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## Features

### Regulars Insurance & Lifestyle

#### How much tax do you pay?

Just looking at the public sector borrowing figures, a rough bit of arithmetic reveals Gordon Brown has his sums horribly wrong. Around £10 billion wrong. No worries – after the election in May, whoever is Chancellor will have to raise income taxes. Good for him; really bad for you. Before the election, we show you how much direct and indirect tax you pay and the legal strokes you can pull to reduce your tax bill. Nick Kettles moans: “The horror, the horror”

Frustrated by delays in processing his application for tax credits, 36-year old Mike Maddison, from Somerset glued his left hand to the enquiry desk at his local tax office. Half an hour later, in the company of police officers and paramedics, Mr Maddison walked from the office clutching a cheque for £400. Extreme measures?

Perhaps. But what lengths would you go against the Inland Revenue in order to claw back what is rightly yours?

But can you be bothered? After all, tax is such a complex business: all them codes and forms. Yet, this is the very attitude that pours still more millions into tax coffers of the Treasury every year. The fact is, the majority of people are blissfully unaware just how much tax they are really paying.

Tax Freedom Day, the hypothetical point at which the average UK employee starts earning money for themselves, will fall this year somewhere around the end of May: 150 days of 2005 simply to pay taxes. Now if you do the maths you'll find that five months worth of payouts of the average national annual wage of £21,949.20 is more – a lot more – than the tax and National Insurance contributions (NICs) deducted by your payroll department. So where else are you paying tax? If you knew, might you not take a leaf out of Mr Maddison's book and reach for the superglue?

#### Mr Average's home comfort at a price

After tax and NIC of £4,920 Mr Average is left with a meagre £17,029. Like everyone else in Middle England he's felt the pain of the one per cent hike in National Insurance to the tune of over £120. But, for the sake of argument, let's say he's in his late forties, living with his wife, who does not work (this situation,

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although rare these days, still seems to exist), and their two teenage children, who are in full-time education. Because of his status, he is entitled to a further £1,393.20 a year in Child Benefit, and £1,169.64 in Child Tax Credits, which brings the household income to £19,591.20. He's probably thankful for this help because, according to research by the Yorkshire Bank, more than one in four UK adults regularly work beyond their contracted hours without further remuneration.

So, from this he then pays an average of £894 p.a. in council tax. By the time he reads this he'll have learnt if his local council has managed to avoid increasing it still further, buttered up as they are likely to have been by the government in search of votes.

And if, like many other homeowners, he's recently moved, possibly to keep pace with an overheating market, he will have paid the national average house price of £162,000 for his new home. This means he will have paid stamp duty at 1 per cent of £1,620.

Despite house-price inflation, the stamp duty threshold has not risen above the £60,000 threshold it was set at in 1993, and has contributed to the Revenue some £4 billion a year from house sales. According to Halifax, UK property taxes are the highest of any major developed country. In 2002, they represented 4.3 per cent of UK GDP compared to other eurozone countries at just 1.9 per cent.

But let's be fair and amortise his stamp duty payment over the average time spent living in any one property, which is seven years, giving him a total of £231 a year. This, with council tax, then whittles down his annual net income to £18,466.20.

He'll be pleased to note then, that when one becomes a new council-tax payer for a dwelling, one has a period of six months within which to challenge the valuation band of the property. If he's successful in being downgraded just one band, depending on where he lives, he may save anywhere between £100 – £300, cancelling out his stamp duty. [www.voa.gov.uk](http://www.voa.gov.uk)

So, now he's comfortably settled in his home, he can start living. Mr Average can have his Jaffa cake and eat it too According to the Office of National Statistics (ONS), in any one year the average household will pay an average of £1,856 in VAT on all goods and services. This would leave Mr Average with a net income of £16,610.20. At least half of this will be on the weekly food bill, assuming a very conservative weekly shop of £100 because Mr and Mrs Average make the most of loyalty schemes and by shopping at one of the cheaper supermarkets. Either way, he'll need to consider the following to get that bill down still further.

