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Year End Tax Planning Guide

Would you like the opportunity to reduce the taxman's take from your own and your family's income? If so read on, as carrying out an annual review of your tax affairs could significantly reduce your own and your family's tax liabilities.

The period leading up to the end of the tax year on 5 April is one of the best times to review your taxes and finances and indeed taking action prior to the end of the tax year in some cases will give even greater saving opportunities, so do not delay! As always we would be delighted to discuss with you the issues involved and any appropriate action you may need to take.

Tax saving tips for the family

Throughout this publication the term spouse includes a registered civil partner. We have included the relevant amounts for 2015/16. The 2016/17 figures are shown in brackets where these are known and different.

Each spouse is taxed separately, and so it is an important element of basic income tax planning that maximum use is made of personal reliefs and the starting and basic rate tax bands. It may be necessary to consider gifts of assets (which must be outright and unconditional) to distribute income more evenly.

Currently, a transfer of just £1,000 of savings income from a higher rate (40%) taxpaying spouse to one with income below the personal allowance of £10,600 (£11,000) may save up to £400 a year. For those paying the additional rate of tax of 45%, which applies to those with taxable income above £150,000, the saving may be £450 a year.

Tip

It is also possible to transfer part of the personal allowance between spouses. A marriage allowance of £1,060 (£1,100) can be transferred between spouses for 2015/16 onwards where neither spouse pays tax at above the basic rate.

Income from assets jointly owned by spouses is generally shared equally for tax purposes. This applies even where the asset is owned in unequal shares unless an election is made to split the income in proportion to the ownership of the asset. The exception is dividend income from jointly owned shares in 'close' companies which is split according to the actual ownership of the shares. Close companies are broadly those owned by the directors or five or fewer people.

Tip

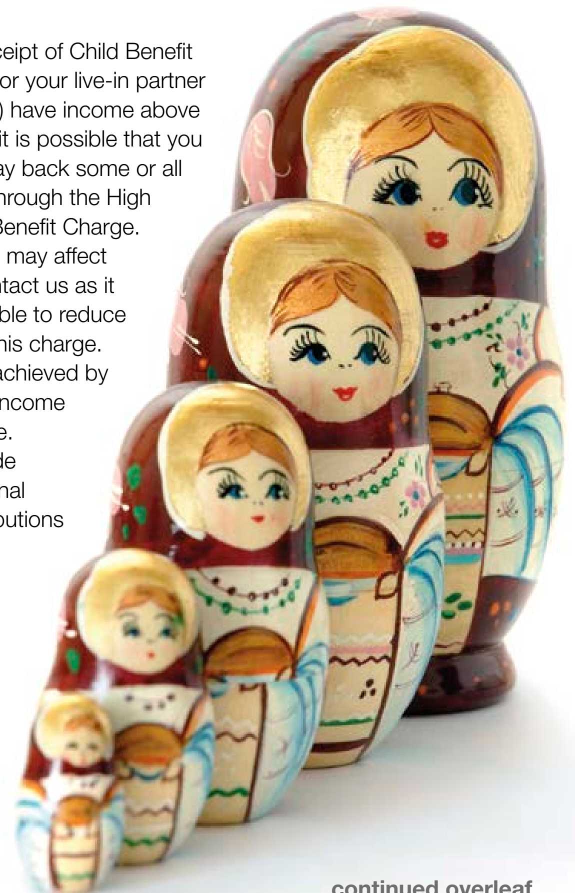
If you are self-employed or run a family company, consider employing your spouse or taking them into partnership as a way of redistributing income. This could be just as relevant for a property investment business producing rental income as for a trade or profession.

Comment

Care must be taken because HMRC may look at such situations to ensure that they are commercially justified. If a spouse is employed by the family business, the level of remuneration must be justifiable and the wages actually paid to the spouse. The National Minimum and Living Wage rules may also impact.

Child Benefit

If you are in receipt of Child Benefit and either you or your live-in partner (widely defined) have income above £50,000, then it is possible that you may have to pay back some or all of the benefit through the High Income Child Benefit Charge. If you think this may affect you please contact us as it might be possible to reduce the impact of this charge. This could be achieved by reducing your income for this purpose. Methods include making additional pension contributions or charitable donations or reviewing how profits are shared and extracted from the family business.



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Children

Children have their own allowances and tax bands. Therefore it may be possible for tax savings to be achieved by the transfer of income producing assets to a child. Generally, this is ineffective if the source of the asset is a parent and the child is under 18. In this case the income remains taxable on the parent unless the income arising amounts to no more than £100 gross per annum.

> **Tip**
>
> Consider transfers of assets from other relatives (eg grandparents) and/or employing teenage children in the family business to use personal allowances and the basic rate tax band.

