TAX AND YOUR FAMILY

Whether you're married, single, with a partner, divorced or widowed, you need to know how the tax rules work

Families come in all shapes and sizes, and so do the tax rules that affect them. We go into the details here and alert you to an important change regarding same-sex couples.

TAX AND MARRIAGE

Husbands and wives in the UK are taxed independently. This means they each have their own personal allowance (the amount they can earn before they start paying income tax). However, if you don't use up all your allowance (£4,895 for 2005-2006), you can't transfer it to your spouse. Since 6 April 2000, you qualify for married couple's allowance only if you, or your spouse, were born before 6 April 1935 – see p40.

JOINT INCOME

If you and your spouse have assets (for example, shares) in joint names, you each pay tax on half the income unless you elect otherwise. If you own the investments in unequal portions, the income can be divided between you in the same ratio as you own the investment by completing form 17 (from the Inland Revenue website or your tax office).

Where one spouse pays tax at the higher rate and the other doesn't, or one is a non-taxpayer, it can make financial sense to transfer income-paying investments to the person paying the least tax. This will save tax but the transfer has to be genuine and without reservation (the investment must be put into your spouse's name, and you can't demand the money back).

The exception is where a married couple own shares in a 'close' company – typically a family company for which one or both work. Since 6 April 2004, you have been taxed on the actual proportion in which you own the shares or the right to income from them.

SAME-SEX COUPLES

The Civil Partnership Act 2004 creates a new legal relationship for same-sex couples. It will allow same-sex couples to have the tax and benefit advantages available to married couples. This is especially important where capital gains tax and inheritance tax are concerned. Unmarried heterosexual couples will not be permitted to form civil partnerships.

Transfers

Special rules for married couples apply when it comes to transfers for capital gains tax and inheritance tax purposes. These rules will apply also to registered same-sex couples who register

Gifts between spouses are free of CGT and IHT liability

under the Civil Partnership Act (see 'Same-sex couples', left).

There's normally no capital gains tax to pay when a gift or transfer is made, unless you are divorced or separated (except in the tax year you separated) or unmarried partners.

A husband and wife can give unlimited amounts of money or possessions to each other without being liable for inheritance tax unless the giver's domicile (broadly, their permanent home) is in the UK and the recipient's is outside, when there is a £55,000 limit. Once a couple divorce, this exemption is lost but there's still no inheritance tax to pay on:

- maintenance payments to a former partner or children, including adopted and step-children, who are under 18 or in full-time education
- money paid as a divorce settlement and, in some cases, money given to you following a change to an agreement made on or before your divorce.

LIVING TOGETHER

If you live together as an unmarried couple, your income tax position is much the same as if you were married, although there are some important differences. You are not entitled to the married couple's allowance, even if you or your partner were born before 6 April 1935; you can't claim any of the state benefits paid on bereavement; and you are not entitled to the exemptions for capital gains tax or inheritance tax.

Making a will is particularly important as another difference is that the surviving partner has no automatic right of inheritance – under the intestacy rules, relatives, rather than the surviving partner, inherit (see 'Inheritance tax', p62). But there are circumstances under which a surviving partner can claim a share of the estate.

SEPARATION AND DIVORCE

Payments you receive under a maintenance agreement are now treated as tax-free income, whether they're from an ex-spouse, parent or step-parent. There is now no tax relief on maintenance payments you make unless you or your ex-partner were born before 6 April 1935. Maintenance reliefs given as a reduction in your tax bill in the same way as is done with married couple's allowance. The amount deducted is equivalent to 10 per cent of either the maintenance you pay or 10 per cent of £2,210 (2004-2005's maintenance allowance), whichever is lower. Maintenance allowance is £2,280 for 2005-2006.

TAX AND CHILDREN

There are some tax concessions available if you have children, and for the children themselves.

Childcare payments

If you're eligible to use a workplace crèche provided by your employer, this benefit isn't taxable. From April 2005, this will be extended to childcare outside the workplace. Staff will be exempt from income tax and National Insurance on up to £50 a week of childcare vouchers or 'employer contracted' childcare (that is, where the employer pays the bill direct). Childcare must be provided by a registered person (a childminder, say) and the benefit must be available to all staff.

Child trust funds

From April 2005, the government will set up child trust fund (CTF) accounts for children living in the UK. Parents or guardians of children born on or after 1 September 2002 will automatically receive a £250 voucher to set up an account on their behalf. Children born between 1 September 2002 and 5 April 2005 will get interest to compensate them for the time that money wasn't invested (see 'Funding the future', above right). Children in households on lower income will receive an extra £250. The government also plans to make a further contribution when a child reaches seven. Family and friends and children themselves can between them contribute up to a further £1,200 a year. CTFs will have the same tax benefits as Isas. Children will not be allowed to access the money until they reach 18.

Children's tax position

The income and capital gains of your children are normally classed as theirs. Children have their own personal allowance of £4,895 and capital gains tax exemption of £8,500 (for the 2005-2006 tax year). This means they can reclaim tax deducted on savings interest (using form R40) or have it paid without tax deducted (via form R85). Where income they receive from money or an investment given by a parent comes to £100 or more a year, it is taxed as the parent's own income unless the investment itself is tax-free. This rule applies to gifts from each parent (so a child can have income of £200 a year from parental gifts), but not to gifts from other friends or relatives, where the income is still treated as the child's.

Payments to pensions

Payments to a stakeholder pension can be made by one person on behalf of another. So a parent can pay up to £3,600 a year including tax relief on behalf of a child. The payment is treated as if it is made by the recipient – thus, even if you're a higher-rate taxpayer, you won't get higher-rate tax relief. The child can't access the fund until the minimum age at which a pension can be taken. ■

FUNDING THE FUTURE

Heike Holes has just received a child trust fund voucher for her son, Daniel. Daniel (left) was born on 9 January 2003 and so qualifies for £250 from the government. As he was born before 6 April 2005 (when child trust funds come in), interest is added, bringing the value to £277. Family and friends can add up to an extra £1,200 a year.

Heike now has to invest the money. She can choose a deposit-based account, a totally share-based plan or a 'stakeholder'. The article on child trust funds in April 2005's *Which?* should help Heike make her decision.

Daniel's brother Christopher was born in April 2001 – too early for the child trust fund. But his mum's keen he's not left out. She's planning to invest extra amounts for him, too, in the future.

Heike plans to invest for her sons

MORE HELP

Which? reports

- Child trust funds, April 2005

Inland Revenue booklets

- IR45 Tax when someone dies
- IR115 Income tax, National Insurance and childcare
- IR121 Income tax and pensioners
- IR170 Blind person's allowance