



Saffery Champness
CHARTERED ACCOUNTANTS



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CLIENT**



September 2009

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We have a new Finance Act, and this edition looks at some important aspects of the Act and its implementation. We first cover the changes to income tax relief on pension contributions, providing an overview and using examples to show how pensions saving has become potentially unattractive in certain circumstances - and how some categories of taxpayer may be disproportionately worse off as a result.

Finance Act 2009 also introduced changes regarding the taxation of furnished holiday lets, with some beneficial tax treatment being abolished on the one hand, but some new potential opportunities also arising on the other in the short term. This edition provides a snapshot. Our third article on Finance Act 2009 assesses the UK's future tax landscape in the wake of the recent changes to income tax. Among other things, we note that, to an extent, important increases to National Insurance contributions have been obscured by the headlines.

This edition also contains a look at the details of HMRC's New Disclosure Opportunity and in our 'News in Brief' section we touch on some issues worth noting for employers who provide their staff with living accommodation. We also bring you news of a recent award that we were delighted to win, as well as a reminder of the services available through our global network, Nexia International.

Tim Gregory



Not such a relief to have a pension?

01

One of the most publicised measures introduced in the 2009 Finance Act was the restriction on tax relief on pension contributions made by wealthier individuals.

Whilst the policy behind the change seems to be to concentrate the UK's resources on the less affluent, those who are affected by the change will need to revisit long-term planning because the longstanding and accepted pension principle that tax relief is granted on contributions in exchange for accepting taxation on annuity payments in retirement has simply been abandoned.

The complexity of various aspects of the new rules is such that it will be very difficult for a taxpayer to know if he or she is caught by additional tax charges or restrictions to relief unless he or she takes professional advice.

Worse still there is considerable unfairness in the new system – it is possible with only a little thought to construct a situation where the marginal tax rate that an individual will suffer on his or her income is well in excess of 100% (see example 1 overleaf).

For many high earners, it will now simply be uneconomic to make further pension contributions, since the post-tax return will be less than if they had invested directly. Such individuals would be advised to cease making pension contributions altogether (see example 2).

What follows is a general commentary on the new rules, although we believe that the post-April 2011 rules may well be amended prior to implementation.

The measures

From 6 April 2011 where a person earns £180,000 or more in a tax year, then he or she will receive only 20% tax relief on his or her pension contributions.

Where the individual earns £150,000 or less then they will still receive full tax relief on their pension contributions. This is currently 40%, and there is some uncertainty as to whether this will increase to 50% on 6 April 2010 when the additional rate of income tax is introduced – with the pension tax relief rules as currently drafted a 50% taxpayer would only receive 40% tax relief for his or her contributions but HM Revenue & Customs have indicated that this may not have been their intention.

Where the individual earns between £150,000 and £180,000 tax relief will be tapered so that some amount between basic and higher rate relief is given.

The legislation will not only have to deal with the “tapering” provisions in a fair manner, but will also have to address the complex issue of whether and if so how superannuation and defined benefit schemes should also



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be subject to restrictions (likely to be an emotive issue with civil service pensions being a superannuation scheme), as well as to consider the impact of employer contributions.

“Anti forestalling measures”

Since the introduction of the new rules is delayed until April 2011, taxpayers might seek to make large pension contributions in 2009/10 and 2010/11 and gain what the Government clearly considers to be an unfair advantage.

To combat this, temporary “anti forestalling” legislation was introduced in the 2009 Finance Act.

Very broadly, the new rules apply where an individual:

- has income in excess of £150,000 in the tax year in question, or had

done so in the last three years; and

- contributes more than £20,000 (£30,000 in some limited circumstances) to a pension scheme in that period.

If both of these criteria are met then a tax charge of 20% will be levied on the excess over £20,000 (or £30,000) via self assessment.

The definition of “income” for these purposes is not straightforward, and includes certain salary sacrifice arrangements as well as unearned income, although some deductions such as charitable gifts are allowed.

Where regular contributions have been made at least quarterly under an arrangement that was in place prior

to the budget, and these continue to be made, these will be exempt from the anti forestalling tax charge, as “protected pension inputs.” Less regular contributions above £20,000 (or £30,000) will suffer the charge.

