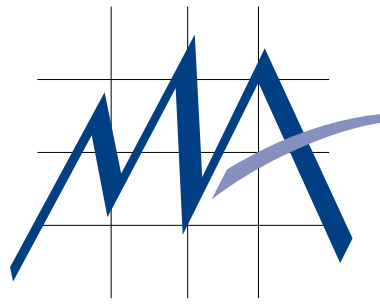


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Registered to carry on audit work by the Institute of Chartered Accountants in England and Wales  
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# NEWSLETTER

## Have you money or other assets abroad?

The Government have made changes to international tax compliance regulations which are designed to open up global tax transparency as part of their commitment to crack down on international tax avoidance. This means that HMRC will be obtaining information on taxpayers' overseas financial accounts, assets and other foreign structures.

HMRC's campaign is to provide opportunities for taxpayers to come forward and disclose information about their overseas tax affairs if they haven't previously done so.

Mabe Allen's Tax Director, Stephen Foulkes, said:

"The UK is now party to a number of international agreements designed to provide tax administrations around the world with the facility to exchange data regarding financial accounts and assets held in different countries.

HMRC are getting an unprecedented amount of information about people's overseas accounts, structures, trusts and investments from more than 100 jurisdictions worldwide. This gives HMRC unprecedented levels of information to check that, the right tax has been paid."

If you have already declared all of your past and present overseas income or gains to HMRC, you don't need to worry. If you are in any doubt or have any questions, please contact your usual Mabe Allen Relationship Partner/Manager.

## SUMMER 2017

# Planning for the reduction in the Dividend Allowance

We are used to tax reliefs being changed when a new government comes into power but it is more unusual to see a tax relief being created and then severely cut by the same government within a two year time period.

In April 2016 higher rates of taxes on dividends were introduced but with a £5,000 'tax-free' Dividend Allowance to compensate. Despite the rise in rates, many taxpayers, particularly higher rate taxpayers, found themselves better off. For example, for an individual with a £150,000 share portfolio yielding 3%, no tax would be payable on the £4,500 income produced whereas in the pre April 2016 regime there would have been a tax liability of 25%. The announcement by the current Chancellor, Philip Hammond, to reduce the Dividend Allowance to £2,000 from April 2018 will put paid to that amount of benefit.

However there is time to mitigate the effects. If your portfolio yields an average 3%, approximately £67,000 will be protected from income tax. If your portfolio exceeds this figure, consideration needs to be given to transferring some shares to a spouse or a civil partner. Equity ISAs should also be one of the first things to consider. By investing the maximum £20,000 into an Equity ISA now with a further £20,000 on 6 April 2018, protection can be given for £40,000 of a portfolio. For a married couple or civil partners, that figure doubles to £80,000.

Your existing shares can be sold and bought back again within the ISA wrapper but one needs to choose carefully which shares will be sold as the transactions will be disposals for capital gains tax (CGT). There are also two lots of annual exemption from CGT to potentially make use of – this year and next. The current annual exemption is £11,300. Married couples and civil partners also have the added facility to make transfers to the other partner prior to selling into an ISA. Any share transfer between such couples is at a 'no gain no loss' price with the result that the transferee will effectively acquire the shares at the transferor's base cost and so will make the gain in selling the shares.

Please do contact us if you have any queries.



# Making Tax Digital – where are we now?

A new term has been invented by the government to reflect the central role of businesses in the Making Tax Digital project - Making Tax Digital for Business - and a new acronym – MTDfB. There are different start dates for businesses however. Unincorporated businesses, including landlords, will be the first to see significant changes in their recording and submission of business transactions.

The government has decided how the general principles of MTDfB will operate. Much of the detail will be set by Regulations which are expected to appear in the summer.

Under MTDfB, businesses will be required to:

- maintain their records digitally, through software or apps
- report summary information to HMRC quarterly through their 'digital tax accounts' (DTAs)
- submit an 'End of Year' statement through their DTAs.

DTAs are areas where a business can see all of its tax details in one place and interact with HMRC digitally.

## When will this start?

Despite protests from many parts of the business community, and committees of the House of Commons and the House of Lords, there was only a relatively small concession to the start date announced in the Budget.

