

CHAPTER 9

TAX REDUCERS

9.1 Introduction

Let us start by reminding ourselves where tax reducers slot into the income tax computation. We start with the taxable income then tax this income at the usual rates. From the resulting figure of tax, we can deduct any available tax reducers. This gives us the tax liability for the year. From the tax liability we deduct tax credits to give us a figure of tax due or tax repayable for the tax year.

	<i>Non Savings</i>	<i>Interest</i>	<i>Dividends</i>
Taxable Income	<u>X</u>	<u>X</u>	<u>X</u>
<i>Tax</i>			
@ 20%		X	
@ 40%/32½%		X	
@ 50%/42½%		<u>X</u>	
		X	
Less: tax reducers		<u>(X)</u>	
Tax liability		X	
Less: tax credits		<u>(X)</u>	
Tax due/(repayable)		<u>X</u>	

We have already seen one tax reducer, the married couples allowance (MCA) of £6,965, (2010/11) available for elderly taxpayers only. Relief is given as a tax reducer at 10%. The minimum MCA is £2,670, which at 10% gives a minimum tax reducer of £267. Watch out for "excess restrictions" where personal age allowances have been reduced to £6,475.

We will now look at the three other tax reducers.

9.2 Maintenance relief

[ITA 2007,
S.453](#)

Maintenance payments are payments made by a taxpayer to his former or separated spouse for the maintenance of that former spouse or of their children. To obtain any tax relief for maintenance payments, such payments must be made by virtue of a Court Order, or by virtue of an Assessment by the Child Support Agency (CSA).

Maintenance payments are always paid gross - i.e. tax is not withheld at source by the payer. The payer of a maintenance payment will only obtain tax relief if **either** the payer **or** the recipient was **born before 6 April 1935**. Therefore, relief is available to elderly taxpayers only.

The payer of the maintenance payment will obtain tax relief on the lower of the amount of the maintenance payments due to be paid, and £2,670 (i.e. the same figure as the minimum amount of the married couples age allowance). Relief will be given to the taxpayer by way of a **tax reducer at 10%**. This will be 10% of the lower of the amount paid or £2,670. This means that the maximum amount of the tax-reducer in respect of maintenance relief for 2010/11 is £267.

Illustration 1

Harry (76) is married to Evelyn (64). His income for 2010/11 is £16,000. He is divorced from his first wife, Sally (64) and pays her maintenance of £200 per month.

Harry's tax reducers for 2010/11 will be calculated as follows:

	£
Married couples age allowance (6,965 @ 10%)	696
Maintenance relief = lower of (a) 200 x 12 = 2,400 (b) 2,670 i.e. 2,400 @ 10%	<u>240</u>
Total	<u>£936</u>

Maintenance payments are always tax-free income in the hands of the recipient, irrespective of the amount paid and regardless of whether tax relief is received or not.

9.3 Enterprise Investment Scheme

[ITA 2007,
s.157](#)

Under the Enterprise Investment Scheme (EIS), a taxpayer obtains **tax relief** when he **subscribes** for shares in an **EIS company** - i.e. a company that satisfies the conditions of the Enterprise Investment Scheme.

In essence the taxpayer gives a capital sum to the company and the company gives the taxpayer shares in return. It is important to note that the investor must **subscribe** for the shares. This means that the company is issuing brand new shares to the taxpayer.

In order to encourage members of the public to invest in these EIS type companies, HMRC gives tax relief on the subscription. The relief is given by way of a tax reducer.

The **tax reducer** will be the **lower** of the **amount subscribed** for the shares and **£500,000**. Tax relief is then given at the **flat rate of 20%**. Therefore, the maximum tax reducer in respect of the EIS subscription is £100,000, being £500,000 at 20%.

[ITA 2007, s. 158](#)

This tax relief from the EIS subscription will reduce a tax liability, but it cannot turn the tax liability into a negative figure. Therefore, if the tax relief on the EIS subscription is greater than the amount that the taxpayer owes for the year, his tax liability is zero. Any tax deducted at source, for instance tax on bank interest or tax under PAYE, would therefore be repaid.

9.4 Venture Capital Trusts

[ITA 2007, s.261](#)

Tax relief on subscriptions for shares in a Venture Capital Trust (VCT) is given in much the same way as tax relief on EIS shares. If a taxpayer **subscribes** for new shares in a company that satisfies the conditions of a **Venture Capital Trust**, tax relief is given by way of a tax reducer.

This tax reducer is the **lower** of the **amount subscribed** for shares in the VCT, and **£200,000**.

[ITA 2007, s. 262](#)

The tax reducer is a **percentage** of the lower of the amount subscribed, or £200,000. For subscriptions in 2010/11, **the percentage is 30%**. The maximum tax relief obtained on a VCT subscription in 2010/11 is therefore £60,000, i.e. £200,000 at 30%. Again this tax reducer can reduce a tax liability to zero, but cannot itself create a repayment.

[ITA 2007, s. 263](#)

EIS and VCTs will be covered in detail in a separate chapter.

9.5 Additional points on married couples relief

The order in which tax reducers are deducted is determined by the taxpayer. In many instances it will not make any difference. However, HMRC do allow us to take **married couples relief last** - i.e. after maintenance, EIS and VCT reliefs.

This is because any unused married couples relief can be **transferred to the other spouse at the end of the year**. This may happen, for example, if the husband / high earner has insufficient income to use up the full amount of the married couples tax reducer. So if we set the married couples relief off last, we make sure that any excess does not go to waste.

If the husband / high earner wishes to transfer excess married couples relief, he must make a claim to this effect within **4 years** of the end of the tax year. The transfer will not happen automatically.

The married couples tax reducer is allocated to the husband / high earner in the first instance. However, the wife / lower earner may make an election to claim 50% of the basic married couples relief. For 2010/11, they may therefore take 50% of £2,670, being £1,335, leaving the other spouse / partner with the rest of the tax reducer. This claim does not need the partner's consent, but must take place before the start of the tax year if it is to be valid. Note that this will not increase the amount of the relief but will simply alter the way it is allocated.

[ITA 2007, s. 47](#)

Alternatively, if the couple both elect, the wife / lower earner may take the whole of the basic married couples relief - ie £2,670 - again leaving their partner with the rest. If the partner cannot use the remainder, the balance may be transferred after the end of the tax year. Remember that whoever claims the allowance, relief is given by way of a tax reducer at 10%. [ITA 2007, s. 48](#)

Example 1

Mike (77) has been married to Anne (72) for over 40 years. His net income (before PAs) for 2010/11 is £31,000.

Mike makes the following payments:

Maintenance to ex-wife	£100 per month
Subscription for EIS shares	£4,000

Calculate his total tax reducers.

Answer 1

PAA (>75)	£
	9,640
Less $\frac{1}{2} \times (31,000 - 22,900)$	<u>(4,050)</u>
	<u>5,590</u>
Excess restriction	
= £4,050 - £[9,640 - 6,475] = £885	
MCAA tax reducer	£
£(6,965 - 885) @ 10%	608
Maintenance relief lower of:	
a) $100 \times 12 = £1,200$	
b) £2,670	
i.e. £1,200 @ 10%	120
EIS relief	
£4,000 @ 20%	<u>800</u>
Total tax reducers	<u>£1,528</u>