Spring Budget Client Summary

The Budget Background

It is less than a year since Rishi Sunak presented his first Budget, after having been in the role of Chancellor for less than a month. His despatch box première featured an allocation of £12bn towards mitigating the impact of the Covid-19. Ironically, on the same day as Mr Sunak revealed that boost to spending, the World Health Organisation declared the outbreak a pandemic. Total expenditure on dealing with the pandemic is now estimated to be around £300bn.

The March 2020 Budget was what should have emerged in the Autumn of the previous year, before being deferred because of the General Election. The March 2021 Budget is the result of a similar delay. Last September the Chancellor decided that the uncertainties created by the pandemic meant it wisest that he waited until Spring 2021 to present the Budget. Since then, Mr Sunak has been kept busy announcing extensions to the various Covid-19 support schemes introduced in 2020. Whether the Chancellor feels the economic outlook today is much clearer than six months ago is a moot point.

One financial aspect which has been painfully clear for some time is that the government's finances have been fundamentally changed by the pandemic. A year ago, the Office for Budget Responsibility (OBR) forecast that the government would borrow around £55bn in 2020/21. Twelve months later its estimate has risen to £400bn. The coming year, 2021/22, should see borrowing more than halve according to the OBR, but the deficit is still projected to be running at over £160bn – more than three times the figure of just two years ago.

Dealing with this level of borrowing is probably not what Mr Sunak signed up for when he moved into 11 Downing Street. He now has to deal with *total* government debt of about £2,100bn, equal to the UK economic output for the year. The last time debt was as high was in the early 1960s, when the UK was still in the business of paying down the bills incurred in the World War II.

Despite the lake of red ink, Mr Sunak was never going to introduce significant tax increases in this Budget. For a start, nearly all economists, regardless of political hue, were saying that economic recovery was *the* priority and sorting out the debt could wait. Secondly, Mr Sunak's boss, Boris Johnson, cannot even bring himself to mention the A-word (austerity) which would ruin his 'levelling up' agenda. As a result, the Budget was one of tax pain largely deferred.

The proposals of most interest were:

- The addition of £70 to the personal allowance and £200 increase in the basic rate band, in line with indexation requirements. However, after 2021/22, the personal allowance and higher rate threshold (outside Scotland) will be frozen for four tax years.

- The inheritance tax nil rate band, the pensions lifetime allowance and the capital gains tax annual exemption will all be frozen at their current levels for the next five tax years.

- For companies with profits of over £250,000, in April 2023 the rate of corporation tax will jump by 6% to 25%. A new smaller companies' rate of 19% for companies with profits of up to £50,000 will be introduced at the same time.

- A new 'super-deduction' 130% first year allowance will be introduced for companies investing in plant and machinery between 1 April 2021 and 31 March 2023.

- The temporary £500,000 0% band for stamp duty land tax will continue to apply for residential property purchases up to 30 June 2021. The band will then be halved for the following three months before reverting to its original £125,000 level from 1 October.

- The coronavirus job retention scheme (CJRS – furlough scheme) and the self-employed income support scheme will be extended to September, albeit with reductions in the final three months of their life.

- The business rates holiday for retail, hospitality and leisure businesses will also be extended. Until June 2021 100% relief will apply and thereafter reduced (and capped) 66% relief will operate until the end of March 2022.

In this Summary we look at the impact of the main changes on various groups of taxpayers. The categorisation is inevitably rather arbitrary, so it pays to read all sections. Similarly, several of the tax planning points – such as those listed below in our 12 Quick Tax Tips – are universal.

If you need further information on how you will be affected personally, as ever, please contact Andrew or Charles.

12 Quick Tax Tips

1. Don't waste your (or your partner's) £12,570 personal allowance in 2021/22.

2. Don't forget the personal savings allowance, reducing tax on interest earned.

3. Don't ignore the dividend allowance, eliminating tax on £2,000 of dividends.

4. Don't dismiss National Insurance contributions – they are really a tax at up to 25.8%.

5. Think *marginal* tax rates – the system now creates 60% (and higher) marginal rates.

6. ISAs should normally be your first port of call for investments and then deposits.

7. Even if you're eligible for a LISA, you still might find a pension is a better choice.

8. Tax on capital gains is usually lower and paid later than tax on investment income.

9. Trusts can save inheritance tax, but suffer the highest rates of CGT and income tax.

10. File your tax return on time to avoid penalties and the taxman's attention.

11. If you are entitled to a company car, going hybrid or electric could slash your tax bill.

12. Don't assume HMRC won't know: automatic information exchange is now widespread.

Investors and Savers

The Personal Allowance

The personal allowance was given a standard inflation-linked increase to £12,570 for 2021/22. The announcement of the minimal uplift was made in November, hidden on page 22 of the Spending Review. For 2022/23 to 2025/26 inclusive the allowance will then be frozen. Many people do not use the current personal allowance to the full and in 2021/22 there will be a gap of just over £3,000 between the allowance and the starting point for National Insurance contributions (£9,568). At the other end of the income scale, some taxpayers will have no personal allowance in 2021/22 (or future tax years up to 2025/26) because their income exceeds £125,140, at which point their allowance is tapered to nil.

