



CHARTERED CERTIFIED ACCOUNTANTS & BUSINESS ADVISORS



Taxes made easy  
2015/16

# Taxes made easy

clear and concise tax guide  
2015/16

Practical tax tips to guide you through the tax system and help you plan to minimise your liability.

Please use this guide to identify areas where you could take action, then contact us for advice and to discuss the most appropriate way forward.



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# A few essentials

## Introduction

In the UK the greater bulk of income tax which flows into the Exchequer does so by deduction at source. The tax is taken from income before it is paid to the taxpayer and most of this happens by way of Pay-As-You-Earn (PAYE). This collection system will no doubt be familiar to almost everyone who is in employment and also to those who receive pensions.

Most other income tax collected at source currently comes from deductions made by banks or building societies from interest paid to savers. Many of us, including children, the retired and working people, will have savings accounts of one sort or another and many might also have shares from which income arises in the form of dividends. These too are treated as having suffered income tax at source.

As these circumstances cover the overwhelming majority of individuals, more than 80% of the population will have little or no regular contact with HM Revenue and Customs (HMRC), the organisation that administers and regulates all taxes in the UK.

Over 10 million taxpayers have something more than just a regular income taxed under PAYE and interest on savings. Instead they might have income from their own business or receive rent from a property. Alternatively, it may

be that their income is significant enough to attract higher or additional rate tax so that the tax deducted at source on their savings income is insufficient. These taxpayers may be asked to complete a self assessment return each year and then they will have direct contact with HMRC.

### Practical Tip

If you are not asked to complete a tax return, it remains your responsibility to advise HMRC if there is a new source of untaxed income, a capital profit that could lead to a tax liability or you are subject to the high income child benefit charge. Please contact us for further advice if this affects you.

Income tax is not the only means by which the government relieves us of our hard earned cash. You may own assets such as a precious antique, a second home or shares. If such an asset is sold, the chances are that a profit will arise and this may give rise to a liability to capital gains tax.

Details of any capital gains may have to be included on the self assessment return.

Inheritance tax may be payable on the assets that you give to others in your lifetime or leave behind when you die. At one time very few individuals had to worry about this tax.

House price increases over the last two to three decades have changed this and many more estates have now become liable so you may need to consider some planning to minimise this tax.

Many of those in business have to understand the principles of Value Added Tax (VAT) because they will have to act as an unpaid collector of this tax. In addition, those who run their business through a limited company need to know about corporation tax which taxes a company's profits. Employing others in your business brings further obligations with recent changes to PAYE reporting with the introduction of Real Time Information (RTI) and the roll out of Pensions Auto Enrolment. We consider these issues later in this guide.

### Practical Tip

Remember to keep all tax related documents such as interest statements, dividend vouchers, pay certificate form P60 etc. Place everything in a folder through the year as it is received. Then you can simply hand this to us when we need to prepare your self assessment return.

HMRC are increasingly emphasising the importance of good records. Failure to maintain adequate records may lead to inaccurate tax returns, which could result in penalties.

This guide is designed to provide you with a simple guide to all of these taxes from seven perspectives - that of the family; the employee; the person running their own business; the taxation of investments; property matters; disposals and capital gains tax and, finally, knowing that nothing is certain except death and taxes, the potential liability on your estate at death.

Please use the guide to help you identify planning opportunities, pitfalls to avoid and areas where you may need to take action and then contact us for further advice.

## Self assessment (SA) timetable

- Income tax and capital gains tax are both assessed for a tax year which runs from 6 April to the following 5 April.
- Shortly after 5 April - SA returns or a notice to complete a return are issued by HMRC.
- 31 October following - non-electronic returns need to be submitted to HMRC by this date.
- 31 January following - final date for submission of the return and all outstanding tax to be paid.
- There is an automatic penalty for late filing of the return of £100.

- Further penalties may be due if the filing of the return is significantly delayed. These may run into hundreds of pounds.

### Practical Tip

The full £100 penalty will always be due if your return is filed late even if there is no tax outstanding. It is therefore essential to submit the return on time either by 31 October (non-electronic) or otherwise by 31 January following the end of the tax year.



# Family matters

## Married couples

The phrase 'spouse' whenever used in this guide includes a registered civil partner.

Spouses are taxed as independent persons, each of whom is responsible for their own tax affairs. In principle all individuals are entitled to a basic personal allowance before any income tax whatsoever is paid. However, some individuals on high incomes may receive a reduced or even no personal allowance. This is explained further below.

The basic 2015/16 personal allowance is £10,600. The tax bands and rates shown opposite are applied to each spouse separately, so that each may have taxable income up to £42,385 before they start to pay higher rate tax. There is no aggregation of income, no sharing of the tax bands and except in limited circumstances detailed later in this section below the basic personal allowance may not be transferred from one spouse to the other.

### Lossing the personal allowance

Where an individual's total income exceeds £100,000 the personal allowance is reduced by £1 for every £2 of income in excess of that limit. This means that an individual with total taxable income of £121,200 or more will not be entitled to any personal allowance.

### Tax Tip

If your income is in the range £100,000 - £121,200 the restriction in your personal allowance is the equivalent of a tax cost of 60%. You may want to consider making or increasing certain payments which are tax deductible to minimise this tax cost.

Examples include pension contributions (which may be subject to restrictions) and charitable donations.

### 2015/16 Income Tax Rates

£	%
0 - 5,000	0*
0 - 31,785	20**
31,786 - 150,000	40***
Over 150,000	45****

\* Only applicable to savings income.

The 0% rate is not available if taxable non-savings income exceeds £5,000.

\*\* 10% on dividends

\*\*\* 32.5% on dividends

\*\*\*\* 37.5% on dividends

Other income taxed first, then savings income and finally dividends.

### Tax rates

For 2015/16 the basic, higher and additional rates of tax remain unchanged at 20%, 40% and 45% respectively.

A 0% rate band is available for savings income in circumstances where an individual has taxable earned income of less than £5,000.



## Tax Tip

This will increase the number of savers who are not required to pay tax on savings income, such as bank or building society interest. Eligible savers can register to receive their interest gross using a form R85.

The increase will also provide a useful tax break for director-shareholders who extract their share of profits from a company by taking a low salary and the balance in dividends. This is because dividends are taxed after savings income and thus are not included in the individual's 'taxable non-savings income'.

## Tax rates for 2016/17

A new Personal Savings Allowance will remove some savings income from income tax, up to £1,000 of a basic rate taxpayer's savings income and up to £500 of a higher rate taxpayer's income.

Also the dividend tax credit, which is currently 10% of the grossed dividend, will be abolished and a new Dividend Tax Allowance of £5,000 a year will be introduced. The new rates of tax on dividend income above the allowance will be 7.5% for basic rate taxpayers, 32.5% for higher rate taxpayers and 38.1% for additional rate taxpayers.

## Minimising the tax bill

It follows from the basic rules set out above that tax is minimised if spouses equalise, as far as possible, their income so that all personal allowances are fully utilised and higher/additional rates of tax are minimised.

## Example

In 2015/16 Ian and Angela have savings income of £100,000 and no other income.

If this is split equally between them, the total tax bill for the couple is £16,806. If only one spouse has income of £100,000 and the other has nothing, the total tax bill leaps to £28,403 - an additional £11,597!

## Tax Tip

If you are feeling charitable, remember that a donation to charity under the Gift Aid scheme benefits from tax relief. It makes sense for a higher rate/additional rate taxpayer spouse to make such donations so that they can benefit from the extra tax relief.

