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INDEPENDENT FINANCIAL PLANNING
& INVESTMENT MANAGEMENT

BUDGET 2014: CONTENT AND CONSEQUENCES

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, the Treasury and the Office for Budgetary Responsibility. All Budget proposals may be subject to change before the relevant Finance Act is passed (which for the Finance Bill 2014 is expected to be in July).

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

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The Background

George Osborne's fifth Budget was, for most practical purposes, the last of this Parliament. While there will be another Spring Budget in 2015, it will contain no changes of any consequence because Parliament is currently due to be dissolved on 30 March. Thus the real 2015 Budget will be a post-election affair.

After last year's difficult Budget, set against the possibility of a triple dip recession, the 2014 Budget was much more upbeat, thanks to the surprisingly rapid bounce back in the UK economy. The Chancellor predictably made much of that turn around in his speech, although he was careful to stress plenty of work remained to be done. In part, this was Mr Osborne as political strategist, but there was also an element of hard financial truth. The recovery has done little so far for the UK government's borrowing numbers, which remain at disconcertingly high levels. The Office for Budget Responsibility (OBR) estimates that adjusted government borrowing for 2013/14 will come out at around £108 billion, down £7 billion from the previous year and close to £50 billion above the level originally forecast in

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2010. 2014/15 is forecast to produce a fall of £12.3 billion, but the OBR says it will still not be until 2016/17 that annual borrowing falls below £50 billion.

With total government debt of over £1,250 billion, the Chancellor was in no position to make any Budget giveaways. Instead what he did was announce a raft of small measures which in overall terms make virtually no difference to the public finances. In any case, with the Autumn Statement little more than three months distant, Mr Osborne had already revealed most of his hand for 2014/15 (and, if he wins the election, some way beyond).

Mr Osborne's future plans implied continuing austerity, although quite where this will bite is unclear. According to the Institute for Fiscal Studies (IFS), probably the leading think tank in budgetary matters, as at April 2014 the UK is a little under half way through the process of consolidating its finances. The good news is that the IFS believes "virtually all of the tightening from tax increases has already been implemented." However, the corollary is that on the IFS's calculation little more than a third of the planned cuts to day-to-day public services spending have been made and 58% of the cuts to benefits are in place. Historically it has been the tax increases that have been much easier to implement than expenditure reductions.

At least the economic backdrop against which the next set of spending cuts will occur is much more favourable. In the space of twelve months the performance of the UK economy has changed significantly:

- Unemployment has fallen from 7.8% to 7.2%, fast enough to destroy the Bank of England's projection of last Summer that 7% unemployment would not appear before about mid-2016.

- Inflation has fallen from 2.8% to 1.9%, measured on the government's favoured CPI basis. The fall below the official 2% target in January was the first such drop since November 2009. CPI inflation is now set to remain below 2% for the next two years, according to the latest Bank of England forecasts. That could mean that in 2014 earnings growth will finally overhaul price inflation as Mr Osborne predicted in his speech, albeit the margin is likely to be barely noticeable.

- Economic growth has moved from a post-Olympic -0.1% in the final quarter of 2012 (originally thought to be -0.3%) to +0.7% in the last quarter of 2013. Across the year as a whole, the UK economy is estimated to have grown by 1.9%. That still leaves UK plc over 1% smaller than at its peak six years ago. Last year's Budget included a 0.6% forecast for 2013 economic growth by the OBR. For 2014 the OBR is forecasting

2.7% growth, slightly lower than the market consensus but 1% below the latest Bank of England bullish estimate released last month.

The headline-grabbing moves announced (or, more commonly, re-announced) in the Budget included:

- A rise of £560 in the personal allowance to £10,000 for 2014/15 and a further increase to £10,500 in 2015/16.
- A £415 increase in the higher rate threshold for 2014/15, with another 1% rise due in 2015/16.
- The continued freezing of the personal age allowances and their date of birth triggers.
- The introduction of the £2,000 Employment Allowance from April 2014 to offset employer's Class 1 National Insurance contributions (NICs).
- The introduction on a phased basis from Autumn 2015 of a new tax-free childcare regime, worth up to £2,000 per child per year under age 12 by the end of the scheme's first year.
- An increase to £11,000 for the capital gains tax annual exemption in 2014/15, followed by another £100 rise in 2015/16.
- A doubling of the annual investment allowance to £500,000 and the extension for one year to 31 December 2015 of this higher level.
- Radical reforms to the way in which benefits can be drawn from pension arrangements, encouraging the use of alternatives to the traditional annuity.
- A reform of ISAs, with a new £15,000 contribution limit from July 2014.
- Further constraints on Venture Capital Trusts (VCTs) and Enterprise Investment Schemes (EISs).
- Yet another freezing of an impending fuel duty increase.

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 these strikes a chord, you are strongly recommended to consult your financial adviser.

PERSONAL INCOME TAX AND NATIONAL INSURANCE CONTRIBUTIONS

The income tax bands and allowances and National Insurance contributions (NICs) rates for 2014/15 were announced last December by the Treasury. The Budget contained no changes to these, so for the new tax year:

- The personal allowance has risen by £560 to £10,000. The allowance will continue to be phased out where total income exceeds £100,000. As a result, you will not receive a personal allowance if your total income in 2014/15 exceeds £120,000. For 2015/16 the Chancellor proposed that the allowance will rise by another £500, although this might not survive the general election.

