



COMPASS

ACCOUNTANTS

TAX ANGLES FOR PROACTIVE PLANNING

Newsletter - February 2019

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Salary v dividend for 2019/20

A popular profits extraction strategy for personal and family companies is to extract a small salary, taking further profits as dividends. Where this strategy is pursued for 2019/20, what level should be the salary be set at to ensure the strategy remain tax efficient?

Salary

As well as being tax effective, taking a small salary is also advantageous in that it allows the individual to secure a qualifying year for State Pension and contributory benefits purposes.

Assuming the personal allowance has not been used elsewhere and is available to set against the salary, the optimal salary level for 2019/20 depends on whether the employment allowance is available and whether the employee is under the age of 21.

The employment allowance is set at £3,000 for 2019/20 but is not available to companies where the sole employee is also a director (meaning that personal companies do not generally benefit).

In the absence of the employment allowance and where the individual is aged 21 or over, the optimal salary for 2019/20 is equal to the primary threshold, i.e. £8,632 a year (equivalent to £719 per month). At this level, no employee's or employer's National Insurance or tax is due. The salary is also deductible for corporation tax purposes.

A bonus is that a salary at this level means that the year is a qualifying year for state pension and contributory benefits purposes – for zero contribution cost. Beyond this level, it is better to take dividends than pay a higher salary as the combined National Insurance hit (25.8%) is higher than the corporation tax deduction for salary payments.

Where the employment allowance is available, or the employee is under 21, it is tax-efficient to pay a higher salary equal to the personal allowance of £12,500.

As long as the personal allowance is available, the salary will be tax free. It will also be free of employer's National Insurance, either because the liability is offset by the employment allowance or, if the individual is under 21, because earnings are below the upper secondary threshold for under 21s (set at £50,000 for 2019/20).

The salary paid in excess of the primary threshold (£3,868) will attract primary contributions of £464.16, but this is outweighed by the corporation tax saving on the additional salary of £734.92 – a net saving of £279.76.

Once a salary equal to the personal allowance is reached, the benefit of the corporation tax deduction is lost as any further salary is taxable. It is tax efficient to extract further profits as dividends.

Dividends

Dividends can only be paid if the company has sufficient retained profits available. Unlike salary payments, dividends are not tax deductible and are paid out of profits on which corporation tax (at 19%) has already been paid.

However, dividends benefit from their own allowance – set at £2,000 for 2019/20 and payable to all individuals regardless of the rate at which they pay tax – and once the allowance has been used, dividends are taxed at lower rates than salary payments (7.5%, 32.5% and 38.1% rather than 20%, 40% and 45%).

Once the optimal salary has been paid, dividends should be paid to use up the dividend allowance. If further profits are to be extracted, there will be tax to pay, but the combined tax and National Insurance hit for dividends is less than for salary payments, making them the preferred option.



Year-end tax planning tips

As the end of the 2018/19 tax year approaches, it is worthwhile taking time for some last-minute tax planning. Here are some simple tips that may save you money.

1. **Preserve your personal allowance:** the personal allowance is reduced by £1 for every £2 by which income exceeds £100,000. For 2018/19, the personal tax allowance is £11,850, meaning that it is lost entirely once income exceeds £123,700. Where income falls between £100,000 and £123,700, the effect of the taper means that the marginal rate of tax is a whopping 60%. Where income is over £100,000, consider making pension contributions or charitable donations to reduce income and preserve the personal allowance. Where this is an option, consider also deferring income until after 6 April 2019 to reduce 2018/19 income.
2. **Claim the marriage allowance:** the marriage allowance can save a couple tax of £238 in 2018/19. Where an individual is unable to utilise their personal allowance, they can make use of the marriage allowance to transfer 10% of their personal allowance (rounded up to the nearest £10) to their spouse or civil partner, as long as neither pay tax at the higher or additional rate. The marriage allowance must be claimed.
3. **Pay dividends to use up the dividend allowance:** family and personal companies with sufficient retained profits should consider paying dividends to shareholders who have not yet used up their dividend allowance for 2018/19. The dividend allowance is set at £2,000 and is available to all individuals, regardless of the rate at which they pay tax. The use of an alphabet share structure enables individuals to tailor dividend payments according to the individual's circumstances.
4. **Make pension contributions:** tax relieved pension contributions can be made up to 100% of earnings, capped at the level of the annual allowance. The annual allowance is set at £40,000 for 2018/19 (subject to the reduction for high earners). Where the annual allowance is not used up in year, it can be carried forward for up to three years.
5. **Transfer income-earning assets to a spouse or civil partner:** where one spouse or civil partner has unused personal allowances or has not fully utilised their basic rate band, considering transferring income earning assets into their name to reduce the combined tax liability (but non-tax considerations such as loss of ownership should be taken into account).
6. **Put assets in joint names prior to sale:** spouses and civil partners can transfer assets between them at a value that gives rise to neither a gain nor a loss. This can be useful prior to selling an asset which will realise a gain in order to take advantage of both partners' annual exempt amount for capital gains tax purposes.
7. **Make gifts for inheritance tax purposes:** individuals have an annual exemption for inheritance tax of £3,000, allowing them to make gifts free of inheritance tax each year. Where the allowance is not used, it can be carried forward to the next year, but is then lost.

