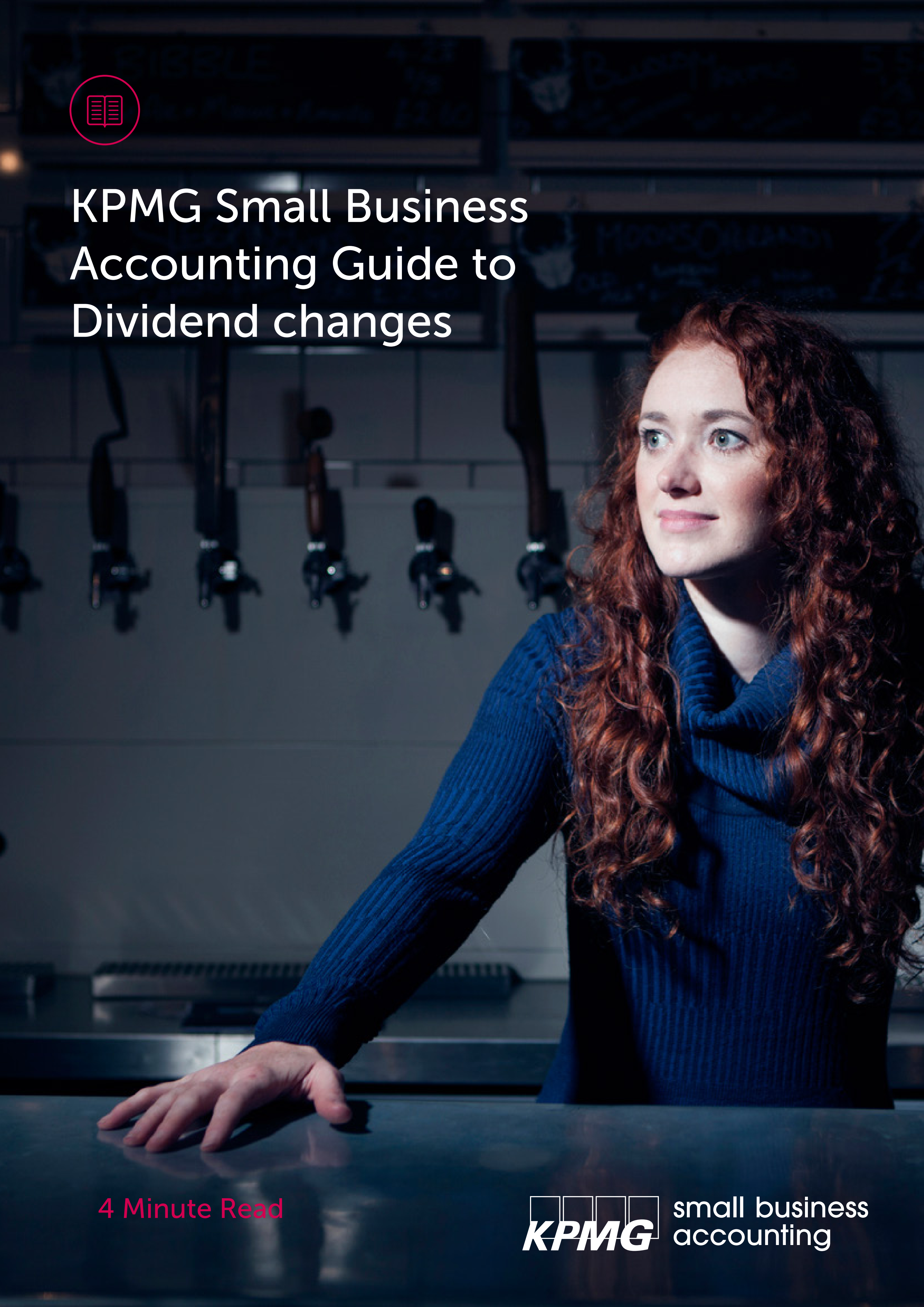
KPMG Small Business Accounting Guide to Dividend changes



4 Minute Read

Introduction

Do you take dividends out of your business? If so, you will need to know about the change in legislation happening this year.

From April 2016 the Dividend Tax Credit will be replaced by a new tax-free Dividend allowance.

With the corporation tax rate continuing to fall, the Government is keen to prevent businesses incorporating in order to achieve tax efficiencies that are not available to sole traders or partnerships.

The UK Government claim that this will be a simpler system, and that only those who have a significant income from dividends will pay more tax.

However, we believe if you have any income from dividends, it is good business sense to be aware of how the changes may affect you or your business.

This change in legislation is going to affect the thousands of small business owners that pay themselves through a combination of salary and dividends.

What's changing?

Currently all UK dividends are paid with a notional 10% tax credit, so non and basic rate taxpayers do not have to pay any further tax on dividends received. Only higher or additional rate taxpayers pay tax on dividends.

Dividend tax rates

Tax band	2015 effective dividend tax rate	2016 effective dividend tax rate*
Basic rate (and non-taxpayers)	0%	7.5%
Higher rate	25%	32.5%
Additional rate	30.56%	38.1%

*tax paid on any dividends you receive over £5,000

After a certain threshold employers must pay employer's national insurance whilst deducting for PAYE and employee's national insurance.

As a result many small business owners pay themselves a salary up to the NI threshold (currently £8,060 a year) with the rest of their income being paid through dividends.

Paying up to the threshold means that you maintain your employment record and are eligible to 'contributory benefits' such as maternity allowance and bereavement benefits, without tax being due.

Business owners can then pay themselves anything further from the company as a dividend, currently with no further tax due until they become a higher rate taxpayer.

However, from April 2016 each individual will receive a £5,000 tax free dividend allowance for each tax year, regardless of earnings.

What that means for you

It doesn't necessarily mean you will be paying more tax. In fact, HMRC claims that if you are an investor with modest income from shares, you'll see either a tax cut or no change in the amount of tax you owe and that only those with significant dividend income will pay more tax.

If you receive less than £5,000 per year in dividends, there will be no tax due. Dividend income will still be eligible for the personal allowance.

What to do next

Individuals setting up new companies may want to consider allotting shares to their partner or children, as each individual can benefit from the tax free dividend allowance.

Companies already trading can also consider this option but there will be other tax consequences of transferring existing shareholdings, such as capital gains tax. Taxpayers must use self-assessment to pay any tax due.

However, perhaps the most important thing you can do is consult with an accountant as to how the changes are going to affect you.

At KPMG Small Business Accounting we believe that a proactive and consultative approach to accountancy is vital for small business growth.

We know you want stay focused on the successful running of your business, and that it's our role to ensure you're aware of changes that might affect your financial interests.

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To find out more about how we could help, please email our team via **accounting@kpmg.co.uk**
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