Unincorporated businesses and unincorporated landlords with annual turnover:

- above the VAT threshold (which has been set at £85,000 from 1 April 2017) will need to comply with the requirements of MTDfB from the start of accounting periods which begin after 5 April 2018

- at or below the VAT threshold but above £10,000 will need to comply from the start of accounting periods which begin after 5 April 2019.

Businesses and landlords with turnovers under £10,000 are exempt from the requirements. Companies (and partnerships with a turnover above £10 million) will not come within MTDfB until April 2020.

## What will quarterly accounting mean?

This is still the big question to which there are no definitive answers at present. The government has made some concessions from its original proposals including:

- if businesses are using a spreadsheet to record data, they will be able to continue to use this for record keeping, but they must ensure that their spreadsheet meets the necessary requirements of MTDfB – this is likely to involve combining the spreadsheet with software
- the requirement to keep digital records will not include an obligation to store images of invoices and receipts digitally. Under the original proposals, HMRC envisaged that a digital record would include not only a record of each item of income and expense but also evidence of each transaction such as copies of invoices and receipts.

Once all the relevant data for a quarter has been compiled into the software, the

business will then feed this data directly into HMRC systems. The information that will be sent to HMRC will be summary data for the quarter, not all income and expense items. Businesses will have one month from the end of the quarter to submit the update to HMRC.

## What is the 'End of Year' statement?

The End of Year statement will be similar to the online submission of a self-assessment tax return but may be required to be submitted earlier than a tax return. Businesses will have 10 months from the end of their period of account (or 31 January following the tax year – the due date for a self-assessment tax return - if sooner).

## Partnerships

In respect of partnerships, the government is proposing to stay with the concept of a nominated partner who is responsible for the requirements of MTDfB for the partnership but then partnerships will be obliged to 'push' each partner's share of any profits (or losses) through to their digital tax accounts as part of the end of year activity.

HMRC are starting a pilot of reporting of income and expenses online with some businesses and their agents. As your accountants, we will continue to monitor the MTDfB project and will continue to assist you with your tax affairs.

## Marriage allowance – now worth £432 for many people

It is now over two years since the Marriage Allowance was introduced and perhaps it is no surprise to learn that most people who are eligible have not claimed the allowance. The allowance lets certain individuals transfer 10% of their personal allowance to their spouse or civil partner. This reduces the tax bill of the recipient of the transfer by up to £212 in 2015/16 and up to £220 in 2016/17. So for anyone who hasn't claimed it yet, they may be due a tax repayment of up to £432.

The main scenario in which the transfer is allowed and worthwhile is where:

- one of the spouses has little income and is therefore not using the personal allowance
- the other spouse does not pay tax at the higher or additional rate.

The default route for applying is online. If you are an employer, it is a good idea to signpost your employees to [gov.uk/marriage-allowance-guide](http://gov.uk/marriage-allowance-guide). This link gives full information as to eligibility, how to apply and a link to the online application. As we have just passed the end of a tax year, couples should have a good idea as to whether they qualified in 2016/17. If a successful application is made, changes to the personal allowances are backdated to 6 April 2015. In future years the allowance will transfer automatically to the spouse until either of the couple cancels the Marriage Allowance or there is a change in circumstances – which means an annual potential reduction in tax bills of over £200.



# 6 April 2017 – attention landlords

It was almost two years ago in the Summer Budget 2015 that the then Chancellor, George Osborne, announced restrictions to income tax relief for interest costs incurred by landlords of residential properties. The proposals became law in November 2015 but it is only from the 6 April 2017 that these provisions came into effect.

In the 2017/18 tax year, the restriction of interest relief to basic rate of tax will apply to 25% of the interest with 75% of the interest getting relief against rental income in the normal way. Landlords will therefore first see the effect in the calculation of their tax liabilities for 2017/18 – the balancing payment for which is due 31 January 2019. A higher rate taxpayer will, in principle, get 5% less relief for finance costs (ie one quarter of 40% higher rate less 20% basic rate). 5% doesn't sound much but it can be worse than this due to 25% of the interest not being deductible from income. So total income may cross a threshold such as:

- £50,000 – in which case Child Benefit may be clawed back
- £100,000 – in which case personal allowances may be reduced.

