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Ways to save tax ahead of the 5 April year end

The end of the tax year on 5 April is fast approaching, and this is always a good time of year to think about ways to structure your business and personal finances so that they are as tax-efficient as possible. With new rates and various legislative changes due in the 2016/17 tax year, here are some of the planning strategies you might wish to consider. Do contact us to discuss how you might benefit.

Utilise personal allowances...

Every individual has their own tax-free personal allowance for income tax purposes, which for 2015/16 is £10,600 for those born after 5 April 1938 and £10,660 for those born before 6 April 1938.

Where a spouse or partner has little or no income, transferring income or income-producing assets to them can help to make the best use of their personal allowance. However, take care to avoid falling foul of the settlements legislation governing 'income shifting', and consider the legal consequences of transfers.

Meanwhile, the Marriage Allowance means that, in this tax year, up to £1,060 of an individual's personal allowance may be transferred by eligible spouses and civil partners to their husband, wife or civil partner, where neither pays tax at the higher or additional rate. This can reduce their tax bill by up to £212.

... and beware of the 'hidden' income tax rate

In 2015/16 the 40% higher rate of income tax begins when your taxable income exceeds £31,785. However, if your income exceeds £100,000 you could actually be liable to an effective rate of 60%! This is because your personal allowances are also clawed back by £1 for every £2 by which your adjusted net income exceeds £100,000. An individual with an adjusted net income of £121,200 or more will not be entitled to any personal allowance at all, resulting in an effective tax rate on this slice of income of 60%.

However, with care, it may be possible to reduce your taxable income and retain your allowances. Possible strategies include delaying income into the next tax year or increasing your payments into a pension. Please be sure to contact us for advice tailored to your circumstances.

Future changes

From 6 April, the personal allowance will rise for all to £11,000 for the 2016/17 tax year. The income tax basic rate band will increase from £31,785 to £32,000.

Take advantage of tax-efficient savings vehicles

Continuing low interest rates may have reduced the attractiveness of Individual Savings Accounts (ISAs), but these tax-free savings vehicles remain popular. They have undergone significant changes in recent years, and the rules for investing are now much simpler.

Adult savers can invest in any combination of cash or stocks and shares up to the overall annual subscription limit, which is set at £15,240 in 2015/16. However, an individual may only pay into a maximum of one Cash ISA and one Stocks and Shares ISA each year. You have until 5 April 2016 to make your 2015/16 ISA investment.

In addition, a tax-free Junior ISA (JISA) is available to all UK-resident children under the age of 18 as a Cash or Stocks and Shares product or both. Total annual contributions are capped at £4,080. Funds placed in a JISA will be owned by the child but withdrawals are not permitted until the child reaches adulthood.

Meanwhile, the new Help to Buy ISA offers unique incentives for those saving for their first home. This has been 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 saved, 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 value of £250,000 or less, or up to £450,000 in London.

An individual may only subscribe to one Cash ISA per year, so an account holder cannot subscribe to a Help to Buy ISA and a Cash ISA.

Future changes

There are no planned changes to ISA rates for 2016/17. However, from April 2016 a tax-free Personal Savings Allowance is to be introduced for interest income. This will apply for up to £1,000 of a basic rate taxpayer's savings income and up to £500 of a higher rate taxpayer's savings income each year. It will not be available for additional rate taxpayers, but will be in addition to the tax advantages currently available to savers through the use of ISAs.

Also from April 2016, banks and building societies will no longer automatically take 20% in income tax from the interest earned on individuals' non-ISA savings.

Plan for your pension

Personal contributions to pension schemes attract tax relief worth up to 60%, making them an ideal tax-free investment regime.

To be applied against 2015/16 income, pension contributions must be paid on or before 5 April 2016. Tax relief is available on annual contributions limited to the greater of £3,600 (gross) or the amount of UK relevant earnings, but also subject to the annual allowance. The annual allowance is normally £40,000, but due to changes aligning Pension Input Periods (PIPs) with the tax year, some individuals may escape a tax charge if annual contributions in 2015/16 are below £80,000 and if significant contributions were made before 9 July 2015.