If you or your partner do not use the personal allowance to the full, you could be paying more tax than necessary. There are several ways to make sure you maximise use of your allowances:

- Choose the right investments: some investments do not allow you to reclaim tax paid while others are designed to give capital gain, not income.

- Couples should consider rebalancing investments so that each has enough income to cover their personal allowance.

- Make sure that in retirement you (and your partner) each have enough pension income. On its own, state pension provision is not enough, be it the new state pension (up to £179.60 a week in 2021/22) or the old state pension of £137.60 a week (if you reached State Pension Age before 6 April 2016).

- If one of you pays tax at no more than basic rate and the other is a non-taxpayer, check whether it is worth claiming the transferable married allowance (£1,250 in 2020/21 and £1,260 in 2021/22).

The Personal Savings Allowance

The personal savings allowance (PSA) first appeared in April 2016 and has been unchanged since then. Broadly speaking, if you are a:

- *basic rate taxpayer*, the first £1,000 of savings income you earn is untaxed;

- *higher rate taxpayer*, the first £500 of savings income you earn is untaxed;

- *additional rate taxpayer*, you do not receive any personal savings allowance.

‘Savings income’ in this instance is primarily interest, but also includes gains made on investment bonds, including offshore bonds. Although called an allowance, the reality is that the PSA is a nil rate tax band, so it is not quite as generous as it seems. The PSA means that banks, building societies, National Savings & Investments and UK-based fixed interest collective funds all pay interest without any tax deducted, but they do report payments to HMRC. Thus, if your interest income exceeds your PSA – no mean achievement at current interest rates – you could have tax to pay. Be warned that if you do not tell HMRC, it will have the data to tell you.

If you and your spouse/civil partner receive substantial interest income, it is worth checking that you both maximise the benefit of the PSA. However, at today’s ultra-low interest rates you might also want to consider whether you could earn a higher income by choosing non-deposit-based investments.

The Dividend Allowance

The dividend allowance also started life in April 2016, originally at a level of £5,000 before it was reduced to the current £2,000.

The allowance means that in 2021/22 the first £2,000 of dividends you receive is not subject to any tax in your hands, regardless of your marginal income tax rate. Once the £2,000 allowance is exceeded, there is a tax charge of 7.5% (for basic rate taxpayers), 32.5% (for higher rate taxpayers) and 38.1% (for additional rate taxpayers). Like the PSA, the dividend allowance is really a nil rate band, so up to £2,000 of dividends do not disappear from your tax calculations, even though they are taxed at 0%.

The pandemic prompted many companies to reduce or stop paying dividends in 2020. As a result, the historic yield on UK shares is now around 3.05% which means in theory a portfolio worth more than about £66,000 could attract additional tax on dividend income, even for a basic rate taxpayer. In practice, that threshold portfolio size could prove to be smaller in 2021 as dividend payments should rise over the next 12 months.

The Starting Rate Band

The starting rate band for savings income was launched at £5,000 in 2016/17 and a tax rate of 0% and will remain on that basis for 2021/22. Sadly, most people are not able to take advantage of the starting rate band: if your earnings and/or pension income exceed £17,570 in 2021/22, then that probably includes you. However, if you (or your partner) do qualify, you will need to ensure you have the right type of investment income to pay 0% tax.

Planning Point: If you don't anticipate using all your personal allowance or PSA in 2020/21 think about creating more income by closing deposit accounts before 6 April and crystallising the interest in this tax year. But beware of early closure penalties and shutting down accounts with better interest rates than are available now!

For next tax year, think about who should own what in terms of investments and savings. The savings and dividend allowances mean it is not simply a question of loading as much as possible on the lower rate taxpayer of a couple. In theory, you will each be able to receive an income of up to £20,570 tax free in 2021/22, but only if you have the right mix of earnings, savings income and dividends.

Capital Gains Tax (CGT)

Capital gains tax was a tax which attracted the Chancellor's attention last year. He asked the Office of Tax Simplification (OTS) to review the operation of the tax. The OTS's first report was published in November, but the Chancellor made no mention of it in his Budget, deciding only to freeze the annual exempt amount at £12,300 for the next five tax years.

Gains are currently taxed as the top slice of income, but the rates are lower than those that apply to income not covered by allowances. Gains are generally taxable at 10% to the extent they fall in the basic rate band (£37,500 in 2020/21 and £37,700 in 2021/22) and 20% if they fall into the higher or additional rate bands. An additional 8% applies to gains on residential property and carried interest. For 2021/22 through to 2025/26, the capital gains tax annual exempt amount will be, as it is now, £12,300. The OTS report suggested the exemption should be cut to a 'true de minimis' of between £2,000 and £4,000.

The current tax rates and annual exemption mean that if you can arrange for your investment returns to be delivered in the form of capital gains rather than income, you will often pay no tax on your profits. While investment decisions should never be made on tax considerations alone, once the £2,000 level of the dividend allowance is exhausted, favouring capital gains over income when setting your investment goals can be a sensible approach.