- While there is a £560 increase in the personal allowance in 2014/15, the basic rate band once again contracts, but this year by just £145. Thus, if you are only entitled to a personal allowance, the starting point at which you pay higher rate tax rises by £415 to £41,865 – an overall and distinctly sub-inflation increase of 1%. Taking into account growing earnings and dividends, the net effect will be a further swelling in the number of higher rate taxpayers. HMRC's latest statistics suggest that in 2013/14 nearly one in six income tax payers were taxed at the higher rate. In 2015/16 the higher rate threshold is scheduled to rise again by another 1% - £420 – election permitting.

- As part of the process to phase out personal age allowances, these have again been frozen, but a year has been added to the minimum age: the allowances are now banded at 67-76 (£10,500) and 77 and above (£10,660). Nevertheless, the income threshold at which allowances start to be reduced was raised in line with RPI inflation, as was the married couple's age allowance (which now only applies to those couples where at least one partner is 80 or more in 2014/15).

- For 2014/15 the starting rate (10%) tax band, only accessible to a few, rose by 3.2%, again in line with RPI inflation. In 2015/16 the starting rate will be reduced to 0% and the band widened to £5,000. The Treasury estimates about 1.5 million people will *potentially* benefit, although half will see benefits of no more than £50 a year.

- The starting points for the additional rate and the phasing out of personal allowances were unchanged: the legislation which introduced these had no automatic indexation provision.

- The basic rate of tax remains at 20% (10% for dividends). The additional rate remains 45% (37.5% for dividends), although this again will be election-contingent for 2015/16.

- There are no major changes to NIC rates this year, but the bands have been adjusted in line with inflation:
    - If you are an employee or self-employed, the starting point at which you begin to pay Class 1 or Class 4 NICs has risen by £4 a week, to £153 a week (£7,956 a year). The upper earnings and upper profits limits, beyond which the NIC rate falls to 2%, will rise to £41,865, in line with the raised starting point for 40% tax.
        - For employers the corresponding starting threshold for NICs has risen by £5 a week, to £153 a week. This means both the employer's and employee's NIC thresholds are the same at last.
        - The lower earnings limit, a trigger for many benefit entitlements, has increased by £2 a week to £111 a week.
- In 2014/15, business and charity employers will benefit from the new Employment Allowance, which covers up to the first £2,000 of employer's Class 1 NICs in a year. In practice this amounts to the NICs chargeable in respect of one employee earning about £22,450 a year. The allowance will not apply to employment connected with family or household affairs, so there is no NIC relief for nannies or au pairs.

Allowing for the tax and NIC changes, most people in employment will be £136 a year better off in 2014/15, as illustrated in the table below, because of the increased personal allowance and higher NICs starting point. Those with incomes of £119,770 and above will be worse off, but their maximum loss will be £47.

Earnings	**2013/14**		**2014/15**		**Overall Change***
£	**Income Tax £**	**NICs £**	**Income Tax £**	**NICs £**	**£**
10,000	112	269	0	245	+136
15,000	1,112	869	1,000	845	+136
20,000	2,112	1,469	2,000	1,445	+136
25,000	3,112	2,069	3,000	2,045	+136
30,000	4,112	2,669	4,000	2,645	+136
40,000	6,112	3,869	6,000	3,845	+136
50,000	9,822	4,214	9,627	4,232	+177
75,000	19,822	4,714	19,627	4,732	+177
100,000	29,822	5,214	29,627	5,232	+177
125,000	43,598	5,714	43,627	5,732	- 47
150,000	53,598	6,214	53,627	6,232	- 47
175,000	64,848	6,714	64,877	6,732	- 47
200,000	76,098	7,214	76,127	7,232	- 47
250,000	98,598	8,214	98,627	8,232	- 47

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

Tax credits

Some elements of working tax credits (WTCs) rise by around 2.8% for 2014/15, in line with the CPI to September 2013, while many others, such as the basic element, rise by 1%. The family element is again frozen.

The tax credit system is due to be replaced by Universal Credit (UC) over the coming years. However, the system has not got off to a good start and, as at October 2013 only 2,720 were being paid UC. While UC was meant to be fully implemented by the end of 2017, the DWP accepts that this is not now achievable and there must be a question mark over whether the next government – of whatever hue(s) – will abandon the idea. A post-election review is inevitable.

Child Benefit

In 2014/15 the benefit is worth £20.50 (up 20p) a week for the first child and £13.55 (up 15p) a week for each additional child. 2014/15 will be the second tax year in which the High Income Child Benefit Charge (HICBC) applies throughout the year, with an effective 1% reduction in benefit for each £100 of income over £50,000. Thus, at £60,000 or more, the tax and the benefit cancel each other out. If you are in that position, HMRC would prefer you to elect not to receive Child Benefit, rather than have one part of government pay the benefit and another collect it back as tax. However, latest reports suggest over 300,000 in this position did not stop Child Benefit in 2013/14. Estimates suggest that up to 100,000 of those abstainers should have completed a self-assessment tax return by the end of January, but failed to do so.

Company Cars

The company car benefit scales are subject to another set of changes in the new tax year. The (theoretical) 5% rate for cars with CO_2 emissions of 75g/km or less stays, but above that level the rates have all been increased by 1%. This means an 11% charge applies to cars with 76g/km-94g/km CO_2 emissions, rising thereafter by 1% for each additional 5g/km. The 3% addition remains for diesels, subject to an overall maximum rate of 35%. The same percentages apply for car fuel benefits. In his speech the Chancellor announced more (revenue-raising) changes for future years.

PLANNING POINTS

Turning child benefit tax to your advantage

If either of you or your partner/spouse has income of £60,000 or more, then the High Income Child Benefit Charge will equal the Child Benefit (CB) paid unless you choose to stop receiving CB payments. If the higher income partner has income between £50,000 and £60,000 then, as a general rule, for each extra £100 of earned income:

- Income tax is at £40;
- NICs are £2;
- You lose £10.66 of CB for your first child and £7.05 for each subsequent child.

