PERSONAL TAX

YEAR END PLANNING

CavanaghKelly

INTRODUCTION

We are our clients' trusted advisors, and with over 100 experts, we will always have someone on hand to provide the guidance you need, whether that's in our audit, accounts, tax or advisory teams.

We aim to provide more than just compliance services. By working in tandem with you, we ensure you and your business are supported and have access to experienced advice when you need it most. We work alongside you to help you take the critical business decisions to grow and develop. We tailor our approach to provide solutions and are dedicated to providing you with the support and service required to succeed in today's challenging business environment.

When thinking about the future, no matter the goal, having a plan in place helps ensure you reach your objectives. Effective tax planning is no different. We challenge our clients to think about their goals and look ahead when considering tax planning not just for the current tax year, but also for years to come.

Our year end tax planning summary covers the main planning opportunities available to minimise tax liabilities arising both for the 2021/22 current tax year and to plan ahead for the 2022/23 tax year. Contact us now to discuss the planning methods we could implement ahead of 6 April 2022 to minimise your tax bill and maximise your tax reliefs.

KEY CONTACTS

Des Kelly
Managing Partner

Catherine Martin
Partner, Accounts

Michael Drumm
Partner, Advisory

Ryan Falls
Partner, Audit

John McCamley
Partner, Accounts

Janette Burns
Tax Director

Leona Leonard
Head of Tax Planning

Shane Martin
Head of R&D and Capital Allowances

Kathy Blair
Senior Manager Private Client

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INCOME TAX PLANNING 2021/22

Allowances

For 2021/22, the tax-free personal allowance is £12,570. Utilising your tax free allowance is a quick way to start your tax planning. The next £37,700 of income is taxed at the basic rate of 20% (7.5% for dividend income). Higher rate tax of 40% (32.5% for dividends) is charged on income above £50,270 and additional rate tax of 45% (38.1% for dividends) is charged on income above £150,000.

Dividends are treated as the top slice of income, so the basic and higher rates are first allocated against other income.

A new health and social care levy is being introduced on **6 April 2022**. This will initially take the form of a temporary 1.25% increase in National Insurance Contributions (NICs), to be replaced on 6 April 2023 by a separate levy, with NICs returning to their previous rates.

Planning Options

- Married couples / civil partners each have a personal allowance of £12,570. This amount will remain in place until April 2026. Couples should ensure, if possible, that they have sufficient income to use their personal allowance. If your spouse or civil partner has little or no income you may want to consider redistributing income producing assets to minimise the couple's tax liability.
- The personal allowance is gradually withdrawn for individuals with adjusted net income above £100,000. If income is above £100,000, then individual pension contributions before 6 April 2022 can reduce income to £100,000 to restore all or part of a 2021/22 personal allowance which would otherwise be lost. (See the pension contribution section for additional information).
- Reducing taxable income below £150,000 can avoid 45% income tax on income above this level.
- Married couples and civil partners have further opportunities for using their allowances and it should not be forgotten that children also have tax free allowances.
- There may be opportunities to divert income from grandparents or other relatives to take advantage of a child's personal allowance. This is typically achieved by creating a family trust which can also be part of an Inheritance Tax (IHT) planning exercise.

Savings & Investments

The Savings Allowance means a certain amount of savings income, such as interest from a bank, could be earned tax free.

For individuals with low income, that includes savings income, the starting rate band for the savings allowance is £5,000. This means that the first £5,000 of interest received, from savings, could be tax free. However, the starting rate band is tapered when earned income exceeds the Personal Allowance. For example, if an individual's income for the year is £14,570, the starting rate band would be reduced to £3,000. The allowance will not be available when total income exceeds £17,570 in the year.

Where interest is due just after 5 April 2022, closing an account just before the tax year end can bring that interest forward to the 2021/22 tax year, which, for example, may help in making better use of any surplus personal savings allowance or nil rate starting (savings) band for the current year.

In addition to the allowance above, the personal savings allowance entitles basic rate taxpayers to £1,000 of tax-free savings income and higher rate taxpayers £500. However, additional rate taxpayers (>£150,000 income) receive no allowance.

You may wish to consider redistributing investment capital between spouses / civil partners to potentially reduce the rate of tax suffered on income and gains. No capital gains tax or income tax liability will arise on transfers between married couples or civil partners living together. It is important to note that should assets be transferred, to ensure that the correct tax treatment applies investments must be fully transferred with no entitlement retained by the transferor.