Alternatively, in some circumstances, donations can be carried back to attract tax relief in the previous tax year.

## Transferable Tax Allowance

From 6 April 2015 married couples and civil partners may be eligible for a new Transferable Tax Allowance.

The Transferable Tax Allowance will enable spouses and civil partners to transfer a fixed amount of their personal allowance to their spouse. The option to transfer is not available to unmarried couples.

The option to transfer will be available to couples where neither pays tax at the higher or additional rate. If eligible, one partner will be able to transfer 10% of their personal allowance

to the other partner which means £1,060 for the 2015/16 tax year.

For those couples where one person does not use all of their personal allowance the benefit will be up to £212 (20% of £1,060).

## Jointly owned assets

Married couples will often own assets in some form of joint ownership. If they do not, then it may be advantageous for tax purposes for transfers to be made to ensure joint ownership.

This can have benefits for income tax, capital gains tax and even inheritance tax.

## Tax Planning

If you and your spouse are both involved in running a business, income can be equalised if you are equal partners or equal shareholders. Alternatively, if only one of you is involved, the other could be employed even if only to use up their personal allowance.

Where assets are owned in joint names any income is deemed to be shared equally between the spouses. If the actual ownership shares are unequal, income is still deemed to be split equally unless an election is made to split the income in the same proportion as the ownership of the asset.

This does not apply to shares in close companies (almost all small, private, family owned companies will be close companies) where income is always split in the same proportion as the shares are owned.

## Example

A buy to let property is owned three quarters by Helen and one quarter by her husband Mark. If no election is made the net rental income on which tax is payable will be split 50:50.

If an election is made the income will be split 75:25. A choice can be made according to which is the most desirable when other income of the spouses is taken into account.

## Capital gains tax

Independent taxation also applies to capital gains tax. Each spouse is entitled to take advantage of the annual exemption of £11,100 before any capital gains tax has to be paid.

This is advantageous where assets are held jointly and then sold as each spouse can use their annual exemption to save tax.

The transfer of assets between spouses is neutral for capital gains tax. This is sometimes done shortly before assets are sold, to minimise tax. Advice should be sought before undertaking such transactions to ensure that all tax aspects have been considered.

Further detail on the operation of this tax is included in the disposals and capital gains tax section of this guide.

## Separation

The breakdown of a marriage will often involve the transfer of assets between spouses. The marriage continues until the divorce is legally finalised but, for transfers of assets to be entirely free of a charge to capital gains tax, the

transfer must be made before the end of the tax year in which the separation takes place.

Separation is deemed to happen when the couple cease to live together as man and wife - quite different to the date the divorce is final, which is often much later.

## Example

If a couple cease to live together on 30 April 2015, transfers of assets must generally be made between them by 5 April 2016 for capital gains tax to be avoided.

Conversely, for inheritance tax, transfers that take place before the divorce is final will continue to be exempt.

There is usually neither tax relief on maintenance payments made by one former spouse to another nor on any payments required by the statutory Child Maintenance Service.

## Children

It is often assumed that children are not taxpayers until they achieve some particular age. In fact HMRC will tax a child just as readily as anyone else if the child has sufficient income to make them liable.

## Transferring income to children

Children have their own personal allowances and tax bands. Where their only income is, at best, a few pounds from a paper round or a Saturday job, there may be some scope for transferring income producing assets to the children to use up their personal allowance.

However, such assets should not be provided by a parent, otherwise the income remains taxable on the parent, unless it does not exceed £100 (gross) each tax year.

## Tax Planning

There is nothing to stop you employing your children in the family business so as to take advantage of their personal allowance. There are age restrictions (with some exceptions the minimum age is generally 13 years old) and legal limitations as to the type and duration of the work. It is also essential that payment is only made for actual work carried out for the business and at a reasonable commercial rate.

## Children and capital gains

Children also have their own annual exemption for capital gains tax so that assets transferred to them which have a bias towards capital growth rather than income may prove to be more advantageous.

## Repayment claims

Where children have significant sources of income from which tax has been deducted, such as bank interest or trust income, they will almost certainly be entitled to a repayment. In such cases a repayment claim should be made.

## Child Trust Funds (CTFs)

The availability of new CTFs ceased from January 2011, as did government contributions to the accounts. Existing CTFs however continue to benefit from tax free investment growth. No withdrawals are possible until the child reaches age 18. However, the child's

friends and family are able to contribute up to the annual limit of £4,080. It is now possible to transfer the investment to a Junior Individual Savings Account.

### Junior ISA (JISA)

A JISA is available for UK resident children under the age of 18 who do not have a CTF account. JISAs are tax advantaged and have many features in common with existing ISAs.

They are available as cash or stocks and share based products but a child can only have one cash JISA and one stocks and shares JISA. The annual investment is limited to £4,080.

### Tax Planning

There are some other limited ways income can be transferred to children tax efficiently such as:

- National Savings Children's Bonds which are tax free.
- Friendly Societies offer 10 year minimum, tax exempt savings plans for children for up to £25 per month.

## High Income Child Benefit Charge

A charge arises on a taxpayer who has adjusted net income over £50,000 in a tax year where either they or their partner are in receipt of Child Benefit for the year. Where both partners have adjusted net income in excess of £50,000 the charge applies to the partner with the higher income.

The income tax charge applies at a rate of 1% of the full Child Benefit award for each £100 of income between £50,000 and £60,000. The charge on taxpayers with income above £60,000 will be equal to the amount of Child Benefit paid.

Child Benefit claimants are able to elect not to receive Child Benefit if they or their partner do not wish to pay the charge.

Equalising income can help to reduce the charge for some families.

### Example

Phil and Jane have two children and receive £1,770 Child Benefit for 2014/15. Jane has little income. Phil's income is over £60,000 for the 2014/15 tax year. So the tax charge on Phil is £1,770.

For 2015/16 the Child Benefit for two children amounts to £1,789 per annum. Phil expects his adjusted net income to be £55,000. On this basis the tax charge will be £895. This is calculated as  $£1,789 \times 50\%$  ( $£55,000 - £50,000 = £5,000 / £100 \times 1\%$ ).

If Phil can reduce his income by a further £5,000 no charge would arise. This could be achieved by transferring investments to Jane or by making additional pension or Gift Aid payments.

## Same-sex couples

All the special rules for married couples, both those dealt with in this section and those covered in other sections of this guide apply

equally to same-sex couples who have entered into a registered civil partnership or marriage.

## What about unmarried partners?

It still pays to equalise income as much as possible, as income tax will be minimised. However, transfers of assets may be liable to capital gains tax and, if substantial, could also lead to an inheritance tax liability. It is vital for unmarried couples to each make a Will if they wish to benefit from each other's estate at death.

### A word of warning

Transferring assets or interests in a business between husband and wife may attract the interest of HMRC especially where it is obvious that it has been done primarily for tax saving purposes. Transfer of ownership of an asset must be real and complete, with no right of return and no right to the income on the asset given up.

If a non-working spouse is given shares in an otherwise one-person, private company, HMRC may, in some circumstances, seek to tax the working spouse on all of the dividends under what is known as the 'settlements legislation'. So you may want to consider obtaining advice from us before entering into this type of arrangement.

### Checklist for Couples

Try to equalise your income.

Consider placing assets in joint names.

If you have children consider making use of their personal allowances.

