Orange Genie

Contractor Management Outsourcing

Accountancy

TAX & WEALTH PLANNING FOR CONTRACTORS

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Paying tax is inevitable but you can manage your financial affairs to minimise the impact of tax for you, your family or your business. Whilst aggressive tax avoidance is now being targeted by HMRC, legitimate tax planning is still available.

The tax rules and rates of relief change regularly, at least every year, so you need to review your own financial situation just as often. This guide reflects the allowances for 2019/20.

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PERSONAL & FAMILY TAX PLANNING

1 **Make sure you tell HM Revenue and Customs (HMRC) which of your properties should be treated as your main home for tax purposes when you buy a second (or even third) home.**

The property that has always been your main home is free of capital gains tax (CGT). Any other property where you have lived for part of the time will attract a tax exemption for the periods you have lived there and have elected for it to be your main home. If a property has been your nominated main home at any time, the gain for the last three years of ownership is free of tax, even if you do not live there during that final period.

2 **If you are getting married or entering into a civil partnership and you both own separate properties which you continue to occupy for some periods, you need to nominate one of them as your main home within two years of your marriage/civil partnership.**

Once married, you can have only one main home between you for tax purposes, so nominate the one that is likely to make the best use of your CGT property exemption. Otherwise HMRC will designate the property that you occupy most as your main residence.

3 **If you own a trading company, then you can reduce the CGT payable on a future sale by spreading the shares between yourself and your spouse.**

If you both hold at least 5% of the ordinary shares, have done so for at least 24 months before the sale and are either employed by the company, or hold the position of director or company secretary, you should both qualify for entrepreneurs' relief on any gains made when the company is sold. The relief applies a reduced rate of CGT of 10% to the first £10 million of lifetime gains made per person for disposals from 6 April 2011.

4 **Contribute up to £4368 each year into your child's junior ISA.**

The fund builds up free of tax on investment income and capital gains until the child reaches 18, when the funds can either be withdrawn or rolled into an adult tax-free ISA. Relatives and friends can also contribute to the child's junior ISA as long as the £4368 limit is not breached. Any child aged under 18 who lives in the UK can have a Junior ISA if they were not entitled to a child trust fund (CTF) account.

5 **If your income is more than £60,000 and you or your partner claim child benefit, you will be subject to a tax charge to claw back the full amount of benefit.**

If you income lies between £50,000 and £60,000 the child benefit tax charge will be equivilent to 1% of the child benefit for every £100 of income over £50,000. The tax charge applies to the higher earner, irrespective of who claims the benefit. to avoid the tax charge you can either stop claiming child benefit, or reduce your income below £50,000.

6 **Check your PAYE tax code. Many PAYE tax codes are incorrect when issued.**

HMRC may have included an estimate of your unearned income that means you will pay on that income earlier than you would if it was assessed through your self assessment tax return. You can ask HMRC to remove this estimated income and also correct any other errors.

7 **If you marriage is permanently breaking up, aim to divide up the valulable assets, such as shares and land, as soon as possible.**

If you complete any such asset swaps in the tax year in which you separate from your spouse, you will not have to pay CGT based on the market value of those items. If you delay until the next tax year, the tax charge could be painful.

8 **Check how much you are paying in national insurance contributions (NICs).**

If you have more than one job, or if you are both employed and self-employed at the same time, you may overpay NICs during the tax year. You can then reclaim any overpaid NICs from HMRC after the end of the tax year. You can also prevent the overpayment by deferring payment of NICs on one of your jobs if you complete the form in the HMRC leaflet CA72A (employees) or CA72B (self-employed).

TAX & YOUR PROPERTY

9

The next time you move house you could let out, rather than sell, your old home so that the rent covers the mortgage interest and other expenses.

When you eventiually sell this property, the proportion of the gain relating to the period when it was occupied as your main home will be exempt from tax. In addition, you can claim a further tax exemption of up to £40,000 per owner because the propery has been let. With the benefit of all these reliefs, you might find that the gain on the let property is less than your capital gains exempt amount (£12,000 for 2019/20) and is therefore tax free. Any remaining gain will be subject to CGT.

10

Pass on a let property to fund future income needs.

Students need an income stream and a let property can provide that. The gift of the property is treated as a sale at market value for tax purposes, but where the current value is low the gain will be small and may be covered by your annual exampt amount of £12,000 (2019/20).

11

Let rooms in your own home.