ISAs and JISAs

Tax free investments, such as Individual Savings Accounts ("ISAs") or Junior ISAs can replace taxable income and gains with tax free income and gains. The current maximum annual ISA allowance is £20,000, the JISA allowance is £9,000.

You must save or invest in an ISA by 5 April or the current years' annual allowance will be lost. Any unused subscription amount cannot be carried forward.

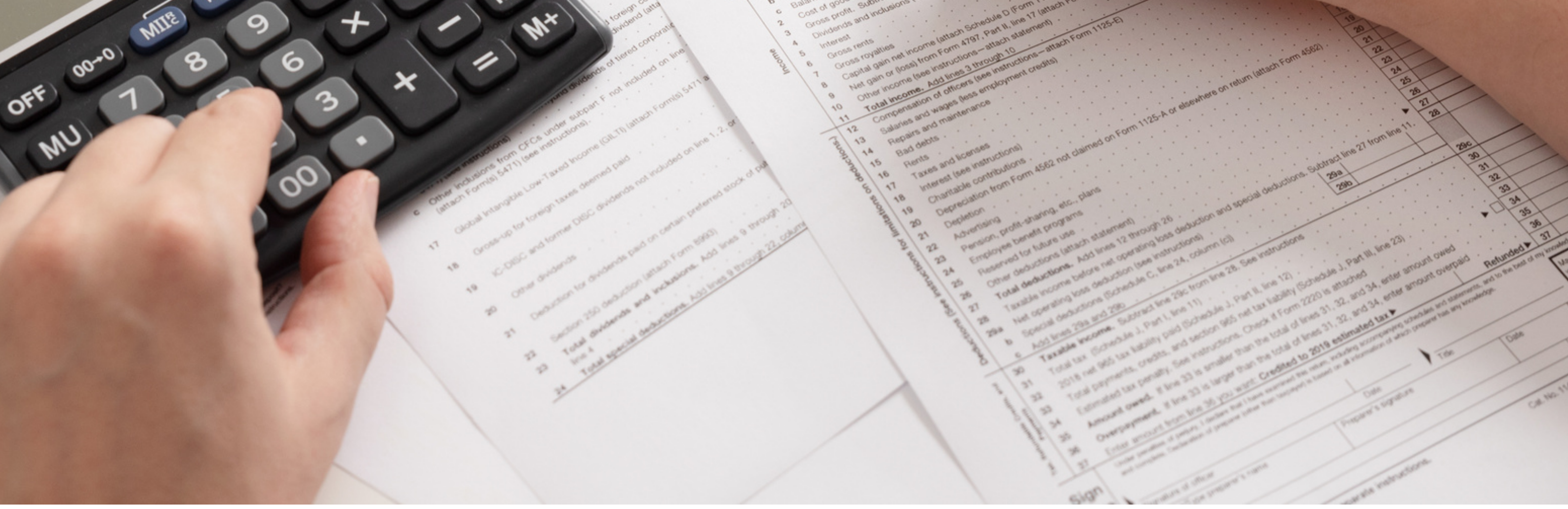
The annual ISA and JISA subscription limits will remain at £20,000 and £9,000 for the 2022/23 tax year.

Investment bonds

Investment bonds are one type of investment that can deliver valuable tax deferment.

It is possible to minimise taxation on encashment, as an investor can consider deferring encashment until later tax years, if other taxable income is likely to be lower, or nil, or you will be a basic rate taxpayer.

If cash is required from the investment, you can avail of the 5% tax-deferred annual withdrawal facility which should not trigger an annual tax charge.



Pension Contributions

Personal and employer pension contributions provide some of the highest rates of income tax relief, and with ongoing suggestions that pensions tax relief could be restricted, this is an excellent time to make additional contributions if you are able to do so.

For example, if your income is in the band £100,000 to £125,000 a gross pension contribution of £10,000 could cost as little as £4,000, after tax reliefs.

Making extra pension contributions not only increases pension provision, but for those who may be subject to a reduced personal allowance, a personal pension contribution could claw back some of this allowance giving an effective tax saving of around 60%.

The pension carry forward rules in respect of the annual allowance (capped at £40,000), in certain circumstances, can allow unused allowances to be carried forward for a maximum of three years.