# Working for others

Few avoid working for others at some time in their life and most will have encountered the PAYE system operated by employers to collect the income tax and national insurance contributions (NIC) due on wages and salaries.

## The tax code

Ensuring the right amount of tax is taken relies on a PAYE code, issued by HMRC and based on information given in a previous self assessment return or supplied by the employer. The employee, not the employer, is responsible for the accuracy of the code.

Code numbers try to reflect both an individual's tax allowances and reliefs and also any tax they may owe on employment benefits. For many employees things are simple. They will have a set salary or wage and only a basic personal allowance. Their code number will be 1060L and the right amount of tax should be paid under PAYE. However, for those who are provided with employment benefits the code number is generally adjusted to collect the tax due so that there are no nasty underpayment surprises. HMRC may also try to collect tax on untaxed income, higher rate tax on investment income and tax owing for an earlier year.

With so many complications and some guess work involved, getting the code exactly right can be difficult and the right amount of tax will not always be deducted.

## Tax Tip

If you are unsure about your code and are anxious not to end the tax year under or overpaid, then you should have it checked. Please talk to us.

## Benefits

The range of benefits available will vary significantly depending on the type of employment. Some attract no tax but even taxable benefits can be efficient as the benefit obtained by the individual can often outweigh the tax cost arising. In addition, for the individual (but not the employer) benefits generally do not attract NIC.

### Company cars

Employer provided cars, commonly known as company cars, remain a popular benefit and for some a real status symbol, despite continued increases in the tax charge they give rise to.

The charge on cars is calculated by multiplying the list price of the car by a percentage which depends on the CO<sub>2</sub> emissions (recorded on the Vehicle Registration Document) of the car. You then pay tax at 20, 40 or 45% on this charge depending on your overall tax position.

The table on the next page shows the percentages for 2015/16. For the majority of



company car drivers the taxable benefit is 2% higher compared to 2014/15.

If the car has a diesel engine the percentage charge is increased by a further 3% supplement (except that it cannot exceed 37%).

## Example

Mark has an Audi A3 TDI (diesel) registered on 1 February 2015. It has an original list price of £20,155 and CO<sub>2</sub> emissions of, say 99 g/km. Mark had extras fitted to the car costing £1,000 (VAT inclusive). In 2015/16 the taxable benefit will be £3,596 ( $[20,155 + 1,000] \times 17\%$ ). If Mark is a higher rate taxpayer the tax due on this will be £1,438.

\* 14% from the table plus 3% diesel supplement.

## Fuel for private use

A separate charge applies where private fuel is provided by the employer for a company car. The charge is calculated by applying the same percentage figure used to calculate the company car benefit to a fixed figure which for 2015/16 is set at £22,100.

2015/16	
CO <sub>2</sub> emissions (g/km)	% of car's price taxed
0 to 50*	5
51 to 75*	9
76 to 94*	13
95	14
100	15
105	16
110	17
115	18
120	19
125	20
130	21
135	22
140	23
145	24
150	25
155	26
160	27
165	28
170	29
175	30
180	31
185	32
190	33
195	34
200	35
205	36
210 and above	37
round emissions down except where*	

## Tax Planning

The fuel benefit charge can be expensive. It may be cheaper for the employee to pay for all the fuel and to reclaim from the employer the cost of business miles driven in a company car based on a specific log of business journeys undertaken.

HMRC publish advisory fuel rates for company cars which are updated on a quarterly basis. See <https://www.gov.uk/government/publications/advisory-fuel-rates> for the latest position or contact us.

### Planning to change your car?

Significant changes to the car benefit rules are planned for 2016/17 to 2018/19 whereby the appropriate percentages of the list price subject to tax will increase by 2% per annum up to a maximum of 37% for all three years.

The existing 3% diesel supplement will be removed from 2016/17.

### Medical insurance

The employee is taxed on the amount of the premium paid by the employer.

### Home and mobile phones

There is no benefit on the provision of a company mobile phone even where it is used privately. However, this is limited to one phone per employee.

Where home telephone bills are paid by the employer, the amount paid will be taxable. The employee may make a tax deduction claim for the cost of business calls only but not the line rental.

## 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.

### Tax Tip

The £10,000 limit on tax free loans is an attractive perk for many employees.

## Childcare costs

Childcare costs paid for by an employer are exempt from both income tax and NIC. This applies to a place in an employer operated nursery or where the employer pays for registered or approved childcare as long as the scheme meets certain requirements. In the latter case the exemption is limited to a maximum of up to £55 per week depending on when the employee first receives employer supported childcare and their tax position. Any excess amounts are subject to tax and NIC.

## New Tax-Free Childcare scheme

The scheme for employer supported childcare is expected to be replaced by a new Tax-Free Childcare scheme to be phased in from early 2017. The scheme will be available to families where all parents are working and meet a minimum income level with each earning less than £150,000 a year. Parents who are receiving support through Tax Credits or the Universal Credit will not be eligible.

Parents will need to register with the government and open an online account with National Savings and Investments. The government will then 'top up'

payments into this account at a rate of 20p for every 80p that families pay in. The scheme is limited to £10,000 per child per year. The government's contribution will be a maximum of £2,000.

### Pension Contributions

Contributions by an employer to a registered pension scheme are generally tax and NIC free for most employees. This may be far better than any other perk.

#### Tax Tip

You may want to sacrifice some of your 'normal' salary to do this. Please talk to us to make sure your salary sacrifice scheme is effective.

## Expense payments

### Reimbursed expenses

Reimbursed expenses are taxable as a benefit but the employee can claim a deduction for those expenses incurred wholly, exclusively and necessarily for business purposes. The overall effect is usually neutral.

What happens is that at the end of each tax year the employer sends a summary, to HMRC, of all benefits provided on a form P11D for each employee. As well as the benefits covered earlier, this form will include all reimbursed expenses.

The employee can then make an expense claim to HMRC either on a self assessment return

or by letter for any business expenses so that these are not taxed.

Often nothing is taxable, so employers can ask to be excluded from the expense reporting process if they apply to HMRC. This is known as a dispensation. The government has announced that it plans to abolish dispensations and replace them with a statutory exemption for expenses.

### Mileage claims

Many employers pay a standard rate of mileage to all employees who use their own cars for business journeys. HMRC set statutory rates for business mileage which are 45p for the first 10,000 miles in a tax year and 25p thereafter.

If the employee is paid for business miles at less than the statutory rates, tax relief is available on the difference. If, however, the employee is paid at more than these rates then the excess is taxable.

If you are paid less than the statutory rates to use your own car for business purposes remember to claim a deduction on your return or write to HMRC to make your claim.

### Example

In 2015/16 Michael travels 14,100 business miles in his own car and is paid 32p per mile by his employer.

Michael can claim tax relief on an additional amount of £1,013  $((10,000 \times 45p) + (4,100 \times 25p)) - (14,100 \times 32p)$ .

### Vans

Where employees are provided with a van and the only private use of this is to travel to and from work (including any incidental private use), then no taxable benefit should arise. If there is private use beyond this, there is a benefit of £3,150 for 2015/16 and an additional £594 if fuel is provided for private as well as business journeys. In order to avoid this charge, it is advisable to have a formal written policy, detailed mileage logs and make use of vehicle tracker records. These will support the limited private use of the van and may avoid problems with HMRC in the future.



# Running a business

Starting up a business of your own is a big step and not one to take lightly. The taxation of your business is only one of many commercial and legal aspects of starting a business that you will need to consider.

Preparation is the key and a proper business plan is one of the first things you should do. However, tax matters are our main concern here.

