By your side

TAXES MADE EASY

2024/ 2025

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Clear and concise tax guide 2024/25

Practical tax tips to guide you through the tax system and help you plan to minimise your liability.

This guide is designed to provide you with an overview of the key tax rules from seven perspectives - that of the family; the employee; the person running their own business; the taxation of investments; disposals and CGT; property matters; and, finally, the potential liability on your estate at death.

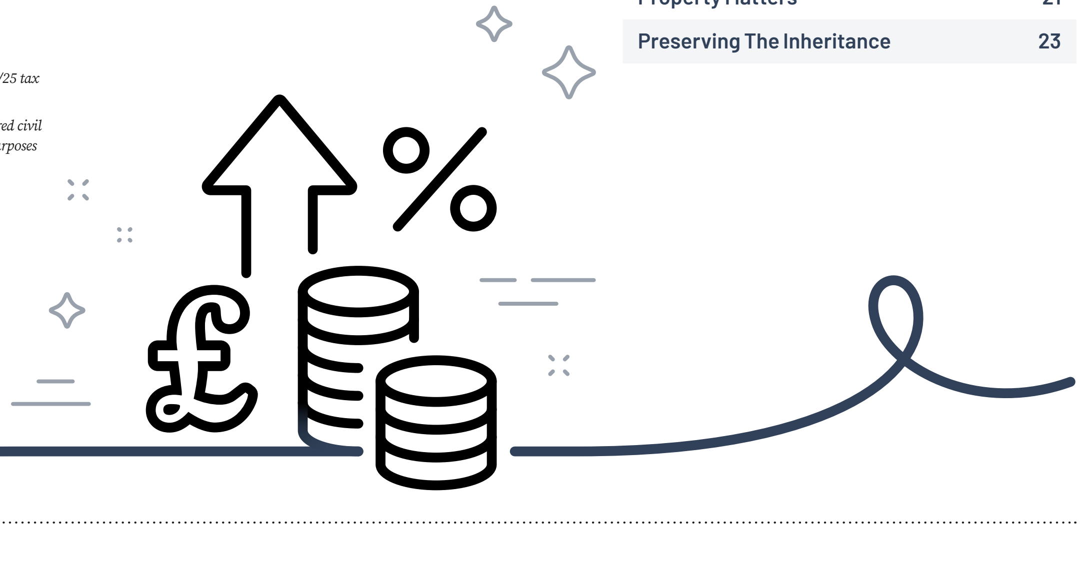
Please use the guide to help you identify planning opportunities, pitfalls to avoid and areas where you may need to take action and then contact us for further advice.

The rules, rates and allowances in this guide relate to the 2024/25 tax year and these may be different for other tax years.

The general effect of the Civil Partnership Act is to treat registered civil partners on a consistent basis with married couples. For the purposes of this guide we have on occasions referred only to spouses.

Contents

A Few Essentials	2
Family Matters	5
Working For Others	8
Running a Business	11
Tax and Your Investments	18
Disposals and Capital Gains Tax	20
Property Matters	21
Preserving The Inheritance	23



A FEW ESSENTIALS

Introduction

Taxation in the UK is administered and regulated by HMRC. Many individuals will have little or no regular contact with HMRC. For employees, income tax is typically deducted at source from earnings before they are paid out by way of Pay as You Earn (PAYE). Often other sources of income, such as savings and dividends, are covered by allowances such that no tax needs to be paid. Without additional income tax payable to HMRC, these individuals do not need to complete income tax returns.

However, over 12 million taxpayers have something more than just a regular income taxed under PAYE or income covered by the savings and dividend allowances. They might have income from their own business or receive rent from a property. Alternatively, it may be that their savings or dividend income is significant enough to result in tax being payable. These taxpayers may be asked to complete a self assessment return each year and have direct contact with HMRC. Other taxpayers may need to complete periodic returns; for example, where they have made a disposal of an asset which is subject to Capital Gains Tax (CGT) or be responsible for collecting and paying the tax on behalf of others such as employers or businesses charging VAT.

Practical Tip

If you are not asked to complete a tax return, it remains your responsibility to advise HMRC by 5 October following the tax year if there is untaxed income, a capital profit that could lead to a tax liability or high levels of employment expenses or savings income. For the 2024/25 tax year, the high income child benefit charge is taxable through PAYE for employees, although the need to register for self-assessment currently remains. Please contact us for further advice if this affects you.

The personal allowance

In principle, all individuals are entitled to a basic personal allowance before any income tax is paid. This means that many individuals do not pay income tax on the first £12,570 (for 2024/25) of income they receive, and individuals who have lower levels of income may not need to pay any income tax at all. The personal allowance is now fixed until April 2028.

Losing the personal allowance

However, the personal allowance is reduced for individuals with higher levels of income. Where an individual's adjusted net income exceeds £100,000 the personal allowance is reduced by £1 for every £2 of income in excess of that limit. This means that an individual with an income of £125,140 or more will not be entitled to any personal allowance.

Tax rates and allowances

The income tax bands and rates for 2024/25 are determined by where you live in the UK and the type of income you have.

For most UK residents the following tax rates and bands apply:

Taxable income £	Non-savings and savings income rate %	Dividend rate %
0 - 37,700	20	8.75
37,701 - 125,140	40	33.75
Over 125,140	45	39.35

Taxable income is income in excess of the personal allowance.

Non-savings income is broadly earnings, pensions, trading profits and property income.

Savings and dividends allowances

Individuals may be entitled to the savings allowance (SA), with savings income within the SA taxed at 0%. The amount of SA depends on an individual's marginal rate of tax (the highest rate of tax to which they are subject). An individual taxed at the basic rate of tax has an SA of £1,000, whereas a higher rate taxpayer is entitled to an SA of £500. Additional rate taxpayers receive no SA.

The dividend allowance (DA) is available to all taxpayers regardless of their marginal tax rate. The DA charges the first £500 of dividends to tax at 0%.

Savings and dividends received above these allowances are taxed at the rates shown in the table. Savings and dividends within the SA or DA still count towards an individual's basic or higher rate band and so may affect the rate of tax payable on income in excess of the allowances.

In addition, some taxpayers may be entitled to the starting rate for savings which taxes up to £5,000 of interest income at 0%. However, this rate is not available if non-savings income exceeds £5,000.

Tax Tip

The DA reduced to £500 for 2024/25. It may be worth revisiting any dividend planning to ensure it is still tax-efficient in light of the reduced allowance.

Rates and bands for Scottish and Welsh taxpayers

For 2024/25 the tax rates and bands applicable to Scottish taxpayers on non-savings and non-dividend income are as follows:

Taxable income £	Band name	Rate %
0 - 2,306	Starter	19
2,307 - 13,991	Basic	20
13,992 - 31,092	Intermediate	21
31,093 - 62,430	Higher	42
62,431 - 125,140	Advanced	45
Over 125,140	Top	48

As above, taxable income is income in excess of the personal allowance.

For 2024/25 the Welsh rate of income tax on non-savings income is set at 10% and this is added to the UK rates, which are each reduced by 10%. For 2024/25, the overall tax payable by Welsh taxpayers continues to be the same as English and Northern Irish taxpayers.

Scottish and Welsh taxpayers continue to pay tax on their savings and dividend income using the UK rates and bands and the personal allowance is set for the UK as a whole.

Income tax reliefs

In order to encourage charitable giving and saving for the future, income tax relief is available for donations made to charity under gift aid and pension contributions to personal pension schemes.

