NLP Financial Management

NLPFM News

News and views from NLP Financial Management

On the threshold of a higher tax world

As we slip, slide and shiver into 2010, the prospect of the new tax year with increased rates looms ever larger. Apart from the introduction of a 50% rate for those with incomes above £150,000, the removal of personal allowances for earnings above £100,000, effectively introduces a 60% tax rate. It is obviously therefore of prime importance to consider how your financial affairs should be arranged to minimise the impact of these changes.

Action prior to 5 April 2010

1. Those with annual income over £150,000 should consider closing any **deposit accounts** where annual interest would be paid *after* 5 April. Account closure would mean interest is paid within the current tax year and charged at the lower rate of 40% rather than the post April 6th rate of 50%. This assumes that accounts cannot be switched into a spouse's name and taxed at a lower rate. Please be aware of penalties for closing accounts.
2. Consider cashing in **investment bonds**, onshore or offshore so gains are taxed at rates of 20% (onshore) or 40% (offshore) rather than encashing such bonds in the new tax year where rates would potentially rise to 30% (onshore), 50% (offshore). This again applies to those with income above £150,000. As one can still take 5% tax-deferred allowances from such bonds, careful planning is required here and again penalties on sales need to be considered.
3. Ensure you utilise your **capital gains tax allowances** as you can make capital gains of up to £10,100 in the current tax year with no tax liability. Utilising these allowances can effectively save capital gains tax of £3,600 for married couples.
4. Consider maximising **pension contributions**, although it should be noted that the level of contribution on which full higher rate tax relief can be obtained will depend on total earnings and income in the current tax year.
5. Maximise **ISA** contributions, noting individuals aged over 50 can now allocate £10,200 into an ISA in the current tax year. This new allowance will be available to everyone from 6 April 2010.
6. Consider other tax-efficient **investment schemes** such as venture capital trusts and enterprise investment schemes which provide income tax relief of 30% and 20% respectively on investments made, along with various other tax benefits.

continues

Inside this issue

continued from cover

Arranging financial affairs for the 2010/11 tax year

1. If you earn over £150,000 and your spouse does not, consider transferring all **income-producing assets** into their name. This could include cash deposits, shares or investment properties.
2. Consider the most tax-efficient way of **structuring investments**, noting that at present, gains are liable to capital gains tax at only 18% whilst income can be taxed at rates in excess of 50%. If in the past you have held investments such as equity funds through offshore bonds, it is now likely to be more efficient to hold them directly. In this case profits will be taxed as capital gains rather than income.
3. If you are going to be a 50% taxpayer, consider deferring any gift aid **charity donations** into the next tax year to maximise tax relief. Similarly, as a 50% taxpayer if you are not planning to make maximum **pension contributions** in both this and the next tax year, it may be beneficial to defer contributions to the next tax year.

As has been illustrated, there is much planning required over the next few months.

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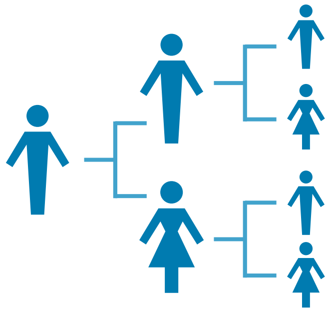
Voluntary Tax?



Financial commentators sometimes refer to inheritance tax as the *voluntary tax*. This is because individuals can potentially arrange their finances to at least significantly mitigate if not completely avoid it.

The 2009 Pre-Budget Report stated that the limit of the IHT nil-rate band for the tax year 2010/11 would be set at £325,000 – the same level as in 2009/10. Below are some of the ways you can reduce your potential IHT liability.

Firstly, it is important to be aware of capital gifts that can be made without incurring tax charges, even if death occurs within 7 years. Currently there is an annual gift-making exemption of £3,000 per individual. Additionally, if you did not take up your allowance from the previous tax year, you can gift up to £6,000. A married couple therefore could potentially make a gift of £12,000 if their previous tax year's allowance was unutilised and then gift a further £6,000 after 6 April 2010. This would effectively provide an inheritance tax saving of £7,200 on a total gift of £18,000.

Similarly, regular gifts made from surplus income immediately fall outside your estate for inheritance tax purposes. If your net income is £200,000 per annum with net expenditure of £150,000, you could make regular gifts of up to £50,000 per annum which would fall outside your estate.

Other capital gifts are generally treated as *potentially exempt transfers* and fall outside the estate, provided you live for 7 years from the gift date. Tax on such gifts also has the potential to fall after 3 years.

When considering gifting, it is probably most appropriate to opt for non-income producing assets such as second homes, although you do need to be careful about capital gains tax. However, as capital gains tax is currently relatively low at 18%, the attractiveness of this route is possibly greater at present than in the past.

Alternative ways of protecting an estate from inheritance tax include taking out an insurance policy to cover liability on death or holding assets that are IHT exempt. For example, investments held for two years in most Alternative Investment Market (AIM) listed shares, should qualify.

Finally, there are many insurance-based schemes which may also be appropriate as a way of mitigating against inheritance tax in appropriate circumstances

Approaching the end of the tax year, we are happy to talk to you about how these ideas can be introduced into your financial affairs so inheritance tax can indeed become a *voluntary tax* for you.

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Discretionary management

You may recall we wrote about our Discretionary Management Service (DMS) in last Winter's newsletter and I am pleased to report that this service has proved extremely popular with clients. Most of our clients have now switched at least some of their investments so they are managed in this way and feedback has been positive.

