Investment

2018

NW BROWN
WEALTH MANAGEMENT

Tax-Free Savings Allowances

What's changed?

In the summer Budget 2017 Philip Hammond followed up George Osborne's summer Budget 2015 with further changes to the way savings are taxed. From April 2018, the Tax-Free Dividend Allowance of £5,000 was reduced to £2,000 with the higher rates of tax introduced above this new allowance remaining. The Personal Savings Allowance has remained the same and enables every basic rate taxpayer to receive up to £1,000 of interest without paying tax on it. This allowance reduces to £500 for higher rate taxpayers and is eliminated altogether for additional rate taxpayers. The recent changes to dividend tax rates are summarised in the table below.

Tax Rate	Previous Nominal Rate	Previous Effective Rate	Rate as of April 2016	Rate as of April 2018
Credit Allowance		10% tax credit	£5,000 tax free	£2,000 tax free
Basic Rate	10%	0%	7.5%	7.5%
Higher Rate	32.5%	25%	32.5%	32.5%
Additional Rate	37.5%	30.6%	38.1%	38.1%

How do the changes impact investors?

- Dividends from shares held in ISAs and pensions remain tax free, so the changes only apply to those investors with shares held outside tax wrappers.
- No investor will pay tax on the first £2,000 of their dividend income, regardless of their level of non-dividend income. However, taxpayers continue to see an effective tax increase of at least 7.5% on dividend income received above their allowance.
- Investors that have not utilised their full income tax personal allowance (£11,850 for the 2018/19 tax year) can do so before using their dividend and interest allowances, meaning that an investor with no other taxable income can effectively receive up to £14,850 of tax free savings income during the 2018/19 tax year.

What can be done in response?

For those that are likely to receive taxable dividend income in excess of the £2,000 allowance, we highlight below some relatively simple and practical strategies that could help reduce dividend tax liabilities under the current rules.

- Make use of your spouse's Tax-Free Dividend Allowance too – married couples and registered civil partners should spread the ownership of a taxable portfolio between them so as to make full use of each spouse's allowance.
- Make optimal use of tax bands and personal allowances – couples should additionally be sure to make full use of their personal allowances and basic-rate tax bands such that any taxable dividends in excess of their allowances are received in the name of the spouse who pays the lowest tax rate.
- Minimise your taxable dividend income – investors in danger of exceeding their allowances should, where practical, look to minimise the dividend income they receive within taxable accounts. One way of doing this is to arrange for a portfolio's higher yielding shares to be held in tax-wrapped accounts such as ISAs and SIPPs.

- Reduce your overall income levels - where practical, investors should consider reducing their other taxable income so as to remain within a more favourable tax band and therefore pay a lower rate of dividend tax. One way of doing this is to reduce income withdrawals being made from a SIPP or other pension wrapper.
- Make full use of your ISA allowances – since dividends from shares held in ISAs will remain tax free, it becomes ever more important that investors utilise their full ISA allowance each tax year. Each investor has an annual ISA allowance (presently £20,000 for the 2018/19 tax year) and funds within ISA wrappers advantageously grow entirely free of tax. Capital and income can also be withdrawn free of tax.
- Make full use of pension wrappers such as SIPPs - like ISAs, pensions are a form of tax wrapper within which dividends will remain tax free. For retirement savings where money is not needed until age 55 or later, the tax benefits of pensions are highly compelling. That said, the rules that govern pensions can be relatively complex and subject to change, so it is important to seek good advice before taking action. Under the current rules, pension contributions attract substantial tax relief that can be used to reduce an investor's income tax liability in a given tax year. Most people can make annual contributions of up to 100% of their relevant earnings, up to a limit of £40,000pa gross (although there are provisions to make larger injections if contribution allowances were not fully utilised in the three previous years). Investors that have started drawing income from a flexible arrangement such as a SIPP may additionally make adjustments to the level of income they draw so as to manage their income/ dividend tax rate and liability.

Do you need to take action?

Those investors that are unlikely to receive dividend income in excess of the new allowance from taxable accounts need not worry – the changes do not affect you. However, those that are likely to receive taxable dividend income above the new allowance should review their situation to see if they are able to reduce their tax bill going forward.

If you feel it would be helpful to review your arrangements in light of the changes, please do contact us - by having a Financial Planning as well as an Investment Management team we are uniquely able to deal with such cross-discipline matters in a joined up and efficient manner.

For more information please contact your wealth manager, or alternatively call us on 01223 720 208.

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