



Minimising Taxable Interest From Savings And Dividend Income

We find that some clients are paying unnecessary tax on interest received on their cash deposits or on dividend income received.



The Problem

Often investments or deposit accounts are held jointly by a couple or by the higher taxed individual. The problem can be compounded due to the way in which the investment is held (ie the vehicle).

For instance, a jointly held Building Society Account producing £1,000 per annum interest in the hands of the higher rate tax payer will leave net interest of only £600 income.

If the partner/spouse is a basic rate tax payer, by transferring the account solely into their name a **tax saving of £200** is potentially possible leaving **£800 net income**.

A similar situation applies to dividend income in that it is often possible to rearrange the ownership of the asset to reduce the tax liability.

Investing to Solve the “Taxable Income” Problem

By reducing or eliminating “taxable income” from an investment, the reduction in tax can be even more significant and in some instances may reduce an individuals personal tax liabilities from higher rate tax, back down into lower rates.

Moving cash or equity holdings into the tax efficient environment of an ISA account can be one solution. However the extent of investment is restricted by the annual allowances which are quite limiting. A more effective route may be to use a “non income

producing asset” such as an investment bond. Investment bonds can provide a regular monthly or annual income and most bonds generally have no upper investment limit. Such investment vehicles can invest in numerous different asset classes to suit your investment objectives and risk profile, from simple cash at the lower end, to international equities, for the speculative investor, or somewhere in between.

Example - based on a £50,000 investment held in cash:

Building Society Account Interest Rate 3% gross

Gross interest	£1,500 per annum
Net basic rate tax payer	£1,200 received as income
Higher rate tax payer	£900 received as income

Tax to pay £300 or £600 dependant upon rate

Investment bond invested in cash fund net of charges 2%

Growth at 2%	£1,000
“Income” received basic rate taxpayer	£1,000
“Income” received higher rate taxpayer	£1,000

Tax to pay now: nil

Income to be declared: nil





The important issue is that the “income” withdrawal of £1,000 from an investment bond does not accrue to your annual taxable income in the year taken, thereby maximising “income” and minimising your annual tax liability.

Withdrawals of up to 5% per annum of the sum invested can be taken for 20 years without having to declare this on your annual tax return. This applies to both higher rate and basic rate tax payers.

Encashment of the bond after 20 years will not necessarily produce any tax liability if the total growth and ‘income taken’, when added to your income in the year of encashment, does not push you into higher rates of tax. A method known as top slicing reduces the gain over the total number of tax years held. Partial encashment or assignment to a lower rate tax payer may enable any additional tax to be avoided altogether.

Additional Benefits

Not only may it be possible to reduce your taxable income **without affecting your net income received**, but also in some cases an increased “income” may result.

Additionally such investments can be usefully utilised in Inheritance tax planning (see separate help sheet on IHT planning) at a later stage when income is less of a priority.



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For further advice and assistance

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