So if you have two children eligible for CB, £59.71 of your £100 extra earned income will pass to HMRC, equivalent to an effective tax rate of nearly 60%.

The reverse is also true: £100 less of taxable income could imply only £40.29 less net income. So, for example, if you reduce your taxable income in exchange for your employer making a corresponding pension contribution, you may be securing £100 of retirement benefit at an effective cost of £40.29 (or even less if your employer takes account of *their* NIC savings).

Turning the tables on the basic personal allowance restriction

The impact of the phasing out of the basic personal allowance once total income exceeds £100,000 has again been exacerbated by the above-inflation increase in the personal allowance. We now have a system under which the marginal rate of tax in the £100,000 - £120,000 band of income is 60% on non-dividend income - a third higher than the top rate of 45% and catching many more taxpayers.

The corollary is that if your income is in that band, or marginally above it, you may be able to obtain 60% tax relief on some pension contributions, as the example below shows.

60% Tax Relief

In 2014/15 Frank has income of £119,000, all of which consists of earnings and interest. His current pension contributions are under £20,000. He can thus make an extra £19,000 gross pension contribution without tax penalty because the aggregate contributions of £39,000 would still fall within the newly reduced £40,000 annual allowance. Depending upon whether he makes the pension contribution, his tax bill would be:

	No Pension Contribution		Pension Contribution	
	£	£	£	£
Gross income	119,000		119,000	
Pension contribution	-		19,000	
Personal allowance	500		10,000	
Taxable income	118,500		90,000	
Basic rate tax	31,865 @ 20%	6,373	31,865 @ 20%	6,373
Higher rate tax	86,635 @ 40%	34,654	58,135 @ 40%	23,254
Total tax		**41,027**		**29,627**

Thus a gross pension contribution of £19,000 will save Frank £11,400 in tax, an effective 60% rate of relief.

CAPITAL GAINS TAX

For 2014/15, the Chancellor made no significant changes. He had previously announced that the annual exempt amount would rise by £100 for 2014/15 and 2015/16 and, at least for 2014/15, that is what will happen.

PLANNING POINTS

18% is better than 20% and 28% is superior to 40% or 45% (or 60%)

Unless you are one of those lucky few who are able to benefit from the 10% rate on savings income, investment returns in the form of capital gains are usually taxed at a lower rate than income. There is also an £11,000 annual capital gains exemption in 2014/15, which is not tapered away. Although capital gains are taxed as the top slice of income, the rates are lower and capital gains tax is not subject to the same payments on account rules as income tax: you pay your full capital gains tax on 31 January in the tax year following the one in which the gains arose.

While the tax tail should never wag the investment dog, the case for favouring growth over income when setting your investment goals is a strong one. There are many anti-avoidance rules which prevent income being transformed into capital gains, but it remains a fact 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 significantly reduce your tax bill.

Use your annual exemption

Would you waste a tax exemption worth over £3,000 a year? That is what your full 2014/15 annual capital gains tax exemption could be worth in terms of tax saving, if you pay tax at above the basic rate.

As far as possible it is important to use the exemption each year (and for your spouse to do the same) because, if unused, it cannot be carried forward.

There is the possibility that the exemption will be cut and capital gains tax rates rise after the election. At last year's party conference, the Liberal Democrats debated the idea of a £2,000 annual exemption and taxing gains at full income tax rates.

If you do not systematically use your annual exemption, you are more likely to reach a point – whoever wins the election – when some of your gains are subject to tax. Unfortunately, you cannot simply crystallise a gain by selling and then immediately repurchasing an investment – what used to be 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 2014/15 the maximum ISA investment from 1 July will be is £15,000.

- *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.

- *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 made separately through the market.

- *Bed-and-something-very-similar* The growing number of funds which track UK and international stock market indices has created an opportunity to replicate the tax benefit of the old bed-and-breakfast strategy. For example, if you hold the ABC UK FTSE All-Share unit trust, you could sell it and immediately reinvest in the XYZ FTSE All-Share Exchange Traded Fund. Your underlying investment – shares in the constituents of the FTSE All-Share index – will not alter but, because the fund provider has changed, you will escape the rules against bed-and-breakfasting.

Keeping down your CGT bill

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

- Maximising the use of ISAs, where there is no capital gains tax.

- Using 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.

- Sharing 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 exempt amount and you have, together you could save tax.

- Use pension contributions to bring your marginal rate of income tax down to basic rate. Pension contributions cannot be offset directly against capital gains, but to the extent that they remove income from higher rate tax, they can cut your capital gains tax bill.

- Take advantage of venture capital trusts (VCTs), enterprise investment schemes (EISs) and seed enterprise investment schemes (SEISs). These are high risk investments, but they are generally free of capital gains tax. While they offer income tax relief at 30% or 50% for SEIS (see page 14 below), they do not reduce your income for tax purposes, so they cannot cut your capital gains tax bill in the same way that a pension contribution can.

INHERITANCE TAX

The inheritance tax nil rate band has now been fixed at £325,000 since 6 April 2009. If it had been indexed-linked, as it used to be, the band would now be about £375,000. The nil rate band will remain frozen at £325,000 until at least April 2018, supposedly as a means of helping to meet the costs of implementing the Care Bill.

Inheritance tax is showing some similarities to higher rate tax, as the failure to adjust bands and allowances drags more people into the tax net and steadily raises more for the Exchequer. The latest statistics from HMRC show that in 2012/13 the tax raised 30% more than in 2009/10.

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 2013/14, you can makes gifts totalling £5,000 covered by the annual exemption in 2014/15.

