

Personal taxation

R03 2016–17 edition

Web update 2: 14 September 2016

Please note the following update to your copy of the R03 study text:

Chapter 1, section K5C, example 1.21, page 1/38

Please amend the example (corrections in **bold**) so that it now reads:

Example 1.21

For 2016/17, a discretionary trust receives dividend income of £2,000.

1. The trustees will pay the standard rate of 7.5% tax on the first £1,000 (the standard rate band), and then 38.1% on the excess.

The tax payable is therefore $(£1,000 \times 7.5\%) + (£1,000 \times 38.1\%) = £456$.

If the trustees accumulate the income within the trust, then **£2,000 – £456 = £1,544** is rolled up within the trust.

However, if they decide to exercise their discretion and pay all the income to one of the beneficiaries, Rob Booth, the situation is as follows:

2. Any income paid by the trustees to Rob is deemed to be trust income and not dividend income.

If a net payment was made to Rob of **£1,100**, this would be grossed-up trust income of $£1,100 \times 100/55 = £2,000$.

As distributed trust income, it is deemed to have been taxed at 45%, i.e. **£2,000 at 45% = £900**.

The trustees have already paid tax of £456 and so have to pay HMRC a further **£444 (£900 – £456)**. The trustees therefore have **£1,544 (£2,000 – £456) – £444 = £1,100** left to pay to Rob.

The consequences for Rob are as follows:

1. If Rob is a non-taxpayer (e.g. because of an unused personal allowance), he can reclaim all the tax actually paid by the trustees, i.e. **£456 + £444 = £900**. This is the 45% tax credit on his gross trust income of **£2,000**. Therefore Rob ends up with **£1,100 + £900 = £2,000**.
2. If Rob is a basic rate taxpayer, he can reclaim some of the tax actually paid by the trustees. Rob is deemed to have received gross trust income of £2,000, on which his tax liability at 20% is £400. He can therefore reclaim **£900 – £400 = £500**. Rob thus ends up with **£1,100 + £500 = £1,600**.
3. If Rob is a higher rate taxpayer, he is deemed to have received gross trust income of **£2,000**, on which his tax liability at 40% is **£800**.

He can therefore reclaim **£100 (£900 – £800)**.

Rob ends up with **£1,100 + £100 = £1,200**.

4. If Rob is an additional rate taxpayer, he would have no further tax liability on the trust income as the 45% tax liability will be covered by the 45% tax credit.

Rob ends up with **£1,100**.

