YEAR END tax planning 2015/16

TIFFIN GREEN

Income tax saving for couples

You might be able to save tax by switching income from one spouse or partner to the other. From the start of the next tax year, you should aim to use up both individuals' personal allowances (£10,600 in 2015/16 and £11,000 in 2016/17) and minimise any higher and additional rate tax.

Income over £150,000 is taxed at 45%, and the personal allowance is withdrawn where income (less certain deductions) is more than £100,000. You and your partner might be able to reorganise your financial affairs to avoid exceeding one of these limits. However, there might be capital gains tax (CGT) to pay on switching ownership of an investment if you are not married or in a civil partnership.

In 2016/17, you will be able to receive £1,000 of savings income tax-free if you are a basic rate taxpayer, and £500 if paying tax at the higher rate. If you or your partner has little or no earnings or pension income, you may also be able to benefit from a 0% tax rate on up to a further £5,000 of savings income. You might be able to shift assets between you to make the best use of these limits, minimising tax on your savings income. In 2016/17, £5,000 of your dividend income will be tax-free regardless of your tax status, so there again could be scope for tax saving by reorganising your shareholdings.

Child benefit – Child benefit is, in effect, withdrawn where either partner has income of £50,000 or more. Withdrawal is total if income is over £60,000, and partial for income between £50,000 and £60,000. You may be able to keep some or all of your child benefit by switching income between you and your partner, or by taking other steps to bring your income below one of these limits.

Partner's salary – If you are in business, you could pay a non-earning partner a salary, on which you will get tax relief. You normally have to keep PAYE records even if the salary is below the national insurance contributions (NICs) limit, which is £486 a month in 2015/16. If, however, the salary is between £487 and £672 a month, your partner will avoid paying any NICs, but will still qualify for state benefits.

As well as salary, you can pay an employer's contribution to your partner's personal pension plan. There is no tax or NICs on the payment itself, and it should be an allowable business expense. Be warned that the total value of your partner's salary, benefits and pension contributions must be justifiable in relation to the work performed. Alternatively, you could plan ahead to share the profits of your business by operating as a partnership in 2016/17. You both need to be genuinely involved as business partners, though not necessarily equally.

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Directors and employees

With the exception of dividends, income over £150,000 is taxed at 45%. You might be able to avoid this additional rate by delaying a bonus until 2016/17 if your income will fall below £150,000 in that year. If your income is less than £150,000 this year but is expected to exceed that figure next year, you could bring forward income into 2015/16 to avoid the additional rate next year.

You can use a similar strategy to keep your income below the level at which you would lose your personal allowance. Alternatively you could sacrifice salary to bring your income below any of the thresholds in exchange for a tax-free employer's pension contribution.

If you are going to work abroad for over a year, it may help to leave the UK before 6 April 2016. You need to be away for a whole tax year for the income from working abroad to be free of UK tax. You will also have to meet the requirements of the statutory residence test, so you should take advice on your particular situation.

This is also a good time to review whether a company car is worth having because the tax on all cars will increase in 2016/17 and again in each of the following three tax years. Switching to a company car with very low CO_2 emissions will save you and your company tax and NICs, as well as reducing other costs.

If your business is affected by the personal service company rules (IR35), it is important to calculate how much salary to draw before 6 April 2016 to avoid being taxed on a 'deemed payment'. If you hold share options, you should look at the tax as well as the investment issues in deciding when to exercise them.

Dividends – The proposed change to the basis of taxing dividends from 2016/17 means that the tax rate on dividends that are not covered by the £5,000 tax-free amount will increase by 7.5% compared to the current year. If you operate your business as a company in which you and your partner both have shares, you could postpone dividends to 2016/17 to benefit from the £5,000 tax-free amount, but otherwise you will generally want to bring dividends forward to 2015/16. Paying a dividend before 6 April 2016 will be beneficial even if it remains within the same tax band, but you will particularly benefit if the dividend will fall into the basic rate band this year for one or both of you, or if at least one of you expects to pay tax at the additional rate next year but not this year.

You could even give shares to your spouse or civil partner shortly before paying a dividend, provided you genuinely transfer ownership. It is advisable to leave as much time as possible between the gift and the subsequent dividend payment.

Self-employed people – You might be able to affect the timing of your taxable profits to avoid paying tax at 45% if you are self-employed, but this will depend on your accounting date.

From 1 January 2016, you can get immediate tax relief on the first £200,000 a year spent on most types of equipment and also many fixtures forming part of a building. Whether this expenditure is made before or after your accounting date may affect the tax rate on your profits. The same goes for the disposal of cars and other equipment.