## Choosing a business structure

The alternative business structures are:

### **Sole Trader**

This is the simplest form of business structure since it can be established without legal formality.

The business of a sole trader is not distinguished from the proprietor's personal affairs. If the business incurs debts which are unpaid, the creditors can seek repayment from the sole trader personally.

### **Partnership**

A partnership is similar in nature to a sole trader but involves two or more people working together.

A written agreement is essential so that all partners are aware of the terms of the

partnership. Again, the business and personal affairs of the partners are not legally separate.

Sole traders and partnerships are often referred to as unincorporated businesses and the individual owners as self-employed.

### **Limited Company**

A company is a legal entity in its own right, separate from the personal affairs of the owners and the directors.

A company provides protection from liability, which means that the creditors of the company cannot make a claim against the owners or the directors except in limited circumstances. Often this advantage is somewhat eroded because a bank, for example, may seek personal guarantees from the directors.

These potential advantages carry the downside of greater legal requirements and regulations that must be complied with.

### **Limited Liability Partnerships (LLPs)**

LLPs are a halfway house between partnerships and companies.

They are taxed in the same way as a partnership but are legally a corporate body. This again gives some protection to the owners from the partnership's creditors.

In this section we consider the differing tax treatments of the alternatives but you should

choose which structure is right for you based on more than just the tax issues alone.

## The tax regime

### **Unincorporated businesses**

A new business should register with HMRC on commencing to trade. Income tax is paid on the profits of the business. The amount that the proprietor, or a partner in a partnership, draws out of the business (referred to as 'drawings') is irrelevant.

Profits are taxed on a current year basis as shown by the example, although a new business will be subject to special rules, which we will be pleased to explain to you.

### **Example**

If the accounting period (or 'year') end is 31 March then, in the tax year 2015/16, the profits for the year ended 31 March 2016 will be taxed.

If the year end was 31 August then, in the tax year 2015/16, the profits for the year ended 31 August 2015 will be taxed.



### Tax Tip

The choice of accounting date on a business start up can affect:

- how profits are taxed
- when tax is payable
- when losses are relieved.

So do contact us to discuss the options available for your circumstances.

### Working out profits

Profits are calculated using accepted accounting practices and crucially this means that profit is not necessarily simply receipts less payments. Instead it is income earned less expenses incurred. However see details of the optional cash basis for smaller unincorporated businesses.

Not all of the expenses that a business incurs are allowed to be deducted from income for tax purposes but most are. It is important that you keep proper and comprehensive business records so that relief may be claimed.

### Tax Tip

Try to incur expenditure just before rather than just after the year end, as this will accelerate the tax relief.

Examples of the type of expenditure to consider bringing forward include building repairs and redecorating, advertising and marketing campaigns and expenditure on plant and machinery.

### Cash basis for smaller unincorporated businesses

An optional basis for calculating taxable profits is available to small unincorporated businesses. If an owner of a business decides to use the cash basis, the business profits would be taxed on cash receipts less cash payments of allowable expenses subject to a number of tax adjustments.

The optional scheme requires an election by the business owner and is only available where the business receipts are less than the VAT registration threshold (or twice that for recipients of the new Universal Credit).

A bit more detail of the scheme:

- Cash receipts include all amounts received in connection with the business including those from the disposal of plant and machinery. The good news is that if a customer has not paid

what is owed by the year end, the amount due is not taxable until next year.

- Allowable payments include paid expenses but these still need to meet the existing tax rule of being wholly and exclusively incurred for the purposes of the trade.
- Payments include most purchases of plant and machinery, when paid, rather than claiming capital allowances. The bad news is that if a supplier is not paid by the year end, the amount is not relieviable until next year.
- Interest payments are only allowed up to a limit of £500.
- Business losses may be carried forward to set against the profits of future years but not carried back or set off 'sideways' against other sources of income.

Do get in touch if you would like us to consider if this optional scheme is appropriate for you and your business.

### Capital allowances

When assets are purchased for the business, such as machinery, office equipment or motor vehicles, capital allowances are available. As with expenses, these are deducted from income to calculate taxable profit.

### Plant and machinery - Annual Investment Allowance (AIA)

The AIA gives a 100% write off on most types of plant and machinery costs, but not cars, of up to £500,000 per annum for the period 1/6 April 2014 to 31 December 2015. From 1 January 2016 the AIA will be set 'permanently' at £200,000.

Where a business has a chargeable period which spans 1 January 2016 there are transitional rules for calculating the maximum AIA for that period and there will be two important elements to the calculations:

- a calculation which sets the maximum AIA available to a business in an accounting period which straddles 1 January 2016
- a further calculation which limits the maximum AIA relief that will be available for expenditure incurred from 1 January 2016 to the end of that accounting period.

### Example

The maximum AIA for a business with a 31 March 2016 will be:

9 months to December 2015 three quarters of £500,000	£375,000
---	----------

3 months from January 2016 one quarter of £200,000	£50,000
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Total annual AIA using first calculation	£425,000
---	----------

This is still a generous figure. However if expenditure is incurred between 1 January and 31 March 2016 the maximum amount of relief will only be £50,000. This is because of the restrictive nature of the second calculation.

Businesses are eligible for a 100% allowance, on certain energy efficient plant and low emission cars.

### Motor cars

The tax allowance on a car purchase depends on CO<sub>2</sub> emissions. For purchases from April 2013 cars with emissions of up to 130g/km attract an 18% allowance and those in excess of 130g/km are only eligible for an 8% allowance. For purchases prior to April 2013 (but after April 2009) the emissions limit was 160g/km for the 18% allowance.

### Paying the tax

The self-employed may have to pay tax and NIC three times a year, namely:

- 31 January in the tax year
- 31 July following the tax year
- 31 January following the tax year.

In certain circumstances, the first two payments can be waived.

### Employer obligations

As an employer you will have many responsibilities. These will include employment law requirements which are not covered in this guide and HMRC requirements to report pay and details of expenses and benefits. There are two developments which place a further burden on employers.

### Real Time Information

Real Time Information (RTI) reporting is mandatory for broadly all employers.

Under RTI employers or their agents are required to make regular payroll submissions for each pay period during the year detailing payments and deductions made from

employees generally on or before the date they pay the employees.

The RTI submission details payments made which include salary, overtime and statutory payments such as statutory maternity pay. It also details the income tax, national insurance contributions (NIC) due together with other deductions such as student loan repayments.

The PAYE and NIC on salaries is payable monthly (or quarterly where the amount due is less than £1,500 per month).

Penalties apply to employers who fail to make returns on time. These penalties range from £100 to £400 per month depending on the size of the employer. Interest and penalties also apply for failing to pay on time.

The employer must also report details of expenses and benefits provided to employees. More information on the valuation of benefits is contained in the Working for Others section of this guide.

### Pensions Auto Enrolment

The introduction of Pensions Auto Enrolment places new duties on employers to automatically enrol 'workers' into a work based pension scheme. Employers have to comply with their obligations from a designated staging date (which varies by size of employer and PAYE reference).

The employer's duties include:

- assessing the types of workers in the business
- providing a qualifying automatic enrolment pension scheme

- automatically enrolling all 'eligible jobholders' into the scheme
- and paying employer contributions.

All employers will need to contribute at least 3% of the 'qualifying pensionable earnings' for eligible jobholders. However, to help employers adjust, compulsory contributions will be phased in, starting at 1% before eventually rising to 3%.