Enterprise Investment Schemes ("EIS")

There are additional investments that can offer a number of tax benefits, such as the tax reliefs offered in respect of shares qualifying for Enterprise Investment Schemes (EIS) or Seed EIS (SEIS) relief.

Under the EIS, your income tax liability for the year may be reduced by 30% of the sum invested. In addition, capital gains from disposals in the previous 36 months or following 12 months may be reinvested into EIS shares, resulting in a deferral of the gain.

Both EIS and SEIS shares are normally exempt from capital gains tax (CGT) and inheritance tax (IHT), subject to detailed conditions being met.

EIS Summary

Up to £1 million can be invested or £2 million where any amount above £1 million is invested in knowledge-intensive companies.

Maximum income tax relief is 30%.

Unlimited capital gains tax deferral relief, provided some of the EIS investment potentially qualifies for income tax relief.

To carry back an EIS subscription for tax relief in 2020/21 it must be paid before 6 April 2022.

It is essential that would-be investors are aware of the likely greater investment risk and lower liquidity that may be received in return for the attractive tax reliefs offered by certain investments.

Dividends

It is important to make the most of the financial rewards of running your own business and consider how to extract your profit in the most tax efficient way.

The dividend tax allowance of £2,000 is available for all taxpayers. Amounts falling within the dividend allowance are taxed at 0%. The allowance will, however, use any part of the lower rate bands that they would otherwise have fallen into. Choosing to take a dividend over a salary or bonus reduces the tax charges for the company, as dividends are paid after Corporation Tax is paid and are free of NICs.

It is important to note that from 6 April 2022 dividend tax rates will increase by 1.25% in line with the new Health and Social care levy. The tax rates for dividends will become as follows:

- 8.75% at the basic rate (up from 7.5%)
- 33.75% at the higher rate (up from 32.5%)
- 39.35% at the additional rate (up from 38.1%)

The extra 1.25% will also apply to overdrawn directors' loans from 6 April 2022 from the current rate of 32.5% to 33.75%.

Planning points

Subject to commercial and other considerations, director shareholders may wish to consider taking a dividend before **6 April 2022** to avoid the tax increase.

But bear in mind:

- The amount of dividends already received in the current tax year.
- Your salary/dividend mix.
- Any co-ownership of shares in your company with your spouse.
- Profit expectations.

It may be beneficial to review your cash extraction strategy in view of the introduction of the new health and social care levy in addition to the expected increase in corporation tax rates.

CAPITAL GAINS TAX

Capital gains tax planning involves taking action ahead of, or at the time of, a disposal of an asset to eliminate or reduce a current of future tax liability. This may involve considering the timing of the transaction, e.g., bringing the transaction forward or delaying it.

Rates

The rate of capital gains tax (CGT) is 10% where the total taxable gains and income is less than £37,700. Any excess gains are taxed at 20%.

Where business asset disposal relief (BADR) applies, that rate of tax on the whole gain is 10% subject to a £1m lifetime allowance per person.

Property

The 10% and 20% rates also apply to gains on commercial property but gains on residential properties are taxed at the higher rates of 18% and 28%.

60 Day Reporting

It is important to note, that generally any gains or losses would be reported on the self-assessment tax return by 31 January following the tax year of sale. However, if applicable a disposal of residential property must be reported to HMRC within 60 days. A payment on account, if applicable, has to be made at the same time.

Capital gains tax planning

It is important to ensure that you:

- Maximise use of this year's annual exemption (currently £12,300). Any amount unused cannot be carried forward – "use it or lose it".
- If required, you may defer the payment of tax for a year, if you make a disposal of non property assets after 5 April 2022.
- Ascertain whether it is prudent to use two annual exemptions in quick succession, make one disposal before 5 April 2022, and another after 6 April 2022
- Try to ensure each spouse / civil partner uses their annual exemption. Assets can be transferred tax efficiently between spouses / civil partners to facilitate this. Any such transfer must be outright and unconditional, and care should be taken not to fall foul of anti-avoidance rules that apply.
- Consider banking gains at the current rates rather than waiting for a future tax year when rates may be higher.
- Make full use of any available losses, including those that would have arisen from old investments, property losses or settlement of personal guarantees.

Crystallise and use capital losses

Capital losses must be offset against capital gains in the same years.

Unused losses are carried forward indefinitely and can then be offset against future gains. A formal claim is required. The claim must be submitted to HMRC within four years of the end of the tax year of the loss, otherwise it will be time-barred.