Basic rate relief is deemed to be given at source. Effectively what this means is that basic rate tax is reclaimed by the charity or pension fund, so you only need to pay £100 for the charity/fund to receive £125.

Relief for higher and additional rate taxpayers is given by extending the bands set out above by the gross amount of the donation (the total receipt by the charity/fund). For example, a higher rate taxpayer making a donation of £100 would pay tax at 20% on the first £37,825 of taxable income rather than £37,700.

Tax Tip

Gift aid donations and personal pension contributions are also deducted from your income to arrive at adjusted net income for the purposes of calculating any reduction in your personal allowance.

If your adjusted net income is between £100,000 and £125,140, you may want to consider making or increasing charitable donations or pension contributions in order to minimise the reduction in the personal allowance.

There are specific rules which determine how much tax relief can be obtained for pension contributions which are discussed further in 'tax and your investments', which also contains details of relief for contributions to occupational pension schemes.

Other taxes

Individuals are not only taxable on the income they receive. You may own assets such as a precious antique, a second home or shares. If such an asset is sold at a profit this may give rise to a liability to CGT. Details of any capital gains may have to be included on the self assessment return if you receive one; alternatively you can complete a 'real time' return.

Inheritance Tax (IHT) may be payable on the assets that you give to others in your lifetime or leave behind when you die. With rising house prices, this has become a concern for many more individuals.

Many of those in business have to understand the principles of VAT because they will have to act as a collector of this tax. In addition, those who run their business through a limited company need to know about corporation tax which taxes a company's profits. Employing others in your business brings further obligations with Real Time Information reporting for PAYE and auto enrolment pension contributions responsibilities. We consider these issues later in this guide.

Self assessment (SA) timetable

Income tax and CGT are both assessed for a tax year which runs from 6 April to the following 5 April. The tax year 2024/25 runs from 6 April 2024 to 5 April 2025.

Shortly after 5 April a notice to complete a return is usually issued by HMRC. Typically the return then needs to be submitted by:

31 October following - non-electronic returns (where you have requested a paper return from HMRC or downloaded a blank return).

31 January following - returns filed online.

These deadlines may be extended in certain circumstances where the notice to submit a return is issued later than expected.

There is an automatic penalty of £100 for late filing of the return. Further penalties may be due if the filing of the return is significantly delayed. These may run into hundreds of pounds.

HMRC is increasingly emphasising the importance of good records. Failure to maintain adequate records may lead to inaccurate tax returns, which could result in penalties.

Practical Tip

Remember to keep all tax related documents such as interest statements, dividend vouchers, form P60 etc. Place everything in a folder through the year as it is received. Then you can simply hand this to us when we need to prepare your self assessment return.

FAMILY MATTERS

Married couples

Spouses are taxed as independent persons, each of whom is responsible for their own tax affairs. The phrase 'spouse' whenever used in this guide includes a registered civil partner.

For spouses, there is no aggregation of income, no sharing of the tax bands and, except in limited circumstances detailed later in this guide, the personal allowance may not be transferred from one spouse to the other.

Minimising the tax bill

However, tax can be minimised if spouses equalise their income so that personal allowances, savings allowances and dividend allowances are fully utilised and higher/ additional rates of tax are minimised.

Example

In 2024/25 Ian and Angela have savings income of £50,000, dividend income of £50,000 and no other income. If this is split equally between them, the total tax bill for the couple is £6,860. If only one spouse has an income of £100,000 and the other has nothing, the total tax bill leaps to £23,092 - an additional £16,232!

Tax Tip

A donation to charity under the Gift Aid scheme benefits from tax relief. It makes sense for a higher rate/additional rate taxpayer spouse to make such donations so that they can benefit from the extra tax relief.

Tax breaks for spouses

Married couples and civil partners may be eligible for a Marriage Allowance (MA). The MA enables spouses to transfer a fixed amount of their personal allowance to their spouse. The option to transfer is not available to unmarried couples.

The option to transfer is available to couples where one party has not used all of their personal allowance and the other does not pay tax at the higher or additional rate. If eligible, one partner will be able to transfer 10% of their personal allowance to their partner which means £1,260 for the 2024/25 tax year.

Relief is given as a basic rate tax reducer with a benefit of up to £252 (20% of £1,260). It is also possible to backdate your claim for previous years - please contact us if you think this might apply to you.

Jointly owned assets

Married couples will often own assets in some form of joint ownership. This can have benefits for income tax, CGT and even IHT.

Where assets are owned in joint names, any income is deemed to be shared equally between the spouses unless an election is made to split the income in the same proportion as the ownership of the asset.

This does not apply to shares in close companies (almost all small, private, family owned companies will be close companies) where income is always split in the same proportion as the shares are owned.

Example

A buy to let property is owned three quarters by Helen and one quarter by her husband Mark. If no election is made the net rental income on which tax is payable will be split 50:50.

If an election is made the income will be split 75:25. A choice can be made according to which is the most desirable when other income of the spouse is taken into account.

Capital gains tax

Independent taxation also applies to CGT. Each spouse is entitled to take advantage of the annual exemption of £3,000 before any CGT has to be paid.

This is advantageous where assets are held jointly and then sold as each spouse can use their annual exemption to save tax.

The transfer of assets between spouses is neutral for CGT. This is sometimes done shortly before assets are

sold to minimise tax. Advice should be sought before undertaking such transactions to ensure that all tax aspects have been considered. Please contact us for CGT advice.

Note that CGT neutral transfers do not apply to unmarried couples.

Children

Transferring income to children

If a child has sufficient income to make them liable, they will be taxed in exactly the same way as an adult. However they also benefit from their own personal allowances and tax bands. Where their only income is low, there may be some scope for transferring income producing assets to the children to use up their personal allowance.

Note that if assets are provided by a parent then the income remains taxable on the parent, unless it does not exceed £100 (gross) each tax year. However, this option could be considered where grandparents or other relatives wish to pass on wealth. Be mindful of capital and inheritance tax implications of the transfers of assets.

Tax Planning

Children may be employed in the family business so as to take advantage of their personal allowance (subject to legal restrictions). It is essential that payment is only made for actual work carried out for the business and at a reasonable commercial rate.

Children and capital gains

Children also have their own annual exemption for CGT, so assets transferred to them which are expected to grow in value may prove to be advantageous.

Child Trust Funds (CTFs)

The availability of new CTFs ceased from January 2011, as did government contributions to the accounts. Existing CTFs, however, continue to benefit from tax free investment growth. No withdrawals are possible until the child reaches age 18. However, the child's friends and family are able to contribute up to the annual limit of £9,000. It is possible to transfer the investment to a Junior Individual Savings Account.

Junior ISA (JISA)

A JISA is available for UK resident children under the age of 18 who do not have a CTF account. JISAs are tax advantaged and have many features in common with existing ISAs.

They are available as cash or stocks and shares based products but a child can only have one cash JISA and one stocks and shares JISA. The annual investment is limited to £9,000.

Other children's savings options are available which may be tax efficient such as National Savings Children's Bonds and Friendly Societies' savings plans.

High Income Child Benefit Charge

A charge arises on a taxpayer who has adjusted net income over £60,000 in a tax year where either they or their partner are in receipt of Child Benefit for the year. Where both partners have adjusted net income in excess of £60,000 the charge applies to the partner with the higher income.