This is one of the more unfortunate aspects of the new legislation and will disproportionately affect entrepreneurs rather than employees, since a business owner would tend to make pension contributions only once or maybe twice a year, after a year’s profits have been determined, and not at all when the business’s performance is less strong.

Such contributions could now give rise to tax charges if made in 2009/10 or 2010/11.

Example 1

Mr A earns £150,000 and pays £80,000 of those earnings into a pension scheme, receiving tax relief of £32,000.

In the same tax year, Mr A later receives a bonus of £30,000, taking his earnings to £180,000. This bonus is taxed at 51.5% (the new higher rates of income tax and NIC), meaning tax of £15,450. But the tax relief on his pension contribution is

now restricted to 20%, meaning that his tax relief falls by £16,000.

The total tax cost to the individual of receiving the bonus is £31,450, a marginal tax rate of 105%.

Example 2

Mrs B is aged 60, intends to retire at 65 and will take her pension at that date. She earns in excess of £180,000 per year, and it is anticipated that she will remain a higher rate taxpayer after retirement.

If she makes a pension contribution of £100,000 this will be worth £125,000 once the 20% tax relief has been given. This will roll up tax free at say 5% per year for five years, becoming around £160,000 on retirement.

£40,000 will be withdrawn as a tax free lump sum, and the remainder will be taxed at 40% when paid as an annuity – tax of £48,000 will be payable on the total fund, and so the after-tax value of her pension will be £112,000.

If she instead keeps the funds in bonds or another liquid investment paying the same 5% per year, this will be taxed at 50%, leaving an after-tax return of 2.5%. After the same five years, if she reinvests her net income, her investment will be worth £113,000.

Mrs B would therefore be better off keeping her money outside of a pension in this case.

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There are also complex rules for defined benefit pension schemes, which require an actuarial valuation to be performed of the value of the benefits available to the taxpayer each year, and tax is in some cases applied to any increase in this value.

It may even be necessary to wait until the last possible day before committing to pension contributions, in case earnings or other income that cannot be determined until very close to 5 April might send you over the limits. We can advise on this, along with any other annual tax planning.

Conclusion

Now, more than ever, careful thought is necessary prior to any material pension contribution or alteration of existing pension arrangements.



Furnished holiday lets: *tax issues and opportunities*

Changes brought in by the 2009 Finance Act to the taxation of Furnished Holiday Lettings (FHLs) create a number of opportunities and issues for anyone with qualifying holiday accommodation, whether in the UK or the EEA.

Furnished Holiday Lettings have for a number of years attracted a very favourable tax treatment. The income is treated not as rental income, but as trading income.

This means that the expenses of running the property and any associated capital allowances can be set-off against other personal income to reduce an individual's tax liability. In addition FHL properties attract favourable capital gains tax rates and reliefs upon sale or other disposal.

Most of the beneficial aspects of this tax treatment will be abolished from 6 April 2010 but, in the meantime, the FHL rules are being extended to include qualifying properties not just in the UK, but anywhere within the European Economic Area (EEA, being the 27 EU Member States plus Iceland, Liechtenstein and Norway).

This extension has retrospective effect, so that amended tax returns for the years 08/09 and 07/08, and potentially earlier years, can be submitted to treat any income and expenses from qualifying properties within the EEA under the same terms that have previously benefited UK properties.

This may result in a worthwhile tax refund for some people, especially where a property that now qualified has since been sold. The treatment can also be applied for the current tax year.

In order for a property to qualify as an FHL, a number of conditions need

to be met: the property must be available to let as furnished holiday accommodation for a minimum of 140 days per year, and must actually be so let at commercial rates for at least 70 days.

In addition, the property must not normally be let to the same person for more than 31 days throughout a period of 7 months in each year.

This still means that there is a significant proportion of the year during which the owner (or anyone else) can use it for their own private, longer-term use without losing the property's 'FHL' status.

The changes in the rules not only create a potential tax refund for past years in respect of EEA properties, but also present a window of opportunity for the immediate future in respect of properties both in the EEA and the UK.