If the employer only pays the employer's minimum contribution, employees' contributions will start at 1% of their salary, before eventually rising to 4%. An additional 1% in the form of tax relief will mean that there is an overall minimum 8% contribution rate.



### Practical Tip

All employers have to plan for and implement Auto Enrolment. We can help you to deal with this process and advise you of your staging date.

## Companies

Unlike sole traders and partnerships who pay tax on profits only (and drawings are ignored), companies have two layers of tax. The first is tax payable by directors and shareholders on money they take out of the company and the second is corporation tax which is due on the company's profits.

### Practical Tip

If you operate as a limited company, there is a legal separation between you as the owner and the company itself. This means you cannot use the company bank account as if it were your own! This requires a certain amount of discipline without which all kinds of legal and tax related difficulties can occur.

## Corporation Tax

Companies pay corporation tax at 20% from 1 April 2015.

### Tax on 'drawings'

Directors of a company will normally be paid a salary and this is taxed under PAYE as for all employees. The cost of this, including the employer's NIC, is generally an allowable expense of the company. Shareholders of the

company in contrast may be rewarded by the payment of dividends on their shares.

### Tax Tip

In most small companies the directors and shareholders are one and the same and so they can choose the most tax efficient way to pay themselves. Using dividends can result in savings in NIC. This requires planning. Please talk to us to decide the best options for you.

## Warning - close company loans to participators

A close company (which generally includes owner managed companies) is taxed in certain circumstances when it has made a loan or advance to individuals or their family members who have an interest or shares in the company (known as participators). The tax charge is 25% of the loan if it is outstanding nine months after the end of the accounting period. The tax charge is repaid to the company nine months after the end of the accounting period in which the loan is repaid.

Further rules prevent the avoidance of the charge by repaying the loan before the nine month date and then effectively withdrawing the same money shortly afterwards.

A '30 day rule' applies if at least £5,000 is repaid to the company and within 30 days new loans or advances of at least £5,000 are made to the shareholder. The old loan is effectively treated as if it has not been repaid. A further rule stops the tax charge being avoided by waiting 31 days before the company advances further funds to the shareholder. This is a

complex area so please do get in touch if this is an issue for you and your company.

### Planning Tip

Ensure that sufficient salary and dividends are drawn from the business to prevent these charges arising unnecessarily on an overdrawn director's current account. We can also ensure that overdrawn accounts are cleared properly. Please contact us if you would like to discuss the right options for you and your business.

### Tax on profits

The profits of a limited company are calculated in a similar way as for unincorporated businesses and the same rules with regard to expenses and capital allowances generally apply. Remember though that the salaries paid to directors, but not the dividends paid to shareholders, are deductible from the profits before they are taxed.

### Tax Planning

In recent years companies have become more popular as they have usually resulted in less tax being paid overall. From April 2016, a new taxation system applies to dividends and this may affect the decision as to whether to trade as a limited company.

We would be happy to discuss the implications of incorporation with you, before you decide whether or not to incorporate your business.

### Payment of tax

Corporation tax is usually payable nine months and one day after the year end, so the choice of accounting date has no tax consequence.

### Practical Tip

HMRC issue toolkits on various tax topics to help taxpayers and their agents comply with tax law. One of the main areas of non-compliance identified by HMRC is poor record keeping and this applies to all types of business. If you would like guidance on what records to keep please get in touch.

### Income shifting

Over recent years, many families have been attracted by the savings that can be made by combining small salaries and large dividends. The savings could be increased by introducing a non-working family member into the business as a shareholder or co-owner, to use up their personal allowance and lower rates of tax.

Care needs to be taken as rules aimed at counteracting this in the 'settlements legislation' could be used to challenge certain arrangements. If you have any questions or concerns, please do not hesitate to contact us.

### Value Added Tax (VAT) and your business

VAT is a tax ultimately paid by the final consumer and businesses act as the collectors of the tax. There are heavy fines for failing to operate the system properly.



### What does VAT apply to?

VAT is chargeable on the supply of goods and services in the UK when made by a business that is required to register for VAT.

A registered business must charge VAT on its sales which is known as output VAT. There are currently three rates of VAT which can be payable on what are known as taxable supplies. These are the standard rate of 20%, the reduced rate of 5% and the zero rate.

The zero rate applies where the supply is deemed to be subject to VAT but the output VAT is charged at 0%, meaning that no VAT is actually payable.



However, a business also pays VAT on the goods and services it buys. This is known as input tax.

If the output tax exceeds the input tax, then a payment of the difference has to be made to HMRC. This calculation is normally done quarterly. If input tax exceeds output tax a repayment of VAT will be made.

This calculation is also done quarterly except that if repayments occur regularly this can be done monthly. Regular repayments would perhaps apply where a business generally makes zero rated supplies.

### Supplies

Certain supplies of goods and services are not subject to VAT at all and are known as exempt supplies. A business that makes only exempt supplies cannot register for VAT and will be unable to reclaim any input tax.

### Tax Tip

When you first register for VAT you can reclaim input tax on goods purchased up to four years prior to registration provided they are still held when registration takes place. VAT on services supplied in the six months prior to registration may also be reclaimed.

As there are three rates which can be applicable to taxable supplies, standard, reduced or zero rated, it is important to identify the type of supplies correctly and apply the correct percentage of VAT.

Some input VAT is not reclaimable by a VAT registered business. Two common examples are VAT incurred on entertaining UK business customers and VAT on the purchase of a car.

### Do I need to register?

A business must register if its taxable supplies exceed an annual figure, currently £82,000. If taxable supplies are less than this a business may still register voluntarily. So, for example, if the business makes only zero rated sales, it can still register and reclaim the input tax suffered.

VAT can affect competition. A plumber, for example, who sells only to the general public, will be at a disadvantage if he has to register for VAT.

He may have to charge up to 20% more than a plumber who is not registered to earn the same profit.

On the other hand, if the same plumber only works for other VAT registered businesses, such as building companies, then it will not

matter whether he is registered because the customer will be able to recover the VAT that is charged.

Indeed, in general, a business that always sells to other VAT registered businesses will normally register, even if below the annual limit, because then it can reclaim VAT on purchases and expenses.

This will improve profit and can be especially relevant for new businesses because there are often high initial set up costs that carry VAT.

On the other hand, registration comes at the cost of having to meet onerous record keeping requirements, a need to submit online VAT returns and pay online and on time. As well as a fundamental need to get it right!

Failure on any of these points exposes the business to penalties which, in some cases, can be substantial.

### Tax Planning

You should consider carefully whether to register voluntarily. If the VAT at stake is relatively small the responsibilities of registering may outweigh the benefit.

### Practical Tip

There are various VAT schemes designed to reduce administration and/or improve cash flow for the smaller business so do contact us for further information.

# Tax and your investments

Setting aside income in the form of savings is important for us all, to provide for the unexpected or to build up a nest egg that we can enjoy in retirement.

## Pensions

Pensions are one of the most tax efficient forms of saving. Most higher rate taxpayers can contribute £100 to a registered pension fund at a cost of only £60 and investment income and capital gains will accrue within the scheme largely tax free.

An individual is entitled to tax relief on personal contributions in any given tax year up to the higher of 100% of earned income or £3,600 (gross).

The contributions are paid net of basic rate tax and the pension provider will then recover that basic rate tax from HMRC. Higher and additional rate relief, if appropriate, can be claimed from HMRC. Contributions in excess of the individual's limit can be made into a scheme but the excess will not attract tax relief.