Where pension savings in any of the last three years' PIPs were less than the annual allowance, the 'unused relief' is brought forward, but you must have been a pension scheme member during a tax year to bring forward unused relief from that year. The unused relief for any particular year must be used within three years.

Pensions are notoriously complex and we strongly recommend that you seek professional advice.

Future changes

From April 2016 the Government will introduce a taper to the annual allowance for those with adjusted annual incomes (including their own and their employer's pension contributions) over £150,000. For every £2 of adjusted income over £150,000, an individual's annual allowance will be reduced by £1, down to a minimum of £10,000.

In addition, the overall tax-advantaged pension savings lifetime allowance will be reduced from £1.25 million to £1 million. However, where an individual has significant pension savings, it may be possible to apply for Fixed or Individual Protection 2016. Certain conditions apply – please ask us for further details.

Extracting business profits: dividend or salary/bonus?

When it comes to extracting profit from your company, it is important to consider both the tax and business implications of the various options available.

The question of whether it is better to take a salary/bonus or a dividend requires particularly careful consideration, especially as major changes to the dividend taxation rules will apply for 2016.

A dividend is paid free of national insurance contributions (NICs), whilst a salary or bonus can carry up to 25.8% in combined employer and employee contributions. However, a salary or bonus is generally tax deductible for the company, whereas dividends are not. 5 April 2016 is the last date for paying a 2015/16 dividend, and any higher or additional rate tax on that dividend will not be due until 31 January 2017.

Future changes

The 10% dividend tax credit is set to be abolished from 6 April 2016 and a new Dividend Tax Allowance of £5,000 a year will be introduced. The new rates of tax on dividend income exceeding the allowance will be set at 7.5% for basic rate taxpayers, 32.5% for higher rate taxpayers and 38.1% for additional rate taxpayers.

These rates replace the current effective tax rates of 0%, 25% and 30.6%. While there will still be benefits for a director-shareholder taking a dividend over a salary, the amount of tax saved will be less than under the current regime. You may therefore wish to consider the possibility of increasing your dividends before 6 April 2016, although there may be other tax issues to consider, such as loss of the personal tax allowance if your total adjusted net income exceeds £100,000. Please talk to us about this before taking action.

Company car considerations

Despite increases in tax charges, company cars remain a popular benefit for many employees – and a key business tool for employers. However, tax and national insurance costs could mean that the company car is not the most tax-efficient option for either employer or employee.

The basis for taxing those who use company cars is to tax a figure calculated by multiplying the car's list price by an emissions-based percentage (the 'appropriate percentage'), with a 3% surcharge on diesel powered cars.

Where the employer pays for any fuel used privately by the employee, there is an additional benefit charge calculated by applying the CO_2-based car benefit percentage to the car fuel benefit charge multiplier of £22,100 (2015/16).

You might want to consider carrying out a complete review of your company car policy, as it could prove more beneficial to pay employees for business mileage in their own vehicles at the statutory mileage rates. In some cases, an employer provided 'van' may be a viable alternative to a company car. Please speak to us about the best option to suit your circumstances.

Future changes

From 6 April 2016 there will be a further 2% increase in the percentage applied by each company car band, with similar increases in 2017/18 and 2018/19. For 2019/20 the rates will increase by a further 3%.

From 2016/17, the car fuel benefit charge multiplier will rise to £22,200, while the van benefit charge will increase from £3,150 to £3,170. Meanwhile, the van fuel benefit charge will rise from £594 to £598.

These are just some of the areas where we can provide advice on ways to minimise your tax bill. Others include estate planning to reduce your personal inheritance tax liabilities, and claiming expenses and capital allowances for your business. Please contact us for further assistance.

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Use Annual investment wisely

AIA limit reduced on 01 January 2016 from its previous limit £500, 000, but the new long-term limit is to be £200,000. So the allowance available for the expenditure between 01 January 2016 to 31 January 2016 is only 3/12 * £200,000 = £50,000.