Make the most of your allowances



The tax system contains a number of allowances which enable individuals to enjoy income and gains tax free. In seeking to maximise your tax-free income, it makes sense to take advantage of available allowances. The following are a selection of some of the allowances on offer.

Trading allowances

Individuals are able to earn income from self-employment of up to £1,000 tax-free and without the need to declare it to HMRC. Where income exceeds £1,000, the allowance can be claimed as a deduction from income in working out the taxable profit, rather than deducting actual costs. Where allowable expenses are less than £1,000, claiming the trading allowance instead will be beneficial.

Property allowance

A similar allowance exists for property income, allowing individuals to receive property income of up to £1,000 tax-free without the need to tell HMRC. Where property income is more than £1,000, the individual can deduct this rather than actual costs when computing profits for the property rental business if this is more beneficial.

Rent-a-room

The rent-a-room scheme allows individuals to earn up to £7,500 tax-free from letting a furnished room in their own home. The limit is halved where two or more people receive the income.

Savings allowance

Basic rate taxpayers are entitled to a savings allowance of £1,000, while higher rate taxpayers benefit from a savings allowance of £500. Additional rate taxpayers do not get a savings allowance. ISAs provide the opportunity to earn further savings income tax free.

Dividend allowance

All taxpayers regardless of the rate at which they pay tax are entitled to a dividend allowance, set at £2,000 for both 2018/19 and 2019/20. This can be useful in extracting profits from a family company in a tax-efficient manner.

Capital gains tax annual exempt amount

Individuals can also realise tax-free capital gains up to the exempt amount each year – set at £11,700 for 2018/19 and at £12,000 for 2019/20. Spouses and civil partners have their own annual exempt amount. Time sales of assets to make best use of the annual exemption.

The above is only a small selection of the allowances available.

Abatement of the personal allowance

Not all taxpayers are able to benefit from the personal allowance – once income exceeds £100,000 the allowance is gradually reduced until it is eliminated in full. However, there are steps which can be taken to reduce income and preserve entitlement to the personal allowance. The personal allowance is set at £11,850 for 2018/19, rising to £12,500 for 2019/20.

When is it abated?

Once an individual's 'adjusted net income' exceeds £100,000, their personal allowance is reduced by £1 for every £2 by which 'adjusted net income' exceeds £100,000.

The measure of income for these purposes is 'adjusted net income'. This is an individual's total taxable income before personal allowances and after deducting certain reliefs, such as:

- relief for trading losses;
- donations to charity through the Gift Aid scheme (deduct the grossed-up amount of the donation); and
- pension contributions (deduct the gross amount).

Example

Polly has taxable income for 2018/19 of £120,000. She makes pension contributions paid gross of £5,000. Polly's adjusted net income for 2018/19 is £115,000 (£120,000 - £5,000).

As her income is more than £100,000, her personal allowance is reduced. The personal allowance for the year of £11,850 is reduced by £1 for every £2 by which her income exceeds £100,000.

The reduction in her personal allowance is therefore £7,500 ($\frac{1}{2}(\text{£115,000} - \text{£100,000})$). Her personal allowance for 2019/20 is therefore £4,350.

Assuming her income remains the same for 2019/20 and she continues to make gross pension contributions of £5,000, she will receive a personal allowance of £5,000 for 2019/20.

When is the personal allowance lost?

With a personal allowance of £11,850 for 2018/19, individuals with income in excess of £123,700 do not receive a personal allowance for that year. For 2019/20, the personal allowance is £12,500, and the personal allowance is lost once adjusted net income exceeds £125,000.

Beware 60% tax in the abatement zone

Where adjusted net income falls within the zone in which the personal allowance is reducing – from £100,000 to £100,000 plus twice the personal allowance – the marginal rate of tax is 60%. This is the combined effect of the application of the higher rate of tax and the reduction in the personal allowance.