There is no VAT on cold food takeouts like sandwiches, which could save him about £70 a year on a daily sandwich. He'll need to be sure to bring his coffee (a hot take-out and subject to VAT) in a flask. If his employer is offering luncheon vouchers he can save a whopping 15 pence a day, providing he can find a shop that will take them. He'll save more if he forsakes a weekly family takeaway. Spending just £20 a week on takeaways places £182 in the VAT man's pocket every year.

There are certain tax and customs regulations that exempt consignments of

goods of low value (under £18) from import VAT. This means you can buy goods like CDs by mail order from countries within the British Isles, like Guernsey and Jersey, and the Isle of Man. At the time of writing, all the top-ten album CDs were available at Tesco's Jersey for just £8.99 each. And, amongst the many insane vagaries of VAT law, is the difference between cakes (judged a necessity and zero-rated), and chocolate-covered biscuits (a luxury and subject to VAT). In 1991, McVities and HM Customs & Excise needed a tribunal to decide whether the humble Jaffa Cake was a cake (no VAT) or a chocolate biscuit (mucho VAT). In the end McVities baked a 12-inch Jaffa Cake to convince the tribunal chairman. Will Mr Average forsake his chocolate digestive in favour of juicy Jaffa Cakes to avoid paying VAT? He'll need a sense of humour to avoid going completely insane when he reads the following.

-Mr Average's duty to the state VAT is a drop in the ocean compared to duty on fuel, tobacco and alcohol. Mr Average is about to realise just how wedded to the state his life is.

Let's say Mr Average drives a Ford Focus i.6i Hatchback 15,000 miles a year. This means he spends as much as £1,513.54 on petrol, of which approximately 60 per cent is duty or £908.13

p.a. (duty at 50ppl out of average of 82.9ppl source: [www.greenfuel.org.uk](http://www.greenfuel.org.uk)). Add vehicle excise duty, (road tax to you and me) at £165 and he's left with £15,537.07 assuming he's managed to avoid the widespread introduction of residents' car parking permits; the increased use of fines for speeding; and congestion charging.

Let's hope it doesn't get worse. Last year Alistair Darling mooted the possibility of a satellite-based system, nationwide, road-pricing scheme forcing motorists to pay tolls of up to £1.30 a mile, possibly as soon as 2014.

Mr Average could save money on road tax with a smaller car, presumably with better fuel efficiency. He might also consider converting his car to Liquid Propane Gas (LPG), provided he brought the car in the last five years. The cost would be £1,938.75 (inc. VAT of course – saving the planet is a luxury) which means he would then save about £692 p.a. by buying LPG at just 36p a litre which only has duty of 4.5ppl (frozen until at least 2007). This means he would have to continue driving his Ford Focus for three years to get his money back – unless he had been successful in applying for a grant to cover part of the cost (about £700) which, alas, from March 2005, has no longer been available in England and Wales.

Being the family book-keeper Mrs Average still smokes to calm her nerves. She's trying to cut down to only ten a day, but at about £2.30 a pack of 10 (tripled in the last 15 years) that's £839.50 p.a., and an incredible £548.96 in duty – whittling the family budget down to £14,987.24. Duty on cigarettes is calculated at 22 per cent of the retail price – plus 9.98 pence per cigarette – a total of £1.50 for her pack of ten. Lung-gasping. To be sure, she'll give up soon.

Of course, Mr Average doesn't know even half of the above yet – and so hasn't quite been driven to drink – but nonetheless still enjoys a pint of a Friday evening.

He's more moderate in middle age, so let's say his weekly consumption is about eight pints of beer. Duty on beer with 5 per cent volume is paid at about 35 pence out of an approximate £2.50 per pint. At that rate, he raises his first weekly pint of the week to the Chancellor to the tune of £145.60 of duty each year. Cheers. Add in his wife's love of vino tinto – her full weekly recommended amount of 12 large glasses of wine (32 pence duty per 250ml glass of 12 per cent volume wine) – and we add a further £199.68 a year, leaving Mr Average's a total net income of £14,641.96

If he wants to avoid getting perilously close to the bread line, he'll book that booze cruise now. John Whiting a tax partner at PWC says: "If you smoke and drink, then buy abroad, its perfectly legitimate if you can show its for your own consumption." With duty rates significantly lower in France, he can expect to save upwards of £300.

