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Ways to save tax ahead of the 5 April year end

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

Utilise personal allowances...

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

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

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

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

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

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

Future changes

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

Take advantage of tax-efficient savings vehicles

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

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

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

Meanwhile, the new Help to Buy ISA offers unique incentives for those saving for their first home. This has been available since 1 December 2015. The account enables first-time buyers to save monthly deposits of up to £200, with an opportunity to deposit an additional £1,000 when the account is first opened. The Government will then provide a 25% bonus on the total amount saved, including interest, capped at a maximum of £3,000 on savings of £12,000, which is tax-free. The bonus can only be put towards a first home located in the UK with a purchase value of £250,000 or less, or up to £450,000 in London.

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

Future changes

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

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

Plan for your pension

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

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

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

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

Future changes

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

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

Extracting business profits: dividend or salary/bonus?

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

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

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

Future changes

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

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

Company car considerations

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

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

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

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

Future changes

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

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

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