Note in this case 'partners' does not just include spouses and civil partners but also couples living together as if they were married or in a civil partnership.

From 2024/25, the income tax charge applies at a rate of 1% of the full Child Benefit award for each £200 of income between £60,000 and £80,000. The charge on taxpayers with income of £80,000 or above will be equal to the amount of Child Benefit paid.

Child Benefit claimants are able to elect not to receive Child Benefit if they or their partner do not wish to pay the charge.

Equalising income can help to reduce the charge for some families.

Example

Phil and Jane have two children and receive £2,213 Child Benefit. Jane has little income. Phil expects his adjusted net income to be £70,000. On this basis the tax charge will be £1,107. This is calculated as £2,213 x 50% (£70,000 - £60,000 = £10,000/£200 x 1%).

If Phil can reduce his income by £10,000 to £60,000 no charge would arise. This could be achieved by transferring investments to Jane or by making additional pension or Gift Aid payments.

Tax-Free Childcare

The scheme is available to families where all parents are working (on an employed or self-employed basis) 16 hours a week and meet a minimum income level (generally £183 a week for over 21 year olds) with each earning less than £100,000 a year. Parents who are receiving support through Tax Credits or Universal Credit are not eligible.

Parents need to register with the government and open an online account. The government 'top up' payments into this account at a rate of 20p for every 80p that families pay in. The scheme is generally limited to £10,000 per child per year. The government's contribution is therefore a maximum of £2,000 per child.

Employer Supported Childcare closed to new entrants on 4 October 2018. Parents who qualify for both schemes are able to choose which scheme they wish to use but families cannot benefit from both schemes at the same time.

15/30 hours childcare

In addition, qualifying families will be entitled to free childcare. Families can receive up to 30 hours of free childcare for three and four year olds. From April 2024, there is an additional 15 hours of free childcare for two year olds. In September 2024, this 15 hours will be available for children aged nine months or over. The free childcare is available over 38 weeks and can be used flexibly with one or more childcare providers.

To find out about all childcare options click here.

What about unmarried partners?

It still pays to equalise income as much as possible, as income tax will be minimised. However, transfers of assets may be liable to CGT and, if substantial, could also lead to an IHT liability. It is vital for unmarried couples to each make a Will if they wish to benefit from each other's estate at death.

A word of warning

Transferring assets or interests in a business between spouses may attract the interest of HMRC especially where it is obvious that it has been done primarily for tax saving purposes. Transfer of ownership of an asset must be real and complete, with no right of return and no right to the income on the asset given up.

If a non-working spouse is given shares in an otherwise one-person, private company, HMRC may, in some circumstances, seek to tax the working spouse on all of the dividends under what is known as the 'settlements legislation'. You may want to consider obtaining advice from us before entering into this type of arrangement.

WORKING FOR OTHERS

Few avoid working for others at some time in their life and most will have encountered the PAYE system operated by employers to collect the income tax and National Insurance contributions (NICs) due on wages and salaries.

The tax code

Ensuring the right amount of tax is taken relies on a PAYE code issued by HMRC and based on information given in a previous self assessment return or supplied by the employer. The employee, not the employer, is responsible for the accuracy of the code.

Code numbers try to reflect both an individual's tax allowances and reliefs and also any tax they may owe on employment benefits and in some cases other types of income. For many employees things are simple. They will have a set salary or wage and only a basic personal allowance. Their code number will be 1257L and the right amount of tax should be paid under PAYE. However, for those who are provided with employment benefits, the code number is generally adjusted to collect the tax due so that there are no nasty underpayment surprises. HMRC may also use the code to collect tax on untaxed income, tax on dividends, the High Income Child Benefit Charge and tax owing for an earlier year.

For Scottish taxpayers a letter 'S' is included in the tax code and denotes that the Scottish income tax rates apply to an employee's pay, rather than the rates and bands which apply across the rest of the United Kingdom.

For Welsh taxpayers a letter 'C' is included in the tax code.

With so many complications and some guesswork involved, getting the code exactly right can be difficult and the right amount of tax will not always be deducted.

Tax Tip

If you are unsure about your code and are anxious not to end the tax year under or overpaid, then you should have it checked. HMRC may update an individual's tax code during the tax year to reflect changes to benefits and to collect tax underpayments. Please talk to us about getting your tax code checked.

Benefits

The range of benefits available will vary significantly depending on the type of employment but can be a key part of a remuneration package. Some are completely exempt from income tax. Benefits can also give an NIC saving for the individual.

Valuation

The general rule is that the value of the benefit is the cost to the company although there are special rules in respect of some benefits. Where a benefit is taken rather than an alternative cash option, the taxable value of the benefit is the higher of the cash foregone or the taxable value under the normal benefits rules. Contact us for the correct valuation of benefits.

Company cars

Employer-provided cars, commonly known as company cars, remain a popular benefit, despite the tax charge they give rise to.

The charge on cars is generally calculated by multiplying the list price of the car by a percentage which depends on the CO_2 emissions (recorded on the Vehicle Registration Document) of the car. For hybrid cars with emissions not exceeding 50g/km, the percentage is determined by the electric mileage.

The percentage applicable may be obtained from HMRC here.

Example

David has a company car, a Hyundai Ioniq, which had a list price of £28,395 when it was provided new on 6 April 2024. The CO_2 emissions are 26g/km and its electric range is 39 miles.

David's benefit in kind for 2024/25 is £3,407, being £28,395 x 12%.

Fuel for private use

A separate charge applies where private fuel is provided by the employer for a company car. The charge is calculated by applying the same percentage figure used to calculate the company car benefit to a fixed figure which for 2024/25 is set at £27,800. No fuel benefit applies to an electric car.

Tax Planning

The fuel benefit charge can be expensive. It may be cheaper for the employee to pay for all the fuel and to reclaim from the employer the cost of business miles driven in a company car based on a specific log of business journeys undertaken.

HMRC publishes advisory fuel rates for company cars which are updated on a quarterly basis. Click here for the latest rates or contact us.

Vans

Where employees are provided with a van and the only private use of this is to travel to and from work (including any incidental private use), then no taxable benefit should arise. If there is private use beyond this, there is a benefit of £3,960 for 2024/25 and an additional £757 if fuel is provided for private as well as business journeys. In order to avoid this charge, it is advisable to have a formal written policy, detailed mileage logs and make use of vehicle tracker records. These will support the limited private use of the van and may avoid problems with HMRC in the future.

Medical insurance

The employee is taxed on the amount of the premium paid by the employer.

Home and mobile phones

There is no benefit on the provision of a company mobile phone even where it is used privately. However, this is limited to one phone per employee.

Where home telephone bills are paid by the employer, the amount paid will be taxable. The employee may make a tax deduction claim for the cost of business calls only but not the line rental.

Cheap or interest free loans

If loans made by the employer to an employee exceed £10,000 at any point in a tax year, tax is chargeable on the difference between the interest paid and the interest due at an official rate - currently set at 2.25% per annum. An exception applies for certain qualifying loans - please contact us for information.

Tax Tip

The £10,000 limit on tax free loans is an attractive perk for many employees. Even for tax-free loans over £10,000, the tax charge may still be more attractive than taking out a loan at current interest rates.

Childcare costs

Childcare costs paid for by an employer may be exempt from both income tax and NICs. This applies to a place in an employer operated nursery and to Employer Supported Childcare as long as the claimant entered the Scheme before 4 October 2018. In the latter case, the exemption is limited and excess amounts are subject to tax and NICs. Employer Supported Childcare is now closed to new claimants and has been replaced by Tax-Free Childcare.

