

Money Matters

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Mind your allowances

Reductions to some tax allowances and the freezing of others will hit many individuals and businesses hard. The tax changes for 2023/24 also require a rethink of the strategy for small company owners of drawing income as dividends rather than salary.

Until fairly recently, it was usually beneficial for tax for shareholder directors to take dividends instead of bonuses, because dividends are taxed at lower rates than earnings. However, from 1 April 2023:

- the main rate of corporation tax (CT) jumped from 19% to 25%;
- companies with profits up to £50,000 remain subject to 19% CT;
- in effect most companies with profits between £50,000 and £250,000 pay CT at 26.5% on profits between these limits.

For income tax, from 6 April 2023:

- only the first £1,000 of dividends an individual receives is tax free, down from £2,000;
- the 45% additional rate (39.35% on dividends and 47% top rate for Scottish non-dividend, non-savings income) is charged on income over £125,140 (previously £150,000).

For higher rate and additional rate taxpayers these changes largely remove the tax benefit of paying dividends out of company profits above £50,000.

Even at £1,000, the tax-free dividend allowance should not be overlooked. But remember to take into account dividends received from other investments, because these might have used all or part of the allowance.

The biggest cut has been to the capital gains tax (CGT) annual exempt amount (AEA), which for individuals is now £6,000 and will fall to £3,000 from April 2024. If you are married or in a civil partnership, spreading investments between you will double up on the exempt amount.

The reductions in the AEA and dividend tax-free allowance increase the attraction of investing in pensions and ISAs, because income and gains within these wrappers are exempt from tax. The ISA subscription limit for 2023/24 remains at £20,000, but key pensions annual allowances have increased. Remember you need salary or self-employment income to support pension contributions.

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Improving employee happiness

High inflation has led to a cost-of-living crisis and strike action by groups of employees demanding pay rises in line with inflation. Strikes are less common in smaller businesses, but their employees will also be feeling the pinch, and the temptation of higher wages elsewhere. What can you do to help?

Financial stress often leads to lower job satisfaction, but increasing employee pay in line with inflation may be unaffordable for many businesses. There are, however, steps employers can take to help bridge the gap between an affordable pay rise and inflation pressures.

- Inflation is predicted to fall. A one-off payment could help staff cope with immediate financial pressures without committing a business to higher salary bills in the longer term.
- Linking pay more closely to performance means that a salary rise at least partly pays for itself by increasing business income.
- Education about budgeting and financial decision making helps employees make their money go further and understand the longer-term consequences of potential money-saving moves such as cancelling pension contributions.
- Employers could even provide additional benefits in kind that they can access more cheaply than individual employees, for

example gym membership or discounted goods and services.

- Likewise a business may be able to provide medical insurance for employees at a lower cost than employees taking out their own policies.
- Setting up a cycle-to-work scheme gives employees the chance to save public transport costs and may provide a tax advantage depending on how it is set up. It also gives rise to potential health benefits for employees.
- Meals in a staff canteen, a mobile phone and some forms of childcare support are valuable tax-free benefits for employees where it is feasible for these to be provided.

Many employee benefits are taxable, but there are some non-financial benefits that can promote employee wellbeing and retention. Flexible working and home working have grown in popularity especially since the Covid-19 lockdowns. Such practices make it easier for employees to manage childcare and other responsibilities and improve work-life balance. Working at home also reduces commuting costs.



Pensions shake up – what it could mean for you

The headline-grabbing announcement from the March Budget was the abolition of the lifetime pension allowance. However, this may not be quite as advantageous for higher paid individuals as some reporting suggests. The other pension changes announced in the Budget should help less well-off taxpayers with their retirement planning.

Lifetime allowance

The lifetime allowance (LTA), which previously set a maximum of tax relieviable pension savings an individual could hold during their lifetime, has effectively been abolished from 6 April 2023. The reason the abolition may not be quite as advantageous as suggested is because of what has not changed:

■ Pension saving is particularly beneficial if the rate of tax relief on contributions going in is higher than the tax rate payable on the pension coming out on retirement. The ability to take a 25% tax-free lump sum greatly helps in this equation, but the tax-free amount has now been fixed at £268,275, which is 25% of

the most recent lifetime allowance. It could be higher if the lifetime allowance has previously been protected.

- Although there is now no maximum to the amount of pension savings that can be built up during a person's lifetime and then passed on to descendants free of inheritance tax (IHT), this is not the complete picture.
- Death benefits only pass completely tax-free on death before age 75, and – with the wealthy having longer life expectancy – this will be the exception rather than the rule.
- For deaths occurring on or after age 75, death benefits are normally taxed as pension income in the hands of the recipient. Although some planning is possible here, the

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tax rate is going to be 45% if pension savings are substantial; higher than the 40% rate of IHT payable on death.

Be warned that when it comes to long-term pension planning, this is an area of tax which sees change every few years. An election is less than two years away, and the Labour party has said they will reinstate the lifetime allowance.

Annual allowance

The annual allowance has been increased from £40,000 to £60,000. Pension contributions are often only made to eliminate higher or additional rate tax liabilities, and covering the 60% charge when the personal allowance is tapered away is particularly beneficial.

The uplift will help any self-employed people who can see wide fluctuations in income from one year to the next.

For example, a self-employed person with anticipated profits of £150,000 will now be able to make a pension contribution of £50,000, with £25,140 of this benefiting from 60% tax relief, and the remainder at 45%. However, the problem – as always – is forecasting profits before the pension contribution deadline of 5 April.

