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CHARTERED ACCOUNTANTS

5 APRIL 2017 TAX YEAR-END PLANNING

Peace of mind in a complex world

Time to review your income tax affairs

The current tax year is due to end on 5 April 2017 and you should be reviewing your financial and taxation affairs in advance of this deadline and for the start of the next tax year. To help you we gathered some planning points you should be thinking about at this time of year.

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INCOME TAX

From 6 April 2017 the annual personal allowance for those aged under 65 will increase from £11,000 to £11,500. Higher allowances apply to more mature taxpayers with incomes below £28,000.

For those with income over £100,000, the allowance will be reduced at the rate of £1 for every £2 of income above that figure. The full allowance therefore becomes extinguished in 2017/18 where income is above £123,000. This results in an effective income tax rate of 60% on income within that band.

There is no change in the additional tax rate of 40% and the additional rate of 45% however the introduction of Scottish Income tax from 6 April 2017 will see the higher rate of income tax threshold staying at £43,000 for non savings income for 2017-18.

If you will be paying tax at a higher rate, the following ideas may be worthy of consideration:

- Married couples and civil partners should consider how the ownership of income producing assets is split to ensure they are both utilising their personal allowances and lower rate bands, particularly if one is subject to 40% or 45% tax rate and/or a restriction in personal allowance.

- If the rate of tax to which you are liable is likely to change from one year to the next it may be worth considering if income can be accelerated or deferred as appropriate to the year of lower rate.

- Businesses should look to fully utilise their Annual Investment Allowance of £200,000 on qualifying capital expenditure as this will help reduce their tax liability.

- When looking at motor vehicles businesses you should consider the capital allowances and benefit in kind charges. Fuel efficient vehicles receive much more favourable tax treatment than certain other cars. It may be worth considering whether a mileage scheme would be more beneficial compared to the provision of a company car.

- Where income is between £100,000 and £122,000 in 2016/17 (and between £100,000 and £123,000 in 2017/18) individuals should consider gift aid donations to charity or pension contributions to preserve the benefit of their personal allowance, and avoid an effective tax rate of 60%. If you have income over this figure this is still a relevant consideration if after deductions your net income will be brought within this band.

- Invest for capital growth rather than income whilst the capital gains tax rate remains considerably lower at 10% or 20% in comparison to the top rate of income tax of 45%.

CAPITAL GAINS

- Capital Gains Tax remains at a rate of 20% (28% for residential properties) for those paying income tax at a higher rate and 10% applies (18% for residential properties) to gains or part of a gain falling within the income tax basic rate band. Where Entrepreneurs' Relief applies to a disposal the rate of CGT is 10% on the first £10 million of lifetime gains.

- Make use of the annual CGT exemption (£11,100 for 2016/17 and £11,300 for 2017/18). If making a large disposal consider splitting it into two disposals immediately before and after the tax year end to make use of two annual exemptions.

- You should also consider the timing of disposals so that the CGT rate applicable to gains above the annual exemption is kept to a minimum.

- If your spouse has unused capital losses or unused annual exemption, consider making an unconditional gift of assets such as shares to him/her prior to a disposal at a gain so they can make use of their otherwise unutilised reliefs.

- Consider reviewing investments to see if any could realise a capital loss. If appropriate, it may be opportune to use them to create a capital loss which can then be set off against any current year or future gain.

- To benefit from Entrepreneurs' Relief on the disposal of shares in an unquoted trading company, for the 12 months prior to the sale an individual must be an officer or employee and own at least 5% of the shares and voting rights. This should be carefully considered and monitored so as to qualify in advance of any disposal.

- Entrepreneurs' relief is also available to external investors on the disposal of ordinary shares in an unlisted trading company that were newly issued to the individual and acquired for new consideration on or after 17 March 2016. The shares must have been held for a period of at least three years starting from 6 April 2016 and the person's qualifying gains for investors' relief will be subject to a lifetime cap of £10 million.

- If within the last two years you have acquired a second residential property that is available for your personal use you may wish to take advantage of principal private residence elections to reduce any potential capital gains tax on future disposal.

SAVINGS & INVESTMENTS

- Use your tax free savings allowance by contributing £15,240 for 2016/17 into an Individual Savings Account (ISA). From 6 April 2017, the new limits for everyone are £20,000.

- The total amount that can be paid into a Junior ISAs for children aged under 18 in the 2016/17 tax year is £4,080. This increases to £4,128 for 2017/18.