The income is completely tax free up to £7,500 per property. If the rent is higher than this, check whether the normal approach of paying tax on the income after deducting allowable expenses is more tax-efficient than claiming the exemption of £7,500.

TAX EFFICIENT SAVINGS AND RETIREMENT PLANNING

12 Employers pension contributions save NICs.

Where your employer pays you a salary which you invest in your pension, both you and your Employer have to pay NICs. If your employer pays a contribution directly into your pension scheme, the employer receives tax relief for the contribution and there are no NICs to pay - saving both the employer and you NICs. Since contractors are often employed by their own limited company you could arrange for your company to cover the cost of the contributions.

13 Take advantage of your annual allowance for making pension contributions, because tax relief is available up to your highest tax rate.

Your annual allowance for 2019/20 is £40,000 plus any usused allowance brought forward from the previous three tax years. This allowance must cover any pension contributions you make yourself, and any contributions paid for you by your employer. Contributions made in excess of your annual allowance will attract a tax charge at your marginal tax rate.

14 Take advantage of the increased individual savings account (ISA) investment limits and generate tax-free income and capiral gains.

The maximum annual amount which can be invested in a ISA is now £20,000 (2019/20). Up to half the maximum limit can be in a cash ISA with the remainder being invested in a stocks and shares ISA. Transferring funds into an ISA early in the tax year will maximise the amount of tax-free income arising. As there are many ISAs on the market, it is worth shopping around to find the best deal, taking account of the rates of return and fees charged.

TAX & YOUR BUSINESS

15 Think about how you should start your business - as a sole trader, partnership or limited company.

Companies still have tax advantages (see Tip 16) but generally only when the business has started to make a profit. With a new venture you might expect to make losses in the early years. As a sole trader or partnership, your initial losses can be carried back to set against your income in the three years before you started the business. the use of losses may be restricted depending on the size of the losses and how much income you have.

16 Incorporation can still be worthwhile.

Based on current personal and corporation tax rates, a business with profits of £40,000 can save tax and NICs of some £3,000 if operated through a company, compared to operating as a sole trader, provided you extract most of your earnings as dividends. Furthermore, corporation tax rates will continue to fall over the next two years - with an expected single, unified rate of 17% by 2020.

17 Do not delay telling HMRC about your new business.

Sometimes it's difficult to know exactly when a business starts, or when a hobby turns into a business. Selling items through online auctions can be fun, but as soon as you start buying items specifically to sell you are deemed to be trading. You will need to register your business through the HMRC website or risk a penalty of up to 100% of the tax due. Some useful information can be found in HMRC's leaflet SE1.

18 Consider the best VAT scheme for your business.

The flat rate VAT scheme may be beneficial if you are not a limited cost trader. Alternatively you may want to opt for the standard scheme. Your accountant can review your expenses and help determine your best option. See our guide to the flat rate VAT scheme in the resources section of our website, orangegenie.com/accountancy.

19 Purchasing a car in your own name rather than having a company car should reduce your tax.

As a company car driver you are taxed on a percentage (5% to 35%) of the original list price of the car. There is no upper limit on the list price and the percentage used is due to increase every year for the next four years.

20 Plan the timing of purchases of new plant and machinery in order to maximise the benefit of the annual investment allowance.

All businesses can deduct against taxable profits the full cost of the first £1000,000 spent on plant and machinery (other than cars) each year. Where more than £1000,000 is spent, the excess will attract writing down allowances at 18% or 8%.

21 Make the best use of trading losses.

A loss made by a company can be set against profits of the previous 12 months, but only after making a current-year claim. A loss made by an unincorporated business can be claimed against total income for the year of the loss and/or the previous year. A tax rebate will be available where a loss is carried back. As noted in Tip 15, the amount of the loss used in this way could be restricted.

22 **Provide your employees with an annual health check and eye test.**

The health check is free of tax, but any medical treatment will generally be a taxable benefit. The eye test is also tax free if the employee needs to use a computer screen or similar display screen as part of their job. Any special corrective lenses required to use that equipment can also be provided tax free.

23 **Pay employees £5 tax free each time they need to stay away from home overnight.**

This tax-free amount can be in addition to the cost of accommodation and meals that can be reimbursed if receipts are produced. If the overnight stay is abroad, the tax-free amount is £10 a night.