The restrictions are only going to get worse, so please talk to us if you want clarification on any aspect of these rules.

HMRC's Making Tax Digital project also has an impact on many property businesses from 6 April 2017. The government considers that all unincorporated businesses except for the larger property business will benefit from using the cash basis rather than the usual accruals basis and so is proposing to make this the default basis.

The cash basis means the business accounts for income and expenses when the income is received and expenses are paid. The accruals basis means accounting for income over the period to which it relates and accounting for expenses in the period in which the liability is incurred.

Property businesses will remain on the accruals basis if their cash basis receipts are more than £150,000. The cash basis also does not apply to property businesses carried out by a company, an LLP, a corporate firm (ie a partner in the firm is not an individual), the trustees of a trust or the personal representatives of a person.

The government proposals are that the cash basis will first apply for the 2017/18 tax year which means that your tax return for 2017/18, which has to be submitted by 31 January 2019, will be the first one submitted on the new basis. There will be an option to elect out of the cash basis and stay with the accruals basis and we are here to help you make a decision on this later in the year.



## Leading your team to success

One of the key ingredients for making your business a success is effective teamwork. This requires you as the business leader to harness the collective efforts of your people and direct them towards achieving your overall business goal. So what are the key characteristics that mark out a team for success and what can you do to put them in place within your team?

### A common goal

Everyone in your team needs to know what the ultimate business goal is. This needs to start from the top with clear strategic goals for the business, supported by the respective departmental goals and then finally with individual team member's goals. Once team members understand what they are aiming for they can pull together and apply their individual and collective efforts towards these goals and not waste time and effort directing them elsewhere.

### Appropriate leadership

Behind every successful team lies an effective leader. Leaders provide the vision and adopt the right behaviours to instil a team approach. They share management and involve others where appropriate. They are able to flex their style of leadership to suit the needs of the situation and the needs of their individual team members. They look to develop and enable their team members, building the future leaders of their businesses.

The leadership style adopted by many business owners is often more directive than consultative, ie telling people what to do and relying on their compliance or even obedience! When the situation allows, a more empowering style of leadership can be much more effective, engendering greater commitment from team members as well as generating new ideas and improvements to current working practices.

### Suitable membership

The team needs the right balance of membership and not just in respect of the number of people and their respective technical skills. An effective team will also have an appropriate mix of personalities who bring a range of other skills, values and motivations. For instance, some of your team members will have great organisation and implementation skills, others will have excellent inter-personal skills. Try and find them roles within the team that allow them to play to their individual strengths, instead of focussing on their weaknesses.

### Team spirit

Where individual team members have a sense of belonging and a spirit of commitment to the aims and purposes of their team, this can lead to remarkable successes.

As the leader of your team how much of your personal energy are you devoting to building the team spirit and supporting your fellow team members? How often do you get your team together to celebrate successes, to discuss team morale or to get their ideas on how team performance can be improved? Team building events outside of the workplace can be great opportunities for developing team spirit but don't underestimate the positive impact that an impromptu lunch trip or round of cakes can also have.

Being an effective business leader and developing a successful team will reap many rewards for you and your team. Are the right ingredients in place for your team to win?



## Financing companies and tax relief

Your company or perhaps a company of a relative requires additional finance to expand. You have the funds to help. What is the best way to provide the funds to the company?

The natural inclination is to make a loan to the company rather than an issue of shares by the company. Loans have the advantage of simplicity in the initial lending to the company and the repayment or partial repayment of the loan when the funds are no longer required by the company. For the issue of shares, the formalities of the issue and repayment of share capital have to be considered.

The optimist, ie the person who thinks the monies will soon be repaid, will prefer the simplicity of a loan arrangement. However, one should always guard against the possibility that the finance will not be repaid because the company may get into such financial difficulties that it is forced to be wound up. A loss will have been made by the provider of the finance but can that blow be softened by any tax relief? Here's where the shareholder wins out over the loan provider.