Employees who qualify for both schemes are able to choose which scheme they wish to use but families cannot benefit from both schemes at the same time.

Pension contributions

Contributions by an employer to a registered pension scheme are generally tax and NICs free for most employees.

Expense payments

An employee can claim tax relief for expenses which are incurred wholly, exclusively and necessarily for business purposes. The main types of expenses are travelling to places for work (but not the normal place of work) and overnight accommodation.

Reimbursed expenses

An employer would normally reimburse an employee for business expenses. Employers are no longer required to report reimbursed tax deductible business expenses and therefore employees do not need to claim tax relief on these expenses.

Mileage claims

Many employers pay a standard rate of mileage to all employees who use their own cars for business journeys.

HMRC sets statutory rates for business mileage which are 45p for the first 10,000 miles in a tax year and 25p thereafter.

If the employee is paid for business miles at less than the statutory rates, tax relief is available on the difference. If, however, the employee is paid at more than these rates then the excess is taxable.

If you are paid less than the statutory rates to use your own car for business purposes remember to claim a deduction on your return or write to HMRC to make your claim.

Example

In 2024/25 Michael travels 14,100 business miles in his own car and is paid 32p per mile by his employer.

Michael can claim tax relief on an additional amount of £1,013 ((10,000 x 45p) + (4,100 x 25p)) - (14,100 x 32p).

RUNNING A BUSINESS

Starting up a business of your own is a big step and not one to take lightly. The taxation of your business is only one of many commercial and legal aspects of starting a business that you will need to consider.

Choosing a business structure

The alternative business structures are:

Sole trader

This is the simplest form of business structure since it can be established without legal formality.

The business of a sole trader is not distinguished from the proprietor's personal affairs. If the business incurs debts which are unpaid, the creditors can seek repayment from the sole trader personally.

Partnership

A partnership is similar in nature to a sole trader but involves two or more people working together.

A written agreement is essential so that all partners are aware of the terms of the partnership. Again, the business and personal affairs of the partners are not legally separate.

Sole traders and partnerships are often referred to as unincorporated businesses and the individual owners as self-employed. The trading profits of both sole traders and partnerships are subject to income tax.

Limited company

A company is a legal entity in its own right, separate from the personal affairs of the owners and the directors.

A company provides protection from liability, which means that the creditors of the company cannot make a claim against the owners or the directors except in limited circumstances.

Companies are subject to corporation tax and individuals are only subject to income tax on any funds withdrawn from the company by way of salary or dividend, for example. In the past, this has been an advantage of incorporation as corporation tax rates have been lower than income tax rates. The recent increase in corporation tax has eroded that tax advantage for companies with larger profits.

These potential advantages carry the downside of greater legal requirements and regulations that must be complied with.

Limited Liability Partnerships (LLPs)

LLPs are a halfway house between partnerships and companies.

They are taxed in the same way as a partnership but are legally a corporate body. This again gives some protection to the owners from the partnership's creditors.

In this guide we consider the differing tax treatments of the alternatives but you should choose which structure is right for you based on more than just the tax issues alone.

Taxation of unincorporated businesses

A new business should register with HMRC on commencing to trade. Income tax is paid on the profits of the business. The amount that the proprietor, or a partner in a partnership, draws out of the business is irrelevant.

From 2024/25, profits will be taxed on an actual basis; an individual will be taxed on any profits arising from the 6 April in one year to the 5 April in the next. Previously an individual would broadly have been taxed on the profits of the period of account ending in the tax year. This may add significant complexity to calculating the income tax payable for a trader who does not have a 31 March or 5 April year end as the profits will need to be apportioned into the tax year itself. We would be happy to assist you with these calculations.

Cash basis for smaller unincorporated businesses

The cash basis is an optional basis for calculating taxable profits. Previously, this was available to small unincorporated businesses upon election. If no election was made, the accruals basis applied. From 2024/25, most unincorporated businesses will have to calculate taxable profits using the cash basis as the default. The historic restrictions on who can use the cash basis have been removed. A business can elect to apply the accruals basis instead.

Under the cash basis, business profits are taxed on cash receipts less cash payments of allowable expenses. This may be more simple for the business owner to calculate. In addition, as the individual is only taxed on income actually received, they will not be subject to income tax on amounts paid late until those amounts are actually paid. Further details about the scheme:

- Cash receipts include all amounts received in connection with the business including those from the disposal of plant and machinery.
- Allowable payments include paid expenses but these still need to meet the existing tax rule of being wholly and exclusively incurred for the purposes of the trade.
- Payments include most purchases of plant and machinery, when paid, rather than claiming capital allowances.
- The interest payments restriction of £500 has been removed for 2024/25 onwards and any amount of interest can be deducted if incurred wholly and exclusively for the trade.
- Cash basis losses will be available to use in the same way as accruals losses, including sideways relief.

The optional accruals basis requires an election by the business owner for the year in which it is to apply. The election will stay in place until revoked by the business.

Do get in touch if you would like us to consider which scheme is appropriate for you and your business.

Working out profits

Not all of the expenses that a business incurs are allowed to be deducted from income for tax purposes but most are. It is important that you keep proper and comprehensive business records so that relief may be claimed.

Non-deductible expenses include those which are not wholly and exclusively for the purposes of the trade - client entertaining and private expenses of the sole trader are common examples of this. Depreciation is another type of expense which is not deductible from trading profits. Instead a tax-standardised version of depreciation, known as capital allowances, may be claimed (see later).

Trading and property income allowances

Trading and property income allowances of £1,000 per annum are available. Individuals with trading or property income of £1,000 or less do not need to declare or pay tax on that income. Those with income above the allowance are able to calculate their taxable profit either by deducting their expenses in the normal way or by simply deducting the relevant allowance.

Paying the tax

The self-employed may have to pay tax and class 4 NICs three times a year, namely:

- 31 January in the tax year
- 31 July following the tax year
- 31 January following the tax year.

The first two payments are based on the income tax and class 4 NIC liability for the previous tax year (less any amounts deducted at source like PAYE) and the final payment is the balancing amount.

Capital allowances

When assets are purchased for the business, such as machinery, office equipment or motor vehicles, capital allowances are available. As with expenses, these are deducted from income to calculate taxable profit. The below allowances are available to both unincorporated businesses (using the accruals basis) and companies.

Plant and machinery - Writing Down Allowances (WDA)

Plant and machinery purchased by a business is eligible for annual WDA of 18% per annum for most plant and machinery and 6% per annum for certain expenditure which is 'integral' to a building such as air conditioning or water systems and other long life assets. These allowances are calculated on a reducing balance basis rather than straight line on cost.

Plant and machinery - Annual Investment Allowance (AIA)

The AIA gives a 100% write off on most types of plant and machinery costs, but not cars, of up to £1,000,000 per annum. Any costs incurred in excess of the AIA will attract an annual ongoing allowance of 6% or 18% depending upon the type of asset.

Motor cars

The tax allowance on a car purchase depends on CO_2 emissions. From April 2021 purchases of cars with emissions not exceeding 50g/km attract an 18% allowance and those in excess of 50g/km are only eligible for a 6% allowance. A first year allowance (FYA) of 100% is available on new zero emission cars (for cars purchased before 1 April 2025).