Money purchase annual allowance

The money purchase annual allowance has been increased from £4,000 to £10,000. This increase could benefit those who have taken funds out of their pension pot to help pay for the rising cost of living. Previously, they would have only been able to rebuild their pension savings by investing a maximum of £4,000 annually but can now save £10,000 if they can afford to do so.

Anyone who has had to dip into their pension savings will be also pleased that it looks as if the plan to bring forward a rise to the State pension age to 68 has been postponed for now.

News in brief...

Non-UK charities excluded from IHT exemptions

Anyone intending to leave 10% of their estate to charity so inheritance tax is paid at the reduced rate of 36% needs to be aware that non-UK charities won't count from 1 April 2024. Wills may need to be amended.

R&D enhanced credit

From 1 April 2023, loss-making R&D intensive SMEs can qualify for a payable credit of 14.5% instead of the normal 10%. Eligibility is based on the company's qualifying R&D expenditure for a period being at least 40% of total expenditure.

IHT on non-UK agricultural property and woodlands

Agricultural property and woodlands generally qualify for 100% inheritance tax relief. From 6 April 2024, relief will be restricted to property situated in the UK, with any property situated in the EEA, the Channel Islands and the Isle of Man no longer qualifying.





New tax year resolution: don't be careless

The former Chancellor, Nadim Zahawi, is reported to have paid a 30% tax penalty as part of a £5 million settlement with HMRC. The penalty was for a careless, but not deliberate, error, raising the question: what constitutes carelessness?

HMRC only charges a penalty if there is a lack of reasonable care. The penalty will be higher if an inaccuracy is deliberate, but can be reduced, sometimes down to nil, if a taxpayer is helpful in correcting the inaccuracy.

Lack of reasonable care

A penalty for carelessness is charged where an error is not deliberate, but a taxpayer has failed to take reasonable care. This will differ depending on a taxpayer's circumstances and abilities. HMRC expects each person to make and preserve sufficient records for them to make a correct and complete tax return.

- A taxpayer who has to deal with a transaction with which they are not familiar should find out about the correct tax treatment or seek appropriate advice. This will generally be the case where an asset is disposed of, with capital gains tax payable as a result.
- If still unsure, the taxpayer should draw HMRC's attention to the entry and the uncertainty when submitting the relevant tax return.

This approach will mean reasonable care has been taken, and, even if the wrong tax treatment has been applied, it will not have been done so carelessly.

Unprompted disclosure

Unprompted disclosure can result in a large penalty reduction, but a disclosure will only be treated as unprompted if the taxpayer has no reason to believe HMRC has discovered the inaccuracy or is about to.

A disclosure will therefore be a prompted one if it is made after HMRC has already informed the taxpayer that they are going to carry out a compliance check into the relevant tax return.

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Increasing company transparency

Small companies and micro-entities will have to file their profit and loss accounts at Companies House when the Economic Crime and Corporate Transparency Bill, currently going through Parliament, becomes law. The aim of the change is to improve transparency by making more financial information available to the public.

At present small companies have to file a balance sheet each year but adding a profit and loss account and directors' report is optional. Most choose not to do so. Putting key information on the public record, including turnover and profit or loss, is intended to help creditors and consumers make better-informed decisions.

The Bill will also give Companies House greater powers to check, remove or decline information filed. Currently all submissions are accepted without questioning their reliability. Other measures aimed at ensuring accuracy include:

- Anyone setting up, running, owning or controlling a UK company will have to verify their identity with Companies House.
- For existing companies, all directors and people with significant control will have to verify their identity within a set period.
- Anyone acting on behalf of companies will also need to verify their identity before they can file information.
- Companies House will be able to challenge suspicious information and inform security agencies of potential wrongdoing.

The legislation will also help company directors to better protect personal information published by Companies House that may put them at risk of fraud or other harm.

In addition, filing processes for small businesses will be digitised. All accounts will have to be filed fully tagged using iXBRL. This is an open standard that enables a single document to provide both human-readable and structured, machine-readable data. Most companies will not be able to file on paper and the number of times a company can shorten its annual reporting period will be limited.

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Do I need to change my year end? Basis period reform for unincorporated businesses

Sole traders and partnerships are currently taxed on their profits from accounts which end in the relevant tax year. These rules are changing with effect from the tax year 2024/25.

The new rules will tax profits within the tax year 6th April to 5th April, regardless of the year end. For example a year ended 31st May 2024 will currently be taxed in the 2024/25 tax year. Under the new rules, profits for the 2024/25 tax year will be based on the 12 months ended 5th April 2025. So, in 2024/25 we need two months profits from the year ended 31 May 2024, and 10 months profits from 31 May 2025. This will result in additional accounting and tax calculations, which may cause confusion when reconciling your profits.

H M Revenue & Customs are 'encouraging' businesses to change to a year end of 5th April or 31st March.

We suggest you consider changing the year end to the 31st March, unless there are fundamental commercial reasons not to. If you choose to change the year end, the transitional period for this will commence April 2023 to ensure business

year ends are ready for the 2024/25 tax year.

This would mean that the year ended 31st May 2022 would be the last year end with that accounting period. This is taxable on the 2022/23 Tax Return as normal.

The transitional reporting period would be from 1st June 2022 to 31st March 2024! This would be taxed in the 2023/24 Tax Return. There are one off tax calculations for this transitional year. If excessive profits are calculated due to this transitional period, there are rules which will allow this extra profit to be spread over five years.

Future year ends will be 31st March, aligned with the tax year. The electronic Making Tax Digital submissions do not start until 2027. Whether you change your year end or not, the deadline for submitting Tax Returns and payment of any tax is still 31st January the following year. There are no changes to Limited Company year end rules.

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