

The 60% Tax Trap

Extra tax for key employees

From April 2010 if your income is above £100,000, you will lose the right to claim some or all of your personal allowance. Once your income exceeds £113,000, you will not be entitled to any personal allowance. This means that income in this band will be taxed at an effective rate of **60%** - higher than the 50% rate being introduced for people earning more than £150,000.

The new rules will come as an unpleasant surprise to many people and could be demotivating for anyone caught in the "trap". Any pay rise or bonus that pushes someone's taxable income (from all sources – salary, share schemes, interest, dividends and property) above £100,000 will be much less valuable to them. A rise of £10,000 will only be worth £3,900 after tax and NICs. Employees may seek higher pay rises to compensate for the extra tax they will suffer.

Planning is essential

Fortunately it will often be possible to avoid the worst effects of the trap by engaging in some straightforward tax planning to ensure that the personal allowance remains fully available. This can include:

- Changing salary payment dates.
- Accelerating or deferring bonus payments and share scheme payouts.
- Extra pension contributions – if made under a salary sacrifice arrangement this can also save NIC costs for both company and employee.
- Charitable donations – an ideal opportunity to promote Give As You Earn.

Your employees will need guidance as, for many of them, it will be the first time they have had to consider actively planning their tax affairs. They will not be pleased to find out they have been hit with the extra tax when their PAYE code changes and their net pay reduces. An active approach to helping employees understand and manage the issue could significantly improve the motivation and incentive value of current remuneration or any pay rise. You should consider identifying those likely to be affected well before next April, alerting them to the effect of the change and helping them plan to reduce their tax bills.

Our experience

Our Tax Strategies team can advise on the impact of this change and provide assistance on implementing planning to mitigate its effect. For more information about this and other tax issues relevant to employees, please contact:

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