Mr Average's taxing time enjoying himself. Still, Mr, Average can still console himself in the knowledge that he can sit in the private comfort of his own front room, put his feet up and watch terrestrial TV... all for cost of the anachronistic TV licence, £121 a year, or £10 a month.

Of course if he's a black and white movie fan, he can always down grade to a black and white set at just £40.50. Or he may decide to give up TV all together and not pay at all. But he may find he soon resents being sent intimidating letters, which pre-suppose he is in violation of the law with regards to the Wireless Telegraphy Act [1949].

If he buys a £1 lottery ticket every week the government claims 12p from every ticket sale in Lottery tax). Altogether, he's a further £177.24 worse off, leaving his total net income at £14,464.72.

Gambling online through websites based overseas, will ease this burden. As will taking a holiday in the UK to avoid Air Passenger Duty £20 per person per flight outside Europe and £5 per person inside.

### **The yoke on**

Mr Average's shoulders

The insurance tax premium is an average of £46 p.a. This is a tax on the premium you pay for most general insurance policies – motor, household, medical (including long-term cover), income replacement, travel and other protection cover – where the risk is located in the UK. It was initially introduced at 2.5 per cent on 1 October 1994 but was increased in stages to the current rate of 5 per cent in July 1999.

The components of 'other indirect taxes' as defined by the Office of National Statistics are: stamp duties on share dealings, legal and commercial documents; and taxi licences at an average of £18 p.a. per person.

Now at this point Mr Average should think about ordering a stiff drink (he'll ignore the 20p duty per 25ml shot of 40 per cent volume spirits for now) because things

are about to get hairy. Especially if he thinks VAT is the only thing that sends his shopping bill soaring.

Total 'intermediate taxes' is that portion of 'indirect taxes' that are passed on to households by businesses. This is a rather nice way of saying that you end up paying for the increased cost of doing business in Blair's Britain. Put bluntly, increases in commercial and industrial rates; employers' National Insurance contributions; duty on hydrocarbon oil; and vehicle excise duty; amongst other intermediate taxes' do not hurt businesses as much as the bleating business press would presume. It hurts you at the checkout, because that's where they offset these increased costs on their goods and services to the tune of an extra £1,062 p.a. per person.

Add custom duties at £27 per person p.a. (the cost of importing goods to the UK, which is also factored into the retail price) and Mr Average has just paid an extra £1,153 in other indirect taxes.

Can he avoid these costs? Only if he breaks the law by buying stolen, smuggled or counterfeit goods. Mr Average is a genuinely law-abiding citizen, so his net income now stands at £13,311.72

Mr Average started off with a gross income including benefits of £24,483.20, which means he's paid some £11,171.48 in tax each year.

This leaves just over £13,000 to cover the cost of the balance of payments i.e the cost of goods and services outlined above before VAT, intermediate tax and duty. Based on a total VAT bill p.a. of £1,865, Mr Average must stump up £7,519. Add the cost of a £80,000 capital repayment mortgage (fixed at 5.49 per cent for 2 years) at £428.80 a month or £5,145 p.a., and there's just under £650 p.a for savings.

With the introduction of top-up fees it's going to cost upwards of £20,000 to pay for each of his children to go to University – he's long since given up hope of providing for them himself. Still, he'll earn interest (about 3.5 per cent) on his £650 savings p.a., yielding about £21 a year in interest; but – of course – this is before tax, leaving enough of the cost of a takeaway for the family perhaps (on which he'll pay VAT – tax on tax on tax).

Mr Blair says he's not interested in taxing David Beckham, but Mr Average surely wishes he would. The top-fifth in the earning scale pay a smaller proportion of their income in tax (34 per cent) than the bottom fifth (42 per cent). The richest 1 per cent has seen its share of national income double from 6.5 to 13 per cent over the past two decades.

### **Is it any wonder the UK is so much in debt?**

It is arguable that, although Mr 'Average UK citizen' seems hard done by, that at least he enjoys the benefits of living in a reasonably civilised society, able to get education and health service free at the point of access. According to the ONS these benefits in kind are worth some £4,276 p.a. – but they don't point out the hidden creeping charges like eye tests, dental charges or prescription charges.

