Paul S. Axcell F.C.A

CHARTERED ACCOUNTANT

10 Springfield Ovington Prudhoe NE42 6EH

Tel: 01661 831490 **Mobile:** 07713 626709

E-mail: paul@axcell.co.uk

Year End Tax Planning Guide

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. Carrying out an annual review of your tax affairs could significantly reduce your own and your family's tax liabilities. As always, we would be delighted to discuss with you the issues involved and any appropriate action you may need to take.

Throughout this publication the term spouse includes a registered civil partner. We have included the relevant amounts for 2016/17.

Fundamental changes to the tax system to take account of this tax year

Savings income

Savings income is income such as bank and building society interest. From 2016/17 the Savings Allowance (SA) applies to savings income. Income within the SA is taxed at a new 0% rate (the 'savings nil rate'). An individual's SA in a tax year will be £1,000, except where:

- they have higher rate income but no additional rate income in the year (in which case their SA is £500)
- they have any additional rate income in the year (in which case their SA is nil).

Alongside the introduction of the SA, banks, building societies and NS&I have ceased to deduct tax from account interest they pay to customers.

Taxation of dividends

When a dividend is paid to an individual, it is subject to different tax rates compared to other income. From 6 April 2016 new rates of tax on dividend income apply - 7.5% for basic rate taxpayers, 32.5% for higher rate taxpayers and 38.1% for additional rate taxpayers. The equivalent tax rates on other income are 20%, 40% and 45%.

However a new Dividend Allowance taxes the first £5,000 of dividends received in a tax year at 0%.

Tip

Be aware of the amount of your entitlement to the SA and the Dividend Allowance. The Dividend Allowance is particularly valuable if you are an investor. Annual dividends of up to £5,000 are tax free no matter what your marginal rate of tax is.

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 2016/17 income is possible for charitable donations made between 6 April 2017 and 31 January 2018 providing the payment is made before filing the 2016/17 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.

Tax saving tips for the family

Each spouse is taxed separately, and so it is an important element of basic income tax planning that maximum use is made of each individual's personal allowance, the starting and basic rate tax band and the SA and Dividend Allowance. It may be necessary to consider gifts of assets (which must be outright and unconditional) to distribute income more evenly.

In 2016/17 the personal allowance is £11,000 and the basic rate band is £32,000.

Currently, a transfer of just £1,000 of savings income from a higher rate (40%) taxpaying spouse, who has used their SA in full, to a basic rate spouse with no other savings income may save up to £400 a year.

> **Tip**
>
> It is also possible to transfer part of the personal allowance between spouses. A marriage allowance of £1,100 can be transferred between spouses for 2016/17 but only 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.

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.

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

Tax free savings

A Junior ISA or a Child Trust Fund (CTF) account 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.

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 this tax year will be higher than the receipt of a dividend last year but generally a dividend will still be more tax effective than paying a bonus. Other tax issues may also need to be considered such as the loss of some or all of the personal tax allowance if total 'adjusted net income' exceeds £100,000.

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 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. The tax charge increased from an amount equal to 25% of the loan to 32.5%, for loans made on or after 6 April 2016. 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.

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.

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.

Landlords and interest relief restrictions

From April 2017, landlords will no longer be able to deduct all of their finance costs from their property income. They will instead receive a basic rate reduction from their income tax liability for these finance costs.

The restriction will be phased in with 75% of finance costs being allowed in 2017/18, 50% in 2018/19, 25% in 2019/20 and be fully in place for 2020/21. The remaining finance costs for each year will be given as a basic rate tax reduction but can't create a tax refund.

Tip

Please note that finance costs do not just include mortgage interest. Interest on loans to buy furnishings and fees incurred when taking out or repaying loans or mortgages are also included.

As the restrictions are being phased in, there is still time to plan to rebalance a property portfolio and the amount of debt financing. Please talk to us if you would like assistance in this matter.

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.

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 a form of investment which is tax free for both income tax and capital gains tax. The maximum investment limits are set for each tax year, therefore to take advantage of the limits available for 2016/17 the investment(s) must be made by 5 April 2017. An individual aged 18 or over may invest in one cash, one stocks and shares and one innovative finance ISA per tax year. The overall total investment is £15,240.

Tip

Bear in mind when considering whether to utilise the ISA investment limit in the current year that with effect from 6 April 2017, the overall ISA subscription limit will rise from £20,000.

Also the new Lifetime ISA will also be introduced in 2017/18. This is intended to allow adults aged under 40 to save up to £4,000 a year towards buying their first home (up to a limit of £450,000), or to save towards their retirement.

Other investments with tax reliefs

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.

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.

Capital gains

Significant changes have been made to the rates of capital gains tax (CGT) in 2016/17:

- for disposals prior to 5 April 2016, CGT rates were 18% on gains falling within the basic rate band. Gains or any parts of gains above the basic rate band limit were charged at 28%
- from 6 April 2016, CGT is charged at the rate of 10% on gains falling within the basic rate band. Gains or any parts of gains above the basic rate band are charged at 20% with a few exceptions. The main exception is a gain on residential property that does not qualify for private residence relief where the previous 18% and 28% rates continue to apply.

Other areas have remained the same as in prior years:

- gains (after deduction of an annual exemption) are added to income to determine the rate of CGT
- Entrepreneurs' Relief gives a 10% tax rate on the first £10 million of qualifying business gains, for each individual over their lifetime.

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 2017 the capital loss can be used in 2016/17. 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.

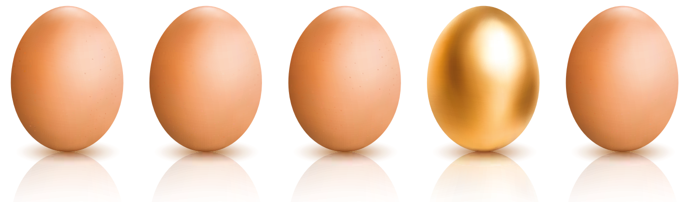
Investors' Relief

A new 10% rate has been introduced in 2016/17. It is aimed at external investors in unlisted trading companies whereas Entrepreneurs' Relief is targeted at directors and employees of such companies. Scenarios in which IR may be attractive to the company raising funds and the investor include:

- asset backed trades which are excluded from EIS and SEIS such as hotels, property development and farming
- larger companies on the Alternative Investment Market. These companies are not regarded as 'listed' and so potentially qualify. Some of these companies could qualify for EIS but EIS is restricted to companies with gross assets of less than £15 million before a further share issue.

Please contact us if you would like further information on Investors' Relief.

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 million. This figure has to be considered when key events happen such as when a pension is taken for the first time. 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.

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.

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.

However, from April 2016, the annual allowance is 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. A lower limit of £10,000 may also apply if you have already started drawing a pension.

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.

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

Disclaimer - for information of users: This newsletter is published for the information of clients. It provides only an overview of the regulations in force at the date of publication and no action should be taken without consulting the detailed legislation or seeking professional advice. Therefore no responsibility for loss occasioned by any person acting or refraining from action as a result of the material contained in this newsletter can be accepted by the authors or the firm.