Structures and Buildings Allowance (SBA)

The SBA gives allowances of 3% per annum to qualifying expenditure on the construction of new or the renovation of non-residential structures and buildings.

Companies

Unlike sole traders and partnerships who are subject to income tax on the trading profits of the business, companies are subject to corporation tax on profits. In addition, individuals may be subject to income tax on the extraction of profits from the company; thus profits may be taxed on both the company and the individual. However, there may be cash savings to operating as a company as the corporation tax rate will be lower in some circumstances than the applicable income tax rate on the profits.

Corporation Tax

The rate of corporation tax payable is dependent on the level of taxable profits in the company (plus certain dividends received by the company).

Taxable profits £	Corporation tax rate %
0 - 50,000	19%
50,000 - 250,000	25% less marginal relief
Over 250,000	25%

Unlike income tax bands, the corporation tax rate is applied to the total taxable profits of the company. Therefore a company with profits of £400,000 would have a corporation tax liability of £100,000 (being 25% of £400,000). The operation of marginal relief acts to gradually increase the rate of corporation tax from 19% to 25% - broadly this results in an effective tax rate of 26.5% on profits which fall between £50,000 and £250,000.

Companies are taxed on the basis of their accounting period which usually aligns to the period for which the company prepares accounts.

Tax Tip

Marginal relief has the impact that any profits falling between £50,000 and £250,000 are effectively taxed at 26.5%. Therefore, maximising deductions available will be particularly important for those companies whose profits fall between these thresholds. We can assist you with identifying any claims for deductions for your business.

Tax on profits

The profits of a limited company are calculated in a similar way as for unincorporated businesses and the same rules with regard to expenses and capital allowances generally apply. Remember though that the salaries paid to directors (but not the dividends paid to shareholders) are deductible from the profits before they are taxed.

Tax Planning

Companies are a popular business structure as they may result in less tax being paid overall.

However, the saving is dependent on profits and withdrawals. We would be happy to discuss the implications of incorporation with you before you decide whether or not to incorporate your business.

Capital allowances for companies - full expensing

In addition to the AIA and general writing down allowances which are available to companies as well as unincorporated businesses, from 1 April 2023 companies investing in qualifying new plant and machinery can claim:

- full expensing providing allowances of 100% on most new plant and machinery investments that ordinarily qualify for 18% main rate writing down allowances
- a first year allowance of 50% on most new plant and machinery investments that ordinarily qualify for 6% special rate writing down allowances.

This relief is not available for unincorporated businesses and will typically be most useful where companies or groups invest over the AIA of £1,000,000 in new plant and machinery.

Tax relief for expenditure on Research and Development (R&D)

Companies with expenditure in qualifying R&D activities can receive tax relief. For accounting periods starting on or after 1 April 2024, the previous SME scheme and the R&D expenditure credit (RDEC) scheme will merge. The new scheme will broadly follow the rules of the RDEC:

- There will be a 20% above the line credit.
- Loss-making companies will benefit from a notional tax rate of 19% (small profits rate) and not 25% (main rate), increasing the benefit.
- Where R&D activity is sub-contracted out, the company who bears the risk will be the one to make the claim.
- Claims will be restricted to UK-based activities and workers, subject to specific exemptions.

R&D intensive companies will operate under a separate scheme, with enhanced relief where R&D expenditure accounts for 30% or more of total expenditure.

This is a complex area. Please get in touch if you would like to know more.

Payment of tax

Corporation tax is usually payable nine months and one day after the year end but payments may be accelerated for large companies.

Tax on 'drawings'

Directors of a company will normally be paid a salary and this is taxed under PAYE as for all employees. The cost of this, including the employer's NICs, is generally an allowable expense of the company. Shareholders of the company in contrast may be rewarded by the payment of dividends on their shares. Dividends are paid out of profits after taxation.

Tax Tip

In most small companies the directors and shareholders are one and the same and so they can choose the most tax efficient way to pay themselves. Using dividends can result in savings in NICs. However, this requires careful planning, especially given the increase in corporation tax rates. Please talk to us to decide what is appropriate for you.

Warning - close company loans to participators

A close company (which generally includes owner managed companies) may be taxed where it has made a loan or advance to individuals or their family members who have an interest or shares in the company (known as participators). The tax charge is currently 33.75% of the loan if it is outstanding over nine months after the end of the accounting period. The tax charge is repaid to the company nine months and one day after the end of the accounting period in which the loan is repaid.

Further rules prevent the avoidance of the charge by repaying the loan before the payment date and then effectively withdrawing the same money shortly afterwards. This is a complex area so please do get in touch if this is an issue for you and your company.

Tax Planning

Ensure that sufficient salary and dividends are drawn from the business to prevent these charges arising unnecessarily on an overdrawn director's current account. We can also ensure that overdrawn accounts are cleared properly. Please contact us if you would like to discuss the right options for you and your business.

Employer obligations

As an employer you will have many responsibilities. These will include employment law requirements and the need to enrol workers into a work based pension scheme (Pensions Auto Enrolment) which are not covered in this guide.

Real Time Information

Real Time Information (RTI) reporting is mandatory for almost all employers.

Under RTI, employers or their agents are required to make regular payroll submissions for each pay period during the year. The submissions detail salary and other employment payments made to and deductions such as income tax and NICs made from employees. These submissions must generally be made on or before the date the amounts are paid to the employees.

Penalties apply to employers who fail to make returns on time. These penalties range from £100 to £400 per month depending on the size of the employer. Interest and penalties also apply for failing to pay on time.

The employer must also report details of expenses and benefits provided to employees.

Value Added Tax (VAT)

VAT is a tax ultimately paid by the final consumer and businesses act as the collectors of the tax.

What does VAT apply to?

VAT is chargeable on the supply of certain goods and services in the UK when made by a business that is registered for VAT (see later).

A registered business must charge VAT on its taxable supplies (broadly the sales made) which is known as output VAT. There are currently three rates of VAT which can be payable. These are the standard rate of 20%, the reduced rate of 5% and the zero rate.

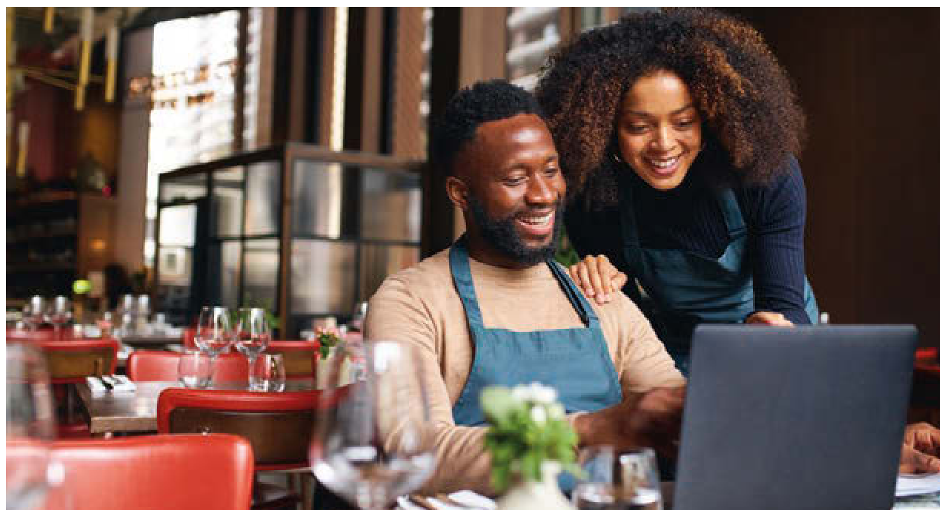
The zero rate applies where the supply is deemed to be subject to VAT but the output VAT is charged at 0%, meaning that no VAT is actually payable.