When an asset has become valueless or worth next to nothing, it may be possible to make a "negligible value claim" in order to crystallise a capital loss.

Main residence

Ownership of two homes in the UK is becoming more commonplace as couples who both own houses marry, houses are inherited, parents buy houses for their children to live in, or people buy a second home as a holiday home.

The gain on your principal private residence is generally exempt from CGT.

If you have more than one private residence, your 'main' residence will normally be, by default, the one in which you spend the greatest time. However, it is also possible to determine that matter by nominating one of them as your main residence.

This requires careful planning, since the flip side of a gain on one residence being treated as exempt is that a gain on the other residence will become chargeable..

Written nominations must be submitted to HMRC within 24 months of any change in residences becoming available.

If you own more than one home, consider whether a principal private residence election is needed. You have two years to make an election so the sooner you speak with us, the better the position we will be in to advise on which property the election should be made over.

Marital Breakdown

If you have permanently separated from your spouse during this tax year, you may want to consider dealing with transferring assets between you before 5 April 2022. This is because assets can pass between separated spouses without capital gains tax in the year of permanent separation. Transfers taking place after this deadline may attract capital gains tax.

Business Asset Disposal Relief

BADR applies to the sale of a trading business carried on as a sole trader or partnership, or to the sale of shares in a trading company. It can also apply to personally held assets that have been used in the trade of a partnership that you are a partner of or a company that you are a shareholder in.

If the qualifying conditions are met a rate of 10% applies to the capital gain arising up to a lifetime limit of £1m.

Business owners should consistently review their BADR position as it is easy to fall foul of the detailed rules.

INHERITANCE TAX

As wealth continues to rise, planning to mitigate inheritance tax should be started as early as possible.

If you can afford to make substantial gifts out of income, you may like to get that planning up and running sooner rather than later in case any rule change occurs in future – in the hope that if a rule change does occur, existing arrangements will be protected.

Certain Inheritance Tax ("IHT") exemptions are available that we should all be aware of and utilise, when possible to do so.

Everyone has an annual exemption of £3,000 to use each tax year. Any unused annual exemption can be carried forward for one year only. Therefore, it would be prudent to use any available annual exemption carried forward from last year before 6 April 2022.

The annual £250 per donee exemption cannot be carried forward. A person can make as many outright gifts of up to £250 per individual per tax year as they wish free of inheritance tax, provided that the recipient does not also receive any part of the donor's £3,000 annual exemption.

For those who have income that is surplus to their needs, it may also be appropriate to establish arrangements whereby regular gifts can be made out of income in order to utilise the normal expenditure out of income exemption. An ideal way of achieving this is to pay premiums into a whole of life policy in trust to provide for any inheritance tax liability.

The Government announced that the inheritance tax nil rate band and residence nil rate band would be frozen at £325,000 and £175,000 until 5 April 2026, and the residence nil rate band taper will continue to start at £2 million.

CONCLUSION

This booklet is to help you identify some of the areas that could have an impact on your tax planning. To ensure that there is enough time to carry out effective tax planning, all individuals should continually review their tax position and specifically before the year end.

Our dedicated tax planning team would be delighted to speak directly to you on the ways in which you could mitigate tax liabilities and potentially avoid any pitfalls.

If you require any further assistance, please contact the CavanaghKelly tax team.

CHECKLIST

- Implement a tax planning strategy
- Make use of the 2021/2022 ISA Allowance
- Utilise all allowances available across the family
- Extract profits from your business tax-efficiently
- Review and update pension arrangements, estate plan and will
- Utilise tax efficient gifting

We have made every effort to ensure the information provided in this document is accurate, but we cannot accept responsibility for the consequences of any action you take in reliance on it contents. If you have any matters which you would like to discuss further, one of our staff will be pleased to help you.

Dungannon Office

36-38 Northland Row
Dungannon
BT71 6AP

T: +44 (0) 28 8775 2990

Omagh Office

43 Dublin Road
Omagh
BT78 1HE

T: +44 (0) 28 8224 4339

Enniskillen Office

1 Broadmeadow Place
Unit 2 Castle Island Court
Enniskillen
BT74 7HR

T: +44 (0) 28 6632 2617

Belfast Office

Scottish Provident Building
7 Donegall Square West
Belfast
BT1 6JH

T: +44 (0) 28 9091 8230