- *The £250 small gifts exemption.* You can make as many outright gifts of up to £250 per individual 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 annual 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 annual exemption available for other gifts.

INVESTMENTS

A range of investment tax changes has taken place over the last few years, with some important changes from 6 April 2014.

Individual Savings Accounts (ISAs)

The main ISA investment limit for 2014/15 will initially rise to £11,880 (of which up to £5,940 may be in cash). The numbers are not round hundreds because the limit is rounded to the nearer £120, so that the corresponding monthly limits are divisible by £10.

However, from 1 July 2014, ISAs will undergo a radical reform:

- All existing ISAs will become new ISA (NISAs), with a total contribution limit of £15,000 in 2014/15, a further increase of £3,120.
- The rule which prevents more than 50% of the total contribution limit being placed in a cash ISA will be scrapped. Thus in 2014/15 100% of the £15,000 NISA contribution can be placed in cash deposits.
- The ban on transfers from stocks & shares ISAs to cash ISAs will be removed, giving full two-way transferability (transfers from cash to stocks & shares have long been possible).

- Investment options will be widened to include, for example, certain retail bonds with less than five years to maturity. There will also be consultation on including peer-to-peer lending.

The original ISA investment ceiling, set in April 1999, was £7,000 and it remained at that level until 2008/09, when it increased by £200. It jumped to £10,200 in 2010/11 and has broadly followed some measure of inflation since then. Anyone who was able to contribute to the maximum each year, up to and including 2013/14, would by now have placed £121,080 into their ISAs and largely out of the taxman's reach.

The introduction of 28% CGT in 2010, the arrival of additional rate tax and the various reductions in both the pension annual allowance and the lifetime allowance have all increased the importance of ISAs as a tax-efficient investment wrapper. This has not escaped the eyes of the Treasury, which was reported last Summer to have asked ISA providers about the practicality of placing a cap of £100,000 on the total value of ISA investments. The reports were not denied, but seem at odds with the Budget changes.

AIM and similarly listed shares became eligible investments for ISAs during 2013/14 and stamp duty on the purchase of such shares will be abolished from 28 April 2014.

Junior ISA

The Junior ISA (JISA) was launched in November 2011 for all children under 18 who were not eligible for the Child Trust Fund (CTF). The exclusion of CTF holders means Junior ISA eligibility is limited to any child born before 1 September 2002 or after 2 January 2011. So far JISAs have had only limited take up, although this is likely to change when legislation permits the transfer of CTFs into JISAs. Unfortunately, this will not happen until at least April 2015, according to the Treasury. In the meantime the maximum annual contribution to a JISA is initially £3,840 for 2014/15, rising to £4,000 on 1 July 2014. Unlike CTFs, JISA contributions are based on tax years.

Venture Capital Trusts and Enterprise Investment Schemes

Changes to the rules for Venture Capital Trusts (VCTs) will be made by the Finance Bill 2014 and take retrospective effect from 6 April 2014. These will – and indeed already have since last Summer – put an end to enhanced buy-back arrangements. By a somewhat convoluted route such buy-backs allowed investors to sell VCT shares and then immediately reinvest in the same VCT at much the same price, picking up 30% income tax relief en route. For 2012/13 enhanced buy-backs accounted for about one third of all VCT capital raising, enough to cost HMRC about £40m.

The Budget also closed down a ploy used by some VCTs to make dividend payments despite generating no profits. This had also been anticipated by VCT providers, with the result that some quoted dividends on offer for the 2013/14 year-end issues were more modest than in the past and some large dividend payments were made before 6 April.

The Budget also saw the Chancellor put an end to VCT and EIS investment in companies that receive government-funded renewable energy incentives: sunset for solar VCTs and EISs.

Seed Enterprise Investment Schemes

The Seed Enterprise Investment Scheme (SEIS) is a junior version of the EIS, introduced two years ago and aimed at young, very small businesses. Its key features are:

- The maximum total individual investment in SEIS is £100,000 per tax year, which qualifies for 50% income tax relief given by way of a reduction in the amount of income tax otherwise payable by the investor in the tax year of investment. Relief is initially available for shares issued until 5 April 2017.

- Initially, for 2012/13 only, there was a capital gains tax exemption where gains realised in the tax year were re-invested in a SEIS. Thus total tax relief could be 78%. This was extended to 2013/14 (and indefinitely thereafter), but with relief for only half of reinvested gains, reducing the maximum theoretical total tax relief to 64%.

- An eligible SEIS company must:

  - Be no more than two years old;
  - Conduct a genuine new business;
  - Have fewer than 25 full-time equivalent employees;
  - Have gross assets of not more than £200,000; and
  - Raise no more than £150,000 in total (*not* per tax year).

While it remains early days for the SEIS, evidence so far suggests that the low maximum capital raising limit of £150,000 per company has not been a disincentive for many would-be entrepreneurs. In November the Treasury released statistics showing that SEIS raised £82m for over 1,100 companies. These numbers help to explain why the Chancellor decided that the SEIS should be made permanent – it was originally due to expire in 2017.

The relative benefits and features of VCT, EIS and SEIS for 2014/15 are shown in the table below.

