

## Taxation Update and Planning May 2018

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### RATES AND ALLOWANCES

#### ***Personal allowances for 2018/19***

For the 2018/19 tax year, the personal allowance is set at £11,850. As in previous years, the allowance is reduced by £1 for every £2 by which income exceeds £100,000. The effect of this is that for 2018/19 individuals with income of £123,700 or more will not receive a personal allowance.

For 2018/19, the marriage allowance is £1,190. Spouses and civil partners can transfer this to their partner, as long as the recipient is not a higher or additional rate taxpayer. Where the allowance would otherwise be wasted, claiming the marriage allowance will save the couple tax of £238 for 2018/19.

The other allowance for married couples and civil partners is the married couple's allowance. This is only available where at least one partner was born before 6 April 1935. The allowance is set at £8,695 for 2018/19, but is reduced by £1 for every £2 by which income exceeds £28,900 until the level of the minimum allowance is reached – set at £3,360 for 2018/19.

The savings allowance is available to basic and higher rate taxpayers only – additional rate taxpayers do not benefit. The recipient is able to enjoy tax-free savings income up to the amount of the allowance (in addition to any savings income sheltered by the personal allowance). For 2018/19, as previously, the savings allowance is £1,000 for basic rate taxpayers and £500 for higher rate taxpayers.

From 6 April 2018, the dividend allowance is reduced to £2,000 from £5,000. Dividends falling within this band are effectively tax-free, being taxed at a zero rate.

#### ***Income tax rates***

Income tax rates for the UK excluding Scotland remain unchanged for 2018/19, with a basic rate of 20%, a higher rate of 40% and an additional rate of 45%. The basic rate applies to the first £34,500 of taxable income, the higher rate to the next £115,500 and the additional rate to taxable income in excess of £150,000. Scottish taxpayers pay income tax on their non-savings non-dividend income at the Scottish rates of income tax (for which new bands and rates apply for 2018/19).

#### ***Dividend tax rates***

The dividend rates are also unchanged for 2018/19, remaining at 7.5% to the extent that taxable dividend income falls within the basic rate band, at 32.5% to the extent to which it falls in the higher rate band and at 38.1% to the extent that it falls within the additional rate band. The dividend rates apply to the whole of the UK, including Scottish taxpayers.

## **Capital gains tax**

For 2018/19 the capital gains tax annual exempt amount is increased to £11,700. However, the rates of capital gains tax remain unchanged with gains chargeable at a rate of 10% to the extent that total income and gains do not exceed the basic rate band (set at £34,500 for 2018/19), and at 20% thereafter. Higher rates apply to chargeable gains on residential property, of 18% and 28% respectively.

## **Corporation tax**

The rate of corporation tax remains at 19% for the financial year 2018, starting on 1 April 2018.

## **TAX EFFICIENT PROFIT EXTRACTION**

The reduction in the dividend allowance for 2018/19 and changes to the rates and allowances will impact on directors of personal and family companies looking to extract profits in a tax-efficient manner. As always, the optimal strategy will depend on circumstances, and professional advice should be sought.

It is generally beneficial to take a small salary, particularly where the recipient does not have the 35 qualifying years needed for the full single tier state pension. Where the employment allowance is not available (as is the case for a company with a single employee who is also a director, or where it is utilised elsewhere), the optimal salary for 2018/19 is one equal to the primary threshold for Class 1 National Insurance purposes, set at £8,424 for 2018/19 (equivalent to £702 per month).

If the employment allowance is available, for example in a family company with a number of employees, the optimal salary is one equal to the personal allowance of £11,850, assuming it is available and not used elsewhere. Above these limits, it will generally be more beneficial to extract further profits as dividends, making use of shareholders' dividend allowances and basic rate bands, where possible.

Before extracting profits from your company, discuss your optimal profit extraction strategy with your professional adviser.

## **REPORTING 2017/18 EXPENSES AND BENEFITS**

Where taxable benefits were provided in the 2017/18 tax year, these need to be notified to HMRC by 6 July 2018 on form P11D, unless the benefit has been payrollled. Employers must also submit their Class 1A return on form P11D(b) by the same date. A P11D(b) is required even if there are no P11Ds to submit because all benefits have been payrollled.

New valuation rules apply from 6 April 2017 where benefits are provided via an optional remuneration arrangement, such as a salary sacrifice arrangement. Unless the benefit is one of a limited range of benefits (which include childcare vouchers and employer-supported childcare, pension contributions and advice, cycles and safety equipment under a cycle to work scheme or low emission cars (75g/km or less)), new valuation rules apply. The effect of these rules is that the benefit is valued by reference to the salary forgone or the cash alternative offered, rather than calculating the cash equivalent value in the normal way. Where the rules apply, the benefit of an exemption is lost where provision is made via a salary sacrifice arrangement. The start date of the new rules is delayed where the arrangement was in place on 5 April 2017.

The P11D has been updated to accommodate the new valuation rule – where salary sacrifice arrangements are in place, care should be taken to ensure the correct value is entered on the P11D.

