

# A Guide to Tax



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**For individuals, there are three main taxes to consider:**

- **Income tax**
- **Capital gains tax**
- **Inheritance tax**

**When planning for your financial future, it is important to understand the characteristics of each type of tax so that you can structure your finances in a tax-efficient way.**

**Your Honister adviser will be able to offer general advice in the area of tax planning.**

## **Income Tax**

Income Tax is a tax on income. Not all income is taxable and you're only taxed on 'taxable income' above a certain level. Even then, there are other types of relief and allowances that can reduce your Income Tax bill - and in some cases mean you've no tax to pay.

Nearly everyone who is resident in the UK for tax purposes receives a 'Personal Allowance', which is an amount of taxable income you're allowed to earn or receive each year tax-free. This allowance increases at age 65 and again at age 75. Married couples' allowance only applies where at least one partner was born before 6 April 1935.

You need to be clear as to how your investments affect your tax position. For example if the level of your income falls below the total of your allowances, investments should be made in areas where gross returns are obtainable, or at least where tax is recoverable. If you are a higher-rate taxpayer, the most appropriate investments are likely to be those which produce tax-free returns or capital growth with minimal interest or dividends.

The starting rate of 10% for the tax year 2011/12 applies to the first £2,560 of taxable savings income (i.e. after allowances and relief). Therefore, if an individual's taxable non-savings income is more than £2,560 the 10% savings rate will not apply.

If you are self-employed there are expenses which you can offset against your income. This can result in a significant reduction in your tax bill.

## **Independent Taxation**

The earnings and investment income of a husband and wife are taxed separately at their individual rates, so that a wife's investment income is taxed at her own rate without regard to her husband's. Careful thought needs to be given, therefore, as to the name in which investments are made. If investments are held jointly, they are normally deemed to be held on a 50/50 basis.

## **Capital Gains Tax**

This tax is payable on profits made on the disposal of assets (e.g. shares, unit trusts, a second property).

There are certain exceptions, most notably your main residence and Gilts (Government stock). Each individual is entitled to an annual exemption and currently transfers between husband and wife are free of tax.

From April 2012 the consumer price index (CPI) will be used as the default indexation assumption for capital gains tax (CGT) annual exempt amount instead of the retail price index (RPI) that is currently used.

For disposals on or after 6 April 2009 there is a single rate of capital gains tax of 18%. The annual exempt amount is £10,600 - 2011/12.

It is possible to offset losses against gains. You should aim to sell assets in a year where you have few other gains. If you have already used up your annual exemption you may wish to defer disposals until after 5 April.

The lifetime limit on gains qualifying for capital gains tax (CGT) Entrepreneurs' Relief was increased from £5 million to £10 million on 6 April 2011.

For individuals, the rate of CGT remains at 18 per cent where total taxable gains and income are less than the upper limit of the income tax basic rate band.

Since 23rd June 2010 the new rate of CGT of 28 per cent applies to taxable gains (or any parts of gains) above the upper limit of the income tax basic rate band. For trustees and personal representatives of deceased persons, the rate of CGT remains at 28 per cent.

Business assets enjoy particularly favourable relief - reference should be made to an accountant for full details. Broadly speaking gains arising on the disposal of certain business will qualify for an effective rate of CGT of 10% (2010/11).

## **Inheritance Tax**

When you die your chargeable estate is valued. This is basically the value of property and investments, less any debts, and excluding certain exempt assets (such as assets left to your spouse, charity or approved national causes).

Tax is then levied on any sum in excess of the IHT zero rated tax band (the "nil rate band") which is usually amended at each Budget (£325,000 per person - 2011/12) In the 2011 budget it was announced that this amount will remain frozen until April 2015 .

For deaths which occur on or after 6th April 2012, a reduced rate of IHT will apply where a deceased leaves 10% or more of his/her net estate to charity. The net estate here is that remaining after deductions of IHT exemptions, relief and the nil rate band. In such cases, the usual 40% rate will be reduced by 10% to 36%.

In addition, from 9 October 2007 it has been possible to add the proportion of unused nil rate band from the first death to the surviving spouse or civil partner' own nil rate band when they die. This can effectively double the current allowance where one nil rate band would otherwise have been wasted.

For a married couple or registered civil partners, this can mean that (at current levels) up to £650,000 of the combined estate could pass free of IHT. Assets that exceed this value on death will be taxed at 40%.

'Potentially exempt transfers' are gifts that do not give rise to an immediate liability, but which carry an underlying charge to tax that crystallises if the transferor dies within seven years of making the gift. If you survive for the full seven years, no tax is payable. Most lifetime transfers to individuals (not covered by the annual IHT exemptions) are potentially exempt. You should plan to use all of the available exemptions before making this type of gift.

The impact of Inheritance Tax can be reduced significantly with careful planning and by the careful construction of a Will. Honister Partners will be pleased to advise you.

## Self Assessment

The Inland Revenue usually dispatches self-assessment forms immediately following the end of the tax year to be assessed.

Do not leave everything to the last minute, if you miss the final filing deadline of 31st January following the end of the tax year, you will leave yourself open to interest, penalties and surcharges. There is, however, a lot to be said for submitting a return before the 30th September initial deadline - this will guarantee the completion of the tax calculations by the Inland Revenue and will give you the option of having small tax underpayments collected through PAYE coding adjustments.

## Tax Tips

- Make sure that you use personal income tax relief and capital gains tax allowances, wherever possible, consistent with your own investment objectives.
- Divide both assets and income between husband and wife to take full advantage of the independent taxation rules.
- Make use of all your entitlements to invest in tax efficient investments such as ISAs and National Savings.
- Consider your options carefully before paying off your mortgage.
- Ensure that your investments are correct for your personal circumstances and sufficiently flexible to allow for changes in family finances and circumstances and tax legislation.
- Review investments each year in the light of Budget changes. What is right for this year may not be next year.
- Advance planning can significantly reduce potential liability to inheritance tax, but take care to ensure that gifting money is not done at the expense of your future financial security.
- Make sure the Trustees of your occupational pension scheme hold an up to date Nomination form setting out to whom you wish any lump sum benefit paid.
- Retain all tax papers, interest details, P60, P11D, etc in a safe place so that you can complete tax returns promptly and accurately.
- Check tax assessments and notices of coding for accuracy. If in doubt, contact the tax office for clarification.

**For further information or to book an initial consultation,  
please call us free on 020 8760 9940.**

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