Planning Point: If you do not use your £12,300 annual exemption by Thursday 1 April 2021 (ie before Easter arrives), you will lose it and a possible tax saving of over £3,400. If you have gains of over the exempt amount to realise, it could be worth deferring the excess until 6 April or later to gain another annual exemption and defer the CGT bill until 31 January 2023. However, remember that CGT on residential property gains (eg. buy-to-let) is payable within 30 days of sale.

Individual Savings Accounts (ISAs)

The annual ISA investment limit for 2021/22 will remain at £20,000. There will be no change in the £4,000 limit for the Lifetime ISA (LISA), which was launched in April 2017 to encourage savings by the under-40s. The limit for the Junior ISA (JISA) was also unaltered, but it was more than doubled to £9,000 last year**,** as was the Child Trust Fund (CTF) limit.

ISAs have long been one of the simplest ways to save tax, with nothing to report or claim on your tax return. The arrival of the LISA complicated matters, as it sits somewhere between the traditional ISA and a pension plan. If you are thinking of a LISA instead of either of these, you would be well advised to seek advice before taking any action.

Over time substantial sums can build up in ISAs: if you had maximised your ISA investment since they first became available in April 1999, you would by now have placed over £240,000 largely out of reach of UK taxes.

Planning Point: The first Child Trust Fund accounts matured in September 2020 as their owners reached 18. The tax benefits continue after maturity as a 'protected account' until instructions to deal with the monies are provided. One option is to transfer to an ISA.

Venture Capital Trusts (VCTs) and Enterprise Investment Schemes (EISs)

VCTs and EISs have been subject to many rule changes in recent years, with some significant reforms being introduced in the Finance Act 2018. Those reforms have changed the nature of schemes by raising the element of risk. For example, they included:

- *A "risk to capital" requirement* This focused the investment made by VCTs, EISs and seed enterprise investment schemes (SEISs) on companies where there is a real risk to the capital being invested and excludes from investment those companies and arrangements intended to provide "capital preservation".

- *Increased limits for investments in knowledge-intensive companies.* The amount an individual may invest under the EIS in a tax year was doubled to £2 million from 6 April 2018, provided any amount over £1 million is invested in one or more knowledge-intensive companies. Similarly, the annual investment limit for knowledge-intensive companies receiving investments under the EIS and from VCTs doubled to £10 million, although the lifetime limit remains at £20 million.

- *Further VCT rules tightening* Several other technical changes were made to VCT rules in the Finance Act 2018, including an accelerated investment of capital raised and an increase in the proportion of VCT funds that must be held in qualifying holdings to 80%.

Interest in VCTs, EISs and SEISs has grown as more aggressive forms of tax planning have come under sustained (and largely successful) HMRC attack and pension opportunities have been further constrained. In 2019/20 VCT fundraising amounted to £685m. Most of the long-established VCTs have started their 2020/21 capital raising last year and some have already reached their target.

Pay Later, Not Now?

For higher and additional rate taxpayers, there can be a case for considering the options for tax deferral, once the decision on which sector to invest in has been made. The potential advantages and disadvantages of tax deferral include:

- What would be going to the Treasury instead remains invested, enhancing potential returns.

- There is the possibility that tax rates will be lower when the investment is realised. The opposite risk is that the 50% top tax rate could reappear following a change of government, although that is now probably over three years away. However, your marginal tax rate could rise anyway because of the impact of tax bands and allowances frozen until 2026.

- Some tax liability might disappear completely. Under current rules there is generally no capital gains tax on death, although several voices, including the OTS, have suggested this relief should be withdrawn.

- The investor may change their country of residence, giving rise to a lower tax rate or possible tax savings during the period of transition between the old and new homes.

There is a variety of tax-deferral options available but, as ever, advice is needed in making the 'customer' a client of HMRC.

Estate planning

Inheritance Tax Nil Rate Band

The nil rate band reached its current level of £325,000 in April 2009. From 6 April 2021 the 12-year freeze had been due to come to an end. However, there was no thaw and the nil rate band will now stay at £325,000 until April 2026. Had the nil rate band been increased in line with CPI inflation, it would be about £415,000 - £90,000 higher – in 2021/22.

To date a dozen years of frozen nil rate bands have dragged more estates into the IHT net and more will be added over the next five years. If your estate is already potentially liable to IHT, the freeze could mean it will suffer more tax in the future as inflation takes its toll. Since April 2009, average UK house prices are up by about 54%, according to Nationwide, and UK share prices have risen by 80% (March 2009 marked their low point in the wake of the financial crisis).

Residence Nil Rate Band

The residence nil rate band (RNRB) came into effect on 6 April 2017 with an initial figure of £100,000. For 2021/22 through to 2025/26 inclusive, the RNRB will remain at £175,000. The threshold above which the RNRB is subject to a 50% taper reduction will also be frozen for five years at £2,000,000, meaning it will be lost altogether for estates valued at £2,350,000 or more (£2,700,000 on second death for couples where the RNRB is unused on first death). While the RNRB does help to ease the burden of IHT for many estates, it is by no means a panacea: after a pandemic-induced dip, in the long term the government's IHT tax take is expected to keep rising according to the OBR projections.