### How much relief is available?

A loss made on a loan made to a trading company potentially qualifies as a capital loss and thus is available to relieve against capital gains in the year in which the loss relief

is claimed or in a future year. The maximum tax relief therefore is 28%, for example if the gain was on the disposal of certain residential properties but other gains may well be taxed at lower rates than this.

A loss made on shares is also a capital loss but there is a potential claim that can be made to offset the gain against income in the year of the loss and/or the previous year. So a higher rate taxpayer could get 40% tax relief.

### So why not make a loan and then convert into shares if problems are anticipated?

We could then have the best of both worlds? The short answer is no. There can be significant problems with such an approach. HMRC may look into the claim to use the loss against income to see if the company was in financial difficulty at the time the shares were issued in exchange for the loan. They may consider various statutory provisions in the tax legislation so as to restrict the acquisition cost of the shares to a lower figure than the amount of the loan given up for the shares.

Alternatively, HMRC may question the loss claim if it is made as a 'negligible value' claim ie there is no actual disposal of the shares but a deemed disposal. One of the seemingly innocuous provisions of such a claim is that the shares, at the time of the claim, have *become* irrecoverable. This may mean that HMRC can argue that no relief is available if the business was in such difficulties at the time the shares were issued that the shares should be regarded as irrecoverable from the outset.

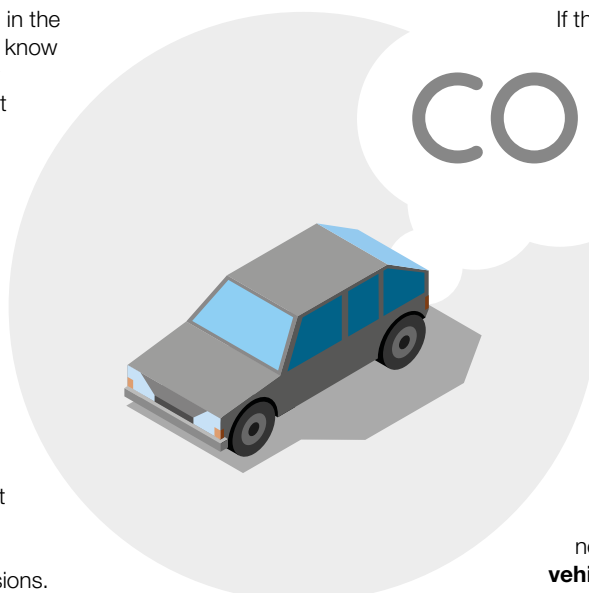
One further tip – if you are considering that the finance should be in the form of shares which are envisaged as being repayable to you in due course, it is often sensible that these shares are of a separate class to the other share capital of the company. This will allow the repayment to be made to you easier (and not create tax issues).

Please do talk to us if you are considering additional finance for your company or any other company. It is better to weigh up the advantages and disadvantages of the different methods at an early stage.

## Did you know there are new car tax rates?

If you have recently purchased or are in the process of buying a new car, you will know that new rates of Vehicle Excise Duty (VED) apply for purchases of cars first registered on or after 1 April 2017.

Most of the rest of the population may be surprised how significant the changes are. The big changes are the charges that apply in the year of purchase of the car. As with the system that applied to cars registered before 1 April 2017, the charges are based on CO<sub>2</sub> emissions but the new charges are typically much higher than under the old system. For example a car with CO<sub>2</sub> emissions of 175 jumps from £220 to £800. But in year two, the new system swings in favour of such a car owner as the charges are not based on CO<sub>2</sub> emissions.



If the car runs on petrol or diesel there is a fixed charge of £140 and an additional rate of £310 if the car has a list price of more than £40,000.