An employer may make contributions to a scheme and a deduction from profits may be available to the employer.

As these reliefs are generous, there are controls which serve to limit high levels of contribution. These are complex but, put simply, they may give rise to a tax charge if annual contributions

exceed £40,000 or if the value of the fund when benefits are taken is greater than a lifetime allowance which, for 2015/16, is £1.25 million (reducing to £1 million from 6 April 2016). Due to changes to the annual allowance system from April 2016, some individuals may escape a tax charge if annual contributions are below £80,000 and significant contributions were made before 9 July.

The rules which apply to accessing personal pension funds have been amended from April 2015. These now allow for more flexibility. Taxpayers have always had the option of taking a tax free lump sum of 25% of fund value and purchasing an annuity with the remaining fund, or opting for income drawdown where limits generally applied.

An annuity is taxable income in the year of receipt. Similarly any monies received from the income drawdown fund are taxable income in the year of receipt.

From 6 April 2015, the ability to take a tax free lump sum and a lifetime annuity remains but some of the previous restrictions on a lifetime annuity have been removed allowing more choice on the type of annuity taken out.

The rules involving drawdown have been changed. There is now total freedom to access a pension fund from the age of 55. Access to the fund may be achieved in one of two ways:



- allocation of a pension fund (or part of a pension fund) into a 'flexi-access drawdown account' from which any amount can be taken over whatever period the person decides
- taking a single or series of lump sums from a pension fund (known as an 'uncrystallised funds pension lump sum').

When an allocation of funds into a flexi-access account is made the member typically will take the opportunity of taking a tax free lump sum from the fund.

The person will then decide how much or how little to take from the flexi-access account. Any amounts that are taken will count as taxable income in the year of receipt.

Access to some or all of a pension fund without first allocating to a flexi-access account can be achieved by taking an uncrystallised funds pension lump sum.

The tax effect will be:

- 25% is tax free
- the remainder is taxable as income.

Getting the right advice at the point of retirement is therefore important.

## Tax free savings

### Individual Savings Accounts (ISAs)

ISAs are free of income tax and capital gains tax. There are maximum investment limits which apply for each tax year but, over several years, large investments can be built up. From 6 April 2015 the overall annual ISA savings limit is £15,240. From 1 July 2014 ISAs were reformed into a simpler product and all existing ISA are able to benefit from the revised investment options.

### Investment choices

Investors are not allowed to invest in more than two separate ISAs in each tax year; a cash ISA and a stocks and shares ISA. Savers are able to subscribe any amounts into a cash ISA or a stocks and shares ISA subject to not exceeding the overall annual investment limit.

Investors are able to transfer their investments from a stocks and shares ISA to a cash ISA (or vice versa).

Details of the new Help to Buy ISA are in the Property Matters section of the guide.

## Other tax efficient investments

The following investments work in varying ways. You should consider your needs in detail before entering into any commitments.

### National Savings and Investment (NS&I) Premium bonds

Premium bonds are tax free and you could win £1 million!

However, the annual rate of return is not predictable. The Premium bonds investment limit from 1 June 2015 is £50,000. The more you invest the more frequently you are likely to win, the smaller prizes at least. However, there is no guarantee of a steady rate of return.

### Single premium insurance bonds

These provide a means of deferring income into a subsequent period when it may be taxed at a lower rate.

### The Enterprise Investment Scheme (EIS)

Income tax relief at 30% is available on new equity investment (in qualifying unquoted trading companies) of up to £1 million in 2015/16. A capital gains tax (CGT) exemption may be given on sales of EIS shares held for at least three years. If the gain on the sale of any chargeable asset (eg quoted shares, second homes, etc) is reinvested in EIS shares, the gain on the disposal can be deferred.

## Tax Planning

It is also possible to obtain income tax relief in the previous tax year for qualifying purchases. Shares acquired up to the annual limit for the previous year at any time in the current tax year may be carried back for tax relief. This may be beneficial where tax relief would otherwise not be obtained due to a low current tax year liability.

### Venture Capital Trusts (VCT)

These bodies invest in the shares of unquoted trading companies. An investor in the shares of a VCT will be exempt from tax on dividends and on any capital gain arising from disposal of the shares in the VCT. Income tax relief currently 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.

### Seed Enterprise Investment Scheme (SEIS)

A more recent addition to the available schemes is SEIS. The tax breaks for the investor are:

- income tax relief at 50% in respect of qualifying SEIS shares up to an annual maximum investment (in all SEIS companies) of £100,000
- a CGT exemption where SEIS shares are sold more than three years after they are issued (as for EIS)
- a further CGT exemption of 50% where an individual makes a capital gain in 2015/16 and reinvests the gain in qualifying SEIS shares before 6 April 2016.

# Property matters

Direct investment in residential property has always been a popular form of investment.

## Buy to let

The UK property market, whilst cyclical, has proved over the long-term to be a successful investment. This has resulted in a massive expansion in the buy to let sector.

Traditionally, buy to let involves investing in property with the expectation of capital growth with the rental income from tenants covering the mortgage costs and any outgoings. However, the gross return from buy to let properties, the rent less expenses, can change. Investors also need to take a view on the likelihood of capital appreciation exceeding inflation. Investors should take a long-term view and choose properties with care.

### Practical Tip

When choosing between investments always consider the differing levels of risk and your requirements for income and capital in both the short and long term. An investment strategy based purely on saving tax is not appropriate.

### Which property?

Investing in a buy to let property is not the same as buying your own home. You may wish to get

an agent to advise you of the local market for rented property. An agent will also be able to advise you of the standard of decoration and furnishings which are expected to get a quick let.

Letting property can be very time consuming and inconvenient. Tenants will expect a quick solution if the central heating breaks down over the bank holiday weekend! Do not cut corners - a correctly drawn up tenancy agreement will ensure the legal position is clear.

### Tax on rental income

Income tax will be payable on the rents received after deducting allowable expenses. Allowable expenses currently include mortgage interest, repairs, agent's letting fees and an allowance for furnishings where the property qualifies as 'furnished'.

### Changes ahead

The government has announced proposals to restrict the amount of income tax relief landlords can get on residential property finance costs to the basic rate of income tax. This restriction will be phased in over four years from April 2017.

From April 2016 the allowance for furnishings will be no longer be available. However residential

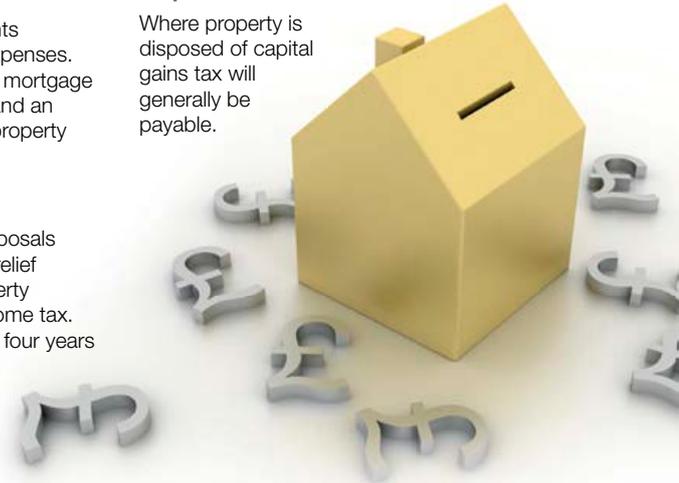
landlords will be able claim the actual costs of replacing furnishings.