Reduce the 60% band and preserve the allowance

To reduce the income falling in the abatement zone (taxed at a marginal rate of 60%) and to preserve as much as the personal allowance as possible, it is necessary to reduce adjusted net income. There are various ways in which this can be achieved.

The first point to consider is the timing of income – can income be deferred to the next tax year, or, if income for the current tax year is less than £100,000 but is expected to be above £100,000 in the following year, can income be brought forward to the current tax year. In a family company scenario, it may be possible to achieve this by adjusting the timing of dividends and bonuses.

Consideration could also be given to putting income earning assets into the name of a spouse or civil partner to reduce income and preserve the allowance.

Adjusted net income is income after pension contributions. Making pension contributions is tax effective, both in terms of benefiting from the relief available and reducing net income to preserve personal allowances.

Alternatively, a person can make charitable donations under gift aid to reduce their adjusted net income. Although they will lose the benefit of their income, the cost will be offset slightly by the preserved personal allowance, and their chosen charity will benefit from the donation plus the associated gift aid.

Does the marriage allowance apply to you?

The marriage allowance can be beneficial to married couples and civil partners on lower incomes. Claiming the marriage allowance is worth up to £238 in 2018/19 and £250 in 2019/20.

Nature of the allowance

The marriage allowance allows one spouse or civil partner to transfer 10% of their personal allowance (rounded up to the nearest £10) to their partner if they are unable to utilise the full allowance. However, it is only available where the recipient pays tax at the basic rate – couples where one party has no income and the other party is a higher or additional rate taxpayer cannot benefit from the allowance. A person can transfer 10% of their personal allowance to their spouse or civil partner if:

- they are married or in a civil partnership;
- they have not used up all of their personal allowance (set at £11,850 for 2018/19 and at £12,500 for 2019/20);
- and their partner pays tax at the basic rate.

For Scottish taxpayers, the marriage allowance is available if the recipient pays tax at the Scottish starter, basic or intermediate rates. For 2018/19 the personal allowance is £11,850 and the marriage allowance is £1,190. For 2019/20, the personal allowance is £12,500 and the marriage allowance is £1,250.

Impact of the marriage allowance

Where the marriage allowance is claimed, the transferor's personal allowance for the year is reduced by the amount of the allowance and the transferee's personal allowance is increased by the amount of the allowance. Instead of that portion of the personal allowance being wasted, it is set against the transferee's income, saving tax at the basic (or relevant Scottish) rate.

Example

Lauren is a stay-at-home mum. She has no income in either 2018/19 or 2019/20.

Her husband Joe works as an electrician earning £20,000 a year. They claim the marriage allowance for both 2018/19 and 2019/20.

For 2018/19, the allowance is £1,190. By claiming the allowance, Lauren's personal allowance is reduced to £10,660 (£11,850 - £1,190) and Joe's personal allowance is increased to £13,040 (£11,850 + £1,190). Their combined personal allowances remain at £23,700, but utilising the marriage allowance to increase Joe's allowance while reducing Lauren's saves them £238 (£1,190 @ 20%) in tax.

If they claim the marriage allowance of £1,250 for 2019/20, Lauren's personal allowance will fall to £11,250 (£12,500 - £1,250), while Joe's personal allowance will increase to £13,750. Claiming the allowance will save them tax of £250 (£1,250 @ 20%) for 2019/20.

The allowance will still be effective where the partner with the lower income does not fully utilise the allowance, even if as a result, they have some tax to pay as a result of making the claim.

Example

In 2018/19, Max has income of £11,000 and his wife Amy has income of £17,000. Claiming the marriage allowance will reduce Max's personal allowance to £10,660, meaning he will pay tax of £68 ((£11,000 - £10,660) @ 20%). However, Amy's personal allowance will increase to £13,040, saving her tax of £238. As a couple they are £170 better off (£238 - £68).

How to claim

The marriage allowance can be claimed online: see www.gov.uk/apply-marriage-allowance. Once a claim is made it will apply automatically for subsequent tax years, unless cancelled or circumstances claim. A claim can be backdated to include any tax year since 5 April 2015 for which the qualifying conditions are met.

The allowance can also be claimed for the year in which one partner dies.

Impact on tax codes

Where the marriage allowance is claimed, both the transferor's and transferee's tax code are amended as a result. A code with a 'M' suffix denotes that the individual has received the marriage allowance, whereas a 'N' suffix denotes that the individual has transferred 10% of their personal allowance to their spouse or civil partner.