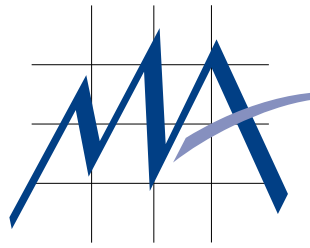
In percentage terms the purchasers who are most affected are people who buy low emission cars. For a petrol or diesel with 120 CO<sub>2</sub> emissions, you would have paid only £30 a year. For new cars the charge is £160 in year one and £140 in subsequent years. Note that a purchase of second hand car such as an 'ex demo' continues with the VED system in operation when the car was first registered. So such purchasers are tied into the old VED rates. You can get details of the new (and old) VED rates at [www.gov.uk/vehicle-tax-rate-tables](http://www.gov.uk/vehicle-tax-rate-tables)

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# Inheritance tax planning

It has often been said that inheritance tax (IHT) is a voluntary tax as action can be taken by individuals before death to reduce or eliminate IHT liabilities on death. However the need for assets and income in retirement limits the giving of gifts during lifetime. In this Briefing we consider some points to consider to reduce the amount of IHT payable on death.

## What is a chargeable estate on death?

When a person dies, IHT becomes due on their 'estate'. IHT can also fall due on some lifetime gifts but most are exempt providing the donor survives for seven years after the gift. The rate of tax on death is 40% and 20% on lifetime transfers where chargeable. For 2017/18 the first £325,000 chargeable to IHT is at 0% and this is known as the nil rate band.

Within the above paragraph lie some basic techniques of IHT planning:

- are there assets which are not in my estate at death?
- to what extent can I make lifetime gifts without prejudicing my standard of living?
- can I make efficient use of the nil rate band?

## Special considerations for married couples and civil partners

For many individuals, there will be an overriding desire to ensure their spouse or civil partner is financially secure after their death. The IHT system facilitates this need.

Lifetime gifts and transfers on death between spouses and civil partners are generally free from IHT. It therefore may be desirable to use this exemption to transfer assets in lifetime to ensure that both individuals can make full use of other lifetime exemptions and the nil rate bands available on death. This exemption does not apply to unmarried cohabiting couples.

If an individual needs to bequeath most of their assets to their spouse or civil partner, the nil rate band may not be utilised. Ten years ago, a special rule was introduced – the transferable nil rate band. A surviving spouse or civil partner will

be able to use their own nil rate band and in addition the same proportion of a second nil rate band that corresponds to the proportion unused on the first death.

## Example

On the death of the first spouse 50% of the nil rate band was unused. The estate of the second spouse would have 150% (own plus 50% from spouse) of the nil rate band existing at the second spouse's death.

## Assets which are effectively not in the estate at death

### Pensions

Pension funds are typically held in trust and unused funds can be passed directly to beneficiaries free of IHT in most cases. A 'nomination' form should be completed detailing the beneficiaries. Prior to April 2015, income tax charges of up to 55% could apply for individuals who died with unused funds on death. Now such lump sum payments on death are mainly only subject to:

- special tax charges to the extent that the pension funds of the deceased exceed their 'lifetime allowance' (broadly funds exceed £1 million)
- income tax if the death occurs after age 75 but the income tax is chargeable on beneficiaries at their marginal tax rate as and when they access the funds.

Thus a key part of IHT planning is to consider using the facility to pass on pension funds free of IHT to any nominated beneficiary.

Please contact us if you would like more details on the tax treatment of pension funds on death and the effect on beneficiaries.



## Reliefs

Some assets which are included in the estate are effectively removed from the estate because of a 100% relief. The main example is Business Property relief. Shares in an unquoted trading company potentially qualify and therefore many shares listed on the Alternative Investment Market can qualify.

## Making lifetime gifts

Many lifetime gifts will be classified as 'potentially exempt transfers' (PETs). IHT is only due if the donor dies within seven years of making the gift. An alternative way of looking at this is that they are potentially chargeable until seven years has passed. The primary example of a PET is a gift to another individual.

Certain lifetime gifts are exempt from IHT which means they are ignored even if the donor dies within seven years. Many of these exemptions are quite a low value, for example, there is an annual exemption of £3,000 for gifts to an individual. Gifts to registered charities are exempt without limit provided that the gift becomes the property of the charity or is held for charitable purposes.

## Topping up the nil rate band - the residence nil rate band

From 6th April 2017, an additional nil rate band is introduced for each individual to enable a 'family home' to be passed wholly or partially tax free on death to direct descendants such as a child, grandchild or their spouses. A step-child, adopted child or fostered child is regarded as a direct descendant.