A business also pays VAT on the goods and services it buys. This is known as input tax and may be reclaimed by a VAT-registered business.

If the output tax exceeds the input tax, then a payment of the difference has to be made to HMRC. If input tax exceeds output tax a repayment of VAT will be made. This calculation is generally done on a quarterly basis. However, where repayments occur regularly, it is possible to opt for monthly VAT returns.

Some input VAT is not reclaimable by a VAT-registered business. Two common examples are VAT incurred on entertaining UK business customers and VAT on the purchase of a car.

Certain supplies of goods and services are not subject to VAT at all and are known as exempt supplies. A business that makes only exempt supplies cannot register for VAT and will be unable to reclaim any input tax.



Do I need to register?

A business must register if its taxable supplies exceed an annual figure of £90,000 (from 1 April 2024). If taxable supplies are less than this a business may still register voluntarily. So, for example, if the business makes only zero-rated sales, it can still register and reclaim the input tax suffered.

VAT can affect competition. A plumber, for example, who sells only to the general public will be at a disadvantage if they have to register for VAT. They may have to charge up to 20% more than a plumber who is not registered to earn the same profit.

On the other hand, if the same plumber only works for other VAT-registered businesses, such as building companies, then it will not matter whether they are registered because the customer will generally be able to recover the VAT that is charged.

Indeed, in general, a business that always sells to other VAT-registered businesses will normally register, even if below the annual limit, because then it can reclaim VAT on purchases and expenses. This will improve profit and can be especially relevant for new businesses because there are often high initial set up costs that carry VAT. On the other hand, registration comes at the cost of having to meet record keeping requirements, a need to submit online VAT returns and pay online and on time.

Tax Tip

When you first register for VAT you can reclaim input tax on goods purchased up to four years prior to registration provided they are still held when registration takes place. VAT on services supplied in the six months prior to registration may also be reclaimed.

Making Tax Digital (MTD)

MTD for VAT

MTD for VAT is part of a government strategy which will ultimately require taxpayers to move to a fully digital tax system.

Under the MTD for VAT rules, all VAT-registered businesses must keep digital records for VAT purposes and provide their VAT return information to HMRC using MTD functional compatible software.

There are some exemptions from MTD for VAT. However, the exemption categories are tightly drawn and are unlikely to be applicable to most VAT-registered businesses.

We can help you to meet your MTD for VAT obligations.

MTD for income tax

MTD for income tax was expected to be introduced from April 2024. This has now been delayed; self-employed individuals and landlords with income over £50,000 will be mandated to apply MTD from April 2026. Those with income over £30,000 will be mandated from April 2027 and the government will review the application of MTD for smaller businesses.

We can help you assess when MTD will be required for your business and to meet your obligations.

TAX AND YOUR INVESTMENTS

Setting aside income in the form of savings is important for everyone, to provide for the unexpected or to build up a nest egg to enjoy in retirement.

Pensions

Making pension contributions

Pensions are one of the most tax efficient forms of saving. Taxpayers benefit from tax relief on contributions at their marginal rate and investment income and capital gains will accrue within the scheme largely tax free.

An individual is entitled to tax relief on personal contributions in any given tax year up to the higher of 100% of earned income or £3,600 (gross).

Where employee contributions are made to occupational pension schemes these are usually deducted from salary before an employee's tax is calculated. Tax relief is therefore given automatically.

Contributions to personal pension schemes are paid net of basic rate tax and the pension provider will then recover that basic rate tax from HMRC. Higher and additional rate relief, if appropriate, can be claimed from HMRC.

Employer pension contributions are an exempt benefit for the employee and a deduction from profits may be available to the employer.

There are controls which serve to limit the availability of tax relief on high levels of contribution. These are complex but, put simply, they may give rise to a tax charge if annual contributions exceed £60,000. This threshold is reduced for high income individuals; generally where a taxpayer has adjusted income in excess of £260,000 the maximum annual contribution possible will be restricted by £1 for every £2 for the excess income. The minimum annual allowance available after this restriction is £10,000.

Tax Tip

Making pension contributions may limit the reduction of your personal allowance where you have income in excess of £100,000. We can assist you with planning your pension contributions.

Pensions freedom

Taxpayers have choice and flexibility when it comes to accessing their personal pension fund. Options include taking a tax free lump sum of 25% of fund value and purchasing an annuity with the remaining fund or opting for a more flexible drawdown.

The flexible drawdown rules allow for total freedom to access a pension fund from the age of 55. Access to the fund may be achieved in one of two ways:

- allocation of a pension fund (or part of a pension fund) into a 'flexi-access drawdown account' from which any amount can be taken over whatever period the person decides
- taking a single or series of lump sums from a pension fund (known as an 'uncrystallised funds pension lump sum').

A taxpayer will typically take their tax-free lump sum from the fund at the same time as making an allocation into a flexi-access account. Where uncrystallised lump sums are withdrawn, 25% of each payment is tax free.

The total amount which can be withdrawn as a tax free lump sum (under whichever option chosen) is generally limited to a total of £268,275, except in certain circumstances where previous protections apply. Other income withdrawn from a fund is taxable as income.

The rules on pensions drawdown are complex and there are a number of options for taking a pension. Getting the right advice at the point of retirement is therefore crucial.

Money Purchase Annual Allowance (MPAA)

The government is aware of the possibility of people taking advantage of the flexibilities by 'recycling' their earned income into pensions and then immediately taking out amounts from their pension funds. The MPAA sets the maximum amount of tax-efficient contributions an individual can make at £10,000 per annum in certain scenarios.

Tax free savings

Tax Tip

Don't forget to use the dividend and savings allowances. These allowances tax £500 of dividends and up to £1,000 of savings income at 0%.

Individual Savings Accounts (ISAs)

ISAs are free of income tax and CGT. There are maximum investment limits which apply for each tax year but, over several years, large investments can be built up. The overall annual ISA savings limit is £20,000. Investors can choose to invest in a cash ISA, stocks and shares ISA or an Innovative Finance ISA as long as they do not exceed the investment limit.

Lifetime ISA

The Lifetime ISA is available to adults aged between 18 and 40. Individuals are able to contribute up to £4,000 per year and receive a 25% bonus from the government (up to £1,000). If £4,000 is invested, the investment limit for the other types of ISAs falls to £16,000.

Funds, including the government bonus, can be used to buy a first home worth up to £450,000 at any time from 12 months after the first subscription or can be withdrawn from age 60 completely tax-free.

Other tax efficient investments

The following investments work in varying ways. You should consider your needs in detail before entering into any commitments.

National Savings and Investment premium bonds

Premium bonds are tax free and you could win £1 million. However, the annual rate of return is not predictable.

Single premium insurance bonds

The growth on insurance bonds is taxed at 20% and paid directly out of the bond. For a higher rate taxpayer bonds provide a means of deferring income into a subsequent period when it may be taxed at a lower rate. Withdrawals of up to 5% of the original investment can be made each year without incurring an immediate tax charge.

Complex tax reliefs can be available on withdrawal or on maturity of the bonds. Please consider taking advice on the implications prior to making withdrawals in excess of the annual 5% limit and on maturity.