IHT Yearly Exemptions

The continued freeze of the nil rate band makes the yearly IHT exemptions all the more important:

- *The £3,000 annual exemption.* Any unused part of this exemption can be carried forward one tax year, but it must then be used *after* the £3,000 exemption for that year. So, for example, if you made a gift of £1,000 covered by the annual exemption in 2019/20, you can make gifts totalling £5,000 covered by the annual exemption in 2020/21 by 5 April 2021.
- *The £250 small gifts exemption.* You can make as many outright gifts of up to £250 per individual per tax year as you wish free of IHT, provided that the recipient does not also receive any part of your £3,000 annual exempt amount.
- *The normal expenditure exemption.* Any gift that you make is exempt from IHT if:
    - They form part of normal expenditure and as part of a habitual pattern of gifting, so around at least three to four years.
    - They are made out of income and not capital, but this can include dividends and regular pension withdrawals or ISA income.
    - The donor is left with enough income to maintain their usual standard of living.

  Also, these gifts do not have to be made to the same recipient every year.

Future Changes?

In July 2019, the Office of Tax Simplification (OTS) made a range of proposals to simplify some of the complexities of IHT. It had been expected (and rumoured) that some of these would be taken up in the 2021 Budget, but instead the Chancellor made no mention of the tax. His silence on this occasion may be for the same Covid-19 focus as last year. However, IHT reform may still be on the agenda, perhaps in the Autumn Budget. With calls for wealth tax growing, restructuring IHT is one way to address the same issue without creating a new tax regime.

As is often the case with 'simplification', the OTS proposals would have created winners as well as losers. Given that there has now been what looks like a delay, if IHT is a concern to you, then it would be wise to seek advice on which category you might fall into.

Will Review

A year ago, the start of the pandemic created a sudden awareness of the importance of having an up-to-date Will, just as Lockdown 1.0 made it difficult to create one. If you still have not updated your Will or do not have one, remember the lesson of last Spring and sort matters out now *before* the unexpected urgency arrives.

Planning Point: If you are making an annual exemption gift by way of a cheque, remember that legally the gift is only made once the cheque is cleared. Thursday 1 April 2021 is the final banking day of the 2020/21 tax year.

Business Owners

Corporation Tax Rate

The rate of corporation tax has been 19% since 1 April 2017. It had been due to fall to 17% last April, but the planned change – which had been legislated for – was reversed. Unlike income tax, National Insurance contributions (NICs) and VAT, corporation tax rates were not given a rate freeze promise in the Conservatives' 2019 manifesto.

19% is a historically low rate of corporation tax, but it will not survive for large companies beyond April 2023. At that point the rate will jump to 25% for companies with profits of £250,000 and over. For companies with profits of up to £50,000 a revived smaller companies' rate of 19% will continue. Between £50,000 and £250,000 of profits there will be a new relief which, to judge by past practice, implies 19% on the first £50,000 of profits and 26.5% on the excess. D1A

Operating via a company creates the opportunity to draw income as dividends, free of NICs, and shelter profits at a corporation tax rate that is below the basic rate of income tax – rather than personal tax rates on earnings of up 45% (46% in Scotland). From April 2023, the higher rate of corporation tax will change that calculation for businesses with profits over £50,000. In the meantime, the government has continued to attack the use of one-person companies, with the latest measure being the introduction of off-payroll working rules to private and third sector employers from 6 April 2021, after a one year deferment in response to the pandemic.

Capital Allowances

Capital allowances have been subject to a variety of changes in recent years, ostensibly to encourage an increase in business investment.

The Annual Investment Allowance (AIA), which gives 100% initial relief for investment in plant and machinery, was 'temporarily' raised to £1,000,000 for two years from 1 January 2019. The AIA has been a favourite measure for Chancellors to tweak, so it is not surprising that last November there was a 12 month extension to the temporary increase. In theory the AIA will now automatically revert to its previous £200,000 level at the start of 2022. In practice another late Autumn announcement of an extension is possible.

In the two years from 1 April 2021 the AIA will be eclipsed by a new 'super-deduction' of 130% of the amount invested in qualifying plant and machinery *by companies*. This will effectively mean a £25 tax reduction for each £100 of investment. For certain long-life assets, the existing 6% writing down allowance will be supplemented by a 50% first year allowance until April 2023.

Losses

The pandemic has led to many businesses trading at a loss. The Chancellor has recognised this and temporarily extended the period over which both incorporated and unincorporated businesses can carry back trading losses from one year to three years.

The extension applies to up to £2 million of an unincorporated business's unused trading losses made in each of 2020/21 and 2021/22. The same limit is relevant separately to companies' unused trading losses, after carry-back to the preceding year, in relevant accounting periods ending between 1 April 2020 and 31 March 2021 and for the following accounting period. The £2 million ceiling will be a group-level limit. As a result, groups with companies that have the capacity to carry back losses above £200,000 will be required to apportion the cap between their constituent companies.