This should encourage owners of furnished holiday accommodation to consider very carefully their future intentions with regard to their properties.

If they are holding the property with the intention of future resale then the removal of the significant capital gains tax (CGT) savings may encourage some to look to sell the property in this current tax year to benefit from the advantageous tax treatment whilst they can.

It is unlikely that the current depressed state of the property market in most countries would encourage a new decision to sell, but if the intention exists in any case, then an adjustment to the timetable could save a significant amount of tax.

On the other hand, if the property is being held as a long-term 'family' asset and the current owner's intention is to pass it on to their children then the removal of the FHL rules means that the property will no longer qualify for CGT holdover relief after 5 April 2010.

It may well be worth considering gifting the property to a younger family member before the end of the current tax year, even if this was not something that was intended for another few years.

Although there has also recently been a tightening up on the rules that allow holiday accommodation to qualify for Business Property Relief from Inheritance Tax (distinct from the FHL rules), there is no indication as yet that this relief might also be in danger of being withdrawn.

Until the pips *squeak*?

The proposed 50% tax rate for 2010/11 and beyond will now be well-known to our readers, but the headlines often hide the detail. The effect of the various recently-announced tax changes will be much more costly, and will affect many more people, than it might first appear.

Boosting the higher tax rate, and then boosting it a little more

Those who are fortunate enough to have income of £150,000 or more will have the new additional rate of tax to contend with. For 2010/11 onwards 50% will be levied on income, other than dividend income, above £150,000.

For dividend income otherwise taxable at the new 50% rate, the rate will be 42.5%. This means that dividend income above the threshold which is currently taxed at an effective rate of 25% after the notional tax credit will be taxed at an effective rate of just

over 36%. This is an increase of more than 44% in the effective tax rate on dividends.

For trustees, the impact is even worse, since they will have to pay the 50% tax rate (42.5% on dividends) on virtually all trust income. Whilst this is mitigated where a beneficiary can reclaim tax in relation to distributions made, retained funds in trusts will suffer a huge additional tax burden.

The personal allowance – now you see it...

From 6 April 2010 the full personal allowance will be restricted for those with income of more than £100,000, by £1 for every £2 that the income exceeds £100,000.

This means that an individual with income of £112,950 or more (based on the 2009/10 personal allowance) will not receive any personal allowance in 2010/11. The consequence of this is income between £100,000 and £112,950 will be taxed at a marginal rate of 60% in 2010/11.

Not just the rich

The future tax landscape has been portrayed by many parts of the media as an attack on the wealthy, and the two changes above can certainly be seen as that. However, the changes to National Insurance contributions (NICs) have been underplayed by both the media and the Government, but these will hit everyone, from the highest to the lowest of earners.

It is proposed that from 6 April 2011, the main rates of Class 1 and Class 4 NICs will be increased by 0.5% to 11.5% and 8.5% respectively. The additional rate (payable on income over the Upper Earnings Limit, £43,875 for 2009/10) will also increase from 1% to 1.5%.



The Class 1 employer rate of NICs will be increased by 0.5 per cent to 13.3% and this increased rate will also apply to Class 1A and Class 1B contributions on benefits in kind and PAYE settlement agreements.

A half of one percent may not sound very much, but for those struggling on a low income, any reduction in their take home pay will clearly have an impact.

Perhaps more crucially, the extra half percent on employers at a time when it seems likely the economy will still be struggling could have serious implications for reducing unemployment levels.

In addition to the proposed increase in rates, the Upper Earnings Limit for NICs has already been amended. For 2009/10 the point at which an employed higher earner starts to pay 1% Class 1 NICs as opposed to 11%

Class 1 NICs was aligned with the level at which people started to pay higher rate income tax.

This means that a higher rate taxpayer will pay £383.50 more in Class 1 NICs in 2009/10 than they would have done in 2008/09. For people who pay Class 4 NI, the increase is £268.45.

These amounts are the same for any higher rate taxpayer, regardless of how much more than the threshold their income is, and so clearly have a greater impact for those with incomes nearer the bottom end of the scale.

It is clear that the UK Government has a big financial hole to fill, and is seeking to do so in any way it can. However, it is interesting that the Treasury itself has forecast that most people will find a way in due course to reduce the impact on them of the new 50% income tax rate.

