stewardship®

transforming generosity

withdrawal of personal allowances for high earners

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Stewardship Briefing Paper

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1 Overview

Entitlement to the income tax personal allowance is progressively withdrawn for individuals with taxable income of more than £100,000. The allowance is fully withdrawn where income exceeds £118,880 (for the 2013/14 tax year). This means that the marginal rate of income tax on income between £100,000 and £118,880 is 60%!

The silver lining of the tax cloud is that the main forms of charitable giving continue to attract tax relief at the donor's highest rate of tax. This briefing paper provides a detailed analysis of how charity tax reliefs interact with the withdrawal of the personal allowance.

2 The detail

2.1 Individuals with *adjusted net income* of over £100,000 will see £1 of personal allowance withdrawn in respect of every £2 earned in excess of £100,000. The personal allowance for 2013/14 is £9,440. Therefore, those earning more than £118,880 will have a nil allowance.

2.2 *Adjusted net income* is total income less certain reliefs, such as pension contributions, loss reliefs and gifts of qualifying shares or property to charity, less the *gross* amount of Gift Aid donations in the year.

Accordingly, Gift aid donations, and gifts of shares or property to charity can come to the rescue! Taxpayers who can make such gifts so as to reduce income below £118,880 will be able to 'reclaim' some or all of their personal allowance.

2.3 For individuals that are able to do this, the effective tax relief for Gift Aid payments will be up to 60%.

Example:

Albert has an income of £100,000. Bobby has an income of £118,880. Their respective tax liabilities are:

	Adjusted net income	Tax liability
Albert	£100,000	£29,822
Bobby	£118,880	£41,150
Difference	**£18,880**	**£11,328**

Bobby's additional income of £18,880 has led to an additional income tax liability of £11,328 (60% of the additional income). This is higher than the income tax rate being paid by those earning over £150,000, solely because of the withdrawal of the personal allowances on earnings between £100,000 and £118,880.

However, if Bobby were to make a Gift Aid payment to charity of £15,104 (net) which equates to a gross gift of £18,880 (the net payment is grossed up at the basic rate of 20%) he will enjoy tax

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relief of £7,552 and the charity will be able to reclaim tax of £3,776 (being the basic rate of 20% on the 'gross' gift of £18,880).

On a claim by the donor to HMRC, the gross gift reduces Bobby's adjusted net income from £118,880 to £100,000 restoring all of his £9,440 personal allowance. His tax liability now matches that of Albert; an effective tax relief of 60%.

The gift worth £18,880 to the charity has in effect cost Bobby £7,552 (that is, 40% of the gross gift made):

Cost of net gift	**£15,104**
Less:	
Tax relief at 40% (higher rate) less 20% (basic rate) on £18,880	£3,776
Tax relief at 40% on restored personal allowance of £9,440	£3,776
Effective cost	£7,552
Charity receives:	
Net gift	£15,104
Gift Aid tax relief (20% x £18,880, gross gift)	£3,776
	£18,880

3 Other forms of charity tax relief that reduce adjusted net income

In the same way that Gift Aid can be used to reduce adjusted net income, so can gifts of qualifying shares and securities and qualifying gifts of land. In broad terms, the amount of the reduction is equivalent to the market value of the qualifying investment at the time that it is gifted to the charity. The transfer to the charity is exempt from capital gains tax that would otherwise arise on the disposal of the asset to a non-charity.

4 Claiming the reliefs

Most, if not all, higher rate taxpayers will receive an annual self assessment tax return. Relief is claimed simply by entering the relevant amount into the Charitable Giving section on Page TR 4 of the return form as set out overleaf. Box and page references are to the Tax Return 2013. You may also find it helpful to refer to the Tax Return Guide (SA150).

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4.1 Gift Aid donations:

For Gift Aid donations, enter the net amount given (i.e. before any tax relief) as follows:

Made, and claimed, in the tax return year	Box 5
Made after the tax year, treated as made in the tax year	Box 8

Notes:

1. Box 7 is for recording gifts that were already carried back on the previous year's tax return. It is too late to be making a 'fresh' Box 7 claim on the current year's return.
2. There are strict time limits for a carry back of relief (Box 8) to be effective. The time limit is 31 January following the end of the tax year to which a donation is to be treated as carried back to, or the date that the Tax Return is submitted *(if earlier)*.

4.2 Gifts of shares and securities:

Made in the tax return year	Box 9

Note:

1. Usually the amount to be entered is the market value on the date that the shares were gifted, plus any incidental costs of transfer (such as brokers' fees), less any sale proceeds (where the shares are sold to the charity at an undervalue) and any benefit received from the charity. If in doubt, refer to the Tax Return Guide, Page TRG 20 (2013) or seek professional advice. Tax anti-avoidance rules apply to the value of the shares transferred where the transaction took place after 15 December 2009 and there is an avoidance motive involved.

4.3 Gifts of land and property:

Made in the tax return year	Box 10

Notes:

1. As for gifts of shares, a sale to the charity at an undervalue will also qualify for relief to the extent of the 'market value' proceeds foregone. The market value on the date that ownership passes to the charity can be increased by the legal and other costs of sale.
2. The transfer must be of the whole of the donor's beneficial interest in freehold or leasehold land in the UK. If property is jointly owned, all of the joint owners must join in making the gift.

If in doubt, refer to the Tax Return Guide, Page TRG 20 (2013) or seek professional advice.

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4.4 Gifts to non-UK charities

If any of your Gift Aid donations were made to non-UK charities, you should use Boxes 11 and 12, rather than Boxes 5, 9 and 10 (Paragraphs 4.1 to 4.3, above). You should then give the additional information requested on Page TRG 20 of the Tax Return Guide (2013) in Box 19.

Charities that are established in other EU countries of in Norway or Iceland can potentially meet the definition of a UK 'tax charity'. Charities based in other countries of the world cannot. Do not assume that just because a charity is established in one of the qualifying countries that it is indeed a charity to which donations will qualify for tax relief. Each individual charity must apply to HMRC and show that it meets the necessary legal requirements.

5 Action points

Donors who find themselves in the 'Personal Allowances Trap' of adjusted net income of between £100,000 and £118,880 should seriously consider the tax efficiency of making sufficient charitable gifts to restore some or all of their personal allowances, whilst providing a major benefit to charitable causes at a relatively low net cost.

Donors with adjusted net income just above £118,880 may wish to consider making charitable gifts sufficient to reduce their taxable income to below this level, or even below £100,000 in order to restore some or all of their personal allowances.

6 Adjusted net income above £150,000

Where an individual's 'Adjusted Net Income' is above £150,000, the individual will be liable to income tax at the 45% rate of income tax. Donors in this position should consult our Briefing Paper 'Charitable giving and the 45% income tax rate'.

7 Stewardship gold account

The Stewardship gold account is an ideal means of a donor obtaining timely tax relief on their charitable donations. Having made their donation to Stewardship, the donor can make requests at any subsequent time for distributions to be made by Stewardship to their favourite charitable causes. In the meantime, the account balance is credited by Stewardship with investment returns.

For further details: stewardship.org.uk/giving/gold-account.

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