He would also be eligible for income support, housing benefit and job seekers allowance, amongst a whole raft of other benefits which he may claim in any one year – theoretically these are also worth about £1,100 a year.

But how many years of his working life might Mr Average be in ill health, or his circumstances otherwise change to enable him to benefit from these?

### **Mr Average's goose lays a golden egg**

The cookie cutter articles he reads in the national press about how much tax he can save if he invests in XYZ fund are not actually aimed at him, because they assume he has money to spare – which, as we know, he clearly doesn't because the taxman gets a sizeable chunk of it. Even in a tax-free ISA, his £650 is only earning about £40. And could he trust their suggestions, even if he did have cash to spare? The financial press has already reported on the over-provision of the Venture Capital Trust market – previously feted by the same press as the ultimate investment by offering 40p in the pound tax relief.

Mark Rayden from [www.hoodlessbrennan.com](http://www.hoodlessbrennan.com) suggests investing in a Self-Select ISA this April to take advantage of personal savings tax benefits. He says: "You can maximise tax-efficient growth on your ISA by investing at the start of the tax year rather than the end. Invest early and compounded growth means that £7,000 over five years at 9 per cent growth pa will return £9879 - 67 per cent growth.-But

if you invest at the end of the tax year, the growth would be only 54 per cent a loss of £889 growth."

The question Mr Average really needs to ask himself is this: just how much does he want to work in a society where you work your fingers to the bone just to stand still?

The first thing he needs to consider therefore is his pension. He may not have any disposable income to speak of to invest in a private pension, but because he's likely to pay the necessary qualifying years contributions (44) he will get the current basic state pension of £4,027 p.a. Unfortunately Mrs Average has already missed 15 years contributions through being a full time mother to the Average's two children. As long as she keeps up with payments from now on, she'll get £2,654 p.a. although this is too great to qualify her for an additional pension because of her marital status.

According to Ian Naismith, Head of Pensions Development, at Scottish Widows, it cost between £300-£400 to pay for any missing years National Insurance Contributions. If the Averages used their savings – presuming the state honoured her right to pay them – it would take about eight years to make up her missing years qualifying her for the same pension as her husband. This will give them a £1,373 return on their investment in just 4 years of Mrs Average turning 60.

Having ensured he and his wife won't endure too much hardship in their retirement Mr Average might also consider this. International research from AXA,

the global insurance company, reveals that 24 per cent of British retired people believe that only in retirement are they able to enjoy their lives. More than a quarter of respondents said that this is because they will finally have time to spend on themselves and on the areas and hobbies that really interest them. But why not start now?

### **Mr Average's Ultimate Salary Sacrifice**

Might not Mr Average adopt a unique form of salary sacrifice scheme allowing him to work less for less but still find his net wealth not much worse off? How on earth would he do this? He would find a job for 3-4 days a week which pro-rata paid about £13,500 (in order to fall below the £14,000 Working Tax Credits threshold). In doing so he would incur tax and NIC of £2,651 giving him a net income of £10,848.

But when we add Working Tax Credits and Child Benefit, at £6,214.32 we find his net income comes to £17,062.32. About £50 per week less than when his net income including benefits was £19,591.20. Mrs Average only has to quit smoking to save a third of this figure.

Theoretically, the Averages may also be eligible for Council Tax benefit, which would be possible at some councils, and possibly housing benefit too, if they rented their home, reducing the difference significantly more. Given that Mr Average has already worked 25 years wouldn't this be a fair pay off for the opportunity to enjoy his life, at least until his children leave school? Better to be just below the Plimsol line and rested than just above and worn out.

Mr and Mrs Average could always sell their clutter on eBay for additional income. As long as they don't buy goods to sell i.e trading (and who would know if they did) that income would be tax-free. Either way, it'll mean they'd avoid the landfill tax that makes hiring a skip almost three times more expensive than it otherwise would be.

This is a decision many people may already be making ...

So, what will happen if we all decide to be takers instead of reluctant givers? The goose that's currently laying the golden eggs is going to get strangled ...

This column was first published in Personal Finance and Savings Magazine. [Click here to find out how you can subscribe to the magazine.](#)

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