Pension Changes

There have been many important pension changes in recent years, with one major measure announced in the 2020 Budget:

- For 2020/21 there was a £90,000 increase to both of the annual allowance tapering trigger points, lifting them to £200,000 (threshold income) and £240,000 (adjusted income). On the downside, the minimum tapered annual allowance was cut from £10,000 to £4,000 (for adjusted incomes of £312,000 and over). The changes mean some higher earners are able to make larger contributions to their pension in this tax year than in 2019/20, although at the highest level the opposite is true.

- In April 2018, the lifetime allowance started to rise in line with inflation, after a series of cuts that reduced the allowance from £1.8m to £1.0m. Indexation has now stopped again, meaning that the allowance will stay at £1,073,100 until 6 April 2026.

- Auto-enrolment minimum contributions into pension arrangements increased in April 2018 and again in April 2019. No further rises are currently scheduled, although it is widely accepted that today's 8% minimum total contribution rate is inadequate. Worryingly recent data showed a decline in both employer and employee pension contributions during the first part of the pandemic.
- The earnings threshold for auto-enrolment in 2021/22 will remain at £10,000, but the upper limit will marginally rise at £50,270, in line with the higher rate tax threshold (outside Scotland). The lower earnings limit, which sets the floor for the contribution earnings band, stays at £6,240.

- Changes to the state pension age (SPA) have finished for the time being with men and women currently sharing the same SPA of 66. The next move to an SPA of 67 is due to be phased in over two years from April 2026.

- From 6 April 2028, the normal minimum pension age for drawing private pension benefits will rise from 55 to 57.

Employer's National Insurance Contributions

Three years ago, the Treasury introduced measures to curtail the use of optional remuneration arrangements (OpRA), sometimes called cafeteria schemes (when cafeterias were open…). These allowed employees to sacrifice salary for less highly taxable (and NICable) benefits. Most newly established arrangements are now subject to employer's 13.8% NICs (and taxed on the employee) based on the amount of salary given up rather than the notional value of the fringe benefit (if any). Transitional provisions for pre-6 April 2017 arrangements gave some limited exemptions, notably for company cars, but these expire on 5 April 2021.

Salary sacrifice for pension contributions remains favourably treated and fully exempt from the rules. Cars with CO_2 emissions of 75g/km or less – electric or plug-in hybrids – are also exempt, which helps to explain why Teslas have become a common sight in the UK.

Planning Point The exemption given from the OpRA rules to low emission vehicles makes these worth considering if you want to exchange salary for a company car.

For 2021/22 there is a new NIC relief for employers of armed forces veterans entering civilian employment. The relief will mean that during the first 12 months of employment, the employer will have no secondary Class 1 NIC liability.

The upper earnings limit for Class 1 (employed) contributions (and the upper profits limits for Class 4 (self-employed) contributions) will be frozen at £50,270 from 2021/22 to 2025/26.

Business Rates

In 2020/21 there was a range of initiatives on business rates and grants based on business rateable values, the most significant of which was probably the one-year business rates holiday for retail, hospitality and leisure businesses, which was due to end on 31 March 2021. The 100% business rates relief for eligible businesses in England will now continue to 30 June 2021. A 66% business rates relief will the apply until 31 March 2022. The new relief will be capped at £2 million per business for properties that were required to be closed on 5 January 2021, or £105,000 per business for all other qualifying properties. Nurseries will also qualify for relief in the same way.

Employment Support Schemes

The Coronavirus job retention scheme (CJRS or furlough scheme) will be extended to 30 September 2021 and will continue to offer employees 80% of their current salary for hours that are not worked. Until 30 June, the government support payment will remain 80% (capped at £2,500 a month), with employers continuing to be responsible for NICs and workplace pension contribution. The government support then reduces to 70% in July, followed by 60% in the final two months of the scheme.

The self-employed income support scheme (SEISS) will also be extended to September 2021, although details are less clear. A previously announced fourth SEISS grant will cover the period from February to April, worth 80% of three months' average profits (capped at £7,500). Claims for this grant can be made from late April. A new, fifth grant, claimable from late July, will cover the remaining period to September 2021. The government says this will be worth:

- 80% of three months' average profits where the claimant's turnover has dropped by 30% or more; and
- 30% of profits (capped at £2,850) where the fall in turnover is below 30%.

The eligibility for the fourth and fifth grants will be broadened to include those who became self-employed in 2019/20 and have filed a tax return for that tax year.

Off-payroll Working

After a 12-month deferral, from 6 April 2021 the off-payroll working rules will start to apply to private and third sector employers. This will place the onus on employers to decide whether a contractor working through a personal service company falls within the IR35 tax rules. In early 2020, before the deferment was announced, some large companies gave their contractors the choice of either transferring to PAYE employment, with the accompanying hit to their net earnings, or leaving.