PLANNING POINT – Given the proposed change to the taxation of dividends, you might want to reconsider any plans to incorporate your business. Although there will still be some tax advantages to incorporation, you will lose the simplicity and cost savings of running a self-employed business.

Capital gains tax planning

Everyone has an annual capital gains tax (CGT) exempt amount, which in 2015/16 makes the first £11,100 of gains free of tax. Gains above the exempt amount are taxed at 18% where taxable gains and income are less than the basic rate limit of £31,785 in 2015/16 and £32,000 in 2016/17. The rate is 28% on gains that exceed this limit.

You should generally aim to use your annual exempt amount by making disposals before 6 April 2016. If you have already made gains of more than £11,100 in this tax year, you might be able to dispose of investments standing at a loss to create a tax loss that can be set against the gains.

If your disposals so far this tax year have resulted in a net loss, the decision whether to dispose of investments to realise gains before 6 April 2016 will depend on the amounts involved. Depending on your level of income, timing your disposals either before or after the end of the tax year could result in more of your gains being taxed at 18% rather than at 28%.

You might be able to save CGT by transferring assets between married couples or civil partners before their disposal. This could save tax where one partner has an unused annual exempt amount, has not fully used their basic rate tax band, or has capital losses available. You should generally leave as much time as possible between the transfer of the assets and their subsequent sale.

CGT is payable on 31 January after the end of the tax year in which you make the disposal. You could delay a major sale until after 5 April 2016 to give yourself an extra 12 months before you have to pay the tax. Shares or assets you own might have become virtually worthless. If so, you can claim the loss against your capital gains without actually disposing of the asset by making a negligible value claim. You can backdate the loss relief to either of the two tax years before the one in which you make the claim, provided that in the earlier year you owned the asset and it was already of negligible value. 5 April 2016 is the time limit for backdating a claim to 2013/14.

Pension tax planning

Investing in a pension plan is usually worthwhile because of the tax privileges. Pension funds are broadly free of UK tax on their capital gains and investment income. Up to a quarter of the fund is normally tax-free, but the pension income will be taxable.

Most people aged 55 and over can draw their pension savings flexibly. Withdrawals above the tax-free amount are liable to income tax at your marginal rate. You should take advice before accessing pension savings as there are several options and they will generally have a long-term effect on your financial position.

Lifetime allowance – The maximum you can hold in a tax-favoured pension scheme is £1.25 million in 2015/16, reducing to £1 million in 2016/17.

Contributions – There is an annual limit of £40,000 on pension contributions that qualify for tax relief. However, you can carry forward unused annual allowances for up to three years to offset against a contribution of more than the annual limit. For people drawing a flexible income from a pension, the annual allowance is reduced to £10,000.

- You can pay up to the whole of your earnings into a pension scheme, but the tax relief is capped by the annual allowance of £40,000 plus any unused allowances brought forward. From 2016/17, the £40,000 allowance will be tapered down to a minimum of £10,000 if your income exceeds £150,000. In preparation for this, transitional rules mean that your actual annual allowance for 2015/16 could be as high as £80,000.
- You don't need earnings to contribute up to £3,600 to a personal pension, so you could set up a pension for your partner or children. This would mean that even if they do not pay any tax they can still benefit from 20% tax relief.
- Tax relief on pension contributions is at least 20%, and if you are a higher or additional rate taxpayer you will get tax relief at 40% or 45%. Limiting your contributions to amounts that qualify for at least 40% tax relief will give you the most benefit.
- Effective relief can be as high as 60% where the personal allowance is being withdrawn, and can be even higher if tax credits are being withdrawn. Pension payments also attract higher rates of relief if, for example, they stop you losing your child benefit or result in some of your dividends no longer being subject to higher rate tax.

PLANNING POINT – With further rises in the state pension age on the cards, low annuity rates and the reduced lifetime allowance, you should keep your retirement savings plans under review to ensure you will have enough income for your needs.

Tax-efficient investments

Some investments have income tax and capital gains tax (CGT) advantages.


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Individual savings accounts – You can invest in one cash individual saving account (ISA) and one stocks and shares ISA in each tax year. The maximum investment is £15,240 in 2015/16, and will stay the same next year. You can invest this in one type of account or split it between the two. ISAs are free of UK tax on investment income and capital gains, and there is a wide choice of investments. An Innovative Finance ISA is to be introduced from 6 April 2016 and this will allow you to bring peer-to-peer lending within the ISA net.

Remember that 16 and 17-year olds can open a cash ISA, but the rules effectively prevent you from opening an ISA for your own children. Parents and others can contribute to a junior ISA for children up to 18 who do not have a child trust fund. The contribution limit is £4,080. Funds are locked in until the child is 18.