Remember that children also have their own capital gains tax (CGT) annual exemption (see Capital gains section).

Tax free savings

A Junior ISA (for children born from 3 January 2011) or Child Trust Fund (CTF) accounts offer tax free savings opportunities for children. Existing CTF accounts continue alongside the Junior ISA (a child can only have one type) but can be transferred to a Junior ISA at the request of the registered contact for the CTF.

Both CTF and Junior ISA accounts allow parents, other family members and friends to invest up to £4,080 annually in a tax free fund for a child. There are no government contributions and no access to the funds until the child reaches 18.

Taxation of dividends

When a dividend is paid to an individual, it is subject to different tax rates compared to other income. An individual who has dividend income which falls into the basic rate band has no tax to pay. For higher rate (40% and 45%) taxpayers, the effective tax rates on a dividend receipt are 25% and 30.6%.

From 6 April 2016 the new rates of tax on dividend income will be 7.5% for basic rate taxpayers, 32.5% for higher rate taxpayers and 38.1% for additional rate taxpayers. However a new Dividend Allowance will tax the first £5,000 of dividends received in a tax year at 0%.

There are winners and losers from the new regime.

An example of a winner is a higher rate taxpayer who has dividend income of £5,000. In 2015/16 he will have a tax liability of £1,250 (25% of £5,000). In 2016/17 he will have no tax liability.

An example of a loser under the regime will be the sole shareholder of a company who takes a small salary and then receives dividends up to the threshold at which higher rate tax is payable. In 2015/16 he has no income tax on the salary (as the salary is below the personal allowance) and no tax on the dividend. In 2016/17 only £5,000 of the dividend will not be taxable.

Family companies

If the payment of bonuses to directors or dividends to shareholders is under consideration, give careful thought as to whether payment should be made before or after the end of the tax year. The date of payment will affect the date tax is due and probably the rate at which it is payable.

For many director-shareholders, the tax cost of receiving a dividend next tax year will be higher than the receipt of a dividend this year. If you do not currently extract all the company profits as a dividend you may wish to consider paying higher dividends before 6 April 2016 to utilise the current lower dividend tax rates. However, other tax issues may come into play, for example the loss of the personal tax allowance if your total 'adjusted net income' exceeds £100,000. There will also be non-tax issues such as the availability of funds or profits in the company to pay the dividend.

Please contact us before you make any decisions about changing the amount of dividends taken so that we can advise on the best approach for you.

> **Tip**
>
> Consider the payment of a pension contribution by the company. This is generally tax and NIC free for the employee (but see Pensions section). Furthermore, the company should obtain tax relief on the contribution, provided the overall remuneration package is justifiable.

Loans

It is common in family companies for a director-shareholder to have 'loan' advances made to them by the company (eg personal expenses paid by the company). These are accounted for via a 'director's loan account' with the company which may become overdrawn.

Where the overdrawn balance at the end of an accounting period is still outstanding nine months later a tax charge arises on the company equal to 25% of the loan. Where the balance is repaid there is no tax charge.

Complex rules exist to catch certain arrangements, for example where loan balances are repaid but shortly afterwards the company provides another loan to the shareholder. These rules do not apply where there is a genuine repayment through the award of a valid bonus/dividend.

If you are concerned about whether the tax charge could apply to your company, we would be happy to review this area.

National insurance

For a family business it is generally worthwhile paying wages to a spouse of between the employee lower earnings limit (£112) and the employee threshold (£155) per week. At this level of earnings no NIC will be due. The spouse will still accrue entitlement to a state pension and certain other state benefits.

> **Tip**
>
> A PAYE scheme would be needed to record the employee's entitlement to benefits and the wages.

For the self-employed there is a requirement to pay a flat rate contribution (Class 2). If your profits are low ie £5,965 you will be exempt but you will have the option to pay Class 2 NIC voluntarily at the end of the year. As the contributions are only £2.80 a week it may be advisable to pay the contributions in order to maintain a contributions record. The alternative voluntary Class 3 contributions are £14.10 a week!

Capital gains

No significant changes have been made to the system of capital gains tax (CGT) in 2015/16 so:

- gains (after deduction of an annual exemption) are added to income to determine the rate of CGT
- Entrepreneurs' Relief (ER) gives a 10% tax rate on the first £10 million of qualifying business gains, for each individual over their lifetime
- an 18% rate applies to other gains to the extent that they fall within the basic rate band and 28% rate applies to remaining gains.

Annual exemption

The first £11,100 of gains are CGT free being covered by the annual exemption. Each spouse has their own annual exemption, as indeed do children. A transfer of assets between spouses may enable them to utilise their annual exemptions. Consider selling assets standing at a gain before the end of the tax year to use the annual exemption.