Practical tip Defer your expenditure until next accounting period if it is substantial, thereby increasing the AIA to £200,000.

Employment Allowance

The allowance increases to £3,000 on 06 April 2016, it can be claimed by submitting an EPS showing the employment allowance of £3000.This can be done at the start of the tax year whether or not full amount is used at that time.

Directors salary under employment allowance

There are 2 issues which affect what level of salary produces the best overall outcome,

-Whether director is over pension age or not

-Whether or not individual has other income

	HR tax payer – salary at NI threshold, no other income	HR tax payer – salary at personal allowance, no other income	HR tax payer – salary at NI threshold, no other income £4,000	HR tax payer – salary at personal allowance, other income £4,000
Profit	50,000	50,000	50,000	50,000
Salary	(8,060)	(11,000)	(8,060)	(11,000)
Taxable profit	41,940	39,000	41,940	39,000
CT	8,388	7,800	8,388	7,800
Net Profit	33,552	31,200	33,552	31,200
Dividend	33,552	31,200	33,552	31,200
Tax on dividend	1,921	1,965	2,794	2,765
Tax on savings income	0	0	212	800
Employee NIC on salary		305	0	305
Total tax liability on £50,000 profits	10,309	**10,070**	**11,394**	11,670

Interest on director loan to company

Where a director takes low salary say - £10,000 and the reminder of profit by way of dividend, the starting rate for savings is still available to him. From April 2015, when the starting rate band is £5,000 and the rate reduced to nil, so it is worth considering paying interest on loans made by directors to their companies.

	Low profits: salary £11,000 no interest	Low profits: salary £11,000, £5,000 interest	High profits: salary £11,000 no interest	High profits: salary £11,000, £5,000 interest
Profit	40,000	40,000	60,000	60,000
Interest charge	0	(5,000)	0	(5,000)
Salary	(11,000)	(11,000)	(11,000)	(11,000)
Taxable profits	29,000	24,000	49,000	44,000
CT	5,800	4,800	9,800	8,800
Net profits	23,200	19,200	39,200	35,200
Dividend income	23,200	19,200	39,200	35,200
Total income	34,200	35,200	50,200	51,200
Tax liability on dividends	1,365	1,065	4,365	4,315
Employee NIC on salary	305	305	305	305
Total tax liability	7,470	**6,170**	14,470	**13,420**

Profits extraction in 2015/2016 and 2016/2017

The effective marginal rate of tax on dividends,

	15/16	15/16	15/16	16/17	16/17	16/17
	BR	HR	AR	BR	HR	AR
Dividend paid	1,000	1,000	1,000	1,000	1,000	1,000
Tax credit	111	111	111			
Total	1,111	1,111	1,111			
Dividend Tax	111	361	417	75	325	381
Less: tax credit	(111)	(111)	(111)			
Net tax	0	250	306			
Effective rate on net dividend	0%	25%	30.6%	7.5%	32.5%	38.1%

If total dividend drawn in future exceeds £5,000, tax payer is still better off than drawing the dividends in 2016/2017 until the dividend forgone in 2015/2016 each following sums:

	HR	HR	AR	AR
	15/16	16/17	15/16	16/17
Dividend	21,667	21,667	25,250	25,250
Tax credit	2,407		2,806	
Taxable amount	24,074	21,667	28,056	25,250
Dividend Tax	7,824	5,417	10,521	7,715
Tax credit	(2,407)		(2,806)	
Net tax	5,417	5,417	7,715	7,715

Therefore it is advisable to debit keep debit balance on director's loan account rather than clearing it with dividends before 06 April 2016.

<u>Incorporation advice</u>

The changes will also impact significantly on advice about the incorporation. Although the tax increases on dividend paid do not in most situations take the ax on incorporated business above the tax burden on the incorporated business, the tax saving offered by simple incorporation is certainty lower.

<u>Personal Income Tax and Savings</u>

<u>Rates and limits for tax 2016/2017 and 2015/2016</u>

Transfer of allowance to spouse is appropriate in either 2015/2016 or 2016/2017.Election can be made up to 2 years after end of the appropriate tax year and relates only to the year elected if done retrospectively.