	VCT	EIS	SEIS
TAX ASPECTS			
Income tax relief	30%	30%	50%
Maximum personal investment per tax year	£200,000	£1,000,000 for income tax relief, no limit for CGT deferral relief	£100,000
Tax relief clawback	5 years	3 years	3 years
Backdating to previous tax year?	No	Yes, up to 100% of investment.	Yes, up to 100% of investment.
CGT reinvestment relief	No	Yes, deferral for gains made 3 years before/1 year after EIS investment	Yes, 50% exemption for gains realised
Investor capital gains tax liability	Nil at any time	Nil after 3 years, except for reinvested gains	Nil after 3 years
Dividends	Tax-free, but no tax credit reclaim	Taxable	Taxable
IHT business property relief	No	Yes, after 2 years	Yes, after 2 years
INVESTMENT ASPECTS			
Structure	Listed investment company	Unlisted company	Unlisted company less than two years old
Listing	Must be traded on EU regulated market	May be listed on AIM or similar, not regulated market	May be listed on AIM or similar, not regulated market
Liquidity	In theory tradeable as listed shares, in practice market may be very thin	Usually nil unless AIM listing. Exit may be by takeover or liquidation.	Probably nil
Qualifying companies for investment	Unlisted small trading companies, subject to various restrictions	Unlisted small trading companies, subject to various restrictions	Unlisted small trading companies, subject to various restrictions
Investments in qualifying companies	At least 70% of qualifying investments must be shares. Balance can be debt.	100% shares	100% shares
Maximum holding in any one company	15% of value	100% - single company structure	100% - single company structure
Non-qualifying investments	Up to 30%, eg in gilts	Ultimately none	Ultimately none
Maximum period to acquire qualifying investments	3 years	80% 1 year, balance 2 years	3 years

ISAs

In April 2008 it became possible to transfer the cash component of an ISA, including anything from a former TESSA, into the stocks and shares component. The option was generally viewed as a somewhat pointless facility when it was first announced: for most investors the value of the income tax saving

from the cash component was greater than the combined income and CGT tax savings offered by the stocks and shares component.

With the hindsight of more than five years of a 0.5% base rate, the facility to move out of cash looks rather more useful. The latest signs are that the Bank of England will not start increasing rates for another year and will then only raise them gradually. Meanwhile, many existing cash ISAs are offering rates of below 1%, with some paying just 0.1%. If you put money in a cash ISA more than a year ago, you would be well advised to check what interest rate you are now receiving. Rates have been declining for some while – despite the unchanged base rate – and you may only be earning a tenth of what you were two years ago.

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 3.75% or more, while the typical UK equity income fund offers a similar yield. Income from either type of fund is tax free via an ISA. 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 could fall as well as rise. Before making the switch – which will now be reversible from 1 July 2014 – you should always take independent advice.

Venture Capital Trusts (VCTs)

Recent Budgets have placed a range of constraints on pension planning for high earners. From 2011/12 the annual allowance was slashed from £255,000 to £50,000, while on 6 April 2012 the lifetime allowance was cut by a sixth. Both allowances fell again from 6 April 2014, with another £10,000 of the annual allowance cut. HMRC has been successful in challenging many aggressive non-pension tax avoidance schemes. Anecdotal evidence, and the number of schemes reported under HMRC's disclosure rules, both suggest that such schemes are becoming rarer. Arguably aggressive schemes have become publicly much less acceptable.

This background has increased the relative attraction of the tax breaks still available for investments totalling up to £200,000 per tax year in VCTs:

- 30% income tax relief on subscription to new VCT shares. This relief is clawed back on disposals within the following five years.
- Dividends are free of income tax, although the 10% tax credit cannot be reclaimed.
- Any gains made on disposal of shares are free of capital gains tax.
- Within the VCT there is no tax on gains.

BUSINESS TAX

The mainstream rate of corporation tax was cut by 2% to 21% from 1 April 2014. For the financial year starting on 1 April 2015 the rate is scheduled to be reduced again to 20%, bringing it in line with the small profits rate. As a result all the marginal rate calculations for profits between £300,000 and £1,500,000 should disappear. However, Ed Miliband has said that a Labour government would reverse the final 1% cut in mainstream corporation tax to finance a reduction in business rates for small firms.

Capital allowances

The Annual Investment Allowance (AIA), which gives 100% initial relief for investment in plant and machinery, was doubled to £100,000 from April 2010 then cut to £25,000 from 1 April 2012 (6 April for unincorporated businesses). However, in the 2012 Autumn Statement the Chancellor announced that for two years from 1 January 2013 the AIA amount would be increased to £250,000. He has now decided to double the AIA from April 2014 and maintain it at that level until the end of 2015.

Employment Allowance

A new Employment Allowance of £2,000 a year for all businesses and charities was introduced from 6 April 2014 to offset business and charity employer National Insurance contribution Class 1 (NIC) costs.

As announced in the Autumn Statement, from 2015/16 employers are also scheduled to benefit from the end of Class 1 NICs for employees under the age of 21 who earn less than the upper earnings limit (£42,285 in 2015/16)

PLANNING POINTS

Dividends or Salary ... or Pension Contribution?

Regular changes to National Insurance contributions and tax rates have altered the mathematics of the choice between dividends and salary, with the lowering of the additional rate in 2013/14 the most recent revision to have had an impact. If you are in a position to choose between salary and dividend, and not caught by the IR35 personal company rules, a dividend remains the more efficient choice, as the example below shows. However, a pension could avoid all immediate tax and NIC costs, provided the newly reduced annual allowance is not an issue.

Still Worth It

Brian has £25,000 of gross profits in his company which he wishes to draw, either as bonus or dividend. Assuming the company pays corporation tax at the 2014 small profits rate of 20% and Brian has annual income in excess of £41,865, his choice can be summarised thus:

	Bonus £		**Dividend £**	
	40% tax	**45% tax**	**40% tax**	**45% tax**
Marginal gross profit	25,000	25.000	25,000	25,000
Corporation tax @ 20%	N/A	N/A	(5,000)	(5,000)
Dividend	N/A	N/A	20,000	20,000
Employer's National Insurance contributions £21,968 @ 13.8%	(3,032)	(3,032)	N/A	N/A
Gross bonus	21,968	21,968	N/A	N/A
Brian's NICs £21,968 @ 2%	(439)	(439)	N/A	N/A
Income tax *	(8,787)	(9,886)	(5,000)	(6,111)
Net benefit to Brian	**12,742**	**11,643**	**15,000**	**13,889**

**after allowing for 10% tax credit on dividends*

The benefit of the dividend route is due to the savings in NICs.