Saffery Champness named *'Accountancy Firm of the Year'*

We are pleased to be able to let you know that Saffery Champness has recently been named 'Accountancy Firm of the Year' at the Citywealth Magic Circle Awards 2009.

Other shortlisted firms in this award category were Deloitte, Dixon Wilson, Ernst & Young, Moore Stephens, PricewaterhouseCoopers, Rawlinson & Hunter and Rees Pollock.

Citywealth is a specialist publisher, providing analysis and articles of interest from global experts in the wealth management sector and leading private client intermediaries. Its Magic Circle Awards are designed to highlight those individuals and organisations that have 'raised the bar' in terms of service, innovation and client care in the areas of trust, private client and private wealth management.

Shortlisted firms were drawn from nominations from peers in the trusts and private wealth industry, with submissions from shortlisted firms

then being scrutinised by a judging panel of industry experts. The panel was comprised of representatives from the fields of investment management, law and the media.

We are obviously delighted to have won this award, having been shortlisted against some highly-regarded accountancy firms. For our firm, it is the second award we have won in recent months, with our specialist Corporate Finance team having been named this summer as 'UK Corporate Finance Adviser of the year' by ACQ Finance Magazine.

News in brief:

two comments on employee housing

The EU's Working Time Directive

Recent reports in the professional and wider press have suggested that employers who provide living accommodation to their employees may find it more difficult to do so without tax being charged on the employee, as a result of EU Working Time Directive implications. We would caution that these reports seem to over-play the position.

Clients who provide living accommodation to employees will be aware that the exemption from tax for their employees on the taxable benefit provided by the accommodation depends on the accommodation being either necessary or customary.

The EU Working Time Directive (WTD) was introduced on 6 April 2000. Together with subsequent case law, it instructs that where employees have to be on call, hours spent "on call" at the place of employment must be paid for, and count towards the maximum hours the employee may work, except for periods when they are asleep.

This position has apparently often led to employers tending to use external on call services rather than requiring the resident employee to be on call. According to the recent press reports, this has, in turn, led to HM Revenue & Customs (HMRC) increasingly taking the view that the use of these services removes the need for provision of living accommodation, and so the tax exemption falls away, causing the benefit to become taxable on the employee.

However, where living accommodation is provided to employees, it would seem to be very unlikely that on call time would need to be spent at the place of

employment, since the point of the accommodation provision is that it is close by.

Accordingly, it seems unlikely that much on call time would need to be paid for. Similarly, since it remains the case, at least for the time being, that an employee can opt out of the maximum hours aspect of the WTD, this aspect can also become irrelevant.

Some arrangements were being made that involved up front payments for a short lease (a lease premium), with subsequent payment of a very small rent. This led to the taxable benefit on the employee being minimised.

Finance Act 2009 introduced a new rule whereby if a lease premium is paid for a lease of 10 years or less, the lease premium will be treated as if



Living accommodation: an update

This year's Finance Act made a small change to the rules on living accommodation, seeking to prevent avoidance of tax by payment of a lease premium by the employer.

Where the accommodation provided is rented by the employer, the taxable benefit on the employee could not exceed the rent paid by the employer.

it is rent paid. The taxable amount in any tax year will, therefore, be treated as the amount of lease premiums, spread over the duration of the lease, plus any rent paid by the person at whose cost the accommodation is provided, less any amount paid by the employee. Properties that are let by the employer mainly for business use (e.g. a factory with a small caretaker's flat) will be exempt from this rule.

Anything to *declare*?

HM Revenue & Customs (HMRC) has recently released the details of the New Disclosure Opportunity (NDO), announced in the 2009 Budget. This follows a previous similar opportunity in 2007.

Anyone with undeclared income or gains that should have been charged to UK tax should be aware that HMRC have stated that this will be the last opportunity to come forward, and failure to do so will result in much higher tax penalties (which can be up to 100% of the tax due), and criminal prosecution in the worst cases.

In 2007, HMRC obtained details of 400,000 individuals and businesses which held overseas bank accounts with one of five UK high street banks.