Importantly, the new rules do not apply to small companies, which in this context means that the company using a contractor meets at least two of the following criteria:

- an annual turnover of not more than £10.2m;
- a balance sheet total of not more than £5.1m; and
- average number of employees of no more than 50.

Dividends or Salary...

Regular changes to National Insurance contributions and tax rates have altered the mathematics of the choice between dividends and salary. For shareholder/directors able to choose between the two, and not caught by the ever-tightening IR35 personal company rules (see above), a dividend remains the more efficient choice even if no dividend allowance is left, as the example below shows. However, a pension contribution (within the annual allowance provisions) could avoid all immediate tax and NIC costs.

The change in corporation tax from April 2023 will mean that the above table will need to be revised for companies with profits of over £50,000.

…. Or nothing at all?

For some business owners, the ultimate way to limit their tax bill is to choose to leave profits in the company rather than draw them either as dividend or salary. With the top rate of income tax currently at 45% (46% in Scotland) - and marginal rates potentially much higher - there is an obvious argument for allowing profits to stay within the company, where the maximum tax rate is currently 19% and will not rise above an overall 25%.

This strategy has tax risks in terms of eligibility for business asset disposal relief and inheritance tax business property relief. There is also a risk that reform to CGT could raise the tax rate, or even re-characterise accumulated profits as income for tax purposes on liquidation or sale of the company. IHT reform might also have an impact. Money left in the company is also money exposed to creditors, so professional advice should be sought before turning a business into a money box.

An Example - Make Mine a Dividend

A director/shareholder has £25,000 of gross profits in his company which he wishes to draw, either as bonus or dividend. Assuming:

- the company pays corporation tax at the rate of 19%;
- the director is not resident in Scotland;
- and they already have annual income in excess of £50,270

the choice can be summarised thus:

	Bonus £		Dividend £	
	Higher rate	**Additional rate**	**Higher rate**	**Additional rate**
Marginal gross profit	25,000	25,000	25,000	25,000
Corporation tax @ 19%	N/A	N/A	(4,750)	(4,750)
Dividend	N/A	N/A	20,250	20,250
Employer's NICs Contributions £21,968 @ 13.8%^	(3,032)	(3,032)	N/A	N/A
Gross bonus	21,968	21,968	N/A	N/A
Director's NICs £21,968@ 2%	(439)	(439)	N/A	N/A
Income tax *	(8,787)	(9,886)	(6,581)	(7,715)
Net benefit to director	**12,742**	**11,643**	**13,669**	**12,535**

^ *The Employment Allowance is assumed to be used or unavailable.*

**Tax on all dividends at 32.5% for higher rate taxpayer and 38.1% for additional rate taxpayer as the dividend allowance is assumed to be fully utilised elsewhere.*

Employees

Company Cars

The company car benefit scales underwent radical changes at the start of 2020/21:

- For cars registered since 6 April 2020, CO_2 emission levels have been based on WLTP figures. The WLTP test is much closer to a 'real world' test, producing results 20%-25% higher than the largely discredited NEDC test, which still applies for cars registered before 6 April 2020.

- The scale charge for zero emission cars (eg. electric-only) fell to nil in 2020/21 and will rise to 1% in 2021/22 and 2% in 2022/23. That helps to explain why the Tesla Model 3 was the UK's best-selling car in December 2020.

- For hybrid cars registered from 6 April 2020 with CO_2 emissions of 1g/km-50g/km, the scale charge is based on the electric-only range figure, varying in 2020/21 from 0% for a range of at least 130 miles to 12% if the range is below 30 miles. In 2021/22 these rates increase by 1%. For older hybrid vehicles with emissions of up to 50g/km, the scale charge in 2020/21 and 2021/22 ranges from 2% to 14%.

For 2021/22, there will be no change in the scale rate for pre-6 April 2020 registered cars, but newer vehicles will generally see a 1% increase. Two other 2021/22 factors to watch are:

- All newly registered diesel cars now have had to meet the RDE2 emission standards (cutting NOx emissions significantly), although in practice many were meeting the revised standard in 2020. Cars that satisfy the RDE2 standard are exempt from the 4% car scale surcharge that would otherwise apply to diesels.

- The maximum charge has remained at 37% and, in 2021/22, will apply for petrol engine and RDE2 diesel engine cars with emissions of 165g/km and above registered from 6 April 2020, and 160g/km and above for older vehicles. The corresponding limits for non-RDE2 diesel engine cars are 145g/km and 140g/km respectively.

Planning Point: If you are changing your car soon, think ahead to what it will cost you in tax terms on these scales. It may make sense to accept cash instead of a new car, switch to a hybrid vehicle or choose an electric-only car.

Pensions

The pensions landscape has altered dramatically in recent years and continues to change. As a reminder:

- For 2020/21 there was a £90,000 increase to both of the annual allowance tapering trigger points, taking them to £200,000 (threshold income) and £240,000 (adjusted income). However, there was a sting in the tail for people with very high incomes: the minimum tapered annual allowance dropped from £10,000 to £4,000 (at an adjusted income of £312,000 or more).