### Tax Tip

The restrictions on loan interest will be an unwelcome development for landlords paying higher or additional rate of tax. For many investors, the restriction on loan interest relief will materially alter their attitude to the amount of debt taken on.

### Disposal

Where property is disposed of capital gains tax will generally be payable.



This is payable on the difference between the sale proceeds and the original cost. Where property has been improved then these capital costs may be available to reduce the value of the gain. The CGT annual exemption results in the first £11,100 of gains, for 2015/16, being tax free. CGT is payable at 18% or 28% on gains depending on the level of your income. This is further explained in the next chapter.

## Main residence

An individual's or married couple's only or main residence is generally exempt from CGT. The exemption extends to grounds of up to half a hectare provided this is not used for any other purpose. There must also be clear evidence of occupation as a main residence and not just ownership.

### Tax Planning

Larger grounds may also be exempt, as can the sale of part of the garden or grounds for development. However, professional advice is recommended to plan for the best outcome.

Subject to exceptions, periods of absence are chargeable but, if the main residence was let during absences, as a result of which a charge arises, a 'letting relief' may apply to reduce the chargeable gain.

### More than one residence

Where an individual (or married couple) have two or more residences, only one residence at any one time can be treated as the main home for exemption. This is done by an election.

Provided a particular residence has been the main home at some time, then the last 18 months of ownership will always be exempt. This applies even if another residence has now become the main home during this time.

### Example

Joe has a house in Luton which is his principal private residence and which he has owned for eight years. Fed up with commuting he buys a flat in central London and elects for this to be his main residence. Exactly five years later he sells his home in Luton.

The Luton home is exempt for the first eight years whilst he was living in it and for the last 18 months because, even though he had another home which was his main residence during this time, the last 18 months is always exempt provided the home in question qualified as the main residence at some point.

9.5/13 of the gain on the Luton home will be exempt from capital gains tax. Upon the eventual sale of the flat the whole of that gain will also be exempt.

The main residence exemption can be complex and often causes a good deal of misunderstanding. Please contact us for further advice before making transactions in property.

### Inheritance tax (IHT)

The general growth in house prices over the last three decades, in particular, has caused

real IHT worries. This is because retaining the family home in the estate when it is often the largest asset could result in an IHT liability of up to 40%. At the same time, finding a way to deal with it efficiently for IHT is difficult because individuals need a place to live. The government is proposing measures to reduce the problem for many families. See the Preserving the Inheritance section of this guide for details of new proposals.

### Help to Buy ISA

The government has announced the introduction of a new type of ISA, the Help to Buy ISA, which will provide a tax free savings account for first time buyers wishing to save for a home.

The scheme will provide a government bonus to each person who has saved into a Help to Buy ISA at the point they use their savings to purchase their first home. For every £200 a first time buyer saves, the government will provide a £50 bonus up to a maximum bonus of £3,000 on £12,000 of savings. The government intends the Help to Buy ISA scheme to be available from 1 December 2015 and investors will be able to open a Help to Buy ISA for a period of four years.

As is currently the case it will only be possible for an individual to subscribe to one cash ISA per year. It will not be possible for an account holder to subscribe to a Help to Buy ISA and a cash ISA.

# Disposals and capital gains tax

Making the most of your investments requires some understanding of capital gains tax (CGT). CGT arises on the sale of most assets and, subject to various reliefs and exemptions, is payable on the difference between the sale proceeds and the original cost. The CGT annual exemption results in the first £11,100 of gains, for 2015/16, being tax free.

CGT is payable at 18% where total taxable gains and income, after taking into account all allowable deductions are less than the income tax basic rate band (£31,785). CGT payable at 28% applies to gains or any parts of gains above this limit. These rates do not apply to gains eligible for Entrepreneurs' Relief.

Certain other CGT reliefs allow chargeable gains to be deferred for a period of time such as gains deferred under the Enterprise Investment Scheme.

In working out the CGT due, taxpayers will be able to deduct losses and the annual

exemption in a way which minimises the tax due.

Some assets are exempt from CGT such as motor cars (including classic cars), personal goods such as jewellery or antiques sold for less than £6,000, UK government bonds and, crucially, your only or main home.

Where a gain is chargeable, there are a number of reliefs which could be considered mainly in relation to business assets. Such reliefs are mainly used to defer tax until a later date rather than reduce the gain permanently. Entrepreneurs' Relief is the exception.

## Entrepreneurs' Relief

Qualifying gains are taxed at a 10% rate of tax. The amount of the gains that can qualify for relief is currently £10 million.

Qualifying business disposals include:

- qualifying shareholdings
- the whole or part of an unincorporated business
- the disposal of assets on cessation of a business.

There also needs to be a qualifying period of ownership of generally one year up to the disposal.

Where an individual makes a qualifying business disposal, relief may also be available on an 'associated disposal'.

An 'associated disposal' is a disposal of an asset:

- used in a qualifying company or group of companies of the individual or
- used in a partnership, where the individual is a partner.

The 'associated disposal' must be part of the withdrawal of the individual from participation in the business and the available relief may be diluted due to various restrictions. For the associated disposal to qualify it must be made in connection with a disposal of at least a 5% shareholding in the company, or a 5% share in the partnership assets.

Trustees may benefit from the relief but only in very limited circumstances.

## Tax Planning

It is essential, to maximise the relief, that various conditions are met over a period of time prior to any such disposals. Please contact us if this is likely to affect you in the future.



# Preserving the inheritance

Inheritance tax (IHT) has some unique features and it is easy to collect because the authorities meet with least resistance. However, it is relatively easy for wealthy taxpayers to at least minimise it, if not avoid it altogether, and consequently IHT is sometimes referred to as a voluntary tax.

Nonetheless, planning to minimise IHT is something that many put off until it is too late and early attention to this tax is almost always worthwhile.

The threshold for IHT (also called the nil rate band) is currently frozen at £325,000 until 6 April 2021. Many estates fall within the charge to IHT and even if your assets are worth less than this you should consider making a Will so that you choose who gets your assets after your death.

## Key features:

- IHT is charged on a person's estate when they die and on certain gifts made during their lifetime
- the rate of tax on death is 40% and 20% on lifetime chargeable transfers. The first £325,000 is not chargeable
- many lifetime gifts are treated as 'potentially exempt transfers' (PETs). So long as the donor lives for at least seven years after

making the PET there will be no possibility of an IHT charge whatever the size of the gift

- there are numerous exemptions and reliefs.

## So what's the problem?

IHT is still a problem because:

- many are simply not in a position to make substantial lifetime gifts because it will leave them with insufficient capital to live on. As a consequence there is likely to be significant value retained in estates on death.
- although the average price of a house in the UK is currently below £325,000, many individuals do have a property which exceeds the average price and this means that the house alone will use up the bulk of the nil rate band and any excess remaining assets, such as investments and cash reserves, may be charged to IHT at 40%. The government has announced the introduction of an additional nil rate band which may help with this issue.

## Mitigating the liability

Do not waste your exemptions. Regularly using IHT exemptions will build up funds outside of the estate without incurring an IHT liability.

Spouses/civil partners can each take advantage of the exemptions, the main ones being:

- an annual allowance of £3,000 per donor per year. This can be carried forward for one year only if unused
- small gifts not exceeding £250 in total per donee per tax year
- gifts made out of income that are typical and habitual
- gifts made in consideration of marriage up to £5,000 if made by a parent, £2,500 by grandparents and £1,000 by others
- gifts to charities whether made during lifetime or on death
- gifts between spouses and registered civil partners, whether made during lifetime or on death.