These taxpayers were written to and invited to take advantage of a disclosure amnesty with reduced penalties for any unpaid taxes. Around 45,000 disclosures were made, this figure including both those written to by HMRC and those simply attempting to take advantage of the lower penalty rates.

On 12 August 2009, HMRC successfully gained an order for over 300 other banks with a UK presence to provide similar information in relation to their customers with offshore accounts, and no doubt will be writing to the 500,000 further individuals and businesses who are reportedly the subject of this new information.

HMRC are rolling out a programme of formal and informal investigations for those who did not respond to the initial amnesty, with penalties for undeclared income and gains reported as being around 35% on average.

The NDO is intended to relate to all other undisclosed tax liabilities from

offshore activities, but also provides a "last chance" for anyone who slipped through the net the first time round. It relates to undeclared income and gains of up to the last 20 years.

The NDO involves two steps:

1. Notification of the intention to disclose must be made to HMRC between 1 September (or 1 October if electronically) and 30 November 2009;
2. Actual disclosure, together with payment of tax, must then be made from 1 September (1 October if electronically) and 31 January 2010 (12 March if electronically).

A penalty rate of 10% will apply to those who were not written to by HMRC as part of the previous tax amnesty in 2007.

Those to whom HMRC did write in 2007 but who did not take advantage of the initial amnesty and now decide to disclose will have an opportunity to do so with unpaid tax attracting a penalty of 20%, assuming an enquiry is not already underway.



With a 31 January 2010 deadline for written submissions, this will of course coincide with the normal filing deadline for tax returns, when personal tax departments tend to be extremely busy anyway.

Our experience with the previous HMRC amnesty was that the more complex disclosures were better made by letter rather than simply on the official forms provided, in order to ensure that a client's case was put in the manner most beneficial to them.

On this basis, it will be necessary to begin work as early as possible given the very high demand at this time of the year and so we would recommend coming forward sooner rather than later.

The NDO should not be confused with a further amnesty specifically for those with bank accounts in Liechtenstein, which was announced at around the same time as the NDO. The Liechtenstein Disclosure Facility (LDF) will cap penalties on unpaid tax at 10% of tax evaded over the past ten years, provided the taxpayer provides full disclosure of his or her financial dealings.

The LDF will run from 1 September 2009 to 31 March 2015 and will relate to unpaid tax liabilities of the last 10 years.

It arose from a new Tax Information Exchange Agreement (TIEA) between the UK and Liechtenstein which provides for the exchange of information, and HMRC has warned that there are arrangements for Liechtenstein accounts to be closed down if account-holders do not make the disclosures.

Where taxpayers have a choice of whether to use the NDO or the LDF, the much longer duration of the LDF, and its scope of only 10 years' liabilities, as opposed to up to 20, will likely be the most significant factors.

Saffery Champness has several partners and staff who specialise in tax investigations and the work required to make an NDO disclosure.



Nexia International: *worldwide advice*

In spite of the worldwide recession, globalisation continues within businesses, within families, and within and across tax regimes. Getting the right tax and other business and financial advice around the world has never been more important.

With offices in almost 100 countries around the world, Nexia International is currently the 10th largest network in the world. Its member firms have representation in 520 offices worldwide, and the organisation is one of the most flexible of similar independent 'mid-tier' global networks.

Our membership of Nexia International means that whenever the interests of our clients acquire an international dimension, we are able to put them in touch with appropriate tax and business advisers to provide the local expertise that may be needed to progress their plans, whilst we continue to work with both the clients and these additional advisers in relation to UK taxation or other applicable issues arising from their overseas activities.

Differences in regional taxation treatment, reporting, culture and other factors particular to that jurisdiction can potentially impede international mobility and, in such circumstances, access to reliable sources of professional knowledge can be invaluable.

Nexia International offers our clients a valuable resource that can help them "get things done" at reasonable cost and to timetable, whenever their plans acquire an international dimension.

Our firm also plays a highly visible role in the future development of the network, with partners of our firm serving on its International and European Boards of Directors, the International Tax Committee, and as Nexia's Deputy Chairman.

If you feel that this might be of use, please do ask your usual client partner for more information.