- Venture capital trust investments (VCT) offer 30% income tax relief on investments up to £200,000 per tax year, the possibility of tax free dividends and any gain is exempt if the shares have been held for 5 years. These are however a highly specialist area of investment with higher risks and financial planning advice should be sought as to their appropriateness in an investment strategy before making any investment decision.

- The Enterprise Investment Scheme (EIS) offers income tax relief at 30% on the cost, up to maximum of £1,000,000 and any gain on the shares held for 3 years is exempt. The investment may also allow investors to defer capital gains tax on the disposal of assets. As with VCTs specialist financial planning advice should be sought before any investment decision is made.

- The Seed Enterprise Investment Scheme (SEIS) aims to encourage investment in start-up companies. The SEIS provides income tax relief of up to 50% for individuals who invest up to a maximum of £100,000 in shares in qualifying companies.

- Investment bonds can provide tax deferral opportunities when income tax rates are high. The underlying investments can grow with no CGT on switches between the underlying funds. The investor can withdraw up to 5% per annum of the original capital sum, on a cumulative basis, deferring the income tax charge until there is a part or full disposal of the bond. Withdrawals across all policy segments above 5% are subject to income tax in the tax year of the policy anniversary. Any chargeable event gain that arises on the disposal of part or all of the bond is subject to income tax rates in the tax year of disposal. Bonds can be segmented to provide flexibility such as assigning segments to individuals subject to lower rates of tax e.g. spouses, children and non-resident individuals.

PENSION CONTRIBUTIONS

- Consider carefully the implication of making full use of available current year pension relief, especially where higher rate relief may be restricted in future.

- Contributions to pension schemes attract tax relief at your highest rate making them a tax efficient investment. To obtain relief against your 2016/17 income the contribution must be paid before 5 April 2017. The basic annual allowance cap on pension savings for 2016/17 is £40,000 (Since 5 April 2016 those tax payers with an adjusted income of £150,000 or more will see the annual allowance of £40,000 reduced by £1 for every £2 of income over £150,000 to a maximum of £10,000).

- Consider payments to stakeholder pensions for non earning spouses or children with no earned income. Basic rate tax relief is added to the contribution so that the annual contribution limit of £3,600 only costs £2,880. Where these provisions are used for the benefit of children or grandchildren the timescales involved and appropriate alternatives should be considered.

- Pensions may also be funded for adult children and this could be part of any planned gifts and a start to pension funding for the next generation.

INHERITANCE TAX

- Gifts up to £3,000 in a tax year are exempt from IHT. If the exemption is not used it may be carried forward one year such that exempt gifts of £6,000 may be made in the next tax year. Consider therefore if you have used your 2016/17 exemption.

- There is an exemption for "normal expenditure out of income" for regular gifts made out of income provided they do not reduce the donor's usual standard of living. Appropriate advice should be taken and documentation retained to support a claim for this exemption.

- The small gifts exemption allows gifts of £250 each year to any number of individual beneficiaries free of IHT. The exemption cannot be used in addition to the annual exemption in respect of gifts to the same beneficiary.

- Certain gifts which do not qualify for exemptions may also be made without IHT cost provided the donor survives for 7 years after making the gift.

- Business assets and agricultural property could qualify for 100% IHT relief. Care in planning gifts is required to maximise the effect of this relief.

- With various tax changes in recent years consideration should be given to Wills being reviewed and brought up to date and where appropriate consideration given to Powers of Attorney.

- Where appropriate ensure life assurance policies are written in trust to mitigate IHT.

- No IHT is payable on the first £325,000 of each person's chargeable estate (the nil rate band) and the prevailing rate remains at 40%. If you however leave at least 10% of your estate to charity your estate could pay the reduced rate of 36% on assets above £325,000.

- From 6 April 2017 each individual can benefit from the new IHT Residence Nil rate band in addition to an individual's own nil rate band. The caveat is that your home must be passed down to direct descendants such as children or grandchildren. It will start at £100,000 from 6 April 2017 and will increase every year by £25,000 until 2020 with the potential then to achieve a £500,000 IHT allowance.

Summary

The changes on 6 April 2017 are likely to result in most taxpayers seeing an increased tax burden. Changes in personal financial planning should therefore be done with careful consideration and so it makes sense for most taxpayers to take stock of whether the present position is likely to continue to be appropriate to current circumstances or future aspirations.

CONTACT US

If you require advice on any of these or other matters taking account of your personal circumstances please do not hesitate to contact Alan Stewart (stewarta@mestonreid.com), Martin Cheyne (cheynem@mestonreid.com) or your usual Meston Reid and Co contact in the first instance.

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