In the above example, Lauren would have a tax code of 1066N for 2018/19, while Joe's tax code would be 1,304M. For 2019/20, Lauren's tax code would be 1125N, while Joe's tax code would be 1375M.



Compass is now approved to provide Probate Services

We are very proud to announce that we are now fully licensed by The Institute of Chartered Accountants in England and Wales (ICAEW) to carry out probate work.

Probate, (the process undertaken throughout the administration the estate of someone who is deceased), was a service limited to solicitors up until recently, and as a result Compass Accountants are one of only a small number of accountancy firms licensed to carry out the services.

Compass Director, Kerry Lawrance said, "I am delighted to now be fully licensed to provide probate work as a new service for Compass Accountants. The organisation of the probate of an estate can be very complicated and a daunting procedure and if not done properly, can be expensive.

We are therefore very pleased to be able to offer probate services for both new and existing clients, during their difficult times. Combining inheritance tax planning and probate services will now enable Compass to act as a one-stop-shop for our client's business advisory services."

We can now guide you through the complications of inheritance tax, income tax and capital taxes, ensuring that the amount of tax that needs to be paid from the estate is minimised.

We can also work with you- and any beneficiaries- to set in place plans to minimise future tax burdens.



Compass launches new and improved app!

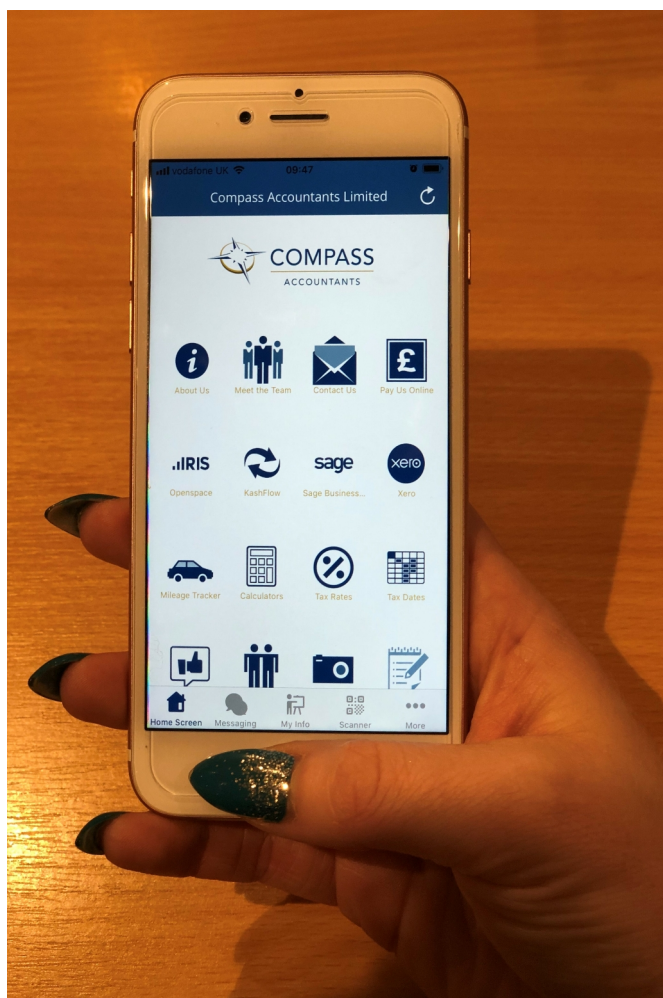
Following the ever-increasing use of mobile phones in business, Compass has now made further improvements to our company app, to ensure that our clients are even more up-to-date and well informed with all the information, data, news, communication tools and reminders they need.

It's still completely FREE of charge and now enables you to collaborate with Compass whilst you are on the go, whilst accessing digital tools and critical information - anytime, anyplace.

The App can still be easily downloaded from the Compass website directly onto your iPhone, iPad or any android device. Just some of the new features include:

- Key dates reminders and push notifications (so you never miss a deadline)
- Help sheets and a support library
- QRCode Scanning
- GPS Mileage Tracker
- Useful Tax information and resources
- Calculators allow you to estimate your tax liabilities
- Log in portals for Sage/ OpenSpace/ Xero/ Iris/ QuickBooks
- Easy access and quick contact with Compass staff members
- Free in app messages direct to and from Compass
- Access to the Compass website, blog and our social media accounts

You can access the links to the app on the Compass Accountants home page- or alternatively search for Accountant Go on Google Play or iTunes, then enter the code- **LKETUV** or search for Compass Accountants on the 'Find Your Accountant Screen'.



