allowance charge
Eric has 'relevant income' of £250,000 in 2009/10, of which only £22,000 is earned income. He has a personal pension to which he has regularly contributed £500 a month. In 2009/10 he makes an additional contribution to the plan of £16,000. Eric's income exceeds the £150,000 threshold and his 'total pension savings' are more than the £20,000 special annual allowance. His 'normal regular ongoing contributions' of £6,000 are not subject to the special annual allowance charge. However, the additional single contribution brings his 'total pension savings' up to £22,000 and £2,000 of this (£16,000 + £6,000 - £20,000) will be subject to a special annual allowance tax charge of £400 (£2,000 x 20%). If Eric had limited his additional contribution to £14,000 he would have avoided the tax charge.

Two Years in One

For 2009/10, the annual allowance is £245,000. This is often interpreted to mean that the maximum that can be placed in your pension plans during the tax year is £245,000. However, such a statement is an oversimplification of the rules. The general principles are:

- There is no limit on how much your employer can contribute. However, pension contributions have to be justified as allowable business expenses if they are to be tax relievable for the employer and their tax relief may be spread when their total pension contributions are £500,000 or more.
- If you make gross personal contributions which total more than 100% of your relevant UK earnings (or £3,600, if greater), the excess will not be eligible for income tax relief.
- If your total income is more than £150,000, you may be caught by the new 'anti-forestalling' rules which limit higher rate tax relief.
- If the total contribution input to all your pension arrangements during a tax year exceeds the annual allowance, the excess is subject to a 40% annual allowance charge. This can only be avoided by drawing all benefits from the relevant pension arrangements in the same year or, more drastically, death.

The calculation of contribution input is not straightforward. What matters are the contributions made during each pension arrangement's 'pension input period' ending in the tax year. For example, if you have two pension schemes, one with a pension input period ending on 30 June and another with a pension input period ending on 31 December, were your employer to make contributions to both in August 2009:

- for the first plan the contribution will count towards the £255,000 annual allowance for 2010/11 i.e. for the input period ending 30 June 2010
- for the second plan this will count towards the £245,000 annual allowance for 2009/10 i.e. for the input period ending 31 December 2009.

This complexity means that by manipulating pension input periods, if you are not caught by the 'anti-forestalling' rules it is possible for contributions of up to £500,000 to be made in 2009/10 without falling foul of the annual allowance charge or special annual allowance charge.

Beating the Special Annual Allowance Charge

The new special annual allowance charge can never apply if your 'relevant income' (see above) for the current and two preceding tax years is under £150,000. If your relevant income is below the £150,000 threshold for 2007/08 and 2008/09, then it could pay you to keep your 'relevant income' down in this tax year (and the next) if you want to make substantial pension contributions. Stay below the £150,000 threshold and there is no risk of losing higher rate tax relief.

There are a number of ways you can limit your 'relevant income', for example:

- Transferring income-generating assets to your spouse. Such transfers would be beneficial, even if you both pay higher rate tax.
- Restructuring investments to produce less taxable income.
- Making Gift Aid contributions.
- If you are self-employed, taking advantage of the £50,000 annual investment allowance to buy plant and machinery, possibly bringing forward planned investments from later years.

APPENDIX – TAX FACTS AND FIGURES AND NICs

MAIN INCOME TAX ALLOWANCES AND RELIEFS

	2008/09	2009/10
	£	**£**
Personal allowance – standard	6,035	6,475
- Age 65 – 74	9,030	9,490
- Age 75 and over	9,180	9,640
Married couple's allowance – minimum amount*	2,540	2,670
- Age 65 – 74□	6,535	N/A
- Age 75 and over*	6,625	6,965
Age-related allowances reduced if total income exceeds ¶	21,800	22,900
Maintenance to former spouse □	2,540	2,670
Employment termination lump sum limit	30,000	30,000

* Relief at 10%. Minimum amount applies for age allowance purposes only.

□ Relief available at 10% only if at least one of the couple was born before 6 April 1935.