The Employment Allowance will generally make no difference to the dividend/salary decision, as there will still be employee NICs to meet out of net pay. Where it does offer some more interesting opportunities is for sole traders who employ their spouses/partners at a salary low enough to mean no NICs is payable. It might now be worth increasing that salary.

Capital allowances timing issue

The doubling and extension of life for the higher 100% AIA in plant and machinery means the timing of a major investment needs to be considered carefully. The change to the AIA will take effect from April 2014 and be pro-rated across business years so, for example, if your company year end is 30 June, its AIA in the financial year ending on 30 June 2014 will be:

+ ¾ x £250,000 + ¼ x £500,000 = £312,500

It will therefore be necessary to time major purchases to make maximise the use of the AIA.

PENSIONS

There has been a raft of changes to pension tax rules in recent years, to which the Budget has now added.

27 March 2014

From this date three changes announced in the Budget started to operate:

For capped income drawdown, the maximum amount that can be withdrawn each year rises from 120% of the equivalent annuity to 150%. This applies for drawdown anniversaries on or after 27 March, so many people will have to wait for up to a year before the increase applies. In practice you should always take advice about the level of withdrawals: the higher the income you take, the greater the risk that you will have to reduce withdrawals in future years or (under next year's rules) see your funds exhausted.

For flexible income drawdown, the minimum income requirement you must meet to use this feature falls from £20,000 a year to £12,000 a year of secure income (broadly pension annuities, final salary scheme and state pensions). As the name suggests, flexible drawdown allows you to draw what you want – even your whole fund – but the withdrawals are fully taxable as income.

Small pots and trivial commutation The rules on converting small pension funds into lump sums (of which 75% will usually be table) will be relaxed. The maximum size of individual pension arrangements that can be turned into cash will be increased from £2,000 to £10,000 and the number of arrangements this can be applied to will be increased from two to three. At the same time the limit for converting *all* pension wealth into cash will be raised from £18,000 to £30,000.

6 April 2014

Two important changes, originally announced in the Autumn Statement 2012, took effect at the start of 2014/15:

- The annual allowance was cut again, from £50,000 to £40,000. However, the £50,000 figure continues to apply for tax years up to and including 2013/14 for carry forward calculation purposes.
- The lifetime allowance was also cut again, dropping from the current £1.5m to £1.25m. Ahead of the change there were two options to take advantage of new transitional protection measures. However, only one is now available.

6 April 2015

The future changes put out for consultation in the Budget are the most radical reform of the pension rules in many years:

Increased flexibility From age 55 you will be able to draw whatever you wish from your pension plan as a taxable payment, without any requirement to have a minimum level of income. The pension commencement lump sum (25% tax free cash) rules will continue, although their structure might be revised. This change has been heralded as meaning an end to the compulsion to buy an annuity at retirement, although in practice alternatives have been available for nearly two decades.

Guidance guarantee If you have a personal pension or other defined contribution pension pot, the government will require your pension provider to offer "free and impartial face-to-face guidance" when you retire. How this will work is unclear, not least because of the numbers and costs involved. One thing is clear: it will be 'guidance', not advice.

October 2015

Class 3A contributions will become an option if you reach (or have reached) State Pension Age (SPA) before the new single-tier state pension begins on 6 April 2016. This will give you the opportunity to top up your pre-April 2016 state pension by making a special lump sum National Insurance contribution payment. You will be able to buy extra pension in £1 a week increments up to a maximum of £25. The costings have not yet been set, but some indicative figures from the DWP suggest the terms will be very attractive. You will only have 18 months to make the contribution.

Unspecified timings

The Chancellor is also considering a number of other potential changes:

The age 75 limit for tax relief on pension contributions could be amended or abolished. It has been unchanged for many years, during which time – as the government constantly reminds us – life expectancy has risen relentlessly.

Dependants' pensions The government is looking to simplify the rules on dependants' benefits, although what it has in mind remains to be seen.

The minimum pension age, which sets the earliest point at which you can normally take benefits from a pension, is set to rise. The government has suggested it will move in line with the SPA from 2028, implying an increase from the current 55 to 57 when the SPA reaches 67 in 2028. However, there is a suggestion that the gap between the two should be reduced to five years.

Don't waste your 2011/12 annual allowance…

Gina's pension contributions, shown on the table below, resemble a random walk. They reflect the impact of the special annual allowance in 2009/10 and 2010/11 and the subsequent failure of a major client that left her with minimal profits in 2011/12.

In the pension input period ending in 2014/15 she can use the carry forward rule to make contributions of up to £90,000 without any annual allowance tax charge, as the table below shows. However, she has already lost the chance to mop up the £30,000 unused annual allowances from 2009/10 and 2010/11, which could only be carried forward to 2012/13 and 2013/14 respectively.

