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Budget 2009 *Proposals that affect financial planning*

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Introduction

The Chancellor's Budget proposals have been well publicised in various forms since he gave his Budget speech. However, based on past experience we have found that our clients and others have welcomed our summary of the proposals that will have a particular impact on financial planning.

This summary also includes comments where appropriate which we hope you will find helpful.

Some of these proposals will no doubt change before they are enacted. However, it is important that financial plans are reviewed in the light of the likely changes detailed here.

ISAs

The ISA limit for those who reach age 50 before 6 April 2010 will increase to £10,200 from 6 October 2009, of which up to half (£5,100) can be invested in a Cash ISA. Prior to 6 October 2009 the limits for all ages remain at £7,200 overall of which up to £3,600 can be in a Cash ISA.

These new limits will apply to everyone from 6 April 2010.

Comment: This increase is certainly welcome as savers and investors need all the encouragement they can get at present. However, the total that can be invested each year into an ISA is still lower than the combination of annual PEP and TESSA tax-free allowances that the ISA replaced. The cost of administering this two stage increase will also be enormous for the industry.

The benefits of building up ISA holdings are not just the avoidance of capital gains tax and income tax on the interest payments and dividends (in the case of higher rate tax payers). The benefits extend to not needing to declare the ISAs on your tax return and the income from ISAs not counting towards the income limit before Age Allowance is reduced.

Pension Contributions

From April 2011, tax relief on pension contributions will be restricted for those with incomes of £150,000 and over, and tapered down until it is 20 per cent.

Those earning up to £150,000 will continue to receive full tax relief. Those earning over £180,000 will be entitled only to basic rate tax relief (currently 20%). Those earning between £150,000 and £180,000 will be entitled to a rate between the basic and higher rates.

This change is not being implemented until April 2011 to allow adequate time for the Government to consult the industry on this.

To prevent very high earners from making substantial contributions before April 2011, there will be a ‘special annual allowance’ of £20,000 for those who have earned over £150,000 in the current tax year or either of the two preceding ones.

In broad terms:

- if there is any single contribution or increase to a regular contribution and the total paid in during the tax year is over £20,000, tax relief is available as normal, but there will be a 20% tax charge on the excess over £20,000; but

- current regular contribution levels of over £20,000 in the tax year will be eligible for tax relief as normal without any special tax charges, but any increase or single contribution will attract the 20% charge.

Those who have never earned in excess of £150,000 a year are unaffected, as are those who continue with their monthly contributions. Contributions that were made before the Budget (22 April) are unaffected. The normal annual allowance (£245,000 in 2009/10) also applies.

Comment: Although this will not affect large numbers of our clients, it is a pity that the Government continues to reduce the benefits of pension funding at a time when it is trying to place the responsibility for pensions firmly on the shoulders of the individual.

This will also do nothing to stop the widening pensions gap between those who work for the Government (central and local) and receive final salary pension benefits, and those who work in the private sector and are reliant upon very much poorer money purchase pension arrangements.

Salary sacrifice will become even more attractive for high earners. It will continue to save National Insurance for both the employer and the employee, but it will also make sense to reduce salaries below £150,000 or, if possible £100,000.

State Pension

The Basic State Pension for the current year is £95.25 per week for a single person and £152.30 per week for a married couple.

Comment: Whilst this is a welcome addition for those with employer or private pensions, everyone will want to try and avoid relying on this as their only source of income.

Pensions Credit

As previously announced, the guaranteed minimum income for pensioners under the Pension Credit has increased to £130 a week of single people and £198.45 a week for couples.

In addition the amount of capital disregarded for Pension Credit, and also for Housing and Council Tax Benefit for pensioners, is increased from £6,000 to £10,000.

Child Trust Fund

From the current tax year, the Government will contribute £100 a year to the Child Trust Fund of children who receive Disability Living Allowance.

For severely disabled children, this will be doubled to £200. These amounts won't count towards the normal £1,200 a year contribution limit for CTF.

Offshore Bonds

The Finance Act will include measures to make it clear that where there is a loss on an offshore life assurance policy this can't be used as the basis of a claim for income tax loss relief.

Venture Capital Trusts

The current requirement is that 80% of the money raised from a share issue must be employed within a year, and the remainder within two years.

This will be simplified so that 100% must be employed within two years. This change will also apply to Enterprise Investment Schemes (EIS).

Comment: High earners will now need to consider replacing part of their pension contributions with an investment into VCTs which still attract 30% income tax relief and pay dividends tax-free.

Investment Trusts

There is to be a new tax framework for investment trusts which will enable tax efficient investment in interest bearing assets such as bonds.

Comment: This looks to be good news for the investment trust industry which has suffered greatly of late through large increases in discounts, particularly as Corporate Bonds are very popular with investors at present.

Income Tax

From April 2010 the highest rate of Income Tax will rise to 50% and it will apply to taxable income over £150,000 a year.

In addition, from April 2010 personal allowances will be reduced by £1 for every £2 of 'adjusted net income' over £100,000. Adjusted net income is net income less gross contributions to pensions and gross gift aid payments. This is a similar device to the way that Age Allowance is reduced where income is above a certain level at present.

The tax rate on dividends for those with taxable income over £150,000 will be 42.5%.

Comment: Most high earners would feel that a 50% top rate of tax for incomes above £150,000 was fair. There is a double whammy here, however, in the reduction in personal allowances at the same time.

The new tax rates of 50% and 42.5% will also apply to trusts making it even more important that trustees use the most tax efficient investments for the trusts in their care.

Gift Aid

For the next three tax years charities will be able to claim Gift Aid tax repayments at a rate of 22%, rather than 20%.

This means that every £1 donated is increased by about 28p.

National Insurance Contributions

From April 2011, grandparents and other family members will be able to gain National Insurance credits toward the basic State Pension for caring for young children.

Comment: This could particularly help women in their 50s who often lose out on pension provision.

Inheritance Tax (IHT)

There have been no changes to IHT except that the nil rate band for the current tax year has been confirmed as £325,000, which is slightly more than expected based on statutory indexation.

As previously announced, the nil rate band will increase to £350,000 in 2010/11.

Capital Gains Tax (CGT)

The CGT annual exemption will be increased in line with statutory indexation to £10,100 for the current tax year.

The equivalent amount for trusts will continue to be half of this amount, ie £5,050.

Stamp Duty Land Tax (residential property)

The increase in the stamp duty threshold from £125,000 to £175,000 will be extended to the end of the year.

Other stamp duty rates are 1% up to £250,000, 3% up to £500,000 and 4% for properties over £500,000.

These Budget notes are intended as a guide only. The information given is based on our understanding of the Chancellor's proposals. Whilst we believe our interpretation of the proposals to be correct, we cannot be responsible for the effects of any future legislation or any change in interpretation or treatment.

You should not make changes to your financial planning on the strength of these Budget notes but talk through your personal situation with an independent financial adviser such as ourselves.

Please note that this information does not constitute personal advice and should not be treated as a substitute for specific advice based on your circumstances.

For personal advice

If you would like to discuss any aspect of your investments or financial planning please ask your usual Arch adviser or contact us via one of the following:

Tel: **0845 3700 661**
or **01483 204600** (if local)
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