¶ For 2009/10 the reduction is £1 for every £2 additional income over £22,900 [£21,800 for 2008/09]. Standard allowance(s) **only** are available if total income exceeds:

	2008/09	2009/10
	£	**£**
Taxpayer aged 65 - 74 [personal allowance]	27,790	28,930
Taxpayer aged 65 - 74 [married couple's allowance]	35,780	N/A
Taxpayer aged 75 and over [personal allowance]	28,090	29,230
Taxpayer aged 75 and over [married couple's allowance]	36,260	37,820

INCOME TAX RATES

	2008/09	2009/10
	£	**£**
Starting rate on savings income- 10%	1 – 2,320	1 – 2,440
Basic rate	20%	20%
Tax on first £[34,800/37,400]†	6,960	7,480
Higher rate - 40%	Over 34,800	Over 37,400
Discretionary and accumulation trusts (except	40%	40%

dividends) *		
Discretionary and accumulation trusts (dividends) *	32.5%	32.5%
Ordinary rate on dividends	10%	10%
Upper rate on dividends	32.5%	32.5%

* Up to the first £1,000 of gross income is generally taxed at the standard rate, i.e. 10%, or 20% as appropriate.

† Assumes 10% band not available. £7,236 (£6,728 in 2008/09) if full 10% band is available.

CAR BENEFITS

The charge is based on a percentage of the car's "price". "Price" for this purpose is

1. The list price at the time the car was first registered plus the price of extras.

2. Where the "price" exceeds £80,000, the "price" used is restricted to £80,000.

For cars first registered after 31 December 1997 the charge, based on the car's "price", is graduated according to the level of the car's approved CO_2 emissions.

For petrol cars with an approved CO_2 emission figure.

CO_2 g/km	% of price subject to tax	CO_2 g/km	% of price subject to tax	CO_2 g/km	% of price subject to tax
	08-10		**08-10**		**08-10**
120 or less	10	170-4	22	210-4	30
121-139	15	175-9	23	215-9	31
140-4	16	180-4	24	220-4	32
145-9	17	185-9	25	225-9	33
150-4	18	190-4	26	230-4	34
155-9	19	195-9	27	235-9	35
160-4	20	200-4	28	240+	35
165-9	21	205-9	29		

Notes

1. The exact CO_2 emissions figure should be rounded down to the nearest 5 g/km for levels of 125g/km or more.
2. For diesels not meeting Euro IV emissions standards or registered after 31 December 2005, add 3%, subject to maximum charge of 35%.
3. Hybrid petrol/electric cars are subject to a 3% reduction, with a minimum 10% charge.

4. LPG, dual LPG/petrol and (for 2008/09 only) E85 cars are subject to a 2% reduction, with a minimum 10% charge. Reduction does not apply to LPG conversions.
5. For electric only cars, a 9% charge applies.

For cars with no approved CO_2 emissions figure, the charge is based on engine size.

Engine Size (cc)	Percentage of car's price charged to tax
0 – 1,400	15
1,401 – 2,000	25
2,001 and more	35

CAR FUEL BENEFITS

For cars with an approved CO_2 emission figure, the benefit is based on a flat amount of £16,900 (£16,900 2008/09). To calculate the amount of the benefit the percentage figure in the above car benefits table (that is from 10% to 35%) is multiplied by £16,900. The percentage figures allow for a diesel fuel surcharge. For example, in 2009/10 a petrol car emitting 165 g/km would give rise to a fuel benefit of 21% of £16,900 = £3,549.

VALUE ADDED TAX

From	1 April 2008	1 Dec 2008	1 May 2009	1 Jan 2010
Standard rate	17.5%	15.0%	15.0%	17.5%
Reduced rate (eg domestic fuel)	5.0%	5.0%	5.0%	5.0%
Annual turnover limit for registration	£67,000	£67,000	£68,000	£68,000
Deregistration threshold	£65,000	£65,000	£66,000	£66,000
Flat rate scheme turnover limit	£150,000	£150,000	£150,000	£150,000
Cash accounting and annual accounting limits	£1,350,000	£1,350,000	£1,350,000	£1,350,000

INHERITANCE TAX

	Cumulative chargeable transfers [gross]			% tax rate on death	% tax rate in lifetime*
	2008/09	**2009/10**	**2010/11**		
	£	**£**	**£**		
Nil rate band†	312,000	325,000	350,000	0	0
Excess	No Limit	No Limit	No Limit	40	20

* Chargeable lifetime transfers only
† On the death of a surviving spouse on or after 9 October2007, their legal personal representatives may claim up to 100% of any unused proportion of the nil rate band of the first spouse to die (regardless of their date of death).

CAPITAL GAINS TAX

Main exemptions and reliefs

	2008/09 **£**	**2008/09** **£**
Annual exemption	9,600*	10,100*
Principal private residence exemption	No Limit	No Limit
Chattels exemption	£6,000	£6,000
Entrepreneurs' relief	$^{4}/_{9}$ths of business gain Lifetime limit £1,000,000	$^{4}/_{9}$ths of business gain Lifetime limit £1,000,000

* Reduced by at least 50% for most trusts.