Tax Year	Contribution	Annual Allowance*	Carried Forward to Next Tax Year	Total Carried Forward
2008/09	£58,000	£50,000	Nil	Nil
2009/10	£20,000	£50,000	£30,000	£30,000
2010/11	£20,000	£50,000	£30,000	£60,000
2011/12	Nil	£50,000	£50,000	£110,000
2012/13	£50,000	£50,000	Nil	£80,000
2013/14	£50,000	£50,000	Nil	£50,000
2014/15	£90,000	£40,000	Nil	Nil

** For carry forward calculation purposes only in 2008/09-2010/11.*

Unless Gina contributes £90,000 to a pension arrangement with a pension input period ending in the current tax year, the unused annual allowance from 2011/12 will also be lost because the maximum carry forward period is three years.

APPENDIX – TAX FACTS AND FIGURES AND NICs

Main Income Tax Allowances and Reliefs

	2013/14	2014/15
	£	£
Personal allowance – standard	9,440	10,000
- Born between 6 April 1938 and 5 April 1948	10,500	10,500
- Born before 6 April 1938	10,660	10,660
Personal allowance reduced if total income exceeds ∞	100,000	100,000
Married couple's allowance* – minimum amount	3,040	3,140
– maximum amount	7,915	8,165
Maintenance to former spouse *	3,040	3,140
Age-related allowances reduced if total income exceeds ¶	26,100	27,000
Employment termination lump sum limit	30,000	30,000

∞ For 2013/14 and 2014/15 the reduction is £1 for every £2 additional income over £100,000. As a result there is no personal allowance if total income exceeds £120,000 (£118,880 for 2013/14).

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

¶ For 2013/14 and 2014/15 the reduction is £1 for every £2 additional income over the total income threshold. Standard allowance(s) **only** are available if total income exceeds:-

	2013/14	2014/15
	£	£
Taxpayer born between 6 April 1938 and 5 April 1948 [personal allowance]	28,220	28,000
Taxpayer born before 6 April 1938 [personal allowance]	28,540	28,320
Taxpayer born before 6 April 1935 [married couple's allowance]	38,290	38,370

Income tax Rates

	2013/14	2014/15
	£	£
Starting rate on savings income- 10%	1 – 2,790	1 – 2,880
Basic rate	0-32,010	0-31,865
Maximum tax at basic rate†	6,402	6,373
Higher rate - 40%	32,011-150,000	31,866-150,000
Tax on first £150,000†	53,598	53,627
Additional rate on income over £150,000	45%	45%
Discretionary and accumulation trusts (except dividends) °	45%	45%
Discretionary and accumulation trusts (dividends) °	37.5%	37.5%
Ordinary rate on dividends	10%	10%
Higher rate on dividends	32.5%	32.5%
Additional rate on dividends	37.5%	37.5%
High income child benefit charge	1% of benefit per £100 income between £50,000 and £60,000	

† Assumes 10% band not available. £6,085 on first £31,865 (£6,123 on first £32,010 in 2013/14) and £53,339 (£53,319 in 2013/14) on first £150,000 if full 10% band is available.

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

Car Benefits

The charge is based on a percentage of the car's "price". "Price" for this purpose is the list price at the time the car was first registered plus the price of extras.

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	
	13-14	14-15		13-14	14-15		13-14	14-15
75 or less	5	5	130–4	18	19	180–4	28	29
76–94	10	11	135–9	19	20	185–9	29	30
95–99	11	12	140–4	20	21	190–4	30	31
100-4	12	13	145–9	21	22	195–9	31	32
105-9	13	14	150–4	22	23	200–4	32	33
110-4	14	15	155–9	23	24	205–9	33	34
115-9	15	15	160–4	24	25	210–4	34	35
120	15	16	165–9	25	26	215 +	35	35
121-4	16	17	170–4	26	27			
125–9	17	18	175–9	27	28			

Notes

1. The exact CO_2 emissions figure should be rounded down to the nearest 5 g/km for levels of 95g/km or more.

2. For all diesels add 3%, subject to maximum charge of 35%.

3. There is no charge for any car which cannot produce CO_2.

Car Fuel Benefits

For cars with an approved CO_2 emission figure, the benefit is based on a flat amount of £21,700 (£21,100 for 2013/14). To calculate the amount of the benefit the percentage figure in the above car benefits table (that is from 5% to 35%) is multiplied by £21,700. The percentage figures allow for a diesel fuel surcharge. For example, in 2014/15 a petrol car emitting 142 g/km would give rise to a fuel benefit of 21% of £21,700 = £4,557.

VAT

From	1 April 2013	1 April 2014
Standard rate	20.0%	20.0%
Reduced rate (eg domestic fuel)	5.0%	5.0%
Annual turnover limit for registration	£79,000	£81,000
Deregistration threshold	£77,000	£79,000
Flat rate scheme turnover limit	£150,000	£150,000
Cash accounting and annual accounting limits	£1,350,000	£1,350,000

Inheritance Tax

	Cumulative chargeable transfers [gross]		tax rate on death %	tax rate in lifetime* %
	2013/14 £	2014/15 £		
Nil rate band†	325,000	325,000	0	0
Excess	No limit	No limit	40∞	20

* Chargeable lifetime transfers only.

† On the death of a surviving spouse on or after 9 October 2007, their 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).

∞ 36% where at least 10% of net estate before deducting the charitable legacy is left to charity.

Capital Gains Tax

Main exemptions and reliefs

	2013/14 £	2014/15 £
Annual exemption	10,900*	11,000*
Principal private residence exemption	No limit	No limit
Chattels exemption	£6,000	£6,000
Entrepreneurs' relief	Lifetime cumulative limit £10,000,000. Gains taxed at 10%	Lifetime cumulative limit £10,000,000. Gains taxed at 10%

* Reduced by at least 50% for most trusts.

