Focus on the new tax brackets and other financial considerations

June 2010

This note has been produced by the General Practitioners Committee (GPC), a branch of practice committee of the British Medical Association (BMA), to highlight the effects of the tax changes which will affect doctors earning over £100,000, and other financial considerations arising as a result. It should be noted that this note is not comprehensive; members should consider their own case in the light of their personal circumstances and **take advice where necessary from an accountant**.

In particular, the reader's attention is drawn to the Mazars LLP letter report of 3 June 2010 and the General Practitioners Defence Fund Limited (GPDF) disclaimer of 15 June 2010, both of which are integral to a proper understanding of this paper and of its accompanying schedules identified as A to E, which are presented for illustrative purposes only.

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Background

The Finance Act 2009 introduced significant changes affecting those earning over £100,000, which came into effect on 6 April 2010. Changes include:

- a new additional rate of income tax of 50% on total income (including all income, not just wages, salaries and profits) over £150,000;
- the gradual withdrawal of the personal allowance for those whose adjusted net income exceeds £100,000. The personal allowance will be reduced by £1 for every £2 of income in excess of the £100,000 threshold. No personal allowance will be available where taxable income exceeds £112,950 (see Table 1 below).

Table 1

Taxable income	Effective average rate of income tax on taxable income above £100k
£112,950	60.00%
£120,000	52.95%
£130,000	48.63%
£140,000	46.47%

Further changes will come into effect in 2011/12:

- National Insurance contributions will be increased (confirmed in the November 2009 pre-budget report);
- tax relief will be restricted on pension contributions for individuals with a taxable income in excess of £130k –
  - the relief will be tapered from 50% to 20% for those with a taxable income of >£180k;
  - the basis of such tapering is awaiting Treasury consultations;
  - transitional legislation has been introduced to restrict tax relief for those with taxable income (net adjusted pay) of >£130k to the 2009/10 and 2010/11 tax years. The purpose of this legislation is to prevent individuals making increased payments in advance of 2011/12 in order to avoid the restrictions on tax relief.

Advice on the effects of the taxation changes

GP partners should be aware that superannuation contributions step up a whole percentage point when superannuable profits reach £100k. In addition, personal allowances (from 2010/11) are reduced to those earning a taxable income of £100k or over (and again at £140k), with proposed income tax rate hikes at the £150k level (from 2011/12). These changes merit careful financial advice from the practice accountant when individuals are closely approaching incomes in this range.

The loss of personal allowance and the step change in superannuation payments means that those earning around £100-110k will be hit particularly badly by the changes. An alternative to paying such high marginal rates of tax could be for partners to improve their work-life balance by reshaping their commitment to their practice by reducing their income and time commitment to their practices. Taking on a new GP partner is one way in which this could be achieved, and may well prove to be more cost effective than employing a salaried GP. As a rough rule of thumb, the true cost of taking on a salaried GP could be up to 40% on top of the actual salary (including items such as employers National Insurance, employers pension contributions, subscriptions and other items as illustrated in the attached **schedule A**, although this will vary from practice to practice).

The effect of tax changes makes it more worthwhile not working full-time, allowing more time for family commitments, training or taking on additional professional roles such as Practice Based Commissioning and areas of special interest (GPwSI). In part time posts, there is a balance between the amount of time spent on core patient contact and working within the practice, and the ability to carry out additional activities. However, this must of course not be detrimental to the patients and must be balanced by the need to maintain someone in the surgery for the sake of continuity.

How recent tax proposals could affect income

Also attached are four spreadsheets (identified as **schedules B to E**) which illustrate how the recent tax proposals could affect income over the years 2009-2012. Headline increases in tax rates have been avoided by a rise in National Insurance, which could hit the self employed, including GPs, very badly indeed.

These spreadsheets do not include the impact of the withdrawal of tax relief on pensions. If the worst case scenario comes to pass it is quite possible that take home pay for practices earning above £130K could drop by £1-2k per month as the result of tax relief withdrawal.

Impact of changes to tax relief on pension contributions

There is considerable uncertainty about tax relief on pension contributions. Following the introduction of a new additional rate of income tax of 50%, applying to taxable income over £150,000, the Chancellor announced that from 6 April 2011, tax relief on pension contributions for high earners will be restricted.

There is further information about this in the BMA guidance, *Impact of the 2009 budget on pensions*:

www.bma.org.uk/employmentandcontracts/pensions/general_pensions_information/impbudg09pens.jsp

Advice on the effects of the National Insurance alterations

Deferment of Class 1 NI contributions – Where the doctor is both employed and self-employed

Where a doctor is both employed and self-employed, HMRC may make special arrangements to avoid excessive contributions being paid in the tax year. HMRC must be satisfied that the total amount of Class 1 NI contributions which are likely to be paid by the doctor, together with any Class 4 NI, will exceed the maximum Class 1 and Class 2 amounts payable for that year.

The doctor will need to apply for the deferment certificate and will be responsible for paying across to HMRC any shortfall, should insufficient NI be paid during the year concerned. It will be in doctors' own best interests to seek appropriate advice in relation to this and other matters described in this note.

Further information on tax and national insurance is available to BMA members on the BMA website: www.bma.org.uk/employmentandcontracts/tax/index.jsp