Rates of tax

Individuals: 18% [2008/09 - 18%]
Trusts and personal representatives: 18% [2008/09 - 18%]

CORPORATION TAX

	Year Ending 31 March	
	2009	**2010**
Main Rate	28%	28%
Small Companies' Rate	21%	21%
Small Companies' Limit	£300,000	£300,000
Upper Marginal Level	£1,500,000	£1,500,000
Effective Marginal Rate	29.75%	29.75%

TAX PRIVILEGED INVESTMENTS [MAXIMUM INVESTMENT]

	2008/09 £	**2009/10 £**
ISA		
Overall per tax year: Born after 5 April 1960 Born before 6 April 1960	7,200 7,200	7,200 10,200†
Cash component Born after 5 April 1960 Born before 6 April 1960	3,600 3,600	3,600 5,100†
Stocks and shares component Born after 5 April 1960 Born before 6 April 1960	Balance up to £7,200 Balance up to £7,200	Balance up to £7,200 Balance up to £10,200†
Maximum in cash for 16 and 17 year olds	3,600	3,600
ENTERPRISE INVESTMENT SCHEME (20% income tax relief)	500,000*	500,000*
Maximum carry back to previous tax year for income tax relief	Lesser of 50% of investment and £50,000 made before 6 October 2008	£500,000

VENTURE CAPITAL TRUST (30% income tax relief)	200,000	200,000

* No limit for CGT reinvestment relief.

† Only £7,200 (£3,600 cash component) may be invested before 6 October 2009

PENSION

	2008/09	2009/10	2010/11
Lifetime allowance*	£1,650,000	£1,750,000	£1,800,000
Lifetime allowance charge: Excess drawn as cash Excess drawn as income	 55% of excess 25% of excess		
Annual allowance	£235,000	£245,000	£255,000
Annual allowance charge	40% of excess		
Special annual allowance	N/A	£20,000	£20,000
Special annual allowance charge	N/A	20%	30%+
Lifetime allowance charge: Excess drawn as cash Excess drawn as income	 55% of excess 25% of excess		
Max. relievable personal contribution	100% relevant UK earnings *or* £3,600 if greater		

* May be increased under transitional protection provisions

\+ To be confirmed

WORKING AND CHILD TAX CREDITS

The main features of the tax credits are:

1. Child tax credit

- Eligibility is assessed on household income.
- The claimant must be responsible for one or more children aged 16 or under, or at least one child under age 20 and in full-time non-advanced education.
- The family element of the tax credit is £545 per annum and is doubled in the first year of a child’s life.
- The child element is £2,235 per annum for each child.
- The disabled child element is £2,670 per annum (where relevant).

- HMRC will pay the CTC to the main carer for the child.

2. Working tax credit

- The claimant, or one of the joint claimants, must be in qualifying remunerative work.

- The amount of WTC will be based on circumstances which are primarily the number of hours worked and the income of the claimant (or joint income for a couple).

- The age and working hours conditions are not straightforward. Generally, the minimum weekly working requirement will be:

  a) 16 hours for families with children and workers with a disability. The claimant can be aged 16 or over.

  b) 30 hours for workers with no children and no disability. The claimant has to be aged 25 or over.

- The basic element of the tax credit is £1,890 per annum.

- The couple or lone parent element is £1,860 per annum.

- A 30 hour element of £775 per annum is payable where the claimant or one of the claimants works at least 30 hours a week (couples with children may aggregate their hours for this purpose).

- A disabled worker element of £2,530 per annum or more is available where the claimant, or his or her partner, has a disability.

- There is 50-plus element and a childcare element, worth 80% of care costs, subject to an eligible maximum of £300.

- For employees, payment will normally be made by their employer with their wages (except the childcare element which is paid direct to the main carer). For the self-employed, payment is made directly by HMRC.

3. Calculating the credits

It is necessary first to total the various elements available to arrive at the maximum available amount of tax credits before any reduction on account of income. All elements can be reduced at the rate of 39% (ie 39p per £1 of income), except the family element of CTC which is reduced at a rate of 6.67%.