Rates of tax

Individuals:	18% on gains within basic rate band, 28% for gains in higher and additional rate bands
Trustees and personal representatives:	28%

Stamp Duty and Stamp Duty Land Tax

Residential	**Commercial**	**Rate**
£125,000 or less	£150,000 or less	Nil
Over £125,000 up to £250,000	Over £150,000 up to £250,000	1%
Over £250,000 up to £500,000	Over £250,000 up to £500,000	3%
Over £500,000 up to £1,000,000*	Over £500,000	4%
Over £1,000,000 up to £2,000,000*	N/A	5%
Over £2,000,000*	N/A	7%
** 15% for purchases by certain non-natural persons*		
Stamp Duty (including SDRT): stocks and marketable securities (excluding AIM shares from 28 April 2014)		0.5%
No stamp duty charge unless the duty exceeds £5		

Corporation Tax

	Year Ending 31 March	
	2014	**2015**
Main rate	23%	21%
Small profits rate	20%	20%
Small profits limit	£300,000	£300,000
Upper marginal level	£1,500,000	£1,500,000
Effective marginal rate	23.75%	21.25%

Individual Savings Accounts (Maximum Investment)

	2013/14 £	**2014/15 (to 30/6/14)** £	**2014/15 (from 1/7/14)** £
ISA			
Overall per tax year:	11,520	11,880	15,000
Cash component:	5,760	5,940	15,000
Stocks and shares component:	Balance up to 11,520	Balance up to 11,880	Balance up to 15,000
Maximum in cash for 16 and 17 year olds	5,760	5,940	15,000
Junior ISA	3,720	3,840	4,000

Venture Capital Investments (Maximum Investment)

	2013/14 £	2014/15 £
ENTERPRISE INVESTMENT SCHEME (30% income tax relief)	1,000,000*	1,000,000*
Maximum carry back to previous tax year for income tax relief	1,000,000	1,000,000
SEED ENTERPRISE INVESTEMENT SCHEME (50% income tax relief)	100,000¶	100,000¶
VENTURE CAPITAL TRUST (30% income tax relief)	200,000	200,000

* No limit for CGT reinvestment relief.
¶ 50% CGT reinvestment exemption

Pensions

	2013/14	2014/15
Lifetime allowance*	£1,500,000	£1,250,000
Lifetime allowance charge: Excess drawn as cash Excess drawn as income	 55% of excess 25% of excess	
Annual allowance **	£50,000	£40,000
Annual allowance charge	20%-45% of excess	
Max. relievable personal contribution	100% relevant UK earnings *or* £3,600 gross if greater	

* May be increased under 2006, 2012 and/or 2014 transitional protection provisions
** Subject to three year carry forward of unused allowance

Working and Child Tax Credits

Working and Child Tax Credits will gradually be replaced by Universal Credit, which begins to be phased in in 2014/15. For the time being 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.
- The child element is £2,750 per annum for each child.

- The disabled child element is £3,100 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) 24 hours for families with children and workers with a disability. The claimant can be aged 16 or over. One of the couple must work at least 16 hours.

  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 £1,940 per annum.

- The couple or lone parent element is £1,990 per annum.

- A 30 hour element of £800 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 £2,935 per annum or more is available where the claimant, or his or her partner, has a disability.

- 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 41% (ie. 41p per £1 of income).

National Insurance Contributions for tax year 2014/15

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 2014/15 the Lower Earnings Limit is £111 per week.

Upper Accrual Point — the upper level of earnings on which an employee's S2P entitlement is

(UAP) — based (or on which any NI Rebate is determined). For tax year 2014/15 (and S2P's final year of 2015/16) 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 2% NI contributions will apply to earnings above this level. For tax year 2014/15 the Upper Earnings Limit is £805 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 via a final salary occupational scheme. This is based on the employee's earnings between the Lower Earnings Limit (LEL) and Upper Accrual Point (UAP). The rebate is 3.4% (employer) and 1.4% (employee) in respect of the employee's earnings between the LEL and UAP. Since 2012/13 contracting out has not been possible via a money purchase occupational scheme or a personal pension scheme. Contracting out for final salary related schemes will end from 2016/17.

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

For tax year 2014/15 this is £153 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 2014/15 this is £153 per week.

Employees - Class 1

Contracted in — Nil on first £153 per week (i.e. up to Primary Threshold)
12% of £153.01 per week to £805 per week.

2% on earnings above £805 per week.

Contracted out via final salary occupational scheme — Nil on first £153 per week (i.e. up to Primary Threshold)

10.6% of £153.01 per week to £770 per week

12% of £770.01 per week to £805 per week.

2% on earnings above £805 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.

Employer - Class 1 Contributions

Weekly Earnings	Contracted In	Contracted Out
	%	%
On first £153	Nil	Nil
£153.01-£770	13.8	10.4
Over £770	13.8	13.8

Although the reduced level of National Insurance contributions only applies to the employee's earnings in the band between the Secondary Threshold (£153 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 (£111 per week) and the Secondary Threshold (£153 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 £111 per week and £153 per week.

Employment Allowance – Class 1

A payment to cover Class 1 NICs of up to £2,000 per employer per tax year (equivalent to Class 1 employer's NICs on an annual salary of £22,448.75 for a single employee). Exceptions apply, including employment connected with family or household affairs (eg nannies).

Self-Employed

Class 2 (small earnings exception)	£2.75 per week flat rate. (applicable where profits are less than £5,885 per annum)
Class 4	9% of profits between £7,956 p.a. and £41,865 p.a.
	2% on profits above £41,865 p.a.

Voluntary Contributions

Class 3	£13.90 per week
Married Women and Widows Reduced Rate	5.85% of £153.01 to £805 per week.
	2% on earnings above £805 per week.

Should you have any questions or require further information please do not hesitate to contact Stephen Watson or Nicholas Wood

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