Bed and breakfasting (sale and repurchase) of shares is no longer tax effective but there are two variants which still work:

- sale by one spouse and a purchase by the other
- sale followed by repurchase via an Individual Savings Account.

These techniques may also be used to establish a loss that can be set against any gains.

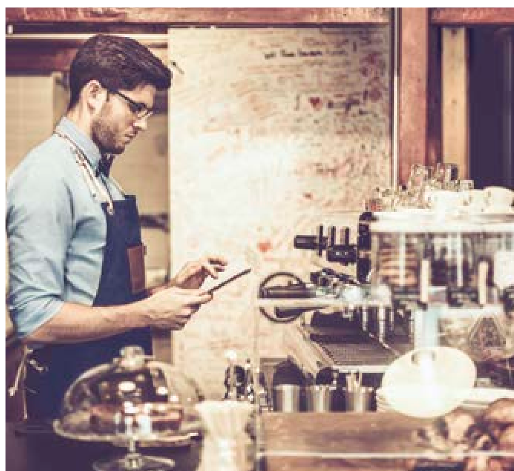
Tip

A capital loss can be claimed on an asset that is virtually worthless. Where the asset is of 'negligible value' by 5 April 2016 the capital loss can be used in 2015/16. There is no need to claim for the loss in the year in which the asset has become of negligible value - if substantial gains are going to be realised in a future tax year, the claim can be delayed until the tax year in which the gains are made.

Capital allowances

Annual Investment Allowance (AIA)

Currently the AIA gives a 100% write off on most types of plant and machinery costs, but not cars, of up to £200,000 per annum from 1 January 2016. Special rules apply to accounting periods straddling January 2016 when the amounts of available AIA changed.



Any costs over the AIA will attract an annual ongoing allowance of 8% or 18% depending upon the type of asset.

Tip

Clearly where full relief is not obtained in the initial period there will be further tax relief in subsequent years but maximising tax relief early has an important impact on tax cash flow.

Please contact us for further advice if you have any plans for new plant and machinery purchases. The timing and method of such acquisitions may be critical in securing the maximum 100% entitlement available.

In addition to the AIA all businesses are eligible for a 100% allowance, often referred to as an enhanced capital allowance, on certain energy efficient plant and low emission cars.

Motor cars

The tax allowance on a car purchase depends on CO_2 emissions. For purchases from April 2013 cars with emissions of up to 130 grams per kilometre (g/km) attract an 18% allowance and those in excess of 130g/km are only eligible for an 8% allowance.

Employee benefits

Cars and fuel

Employer provided car benefits are calculated by reference to the CO_2 emissions and the car's list price. Percentage charges are increasing year on year, and for 2015/16 range from 5% to 37% increasing for 2016/17 to 7% to 37% of the list price of the car.

Tip

Check your position to confirm that an employer provided car is still a worthwhile benefit. It may be better to receive a tax free mileage allowance of up to 45p per mile for business travel in your own vehicle.

Where private fuel is provided, the benefit charge is also based on CO_2 emissions. We can review your procedures to ensure no unnecessary tax charges arise.

Cheap or interest free loans

If loans made by the employer to an employee exceed £10,000 at any point in a tax year, tax is chargeable on the difference between the interest paid and the interest due at an official rate - currently 3%. An exception applies for certain qualifying loans - please contact us for information.

Giving to charity

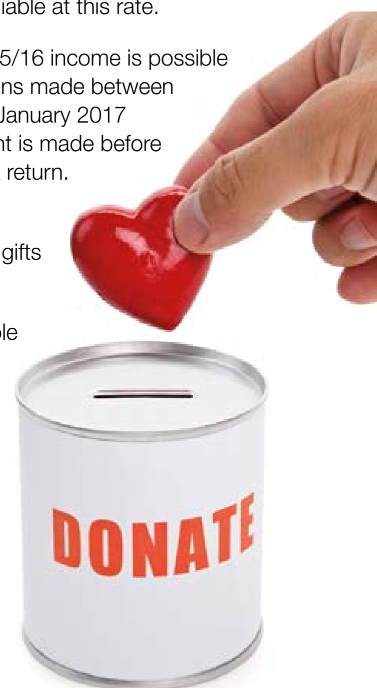
Charitable donations made under the Gift Aid scheme allow a charity to claim back 20% basic rate tax on any donations and if the donor is a higher rate taxpayer they can claim back the tax difference between the higher rate and the basic rate on the donation. Therefore a cash gift of £80 will generate a refund of £20 for the charity so that it ends up with £100. The donor can claim back tax of £20 so that the net cost of the gift is only £60.

Where the 45% additional rate of tax applies, the net cost of the gift in this example would be only £55 for an individual liable at this rate.