NATIONAL INSURANCE CONTRIBUTIONS FOR TAX YEAR

Definitions

Lower Earnings Limit (LEL)	the minimum level of earnings at which an employee will qualify for a State Second Pension (S2P). This is also the lower level of earnings which will be used in determining any NI Rebate. For tax year 2009/10 the Lower Earnings Limit is £95 per week.
Upper Accrual Point (UAP)	the upper level of earnings on which an employee's S2P entitlement is based (or on which any NI Rebate is determined). For tax year 2009/10 and subsequent years the Upper Accrual Point is fixed at £770 per week.
Upper Earnings Limit (UEL)	the upper level of earnings on which full NICs are charged. The reduced 1% NI contributions will apply to earnings above this level. For tax year 2009/10 the Upper Earnings Limit is £844 per week.
NI Rebate	the Rebate of employer's and employee's National Insurance contributions that is available where an employee is contracted out of S2P. This is based on the employee's earnings between the Lower Earnings Limit (LEL) and Upper Accrual Point (UAP). The Rebate will vary depending on the type of pensions vehicle used to contract out of S2P. Where this is a final salary occupational scheme this will be 3.7% (employer) and 1.6% (employee) in respect of the employee's earnings between the LEL and UAP. Where this is a money purchase occupational scheme or contracted out money purchase stakeholder pension scheme the Rebate will be 1.4% (employer) and 1.6% (employee) in respect of the employee's earnings between the LEL and UAP. The aggregate Rebate will be determined on an age related basis (varying from 3.0% to 7.4%) and any further Rebate due (ie over and above the amounts mentioned earlier in this paragraph) will be paid by the HMRC NICO to the scheme after the end of the tax year. Where this is a personal pension or stakeholder scheme National Insurance contributions will be paid at the

contracted in rate and the Rebate, which will be determined on an age related basis, will be paid directly to the member's personal pension by the HMRC NICO after the end of the tax year to which it relates.

The Rebates will also vary in accordance with an individual's earnings, in each of the following bands:

Band	Age related Rebate
1 (£4,940 - £13,900)	9.4% - 14.8%
2 (£13,901 - £31,800)	2.35% - 3.7%
3 (£31,801 - £40,040)	4.7% - 7.4%

Primary Threshold

the level of earnings at which employees start to pay Class 1 National Insurance contributions.

For tax year 2009/10 this is £110 per week.

Secondary Threshold

the level of an employee's earnings at which the employer starts to pay Class 1 National Insurance contributions.

For tax year 2009/10 this is £110 per week.

Employees - Class 1

Contracted in

Nil on first £110 per week (i.e. up to Primary Threshold)
11% of £110.01 per week to £844 per week.

1% on earnings above £844 per week.

Contracted out via occupational scheme

Nil on first £110 per week (i.e. up to Primary Threshold)
9.4% of £110.01 per week to £770 per week

11% of £770.01 per week to £844 per week.

1% on earnings above £844 per week.

The employee's NI Rebate is still payable in respect of the employee's earnings between the LEL and UAP including those in excess of the LEL and up to and including the Primary Threshold. In the first instance, the Rebate reduces the National Insurance contributions payable by the employee. However, where the National Insurance contribution payable by

	the employee is reduced to nil, the excess Rebate will be available for the employer to set against his overall National Insurance contribution bill.
Married Women and Widows Reduced Rate	4.85% of £110.01 to £844 per week.
	1% on earnings above £844 per week.

Employer - Class 1 Contributions

Weekly Earnings	Contracted In	Contracted Out	
		COSR	COMP**
	%	%	%
On first £110	Nil	Nil	Nil
£110.01-£770	12.8	9.1	11.4
Over £770	12.8	12.8	12.8

Although the reduced level of National Insurance contributions only applies to the employee's earnings in the band between the Secondary Threshold (£110 per week) and the UAP (£770 per week), the NI Rebate is still available in respect of the employee's earnings between the LEL and UAP, including those earnings between the LEL (£95 per week) and the Secondary Threshold (£110 per week). Employers are able to reduce their overall National Insurance contributions liability to reflect the Rebate applicable to the employer's contributions on the employee's earnings between £95 per week and £110 per week.

** Where a COMP (Contracted Out Money Purchase Occupational Scheme) is involved the Rebate is determined on an age related basis and any additional Rebate due over and above that shown above will be payable by HMRC NICO to the scheme after the end of the tax year. This will also apply to a Contracted Out Money Purchase Stakeholder Pension Scheme (COMPSHP).

COSR is a Contracted Out Salary Related Occupational Scheme.

Self-Employed

Class 2 (lower profits limit)	£2.40 per week flat rate. (applicable where profits are less than £5,075 per annum)
Class 4	8% of profits between £5,715 p.a. and £43,875 p.a.
	1% on profits above £43,875 p.a.

Voluntary Contributions

Class 3	£12.05 per week

Past performance should not be used as a guide to the future

Do not act on this information alone!

If you would like to discuss any point in more detail, please contact:

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