The 'residence nil rate band' (RNRB) is £100,000 for deaths in 2017/18, rising to £125,000 in 2018/19, £150,000 in 2019/20, and £175,000 in 2020/21. It is then set to increase in line with the Consumer Price Index from 2021/22 onwards.

The additional band can only be used in respect of one residential property which does not have to be the main family home but must at some point have been a residence of the deceased.

Whilst an additional relief is to be welcomed, planning to take advantage of the relief makes IHT even more complex. This is particularly so if any of the following apply:

- individuals want their share in the property to pass to a surviving spouse or civil partner
- an individual wants to downsize or cease to own the main residence
- the total estate is expected to be in excess of £2 million.

For the first two items, special provisions are contained within the RNRB rules so that the RNRB is not lost.

## Effect of RNRB on spouses

Individuals who want their share in the property to pass to a surviving spouse or civil partner will not utilise the RNRB. Any unused RNRB will then be available to the surviving partner. The amount transferred is expressed as a percentage of the amount unused at the first death in a similar way as it is for the main nil rate band.

It doesn't matter when the first of the couple died, even if the death occurred before the RNRB was available.

## Downsize or ceasing to own a residence

A special relief – downsizing relief - is available to individuals who:

- downsize with the result that they will probably be passing a residence of a lower value to their direct descendants on death
- cease to own a residence and move into, for example, rented 'later living' accommodation.

The RNRB will be available when a person downsizes or ceases to own a home on or after 8 July 2015 where assets of an equivalent value, up to the value of the RNRB, are passed on death to direct descendants.

## Effect of total estate being above £2 million

If the net value of a death estate (after deducting liabilities but before reliefs and exemptions) is over £2 million, the RNRB is reduced by £1 for every £2 that the amount exceeds the £2 million taper threshold. For 2017/18 this means that a person with an estate of more than £2.2 million will not benefit. By 2020/21 the limit will be £2.35 million. For spouses it applies on each death estate calculation. This reduction only applies where the estate at death exceeds the limit. It does not include lifetime gifts within seven years of death.

## Making efficient use of nil rate bands

From April 2017 an individual who is not married or in a civil partnership has two nil rate bands to consider. The standard nil rate band has remained at £325,000 since April 2009 and is set to remain frozen at this amount until April 2021. From April 2020 that figure increases to £500,000 if the RNRB is used. Wills need to be reviewed to check that the residence is a qualifying residence and is bequeathed to the correct beneficiaries. If downsizing is contemplated, special care is needed to include provisions in a will which will satisfy the conditions of obtaining the additional band.

For married couples and civil partners we have four nil rate bands to consider. If all assets of the married couples or civil partners need to be retained until the death of the surviving partner, the nil rate band of the surviving partner increases to £650,000 and from April 2020 the use of the RNRB provides a total nil rate band of £1 million.

If some assets can be given away to the next generation on the first death, it may be better for the first deceased spouse or civil partner to do so in order to utilise part or all of the nil rate bands available.

Relevant considerations for assets other than a residence include:

- beneficiaries will have assets at a period in their lives when they have higher outgoings
- if beneficiaries do not have an immediate need for the assets but will invest them, the future capital growth in those investments will be protected from the additional IHT that could arise on the death of the surviving spouse or civil partner.

Planning considerations for a main residence will often be more problematical especially where each spouse has an estate of more than £1 million. From a non-tax perspective, it may be preferable for the surviving person to own the property but that may result in a loss of the RNRB as the surviving spouse may have assets well over £2 million on their death. If a share in the property passes to direct relatives on the first death, the RNRB will be available on the first death and may be available on the second death.

There are also capital gains tax (CGT) considerations. Assets passing on death are acquired by beneficiaries at their market value and no CGT is payable by the estate. Once in the beneficiaries' estates, accruing gains are potentially subject to CGT if a disposal is made of the assets.

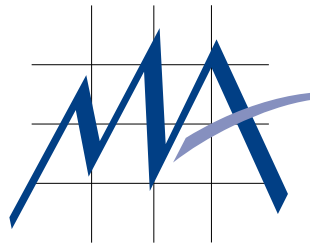
What is the best course to take in any particular will depend on a wide range of factors and there will often be no 'right' answer. But it is better to have considered the advantages and disadvantages of different strategies and writing wills with the relevant considerations in mind. Do please talk to us if you would like more information or advice on any matters raised in this briefing.

