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The information in this Newsletter is to be viewed as general information and does not constitute advice. It is based on our understanding of the current legislation and market conditions, all of which are subject to change. If specific, individual advice is required, we urge you to contact your IFA.

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## Introduction – The Budget Proposals

The Budget proposed new rules which will cap tax breaks on pension funding for high income individuals with relevant income of £150,000 a year or more during a year in which a pension contribution is made or the previous two tax years. One issue is to define what income counts as 'relevant income' under these proposals. Relevant income is defined as your total income chargeable to income tax for the tax year, before any personal allowances or other reliefs, subject to certain adjustments. This includes:

- ◆ Employment income
- ◆ Income from self employment or partnerships
- ◆ Pension income
- ◆ Savings interest
- ◆ Dividends
- ◆ Chargeable gains from life assurance contracts or bonds (without top slicing relief)
- ◆ Rental income
- ◆ Income from trust

If a salary sacrifice arrangement is set up after 21<sup>st</sup> April 2009 for pension contributions by the employer, that amount will be added back to the income.

Certain amounts are then deducted from this total income figure to establish the relevant income for the tax year these include:

- ◆ Relievable pension contributions up to £20,000 made by the individual, or a third party on their behalf, in the tax year (but not employer pension contributions)
- ◆ Donations made during the tax year qualifying for Gift Aid
- ◆ Relief for trading and certain other losses

## Examples for Salary Levels and Possible Tax Savings by Pension Contributions

### 1. Earnings of £150,000 - £169,000

The definition of 'relevant income' used in the interim rules is not straightforward. The calculation includes income from all sources; earnings, bank interest, dividends etc as well as any salary sacrifices agreed after budget day.

So, someone earning £169,000 with a £100,000 employer contribution would be liable for a 20% tax charge on the excess contribution over £20,000. This amounts to £16,000 (i.e. 20% of £80,000).

But, also permitted in the calculation of relevant income is deduction of personal (but not employer) pension contributions of up to £20,000, so assuming that the person in our example made a £20,000 contribution, this would put their relevant income back below £150,000, thus exempting them from the new rules.

Factoring into account the 40% tax relief available on their pension contribution, and the saving of £16,000 tax on the employer contribution means that their net income has actually gone up by £4,000!

Perhaps someone earning £169,000 may not receive an employer pension contribution of £100,000. But even assuming an employer pension contribution of £50,000 and a personal contribution of £20,000, the effective rate of tax relief is still 70%.

Even those with income above £170,000 should make sure they take advantage of the £20,000 limit (or higher for existing regular contributions) for the next two years. They will also get 50% pension tax relief in 2010/11.

### 2. Income Above £100,000

From April 2010, those earning more than £100,000 will have their personal allowance withdrawn at a rate of £1 for every £2 of taxable income over this limit. This means that personal pension contributions reducing taxable income just below £100,000 are an effective way to retain the full personal allowance. A pension contribution equalling excess income above £100,000 of up to £12,950 will generate an effective tax relief rate of 60%. Even better is salary sacrifice, which generates an effective rate of tax relief of up to 65.4%.

### 3. Income less than £100,000

This group also benefits from 40% pension tax relief with salary sacrifice pushing that up to an effective tax relief rate of 47.7% for those in the higher rate income tax bracket.

# ESTATE PLANNING

There are many schemes available for the potential mitigation of Inheritance Tax and two of our favourites include the Loan Trust and Discounted Gift Trust. One allows access to the capital sum and can generate income whilst moving all of the growth outside of the Estate. The other offers a regular monthly income to the Settlor for their lifetime and usually takes part of the initial lump sum and all of the future growth outside of the estate for Inheritance Tax. Both can be set up as Chargeable Lifetime Transfers (CLT) or Potentially Exempt Transfers (PET) depending on the type of trust wording.

In simple terms, a loan trust is a trust set up with an interest free loan from the Settlor to a Trust, which is repayable on demand. 'Income' can be taken by the gradual repayment of the loan, and this is commonly at 5% per year over 20 years but can be a lower amount over a longer period. The Settlor can however request your loan to be repaid at any time as it is repayable on demand by the Trustees. This means that the person does not lose access to the capital, and can call on it in the event of unforeseen circumstances, which is something that many people are concerned about when gifting money. Any growth on the money is outside of the investor's estate for Inheritance Tax purposes and cannot be accessed by them.

For the Discounted Gift Trust, an investment is placed into trust by the Settlor who retains the right to a predetermined set income. Part of the money is deemed to be a CLT or PET and after 7 years would be completely outside of the estate. The other part may be outside of the estate straight away, so reduces the value immediately. In other words, the total investment value is discounted for tax purposes (hence the name). It is the income, predetermined as previously mentioned, that creates the discount. These trusts can be extremely effective, and although they mean you lose access to the actual capital, you do retain access to the agreed income payments.

As with all of these plans there are many factors to consider, and they are not ideal for everyone, so if you would like further information on them please contact us on 01285 886111 to see how we may be able to help you.

## WILL YOU BE WORKING IN 2012? IMPORTANT PENSION INFORMATION

Further new pension legislation, due in 2012, will affect all employers, with the introduction of Personal Accounts: a new form of pension for employees. Broadly speaking, it is planned that all employees will have to be offered a pension contribution of 3% of income, with the employee obligated to make a contribution to the same scheme of (eventually) 4% of income. Employees would have to opt out of auto enrolment if they did not wish to participate and the auto enrolment process would be repeated at regular intervals in the future. Although this is not due to become legislation until 2012, we believe forward planning is essential – for businesses, so there are no unwelcome surprises for companies who have not built this into their plans and budgets, because companies cannot opt out and for employees, who may find themselves wanting help with their budgeting if they go with auto enrolment, happy to save for their future while young, but find they have a smaller pay cheque as a result.

## FURTHER EXAM SUCCESS!

We are delighted to announce that Kathy Atkins, who works with Rod Holliman and Geoff Pollock, two of our advisers in Park Street, has achieved her third examination success: she received 86% in her CF3 examination recently, which centres on financial protection. Kathy has already passed CF1, which tests knowledge of UK financial services, regulation and ethics and CF2, which concentrates on investment and risk.

RTFP has always championed staff in the furthering of their professional knowledge and with her own hard work and the company's help Kathy is now set to study for CF4, which concentrates on Retirement Planning.

**Our congratulations to Kathy for her achievement  
- and to all our staff who have taken, or are currently  
studying for, industry examinations.**

If you would prefer to receive our Newsletter in e-mail format in future, please let us know. Write, phone or email Valerie Kiertzner ([v.kiertzner@rtfp.co.uk](mailto:v.kiertzner@rtfp.co.uk)) and she will ensure you receive soft copies in future. Similarly, if you know anyone who would be interested in receiving a copy of our Newsletter, do please ask them to get in touch.

We are still sending client questionnaires with policy documents and they have provided extremely helpful and useful feedback, so our thanks go to all those who have spent time completing them. If you would like to complete a questionnaire do please ask your adviser to let you have a copy, they are not restricted to people who have recently completed business.