Enterprise investment scheme – The enterprise investment scheme (EIS) gives tax relief for investing in new shares in relatively small qualifying trading companies that are not listed on any Stock Exchange.

- Income tax relief is given at 30% on up to £1 million invested in 2015/16.
- Gains on those shares escape CGT after three years.
- It is possible to defer CGT on a gain of any size, on the disposal of any asset, by reinvesting the gain in shares that qualify under the EIS. An EIS investment can be used to defer gains made up to three years earlier.

Seed enterprise investment scheme – Through the seed enterprise investment scheme (SEIS), individuals can get 50% income tax relief on investments of up to £100,000 a year in start-up companies. In addition, potentially half the investment can be matched with gains arising on the disposal of assets in 2015/16, giving total tax relief of up to 64% (50% income tax relief plus 14% CGT relief (half of the higher CGT rate of 28%). To the extent that you did not use up your £100,000 limit in 2014/15, an investment made during 2015/16 can be carried back and relieved as if you had made it in the previous year.

Venture capital trusts – You can obtain income tax relief of 30% by subscribing up to £200,000 for shares in venture capital trusts (VCTs) in 2015/16. Gains are generally exempt from CGT. VCTs are investment trusts that invest in a range of relatively small trading companies. It is important to remember that EIS and SEIS shares and VCTs are high-risk investments. They may be difficult to sell and you should take specialist advice.

PLANNING POINT – Stamp duty rates when purchasing a buy-to-let property or a holiday home (excluding Scottish property) will substantially increase from 6 April 2016, so act quickly if you are thinking of making such a purchase.

Inheritance tax planning

Inheritance tax (IHT) is payable if a person's assets at death, plus gifts made in the seven years before death, add up to more than the nil rate band, currently (and until 2020/21) £325,000. An additional nil rate band, initially set at £100,000, will be introduced from 2017/18 where a main residence is left to direct descendants. There will be protection for people who downsize or sell.

When a surviving spouse or civil partner dies, their estate will benefit from any unused IHT nil rate band of their previously deceased spouse or partner. The transferred proportion is uplifted to the same fraction of the nil rate band in force at the date of the second death. However the maximum transfer is £325,000.

Most IHT planning is not related to the tax year end, though this is as good a time as any to review your will. There are a number of reliefs and exemptions, some of which are related to the tax year.

- Gifts totalling up to £3,000 in a tax year are exempt from IHT. If you made no gifts to use this exemption in 2014/15, you can make IHT-free gifts of up to £6,000 before 6 April 2016. If you have already used your exemption for 2015/16, you could delay your next gift until after 5 April 2016 to take advantage of the 2016/17 exemption.

- Regular gifts out of excess income can also be exempt. You need careful documentation to prove that you make the gifts from income rather than capital.

PLANNING POINT – You could reduce future IHT by investing in business assets that benefit from 100% IHT relief once you have held them for two years. They include shares listed on the Alternative Investment Market.

Charitable giving

You can get tax relief for any gifts to charity if you make a gift aid declaration.

You make the gift out of your taxed income and the charity benefits by claiming back basic rate tax on the value of the gift. Higher and additional rate taxpayers can claim an extra 20% or 25% in relief.

- You can elect for donations made in 2015/16 to be treated for tax purposes as if you had made them in 2014/15. This will benefit you if you paid tax at a higher rate in 2014/15 than in 2015/16. The election must be made in writing at the same time as, or before, filing your 2014/15 tax return and this must not be later than 31 January 2016.

- You can obtain both income tax and capital gains tax relief on gifts to charities of shares listed on the stock market and certain other investments.

- Gifts to charity are free of IHT, so remembering a charity in your will can reduce the total amount of IHT that will be paid on your estate. If 10% of your net estate is left to charity, then the rate of IHT payable will be reduced from 40% to 36%.

✔ CHECKLIST

- ✔ If you are aged over 55, have you taken advice about the options for drawing your pension savings?
- ✔ Have you considered the timing of dividends and bonuses to minimise tax rates?
- ✔ Have you used this year's ISA allowance and made any other tax-efficient investments before 6 April 2016?
- ✔ Could you exempt half of this year's or last year's capital gains by reinvesting the gains in a SEIS?
- ✔ Could you transfer income to your partner to minimise higher and additional rate taxation next year, to maximise the tax-free savings and dividend income limits, or to avoid losing child benefit?
- ✔ Have you used your annual capital gains tax exempt amount by making any available disposals before 6 April 2016?
- ✔ Have you made gifts to use your annual inheritance tax allowances?
- ✔ Are you investing enough in your pension if you wish to, or have to, retire earlier than state pension age, which is likely to keep going up?

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