## **AGREEING A PSA TO SAVE WORK**

A PAYE Settlement Agreement (PSA) allows an employer to settle the tax on certain benefits and expenses on the employee's behalf. This can be useful, for example, to generate goodwill and preserve the beneficial nature of a benefit. Items included in a PSA do not need to be reported to HMRC on the employee's P11D.

The administration of PSAs has been simplified such that it is no longer necessary to set up a PSA each year. Once a PSA is in place, it is an enduring arrangement until such time as it is changed by either the employer or HMRC.

Contact your professional adviser to discuss how a PSA can help you save work.

## **NEW RULES FOR TAXING TERMINATION PAYMENTS**

New rules apply to tax termination payments received after 6 April 2018, where the employee's employment terminated on or after that date. Under the new rules, PILONs will no longer be able to benefit from the £30,000 exemption, unless the amount of the PILON and other termination awards exceeds the basic pay that the employee would have received had he or she worked their notice period.

A further change is to be introduced from 6 April 2019. From that date, any termination awards benefitting from the £30,000 threshold will attract a Class 1A (employer-only) National Insurance liability to the extent that the £30,000 threshold is exceeded. Amounts in excess of the £30,000 threshold are taxable, but will remain free of employee's National Insurance contributions.

The rules can be complicated – contact your professional adviser to make sure payments made on termination are taxed correctly.

## **RELIEF FOR LANDLORDS' INTEREST COSTS**

Changes are being phased in which restrict the amount of relief available for mortgage interest and other finance costs when calculating the profits of an unincorporated property business. The changes gradually move the mechanism by which relief is obtained from one by deduction to one in the form of a basic rate tax reduction. This will eventually cap all relief for interest and finance costs at the basic rate – where relief is by deduction, it is given at the taxpayer's marginal rate of tax.

For 2017/18, relief for 75% of the interest cost was given as a deduction in computing profits, with relief for the remaining 25% as a basic rate tax reduction. For 2018/19, the boundary shifts, with relief for 50% of the costs by deduction and relief for the remaining 50% as a basic rate income tax reduction.

For 2019/20, only 25% of the interest costs can be relieved by deduction, with relief for the remaining 75% as a basic rate tax reduction. From 2020/21 onwards all relief will be in the form of a basic rate tax reduction.

Check with your professional adviser what the changes will mean for your tax liabilities.

## PARTNERSHIP RETURNS

The rules requiring the inclusion of the unique taxpayer reference (UTR) for each and every partner in the partnership return have been relaxed. For returns made after 15 March 2018 there is no longer a need to include every partner's UTR where the partnership is making a return under the Common Reporting Standard or under the Foreign Tax Compliance Act (FTCA). However, the partnership return must include a statement confirming the relevant provisions have been met.

Changes have also been introduced to the reporting requirements requiring a beneficiary of a nominee or bare trust arrangement to be treated as a partner and named on the partnership return.

Where you operate your business as a partnership, speak to your professional adviser to ensure that all the reporting requirements are being met.

## GETTING READY FOR MTD FOR VAT

Under Making Tax Digital (MTD), taxpayers will need to maintain digital records and provide HMRC with digital reports. Under the revised timetable, MTD will start with VAT from April 2019. From the first VAT accounting period to start on or after 1 April 2019, VAT-registered businesses whose turnover is over the VAT registration threshold (frozen at £85,000 for two years from 1 April 2018) will need to maintain digital records and calculate the return using 'functional compatible software' and submit it to HMRC via an application programme interface. For VAT-registered businesses whose turnover is below the VAT registration threshold, compliance with MTD for VAT is optional rather than mandatory.

The clock is ticking and VAT-registered businesses need to start preparing. Speak to your professional adviser to make sure that you understand what you need to have in place to be ready for MTD for VAT by April 2019.

## PENSION CHANGES

From 6 April 2018 the level of minimum contributions which must be paid into a qualifying pension scheme under auto-enrolment went up to 5% of qualifying earnings, of which employers must make a minimum contribution of at least 2%, with employees contributing the balance. Prior to 1 April 2018, the minimum contribution was 2%, of which employers were required to contribute a minimum of 1%. Employers should ensure that they are meeting the new minimum contribution requirements, and advise employees of the increase in their contributions from 1% to 3%.

The pension annual allowance remains unchanged at £40,000 for 2018/19. Unused allowances can be carried forward for up to three years. However, as previously, the annual allowance is reduced where income excluding pension contributions is £110,000 or more and income including pension contributions is £150,000 or more. Where this is the case, the annual allowance is reduced by £1 for every £2 by which income exceeds the £150,000 limit until the minimum allowance of £10,000 is reached. Consequently, anyone who has income of £210,000 or more (inclusive of pension contributions) for 2018/19 will only receive the minimum allowance of £10,000.

For 2018/19 the money purchase annual allowance remains at £4,000.

The lifetime allowance is increased in line with inflation to £1,030,000 for 2018/19.

Contact your professional adviser to discuss your obligations under auto-enrolment and your retirement planning options.

*This bulletin deals with a number of topics which, it is hoped, will be of general interest to clients. However, in the space available it is impossible to mention all the points which may be relevant in individual cases, so please contact us for personal advice on your own affairs.*

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