24 **Don't forget to party!**

Even the smallest business can host an annual tax-free social function for its entire staff, including the directors and their partners. As long as the cost per head is less than £150 (including VAT), employees are not taxed for having a good time and the company benefits from full tax relief on the expense incurred.

25 **Supply your employees with one tax-free mobile phone each.**

Mobile phones, including smart phones, provided to employees are tax free as long as it's the employer rather than the employee who owns the phone and takes out the contract with the telecoms company. Ensure your mobile phone contract is in the name of your company.

26 **Continue to pay your employees who have children partly with childcare vouchers that they can use to fund nursery and after-school care.**

The First £55 a week paid as childcare vouchers is free of both tax and employers' and employees NICs. You have to offer the childcare vouchers to all your empolyees who work at the same site, and the vouchers must not be exchangeable for cash. This scheme has been unavailable to new members since October 2018.
Alternatively parents are now able to open a Childcare Account. For every £8 paid in by a parent, the government will pay in £2, up to a maximum of £10,000.

TAX & YOUR ESTATE

27 **Inheritance tax (IHT) is charged at 40% on the value of your estate over £325,000.**

There is no IHT where assets pass from one spouse to another, and the unused proportion of the nil rate band when the first of the couple dies can be transferred to the estate of the surviving spouse.

28 **An additional nil rate band for inheritance tax purposes was introduced from 2017/18 for the value of the main residence.**

The allowance is£150,000 in 2019/20 rising to £175,000 for 2020/21 providing an individual with £500,000 total tax free estate, or £1 million for a couple.

29 **Make a will and review it regularly.**

If you die without making a will, your assets will be divided between your relatives according to the intestacy rules. This will be after IHT is paid at 40% on any value above £325,000 that goes to anyone other than your spouse or civil partner. If you have no surviving relatives, the same tax will be paid but the Crown (i.e. the government) will claim the balance.

30 **Rewrite your will to ensure that at least 10% of your net estate, after deduction of the nil rate bank of £325,000, is left to charity.**

This will reduce the IHT rate on your taxable estate from 40% to 36%. The exact calculation of your net estate is quite complicated, so take professional advice when drawing up or amending your will.

31 **Rather than just living together as a couple, get married or register a civil partner ship.**

Otherwise your surviving partner will have to pay IHT on anything inherited from you that exceeds the nil rate band, currently £325,000. Do not forget that there are some potential tax and other costs to consider. But your spouse or civil partner can now inherit your unused nil rate band when you die, potentially saving even more tax.

32 **Make regular gifts out of your annual income to whomever you choose.**

As long as you establish a pattern of gifts that can be shown to be covered by your net income, without reducing either your capital assets or your normal standard of living, those gifts are free of IHT. The recipients of these gifts need not be the same people each year.

33 **Make gifts totalling £3,000 each tax year from your capital resources.**

These gifts are free of IHT and, if you forget to make your £3,000 gift one year, you can catch up in the next tax year by giving a total of £6,000, Remember, both you and your spouse or civil partner can each give £3,000 every tax year in addition to gifts you make out of your regular income.

34 **Use the IHT marriage exemption for gifts.**

If your son or daughter is about to marry or register a civil partnership, then you and your spouse or civil partner can each give them £5,000 in consideration of the marriage, and the gift will be free of IHT. This is in addition to any smaller gifts you make out of your regular income each year. The marriage exemption can also be combined with your £3,000 a year annual exemption to allow you to make bigger exempt gifts. The IHT-free gift you can make on the occasion of a grandchild's wedding is £2,500. Civil partnerships attract the same exemptions.

35 **Check whether your elderly relatives have ever been widowed.**

Widows and widowers inherit the unused proportion of their late spouse or civil partner's nil rate band - even if the spouse died many years ago. This could mean that up to an extra £325,000 of the estate will be tax free.

GENERAL APPROACH TO TAX PLANNING

36 **If a tax planning scheme sounds too good to be true, it probably is.**

In particular, do not get involved in a tax scheme that relies on the non-declaration of income or captical gains, as that would be illegal. The introduction of a general anti-abuse rule from April 2013 counteracts tax advantages arising from abusive tax avoidance arrangements.

37 **Bear in mind that the effect of a tax decision is only one element to consider.**

The commercial, practical and financial implications of the decision should always be taken into account.

38 **Tax planning can be undone by not submitting the correct tax forms on time or not paying your tax liabilities by the due date.**

In either case, HMRC will levy penalties which could exceed the tax due, or wipe out any tax savings made.

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