- Automatic enrolment for employees in a workplace pension arrangement is now fully in force, with new employees automatically enrolled. A second increase in the minimum contribution rates took place from April 2019, raising the total (employer and employee) contributions from 5% of "band earnings" (£6,240 - £50,270 in 2021/22) to 8%. No further increases are scheduled at present. Nevertheless, pension experts generally agree that the current overall contribution rate is too low to achieve an adequate retirement income.

- The new state pension started in April 2016, replacing both the basic state pension and the second state pension (S2P). In the long term the reform will create more losers than winners as the earnings-related element has been removed.

- State pension age (SPA) increases have stopped for the time being at age 66. An increase to 67 is due between April 2026 and March 2028. The rise to 68 is scheduled between April 2037 and March 2039, although the necessary legislation has been deferred and the dates could change due to a slowing rate of life expectancy increases. By 2050 – so if you are under 40 now – you could be facing a SPA of 69.

- The government has confirmed that from 6 April 2028 the normal minimum age at which you can draw benefits from a private pension will rise from 55 to 57.

- The lifetime allowance was due to be increased in line with inflation, but instead has been frozen at its current £1,073,100 until 6 April 2026. By coincidence, that date will mark the 20th anniversary of the lifetime allowance introduction – at a level of £1,500,000.

Planning Point: The carry forward rules allow unused annual allowances to be carried forward for a maximum of three tax years. Thus, 5 April 2021 will be your last opportunity to rescue unused allowance of up to £40,000 from 2017/18.

Salary Sacrifice

National Insurance contributions (NICs) can cost up to 25.8% of gross pay – up to 13.8% for the employer and 12% for the employee. The corollary is that avoiding NICs can save up to 25.8% of pay. A widely applied example of turning NICs to an advantage is in the use of salary sacrifice to pay pension contributions. Instead of the employee making personal contributions out of their net pay, the employee accepts a lower salary and the employer makes a pension contribution. If the employer passes on all of the NIC saving, the pension contribution could be up to almost 34% higher, as the example shows.

A Worthwhile Sacrifice

	Personal Contribution		**Salary Sacrifice Employer Contribution (sacrificed amount + NIC saving)**	
Tax Rate	**20%**	**40%**	**20%**	**40%**
	£	**£**	**£**	**£**
Gross Salary	1,000	1,000	Nil	Nil
Employer Pension Contribution	Nil	Nil	1,138	1,138
Employer NI Contribution (13.8%)	138	138	Nil	Nil
Total Employer Outlay	1,138	1,138	1,138	1,138
Employee Salary	1,000	1,000	Nil	Nil
Less Income Tax	(200)	(400)		
Less NI Contributions (12%/2%)	(120)	(20)		
Net Pay = Net Pension Contribution	680	580		
Tax Relief	170	387		
Total Pension Contribution	**850**	**967**	**1,138**	**1,138**

Planning Point On 6 April 2016 the standard lifetime allowance was reduced to £1,000,000. It has since been increased in line with inflation twice and will now remain to £1,073,100 until 6 April 2026. However, there is still the possibility of claiming transitional protection of up to £1,250,000.

Retiree/At Retirement

The Pension Landscape in Spring 2021

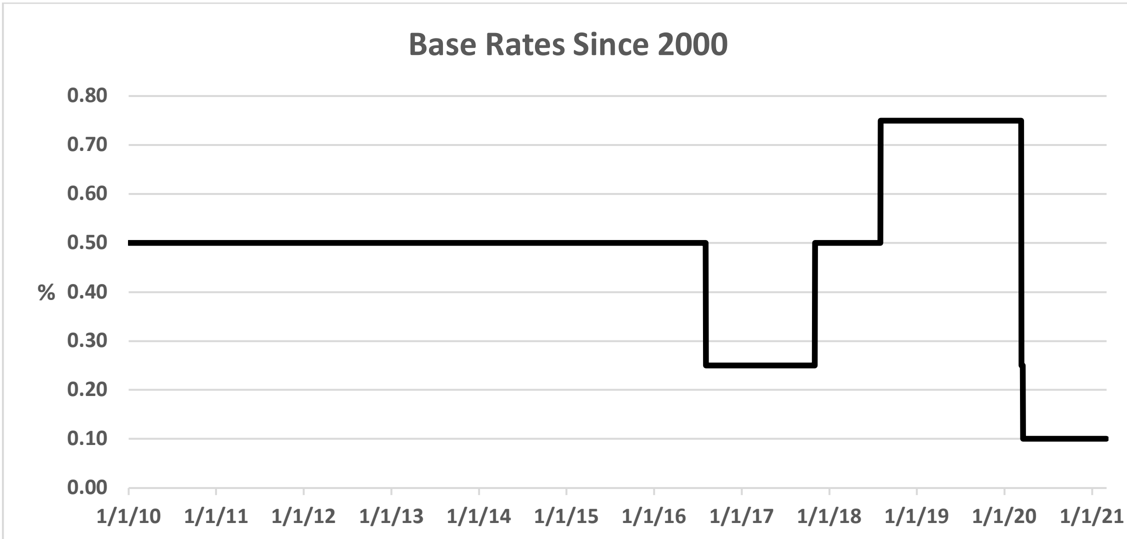
There have been many changes to pensions in recent years, with another significant set of reforms having taken effect in April 2016. These include:

- Three reductions in the standard lifetime allowance brought it down from £1.8m in 2011/12 to £1m for 2016/17. This allowance effectively sets a tax-efficient ceiling for the value of pension benefits and, from April 2018, started to rise annually in line with CPI inflation. However, that has now ceased, meaning the allowance will remain at £1,073,100 until 6 April 2026.