<u>Personal savings allowance</u>

New allowance will be introduced from April 2016 which exempts some savings income from tax for taxpayers. The allowance will be:

- £1,000 for basic rate tax payers
- £500 higher rate tax payers, and
- Nil for additional rate tax payers

<u>Cars – the appropriate percentage for the benefit in kind</u>

The benefit in kind rate applying to company cars with various emissions ratings will be further increased.

<u>Increase in rent a room relief</u>

The amount of rent a room relief will rise from £4,250 to £7,500 from April 2016.The exempt amount is halved if the property is jointly owned.

Removal of wear & tear allowance

From April 2016 the wear and tear allowance will end, to be replaced by a deduction for landlords when they actually spent the money.

Practical tip As the new replacement allowance will be available to all landlords, delaying replacement expenditure until after 5 April 2016 would be benefitted.

Restriction on tax relief on interest in respect of let domestic property.

From April 2017, tax relief in interest in property business will be restricted so that by 2020, interest will not be an allowable expense in computing the profits of the business, but will attract tax relief at 20%.
The change does not affect furnished holiday lettings.

The effective interest deduction will therefore be:

2016/2017 – 100%
2017/2018 – 80%
2018/2019 – 60%
2019/2020 – 40%
2020/2021 – 20%

Practical tip Letting activities that has higher borrowing will badly affected and some solutions for them, - Full incorporation – move properties and loan - Partial incorporation – personal borrowing to invest in shares in a property letting company (but this may be closed as a “loophole”) -Pay down borrowings -Sell up

Pension lifetime allowance

The current limit of 1.25 million will reduce to £1 million in April 2016.

Pension input periods (PIPs) changes

All PIPs come to end on 8 July 2015 (pre – alignment tax year) and new PIPs started all contributors on 9 July and will run to 06 April 2016(post – alignment tax year).

So some of you may have either 2 or 3 PIPs falling in the tax year 2015-2016, depending on when their previous PIP end date was.

Pension annual allowance for 2015 – 2016

There will be annual allowance of £80,000 for all pension savings made in PIPs ending in 2015/2016.So you will be able to save further £40,000 in March 2016 without incurring annual allowance charge.

Restriction of annual allowance for high income individuals

Pension annual allowance will be restricted for high income individuals from April 2016.
The annual allowance of £40,000 will be tapered by £1 for every £2 that the adjusted income exceeds £150,000, up to maximum of £30,000 taper, which will arise at income of £210,000, leaving the tax payer with an annual allowance of £10,000.

ISA and JISA limits

From 6 April 2016 the limits for annual subscriptions will be:

- ISA limit £15,240
- JISA limit £4,080

The flexible ISA

From autumn 2015 individuals will be able to withdraw money temporarily from their ISA and replace it in the same tax year without affecting their overall ISA investment limit for that year.

Capital and Property Taxes

CGT annual exemption

Exempt amount will be £11,100 for 2015/2016.

Capital gain tax – Non resident individuals(NRI)

NRI will be liable to capital gain tax on the disposal of UK residential property from 06 April 2015.

Non resident capital gain tax applies to disposal of UK residential property in a period when a disposer is not UK resident for tax purposes.

Losses on residential property owned by non resident can only be set against gain on the same type of property.

Rollover relief is amended to allow rollover relief where NRCGT gains are reinvested in UK dwellings used in the trade most probably when letting furnished holiday accommodation.

PPR claims – non residents

If you are currently non resident and still own a home in the UK. If the property has ever been their PPR, the exempt period expires on 5 October 2016.The letting relief may also be available in addition to PPR relief but only in relation to the post 2015 gain.

ATED(Annual Tax on Enveloped Dwellings) – increased rates and administrative changes

The rates on ATED on properties valued at more than £2 million have been further increased for 2015/2016.

If you are affected by the reduction in the threshold for ATED are ready to complete ATED returns. These are due by 30 April 2016 for the year ended 31 March 2017.