## Planning in lifetime

If possible you should make absolute gifts in lifetime. A gift to an individual will be a PET so there will be no liability if the donor survives seven years. Even if the donor fails to survive for all of that period there may be a tax saving because the charge which will arise on the PET will be based on the value of the asset when it was originally gifted and not on the value at the date of death. If the value of the gift is below the threshold there will be no charge on the PET but the gift will use up some of the nil rate band on death. This means that there may be

more tax to pay on the assets still in the estate on death.

## Tax Planning

Each spouse/civil partner can take advantage of the IHT nil rate band. Furthermore, gifts between them are exempt (but with special rules for non-UK domiciles). Therefore it pays to use this exemption to broadly equalise estates so that both partners can make full use of exemptions and the nil rate band.

Remember that you cannot continue to benefit in any way from the asset gifted because this will render the gift ineffective for IHT purposes. You cannot, for example, give away your home to your children but continue to live in it rent free.

### Use available reliefs

Important reliefs of up to 100% are available on business assets such as shares in a family trading company or on agricultural property. It is important that these reliefs are utilised because once the asset concerned is sold the relief will be lost. They can only be used in connection with transfers that are chargeable to IHT.

In lifetime it may be worth considering transfers of such assets into trusts for members of the family.

On death such assets should not automatically be left to the surviving spouse because that transfer will be exempt and, if the survivor subsequently sells the asset, the relief will have been wasted.

### Consider using trusts

As stated previously, many lifetime gifts are PETs. So if the donor lives for at least seven years after making the gift the PET is removed from any charge to IHT on death. However, the donor ceases to have any control over what the beneficiary does with the gift.

This is where trusts can be useful. Most transfers into trust are immediately chargeable to IHT but if the value of the assets transferred into trust within a seven year period is below the nil rate band, there is no charge. The assets (and their subsequent growth in value) are removed from the donor's estate.

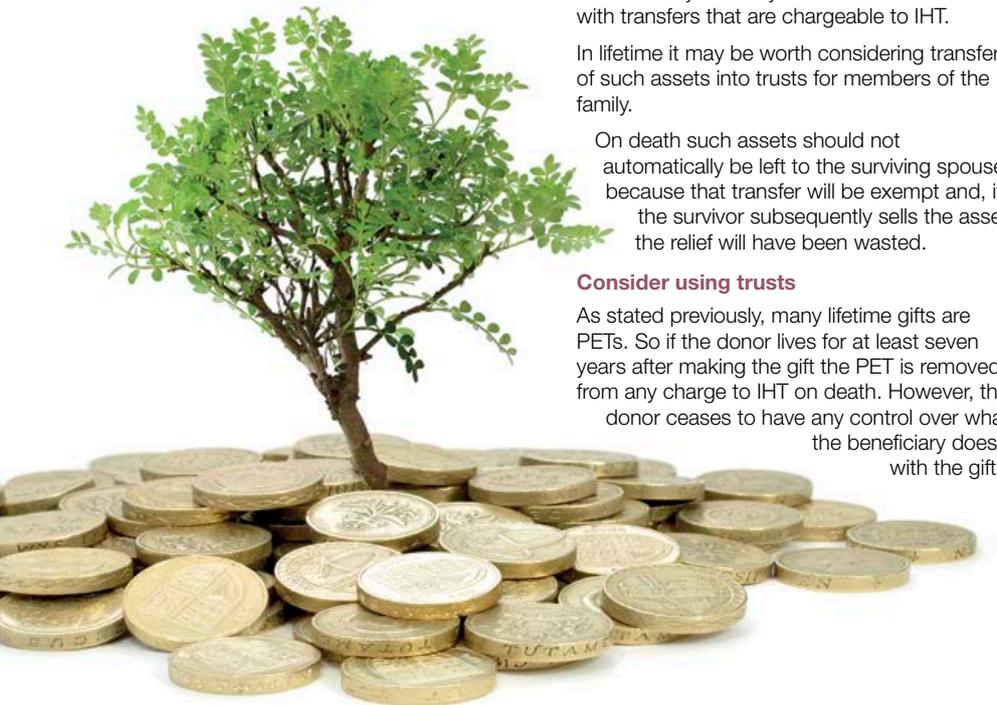
The rules are complex but significant tax savings can be achieved with careful planning. Trusts can also be an effective way of using important reliefs on businesses and agricultural properties.

## Tax Planning

Using trusts can provide an effective means of removing assets from an estate but still allow flexibility in their ultimate destination and allow the donor to retain some control.

### Use the nil rate band on death

On death, assuming the nil rate band has not already been utilised in the last seven years, it pays to ensure that it is not wasted. This gave rise to practical problems in that if assets equal to the nil rate band were bequeathed to children in the Will, the surviving partner may be left short of funds. The rules were therefore altered several years ago to allow any unused nil rate band on the death of the first spouse to be transferred to the estate of the surviving spouse. The transferred nil rate band can only be used against the estate of the second spouse on death.



## Example

Tom died leaving the whole of his estate of £800,000 to his wife Pru. A few years later Pru died leaving her whole estate of £900,000 to her children.

Under the current rules, the portion of any nil rate band unused on the death of Tom will be allowable against Pru's estate. In this case as Tom's estate was left to Pru, none of his nil band was utilised, so 100% is available. This is in addition to Pru's own nil rate band. Using the current rates the IHT payable on Pru's death is based on £250,000 (£900,000 - [£325,000 x 2]).

### IHT and the main residence nil rate band

An additional nil rate band is to be introduced where a residence is passed on death to direct descendants such as a child or a grandchild. This will initially be £100,000 in 2017/18, rising £25,000 per annum to £175,000 in 2020/21. The additional band can only be used in respect of one residential property which has, at some point, been a residence of the deceased.

Any unused nil rate band may be transferred to a surviving spouse or civil partner.

It is also proposed, subject to consultation, that the additional nil rate band will also be available when a person downsizes or ceases to own a home on or after 8 July 2015 and assets

of an equivalent value, up to the value of the additional nil rate band, are passed on death to direct descendants.

There will also be a tapered withdrawal of the additional nil rate band for estates with a net value (after deducting any liabilities but before reliefs and exemptions) of more than £2 million. This will be at a withdrawal rate of £1 for every £2 over this threshold.

It is important therefore to consider ways of reducing any potential IHT liability.

### Charitable giving

Legacies to registered charities will reduce the value of the chargeable estate and thus save 40% IHT. In addition the legacies may result in a lower IHT liability on the estate which remains chargeable.

A reduced rate of IHT applies where 10% or more of a deceased's net estate (after deducting IHT exemptions, reliefs and the nil rate band) is left to charity. In those cases the 40% rate will be reduced to 36%.

### Make a Will

If you die without a Will, the intestacy provisions will apply and may result in your estate being distributed in a way you would not have chosen. Keep your Will up-to-date to reflect changes in the family situation. In particular, Wills need to be reviewed and amended as



necessary on marriage or on divorce. The precise position depends on whether English or Scots law applies.

### Use life assurance

Life assurance arrangements can be used as a means of removing value from an estate and also as a method of funding IHT liabilities. A policy can be arranged to cover IHT due on death. It is particularly useful in providing funds to meet an IHT liability where the assets are not easily realised, eg family company shares.

*This guide 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 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 guide can be accepted by the authors or the firm.*

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