- Further increases to State Pension Age (SPA), both legislated for and planned. For men and women, SPA reached 66 last year. The next step up to a SPA of 67 will start in April 2026.

- New rules, which have given much greater flexibility in drawing benefits from money purchase schemes, started on 6 April 2015 and have encouraged many people to turn their entire pension pot into (mostly taxable) cash. The new flexibility was accompanied by more generous tax treatment of death benefits, adding to the opportunities that pensions offer for estate planning.

Interest Rates: Lower for longer and longer…



When 2020 began, the Bank of England base rate was at the dizzying height of 0.75%. Two cuts during March in response to the impact of the pandemic on the economy took it down to 0.1%. There remains talk that the Bank might yet choose to push rates into negative territory.

The main UK banks seem to have long since given up competing for deposits in this low-interest-rate environment, as has National Savings & Investments after its latest round of cuts (which generally took effect in November). The best instant access rates for new accounts are now from new and challenger banks at around 0.5%. A similar picture emerges for instant access cash ISAs. If ultra-low interest rates are a concern to you:

- Make sure you take maximum advantage of your personal savings allowance and, where possible, your starting rate band.
- Maximise your cash ISAs, which pay interest tax free.
- Regularly check the interest rate on all your deposit accounts. It is especially important to watch accounts with bonus rates – once the bonus period ends they can look very unattractive. Do not simply wait for the next statement: if you are only earning 0.001%, you need to know now. Note that the NS&I Income Bonds and Investment Account now both pay only 0.01%. By a curious twist, the best NS&I offerings are Premium Bonds, which have a prize fund (tax-free) rate of 1%.
- Be wary of tying your money up in a fixed-term deposit for five or more years simply to achieve an interest rate above 1.0%. A lot can happen in five years – just think back to 2016...

Parents

Child benefit

The High Income Child Benefit Tax Charge – the child benefit tax – means that if you or your partner has income of £60,000 or more in the current tax year there will be a tax charge equal to your total child benefit unless you have taken a decision to stop benefit payments.

Between £50,000 and £60,000 of income, the tax charge is 1% of benefit for each £100 of income above £50,000 – a threshold in 2021/22 that will be below the starting point for higher rate tax (other than in Scotland). The result can be high marginal rates of tax in the £50,000-£60,000 income band. If you have three children eligible for child benefit, the marginal rate is over 65%.

Planning Point: As the High Income Child Benefit Tax Charge is based on taxable income, you could reduce the impact of the tax by making a pension contribution.

Junior ISAs

Junior ISAs (JISAs) were launched in November 2011 with an annual investment limit of £3,600, which has since been increased to £4,380 in 2019/20. For 2020/21 the limit was more than doubled to £9,000, the same limit that will apply for 2021/22. JISAs can be invested in cash deposits and/or stocks and shares in any proportion and can usually be arranged for any child aged under 18 who was born before 1 September 2002 or after 2 January 2011. A child cannot have both a JISA and a Child Trust Fund (CTF) account (which has the same investment limits). It is possible to transfer CTF accounts to a JISA, a move that may result in reduced fees and a wider investment choice.

The first CTF accounts, for children born in September 2002, reached maturity last September. By default, matured CTF accounts have continued to enjoy the current UK ISA tax exemptions as a 'protected account'. If instructions are given, they can be transferred to an adult ISA, with any such transfer not counting as a contribution for the tax year, unless it is to a Lifetime ISA.

University funding

The £9,250 a year maximum tuition fee for new 2021/22 students in England and Wales is, for now, a fact of student life, even if the educational process is much less certain.

If you have children likely to go to university, it makes sense to consider your funding options. For example, JISAs are a potentially valuable tool to build up a fund by age 18. For those who prefer a greater degree of control over the student's access to the investment at age 18 (while retaining tax efficiency) collective investments held subject to an appropriate trust can look attractive, as could an offshore investment bond. Despite these tax-efficient "pre-funding" opportunities, under the current rules many experts consider that it makes sense to take the student fee loans while at university rather than pay fees from capital. That is because repayment for most recent and new English and Welsh loans only begins once earnings reach £26,575 (£27,295 from 2021/22) and any debt is currently written off after 30 years from the April after graduation.

Source: Technical Connection. This document is a general overview of the Spring 2021 Budget and does not constitute individual financial advice. If you would like financial advice or have any questions on the topics covered, please contact Andrew or Charles. The value of investments can fall as well as rise and is not guaranteed.