Tax relief against 2015/16 income is possible for charitable donations made between 6 April 2016 and 31 January 2017 providing the payment is made before filing the 2015/16 tax return.

Always remember to keep a record of any gifts you make.

It may also be possible to make gifts of quoted shares and securities or land and buildings to charities and claim income tax relief on the value of the gift. This may be tax efficient for larger charitable donations.



Pension contributions

There are many opportunities for pension planning but the rules are complicated and there have been significant changes recently so do check the position before making any decisions.

The rules currently include a standard lifetime allowance of £1.25 million. This figure has to be considered when key events happen such as when a pension is taken for the first time. There is also an annual allowance of £40,000 which sets the maximum amount which can be invested with tax relief into a pension fund. The annual allowance includes employer pension contributions as well as contributions by the individual. Any contributions in excess of the annual allowance are potentially taxable on the individual. Due to changes aligning ‘pension input periods’ with the tax year, some individuals may escape a tax charge if annual contributions in 2015/16 are below £80,000 and significant contributions were made before 9 July 2015.

In addition, many individuals may have unused annual allowances from previous years which can be utilised. Where pension savings in any of the last three years were less than the annual allowance, the ‘unused relief’ is brought forward for use in the current tax year.

Tip

Unused annual allowances are only carried forward for three years but cannot be utilised before the current year’s annual allowance is used up. But once the allowance for the current year is used, the unused allowance from three years prior is used first. Bear this in mind if a substantial pension contribution is being considered.

Tax relief is available on pension contributions at the taxpayer’s marginal rate of tax. Therefore a higher rate taxpayer can pay £100 into a pension scheme at a cost of only £60. An additional rate taxpayer can pay £100 in at a cost of only £55. Indeed for some individuals, due to the complexity of the tax system, the effective relief may actually exceed 45%.

All individuals, including children, can obtain tax relief on personal pension contributions of £3,600 (gross) annually without any reference to earnings. Higher amounts may be paid based on net relevant earnings. There is no facility to carry contributions back to the previous tax year.

Directors of family companies should consider the advantages of the company making employer pension contributions. Additionally, if a spouse is employed the company could make reasonable contributions on their behalf.

From 6 April 2016 the standard lifetime allowance is to be reduced to £1 million. For those with significant pension savings it may be possible to protect an increased pensions entitlement by utilising Fixed or Individual protection. Please contact us for details.

From 6 April 2016 the annual allowance will be tapered for those with adjusted annual incomes (including pension contributions) over £150,000. For every £2 of income over £150,000 an individual’s annual allowance will be reduced by £1, down to a minimum of £10,000

Tip

Clearly, those with expected incomes above £150,000 should be considering using their available current year annual allowance and unused allowances from the previous three years.

We would be happy to advise you on your pensions position.

Investments - are yours tax efficient?

There are a wide range of investments available and we consider some of the main ones with special tax rules.

Individual Savings Accounts

Individual Savings Accounts (ISAs) provide an income tax and capital gains tax free form of investment. The maximum investment limits are set for each tax year, therefore to take advantage of the limits available for 2015/16 the investment(s) must be made by 5 April 2016. An individual aged 18 or over may invest in one cash and one stocks and shares ISA per tax year. The overall total investment is £15,240.

The new Help to Buy ISA offers incentives for those saving for their first home. Available since 1 December 2015, the account enables first-time buyers to save monthly deposits of up to £200, with an opportunity to deposit an additional £1,000 when the account is first opened. The government will then provide a 25% bonus on the total amount invested, including interest, capped at a maximum of £3,000 on savings of £12,000, which is tax free. The bonus can only be put towards a first home located in the UK with a purchase price of £250,000 or less or up to £450,000 in London.

Other investments with tax reliefs

Both the Enterprise Investment Scheme (EIS) and the Seed Enterprise Investment Scheme (SEIS) allow income tax relief on new equity investment (in qualifying unquoted trading companies). For EIS that is 30% relief on investments of up to £1 million and for SEIS up to 50% relief on £100,000. CGT exemption is given on qualifying shares held for at least three years.

Capital gains realised on the sale of any chargeable asset (including quoted shares, holiday homes etc) can be deferred where gains are reinvested in EIS shares.

A capital gain may be relieved potentially saving up to 14% CGT where a qualifying investment is made in the SEIS.

A Venture Capital Trust (VCT) invests in the shares of unquoted trading companies. An investor in the shares of a VCT will be exempt from tax on dividends (although the tax credits are not repayable) and on any capital gains arising from disposal of shares in the VCT. Income tax relief at 30% is available on subscriptions for VCT shares up to £200,000 per tax year so long as the shares are held for at least five years.

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