Venture Capital Trusts (VCT)

These bodies mainly invest in the shares of unquoted trading companies. An investor in the shares of a VCT will be exempt from tax on dividends and on any capital gain arising from disposal of the shares in the VCT (note limits apply where large investments have been made in any one tax year). Income tax relief of 30% is available on subscriptions for VCT shares, up to £200,000 per tax year, as long as the shares continue to be held for at least five years.

The Enterprise Investment Scheme (EIS)

The tax reliefs for EIS investors are:

- Income tax relief at 30% is available on new equity investment (in qualifying unquoted trading companies) of up to £1 million. A higher limit of £2 million may apply to investments in 'knowledge intensive companies'.
- A CGT exemption on sales of EIS shares held for at least three years.
- If the gain on the sale of any chargeable asset (eg quoted shares, second homes, etc) is reinvested in EIS shares, the gain on the disposal can be deferred.

Seed Enterprise Investment Scheme (SEIS)

The tax reliefs for SEIS investors are:

Income tax relief at 50% in respect of qualifying SEIS shares up to an annual maximum investment (in all SEIS companies) of £200,000.

- A CGT exemption where SEIS shares are sold more than three years after they are issued (as for EIS).
- A further CGT exemption of 50% where an individual makes a capital gain and reinvests the gain in qualifying SEIS shares. Note this is an exemption rather than a deferral as for EIS.

DISPOSALS AND CAPITAL GAINS TAX

Making the most of your investments requires some understanding that CGT arises on the sale of most assets and, subject to various reliefs and exemptions, is payable on the difference between the sale proceeds and the original cost. Where property has been improved then these capital costs may be available to reduce the value of the gain.

The disposal of your main residence does not usually result in a chargeable gain.

The CGT annual exemption results in the first £3,000 of gains for 2024/25 being tax free.

Tax Tip

The amount of the annual exemption is reduced from £6,000 to £3,000 from 2024/25. Plan disposals to ensure reliefs are used where available to minimise chargeable gains. Consider transferring assets to spouses to take advantage of unused exemptions.

In general CGT is payable at 10% where total taxable gains and income, after taking into account all allowable deductions are less than the income tax basic rate band. CGT is payable at 20% on gains, or any parts of gains, above this limit. However, higher rates (18% and 24%) apply for chargeable gains on residential property that do not qualify for private residence relief.

Reporting of CGT

For non-residential property disposals, these can be reported on the self assessment tax return or via a 'real-time return' if they are not otherwise required to submit a tax return. Payment of CGT is due by 31 January following the tax year of the disposal.

CGT on residential property disposals must be reported and a 'best estimate' payment of account made within 60 days of completion of sale.

Business Asset Disposal Relief

Business Asset Disposal Relief (BADR) may be available on the first £1 million gains from the disposal of certain businesses during an individual's lifetime. Qualifying gains are taxed at a 10% rate of tax. Qualifying business disposals include:

- qualifying shareholdings in a trading company (broadly where an employee or office holder owns over 5% of shares and voting rights)
- the whole or part of an unincorporated business
- the disposal of assets on cessation of a business.

There needs to be a qualifying period of ownership of two years up to the date of disposal.

Where an individual makes a qualifying business disposal, relief may also be available on an 'associated disposal'. An 'associated disposal' is a disposal of an asset which is used in a qualifying company of the individual or used in a partnership where the individual is a partner.

The rules on qualifying disposals, particularly in relation to qualifying shareholdings, can be complex. Please do get in touch if you would like to discuss whether BADR might be available or how to meet the requirements.

Investors' Relief

A 10% CGT rate applies to external investors (i.e. not employees or officers of the company) in unlisted trading companies. Conditions apply:

- shares must be newly issued and subscribed for by the individual for new consideration
- be in an unlisted trading company, or an unlisted holding company of a trading group
- have been issued by the company on or after 17 March 2016
- have been held continuously for a period of three years before the disposal.

An individual's gains for Investors' Relief will be subject to a lifetime cap of £10 million.

PROPERTY MATTERS

Direct investment in residential property has always been a popular form of investment.

Buy to let

The UK property market, whilst cyclical, has proved over the long term to be a successful investment. This has resulted in a massive expansion in the buy to let sector.

Traditionally, buy to let involves investing in property with the expectation of capital growth with the rental income from tenants covering the mortgage costs and any outgoings. However the gross return from buy to let properties can change. Investors also need to take a view on the likelihood of capital appreciation exceeding inflation. Investors should take a long-term view and choose properties with care.

Practical Tip

When choosing between investments always consider the differing levels of risk and your requirements for income and capital in both the short and long term. An investment strategy based purely on saving tax is not appropriate.

Devolution of Property Taxes

Stamp Duty Land Tax (SDLT) applies in England and Northern Ireland, Land and Buildings Transaction Tax (LBTT) in Scotland and Land Transaction Tax (LTT) in Wales.

Higher rates of SDLT, LBTT and LTT apply on purchases of additional residential properties. The rates are 3% above the SDLT rates, 6% above the LBTT rates and 4% above the LTT rates.

There are some exemptions from the rules. One of these covers the replacement of a main residence within certain time limits. Please contact us for further advice on this area.

Tax on rental income

Income tax will be payable on the rents received after deducting allowable expenses. Allowable expenses include mortgage interest on non-residential properties only, agent letting fees and the cost of replacing furnishings. A property allowance is available such that property income of £1,000 or less does not need to be reported to HMRC.

Restriction of relief for finance costs on residential lettings

The amount of income tax relief landlords can get on residential property finance costs is restricted to the basic rate of income tax. Relief is given by way of a tax reducer rather than the costs being deductible in full from the rental income.

Property investment company

Sometimes it may be preferable to operate the property investment business through a company. Clearly there will be non-tax issues to consider (as for 'running a business') but some of the key tax differences are:

- generally lower rates of corporation tax than income tax on rental profits
- interest on loans to purchase the property will be deductible from profits in a company (rather than as a tax reducer for interest on residential property for individuals)
- capital gains for companies are subject to corporation tax rather than CGT
- no annual exempt amount for companies
- extraction of funds from the company will often result in additional tax charges
- additional taxes may be payable where residential properties worth more than £500,000 are held through a company.

Renting a room

There has been an increasing number of individuals seeking to generate income from their own home either by taking on a lodger or through ad-hoc lettings such as Airbnb or Vrbo.

Rent a Room relief

Income from letting a room within your main residence is property income. However, if gross rents for a tax year do not exceed £7,500, no income tax is payable. This relief is known as Rent a Room relief.

If rents exceed £7,500, the taxpayer has a choice whether to deduct actual expenses or £7,500.

The £7,500 limit is a maximum which can apply to either a property or a person, so if two individuals jointly own a property and take in a lodger, they must share the limit at £3,750 each.

Capital gains

Having a single lodger sharing the use of facilities such as the kitchen should not impact a taxpayer's ability to claim private residence relief (below).

Main residence - other considerations

An individual's or married couple's only or main residence is generally exempt from CGT under a relief known as private residence relief. The exemption extends to grounds of up to half a hectare provided this is not used for any other purpose.

Tax Planning

Larger grounds may also be exempt, as can the sale of part of the garden or grounds for development. However, professional advice is recommended to plan for the best outcome.

There must also be clear evidence of occupation as a main residence and not just ownership. Certain periods of absence from the property can be deemed to be periods of occupation and as such, can count towards the exemption from CGT.