The DMS enables us to monitor investments on a regular basis and action switches in a quicker and more efficient way. Weekly meetings are conducted by the investment management team and any anomalies identified, for example where a client's spread of assets is not in line with our allocation model or where they are holding funds no longer on our investment panel. Action is then taken in the following week to ensure these anomalies are addressed.

It is easy to arrange income payments to clients if required. We can also ensure clients utilise their capital gains tax allowances each year through making appropriate investment sales.

For all the above reasons, we would recommend that the DMS is considered by all clients.

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Cash deposits

With interest rates currently at an all time low, investors are actively seeking advice on where to place cash deposits. We can hopefully point you in the right direction.

We view cash as an important asset class and normally allocate between 20% - 30% of a client's assets thus. As a consequence, it is important the returns are as competitive as possible.

When recommending cash accounts there are a number of factors we consider in addition to the rate on offer. These include the level of access required, future central bank rates, terms of any accounts and the financial strength of the deposit taker.

We update our research weekly and all our consultants are able to provide you with an up to date guide on rate availability. Whether you are a personal, trust, pension or corporate investor we aim to ensure that you access the best deals.

Whilst it is inevitable that interest rates will rise over the next few years, there is an expectation they may remain low in the short term. Accordingly, it is always a difficult judgement as to whether to seek higher rates by fixing funds for a number of years or leave them available on instant access or short notice. The latter means you can benefit from rising interest rates or indeed can possibly lock-in to higher interest rates over specific fixed terms simply by waiting a few months. The final decision must depend upon opportunities available and our advice is normally to spread risk by leaving some funds on instant access and fixing others over the short to medium term.

It is often harder to get competitive rates on corporate, pension and trust funds. However we do actively research the best rates for all types of investors and can advise you in all situations.

Finally, it may be appropriate to hold cash funds through offshore bonds where tax can be deferred, especially for personal investors. This can enable you to access a wide range of accounts from different institutions through one bond, with administration being relatively simple. We can manage such bonds for you on either a discretionary or advisory basis.

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Healthy savings

We are conscious that in the current economic environment, everybody is reviewing outgoings to ensure they receive the best value for money in all areas including their insurance arrangements.

As a specialist **Private Medical Insurance Broker**, our healthcare company, Get Private, is constantly researching the market to ensure clients receive the best value for money based on their particular circumstances.

Whether insuring an individual or a company, a discount can often be obtained with your current insurer or you can be moved on a **'like for like'** basis to an alternative insurer at a more favourable rate. If you do not have health insurance, suitable cover can be arranged at a cost to suit your budget. The service is non committal and no fee is charged as a commission is received from the Insurance Company.

Get Private can also arrange extremely competitive and comprehensive **Group Dental Insurance** for five or more members. For £12 per person per month, you will receive up to £2,000 per year towards routine check ups, hygienist costs, crowns, bridges, fillings and other maintenance costs. There is no waiting period and cover is effective immediately. You may use any dentist you wish and this is proving to be extremely popular amongst our clients.

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Please remember that past performance should not be seen as an indication of future performance. The value of investments and the income from them may go down as well as up and investors may not get back the amount they originally invested. Changes in rates of exchange may also cause the value of investments to go up or down. Tax information is based upon current legislation and this may change in the future. Not all the products and services mentioned in this Newsletter are regulated by the Financial Services Authority.

Pension update

In the Summer 2009 edition we outlined the anti-forestalling measures introduced by Chancellor Alistair Darling in the April 2009 Budget. Such is the fast paced world of British politics, that just 6 months later there were new amendments brought forward in the December 2009 Pre-Budget Report.

In simple terms, the result of the new regulations, effective on 9 December 2009, is to create a floor to the *Relevant Income* figure, reducing it from the previous £150,000 to £130,000. Individuals whose income, excluding employer funded pension benefits, is below this level, will escape the proposed restriction.

Relevant income is not the same as relevant UK earnings for pension contribution purposes. It includes pension income, interest on savings, dividends, rental and trust income and chargeable event gains on a life policy. Additionally it must be measured across the current and two previous tax years.

It predominantly affects those whose Relevant Income is £130,000 or more and who, on or after the above date, amend their normal pattern of regular pension contributions or accruals and breach their £20,000 (in some cases up to £30,000) per annum Special Annual Allowance.

It is possible to reduce Relevant Income and thereby be removed from the scope of the Regulations by making appropriate pension contributions (within limits) as well as charitable donations, which, so long as they attract Gift Aid, can be unlimited in size.

"In seeking to maximise the benefit from pension arrangements, do not overlook the Salary Exchange arrangement."

The anti-forestalling measures (in effect until April 2011, when legislation restricting higher rate relief for high earners takes over) are complex. There are likely to be nuances in the circumstances of each individual that will determine to what extent they are affected. If you are likely to fall into this category, you should speak with your NLPFM adviser prior to making (or accepting) additional contributions to your retirement schemes. Effective planning prior to 5 April 2010 could be critical in preserving your higher rate relief until 2011.

In seeking to maximise the benefit from pension arrangements, do not overlook the Salary Exchange arrangement. This is often considered too complicated to merit further consideration but this is not necessarily the case and it can prove a superb tool in helping to enhance pension benefits for employees at no additional cost. For the employee this is a very useful way of securing significantly greater pension contributions. Indeed in certain circumstances, an employee's pension contribution could be bolstered by over 30%, for no additional expense.

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