

New dividend tax regime

What could the new system mean to you?

From April this year, the notional 10% tax credit on dividends is to be abolished and will be replaced by a new tax-free Dividend Allowance. The Dividend Allowance means that you won't have to pay tax on the first £5,000 of your dividend income, no matter what non-dividend income you have.

The allowance is available to anyone who has dividend income, and headline rates of dividend tax are also changing.

Income tax will apply to any dividends received over £5,000 at the following rates:

- 7.5% on dividend income within the basic rate band
- 32.5% on dividend income within the higher rate band
- 38.1% on dividend income within the additional rate band

This new system will mean that only those with significant dividend income will pay more tax. If you're an investor with modest income from shares, you'll see either a tax cut or no change in the amount of tax you owe.

Dividends received by pension funds that are currently exempt from tax, and dividends received on shares held in an Individual Savings Account (ISA), will continue to be tax-free.

From 6 April 2016, you have to apply the new headline rates on the amount of dividends you actually receive, where the income is over £5,000 (excluding any dividend income paid within an ISA).

The Dividend Allowance will not reduce your total income for tax purposes. However, it will mean that you don't have any tax to pay on the first £5,000 of dividend income you receive.

Dividends within your allowance will still count towards your basic or higher rate bands, and may therefore affect the rate of tax that you

pay on dividends you receive in excess of the £5,000 allowance.

These are two examples of how the new Dividend Allowance works:

You don't need to pay any tax on dividends up to £5,000, no matter what other income you get. That first £5,000 is tax-free under the new rules.

EXAMPLE 1 – YOU HAVE A (NON-DIVIDEND) INCOME OF £18,000, AND RECEIVE DIVIDENDS OF £22,000 OUTSIDE OF AN ISA

Tax you need to pay on the £22,000 dividend income:

- The Dividend Allowance covers the first £5,000
- The remaining £17,000 of dividends to be taxed at the new basic rate of 7.5%. This would need to be done through a tax return

Had your other non-dividend income been £30,000, the tax due on the £17,000 dividend income would be made up of 7.5% for the amount within the basic rate band, and 32.5% on the balance.

EXAMPLE 2 – YOU RECEIVE DIVIDENDS OF £600 FROM SHARES INVESTED IN AN ISA

As is the case now, no tax is due on dividend income within an ISA, whatever rate of tax you pay.

SHAREHOLDING DIRECTORS

If you're a company director who takes dividends instead of a salary, you should obtain professional financial advice to find out how you could be

affected by the upcoming changes in the next tax year and what steps you can take to be as tax-efficient as possible.

Taking dividends may still be a good option, but there are other tax planning opportunities to explore, such as paying into a pension, that might reduce the amount of tax you pay. ■

WANT TO DISCUSS YOUR OPTIONS?

If you would like to discuss your options or review any aspects of your portfolio, please contact us.

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