The exemption from CGT only applies where the whole property is occupied. Apportionment may be required where part of the property is used for business purposes or is let out with resulting gains being potentially taxable.

Letting relief may apply where you have multiple lodgers or let out part of your home. We would be happy to discuss your specific circumstances with you.

More than one residence

Where an individual (or married couple) has two or more residences, only one residence at any one time can be treated as the main home for exemption. This is done by an election. Provided a particular residence has been the main residence at some time, then generally the last nine months of ownership is exempt. This applies even if another residence has become the main residence during this time.

Example

Joe's house in Luton is his private residence, which he has owned for eight years. Fed up with commuting, he buys a flat in central London and elects for this to be his main residence. Exactly five years later he sells his home in Luton.

The Luton home is exempt for the first eight years whilst he was living in it and for the last nine months because, even though he had another home which was his main residence during this time, the last nine months is always exempt provided the home in question qualified as the main residence at some point.

8.75/13 of the gain on the Luton home will be exempt from CGT. Upon the eventual sale of the flat the whole of that gain will also be exempt.

The main residence exemption can be complex. Please contact us for further advice before making transactions in property.

Inheritance tax

The general growth in house prices has caused real IHT worries because retaining the family home in the estate when it is often the largest asset could result in an IHT liability of up to 40%. At the same time, finding a way to deal with it efficiently for IHT is difficult because individuals need a place to live. See 'preserving the inheritance' for further details.

PRESERVING THE INHERITANCE

IHT has some unique features and may be charged on some lifetime gifts, not just on an individual's death estate. In addition, the threshold for paying IHT (also called the nil rate band) is currently frozen at £325,000 until April 2028 and has been at this level since 2009/10. Therefore, increasingly more estates are falling within the charge to IHT.

Planning to minimise IHT is something that many put off until it is too late and early attention to this tax is almost always worthwhile.

Practical tip

If you die without a Will, the intestacy provisions will apply and may result in your estate being distributed in a way you would not have chosen. Keep your Will up to date to reflect changes in the family situation. In particular, Wills need to be reviewed and amended as necessary on marriage/civil partnership or on divorce. The precise position depends on whether English or Scottish law applies.

Key features

- IHT is charged on a person's estate when they die and on certain gifts made during their lifetime.
- The rate of tax on death is 40% and 20% on lifetime chargeable transfers. The first £325,000 is not chargeable.
- Many lifetime gifts are treated as 'potentially exempt transfers' (PETs). So long as the donor lives for at least seven years after making the PET there will be no possibility of an IHT charge whatever the size of the gift.
- There are numerous exemptions and reliefs.

So what's the problem?

IHT is still a problem because:

- Many are simply not in a position to make substantial lifetime gifts because it will leave them with insufficient capital to live on. As a consequence there is likely to be significant value retained in estates on death.
- Despite the introduction of the residential property nil rate band, which gives some measure of relief, many individuals have a home which will use up the bulk of the nil rate band and any excess remaining assets, such as investments and cash reserves, may be charged to IHT at 40%.

Mitigating the liability

Do not waste your exemptions. Regularly using IHT exemptions will build up funds outside of the estate without incurring an IHT liability.

The main exemptions are:

- an annual allowance of £3,000 per donor per year (can be carried forward for one year only if unused)
- small gifts not exceeding £250 in total per donee per tax year
- gifts made out of surplus income that are typical and habitual
- gifts made in consideration of marriage up to £5,000 if made by a parent, £2,500 by grandparents and £1,000 by others
- gifts to charities, whether made during lifetime or on death
- gifts between spouses and registered civil partners, whether made during lifetime or on death.

Note that spouses/civil partners each have their own exemptions.

Planning in lifetime

If possible you should make absolute gifts in your lifetime. A gift to an individual will be a PET so there will be no liability if you survive seven years. Even if you fail to survive for all of that period there may be a tax saving because the charge which will arise on the PET will be based on the value of the asset when it was originally gifted and not on the value at the date of death. If the value of the gift is below the threshold there will be no charge on the PET but the gift will use up some of the nil rate band (NRB) on death. This means that there may be more tax to pay on the assets still in the estate on death.

Tax Planning

Each spouse/civil partner can take advantage of the NRB. Furthermore, gifts between them are generally exempt. Therefore it pays to use this exemption to broadly equalise estates so that both partners can make full use of exemptions and the NRB.

Remember that you cannot continue to benefit in any way from the asset gifted because this will render the gift ineffective for IHT purposes. You cannot, for example, give away your home to your children but continue to live in it rent free.

Use available reliefs

Important reliefs of up to 100% are available on business assets such as shares in a family trading company or on agricultural property. It is important that these reliefs are utilised because once the asset concerned is sold the relief will be lost. They can only be used in connection with transfers that are chargeable to IHT.

Consider using trusts

As stated previously, many lifetime gifts are PETs (so may be removed from the charge to IHT entirely). However, the donor ceases to have any control over what the beneficiary does with the gift.

This is where trusts can be useful. Most transfers into trust are immediately chargeable to IHT but if the value of the assets transferred into trust within a seven-year period is below the NRB, there is no charge. Where above the NRB, a lower IHT rate applies to lifetime gifts than the death estate.

The rules are complex but significant tax savings can be achieved with careful planning. Please get in touch if you are interested in making gifts to trusts.

Use the NRB on death

On death, assuming the NRB has not already been utilised in the last seven years, it pays to ensure that it is not wasted. This gave rise to practical problems in that if assets equal to the NRB were bequeathed to children in the Will, the surviving partner may be left short of funds. The rules were therefore altered several years ago to allow the proportion of unused NRB on the death of the first spouse to be transferred to the estate of the surviving spouse. The transferred NRB can only be used against the estate of the second spouse on death.

Use the main residence nil rate band (RNRB)

An additional nil rate band, the RNRB, may be available where a residence is passed on death to direct descendants such as a child or a grandchild. The RNRB is £175,000 in 2024/25 and is frozen until April 2028. The RNRB can only be used in respect of one residential property which has, at some point, been a residence of the deceased.

Any unused RNRB may be transferred to a surviving spouse or civil partner.

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

There is a tapered withdrawal of the RNRB for estates with a net value (after deducting any liabilities but before reliefs and exemptions) of more than £2 million. The withdrawal rate is £1 for every £2 over this threshold.

Example

Tom died leaving the whole of his estate of £800,000 to his wife Pru. A few years later Pru died leaving her whole estate of £1,100,000 to her children including the family home worth £600,000.

As Tom's estate was left to Pru, 100% of his NRB and RNRB is available. This is in addition to Pru's own NRB and RNRB. Therefore IHT on Pru's death would be calculated on just £100,000 (£1,100,000 - [£325,000 x 2] - [£175,000 x 2]).

Charitable giving

Legacies to registered charities will reduce the value of the chargeable estate and thus save 40% IHT.

In addition the legacies may result in a lower IHT liability on the estate which remains chargeable. A reduced rate of IHT applies where 10% or more of a deceased's net estate (after deducting IHT exemptions, reliefs and the nil rate band) is left to charity. In those cases the 40% rate will be reduced to 36%.

Use life assurance

Life assurance arrangements can be used as a means of removing value from an estate and also as a method of funding IHT liabilities. A policy can be arranged to cover IHT due on death. It is particularly useful in providing funds to meet an IHT liability where the assets are not easily realised like family company shares.

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