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# Tax efficient profit extraction for the family company

Another tax year has started and, as always in the world of tax, nothing stays the same. There are a number of methods of extracting funds from your own limited company and in this Briefing we consider the main options for extracting profit.

The main options are

- remuneration
- dividends
- pension contributions.

Recent changes in the taxation of interest receipts give further opportunities for tax savings, so we will consider this option as well.

## What is better, pay or dividends?

As always, it depends. Dividends are often used in combination with remuneration to obtain the most tax effective extraction of profits when the business is carried on through a company. For many years it has been attractive to pay a small salary to allow the tax efficient use of the personal allowance, to provide a corporation tax deduction for the company but not to pay National Insurance contributions (NICs). This means a salary of £8,164 in 2017/18, corresponding to the primary NICs threshold. The payment of this level of salary also provides a qualifying year entitlement to the state pension.

When the new tax regime for dividends was introduced in April 2016, many director-shareholders found that the tax bill on the dividends was higher than before. So does this change the strategy of low salary and the balance as dividends?

The Dividend Allowance of £5,000 does not change the amount of income that is brought into the income tax computation. Instead, it charges the first £5,000 of dividend income at 0% tax - the dividend nil rate. This means that:

- the payment of low salary below the personal allowance will allow some dividends to escape tax as they are covered by the personal allowance, and
- the £5,000 allowance effectively reduces the available basic rate band for the rest of the dividend.

The practical effect of the new regime is that a strategy of low salary and the balance of income requirements taken as dividends will still be a tax efficient route for profit extraction for many director-shareholders. This is likely to be the case even when the Allowance reduces to £2,000 in April 2018.

## Example – higher rate taxpayer

George wants to receive £60,000 after all taxes from his family company. He has a marginal income tax rate of 40% (32.5% if dividends) for 2017/18. He already has earnings above the employee upper earnings limit for NICs purposes so that any bonus will only be liable to employee NICs at 2% rather than at 12%. The company pays corporation tax at 19%.

To provide George with £60,000 after taxes, the company would have to pay a dividend of £88,889 or a bonus of £103,448.

## How much does the above cost the company?

The cost to the company of paying a dividend will be £88,889. The company will have to pay employer NICs @ 13.8% of £14,276 on the bonus making the gross cost £117,724. It will get tax relief on this however so the net cost will be £95,356.

The bonus therefore costs the company rather more than the cost of the dividend. The savings would be higher if George has only taken so far a basic salary of £8,164. Part of the bonus would then trigger an employee NIC cost at 12% rather than 2%.

## What if the director-shareholder has made loans to the company and could charge interest?

Interest receipts are the main category of savings income. There are two tax breaks which can apply to savings income. One is the Savings Allowance which was introduced from April 2016. The Savings Allowance, which is £1,000 for basic rate taxpayers and



£500 for higher rate taxpayers, charges interest up to these amounts at 0%.

The other tax break on savings income, the 0% starting rate of tax on savings income, has been around for many years but until recently it did not provide significant tax savings. The 0% starting band now potentially applies to £5,000 of savings income. This rate is not available if 'taxable non-savings income' (broadly earnings, pensions, trading profits and property income) exceeds the starting rate limit. However, dividends are taxed after savings income and thus are not included in the individual's 'taxable non-savings income'.

Where does the interest come from? The director-shareholder may have provided loans to their company. Many have not charged interest on such loans but there is now an added incentive to do so.

### Example

Mary is a director-shareholder and has made loans to her company to provide for the long-term capital needs of the company. She has not charged interest on the finance in the past but she may be able to charge £5,000 a year based on the amount she has lent and a market rate of interest. She takes a small salary (approximately £8,000) and the balance as dividends (typically about £50,000). The salary would be covered by the personal allowance (which is £11,500 for 2017/18), with the dividend receiving the benefit of the remainder of the personal allowance – so £3,500. The rest of the dividend would be taxed at Dividend Allowance rate (0%), basic rate (7.5%) and higher rate (32.5%).