Client Focus - Bascule Disability Training

This month, we catch up with Chris Jay, founder and Managing Director of Bascule Disability Training- a social enterprise that provides disability awareness training for businesses ...

Chris Jay, the Managing Director and Founder of the recently launched social enterprise, Bascule Disability Training- is no stranger to Compass Accountants. In his role as Executive Chairman for the charity Enable Me, Chris had also previously been a client of Compass.

Sadly, in July 2018, due to a number of contributing factors including a lack of funding for schools and difficulties in recruiting, supporting and retaining volunteers, the charity was forced to close its doors after 14 years of working with schools, businesses and universities.

"Eventually, I had to separate the value of the work Enable Me was doing, from the vehicle that was delivering it." Explains Chris. "Budgetary restraints and financial pressures have inevitably forced schools to make many cutbacks, leading to a significant reduction in extracurricular activity, resources and training. As a result, the necessity for disability awareness training in schools has become increasingly overlooked." Says Chris.



After the closure of the charity Chris decided to focus on continuing to deliver disability awareness training for businesses and universities- but through a new social enterprise that would donate 75% of its profits to the provision of free disability awareness training in state schools.

"You could say that Bascule Disability Training is the spiritual successor to Enable Me." Says Chris.

The unique disability awareness training Bascule provides empowers businesses to provide open, inclusive organisations, for both their staff and their target clientele. Through these user-led, interactive modules and workshops, workforces gain a firmer understanding of disability and its organisational benefits.

"Most importantly, for every business that implements disability awareness training, we are able to deliver two school training sessions, free of charge." continues Chris.

Facing facts

"Most people are shocked to learn, that ignoring the needs of people with disabilities costs UK businesses around £1.8 billion per month." Says Chris. "At Bascule we aim to help businesses become disability aware so that they can build the bridge between people, policy and inclusive practice."

"Another amazing statistic is that 67% of the British public admit to feeling 'uncomfortable' and 'awkward' when talking to people with disabilities. This is also something we help businesses with, by making staff more aware and understanding of people with disabilities - especially team members that work with the general public."

Reappointing Compass

As soon as Bascule was in a position to launch, Chris made no hesitation in contacting Compass to reinstate the team.

"I didn't even consider another accountancy firm" says Chris, "I had no reason to and it wasn't just for the quality of their core work. It was also because of the 'family feel' that runs through the company."



Having aspired to be a more inclusive business itself, Compass was one of Bascule's first clients, and the Compass team were provided with an introduction to disability awareness in October 2018.

Compass Director Stuart Lawrance explains: "It is our aim to be in a more favourable position in terms of our appeal to both potential clients and employees with disabilities. Bascule's introduction was very insightful, informative and enjoyable for all of our team. We already feel more equipped to help facilitate any clients with disabilities in terms of making reasonable adjustments and the whole team has certainly gained a more in-depth understanding of disability."

Chris added, "Everyone at Compass has a genuine desire to understand and support your business in its development and that counts for so much. You can pick up the phone and talk to someone and not just anyone, but someone experienced and knowledgeable. Being with Compass makes you feel like you are in very safe hands and as someone steering a new business, that reassurance is very important."

If you are interested in Bascule's disability awareness training, or would like to ask Chris more about how Bascule can help your business- call now on **0330 3800662** or email **info@bascule.com** or to visit the Bascule website go to: www.bascule.com

Tax Diary February/March 2019



1st February 2019 Due date for Corporation Tax for years ended 30th April 2018.

19th February 2019 PAYE and NIC deductions due for month ended 5th February 2019. (If you pay your tax electronically the due date is 22nd February 2019)

19th February 2019 Filing deadline for the CIS300 monthly return for the month ended 5th February 2019.

19th February 2019 Due date for CIS tax deducted for the month ended 5th February 2019.

1st March 2019 Due date for Corporation Tax for years ended 31st May 2018.

19th March 2019 PAYE and NIC deductions due for month ended 5th March 2019. (If you pay your tax electronically the due date is 22nd March 2019)

19th March 2019 Filing deadline for the CIS300 monthly return for the month ended 5th March 2019.

19th March 2019 Due date for CIS tax deducted for the month ended 5th March 2019.

Contact us

For further information on any of the stories in this month's newsletter, or for any other matter that Compass Accountants can assist you with, please contact us on 01329 844145.



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