If £5,000 of interest was received and the dividend reduced by £5,000 to compensate, there is an opportunity to benefit from the 0% starting rate on £5,000 of the interest. Personal allowances can be allocated in the way which will result in the greatest reduction in the taxpayer's liability to income tax and so, in this example, £3,500 would still be allocated to dividends as in the previous paragraph. Mary would have the benefit of the £5,000 interest being tax free rather than £5,000 dividends taxed at 7.5% (a saving of £375). There would also be a saving to the company as the interest paid is generally deductible from taxable profits which gives a saving of £5,000 at 19% (£950).

This is just another example of how complex our tax system has become.

### What about family members?

Companies often seek to minimise the tax position of director-shareholders by involving members of the same family and using personal reliefs and lower rate tax bands of each person. Income is therefore diverted from the higher rate taxpayer. However, anti-avoidance rules need to be considered as to whether a diversion is effective. This is particularly relevant for married couples.

Where it is considered that arrangements have been made by one spouse which contain a gift element, then the 'settlements' rules may apply and the person who made the gift, rather than the recipient of the income, will be taxable on that income. A key purpose of these rules is to ensure that income alone or a right to income is not diverted from one spouse to the other. Genuine outright gifts of 'normal' share capital from which income then wholly belongs to the other spouse are not caught by the rules because of a specific exemption from the settlement rules.

Family company shares and the dividend income derived therefrom can be challenged by HMRC in some cases. An example of a structure which may be challenged is the issue of a separate class of shares with very restricted rights to a spouse, with the other spouse owning the voting ordinary shares. Another area of potential risk is the recurrent use of dividend waivers particularly where the level of profits is insufficient to pay a dividend to one spouse without the other waiving dividends.

Basic tax planning is still an activity that many will seek to use to mitigate tax liabilities but care has to be taken in the current anti-avoidance environment to avoid the traps. If we can be of assistance in reviewing your position please do not hesitate to contact us.

### Pensions

Pensions are much maligned but there aren't many other investments where the government is keen to give 40% tax relief for higher rate taxpayers.

#### Relief for individuals' contributions

An individual is entitled to make contributions and receive tax relief on the higher of £3,600 or 100% of earnings in any given tax year, so with a small salary as referred to above, this doesn't take director-shareholders very far.

#### Company contributions

A company will normally obtain a tax deduction against its profits for pension contributions. The contributions must be paid before the end of the accounting period in order to obtain a tax deduction in that period. Employer pension contributions are tax and NIC free to the director-shareholder as long as the 'Annual Allowance' of the director-shareholder is not exceeded.

Broadly, the Annual Allowance is £40,000 per tax year but unused amounts of £40,000 from three previous years may be able to be brought forward. However, there are complex rules which apply to those with 'adjusted income' over £150,000, which can reduce the Annual Allowance to as little as £10,000, so detailed advice should be taken before any pension planning is undertaken. The following example helps explain the potential benefits.

### Example

Albert is the director-shareholder in a company which has a 31 March year end. In the past he has taken low salaries and high dividends. The company expects to make large profits in the year to 31 March 2018.

The company has made annual contributions into Albert's pension scheme of £20,000 for a number of years. He wants to consider the effects of the company making larger pension contributions on his behalf.

#### What amounts could be paid into a pension scheme on his behalf in 2017/18?

In simple terms inputs made in each of the three previous years have been £20,000.

Albert could have a £100,000 contribution without an Annual Allowance charge arising on him. This is made up of £40,000 for 2017/18 and unused relief in each of the three previous years of £20,000 a year.

The minimum amount that should be considered if Albert wishes to avoid any loss to allowances would be £60,000 as that would use up his 2017/18 AA and the 2014/15 unused AA. Next year a further payment could be paid (using up his 2018/19 AA and the unused AA from 2015/16). His 2016/17 unused AA could be used in 2019/20.

For years after that, payments would be limited to the AA.

#### So where does this leave us?

It is always important that the tax tail does not wag the commercial dog. It is also clear that the tax system allows savings with appropriate planning but also that care is required. We are here to help guide you through the tax maze and if anything in the Briefing has sparked your interest, please do get in touch.