

## **Family shares and rent a room (Lecture B1312 – 10.17 minutes)**

Transferring shares around family members has always had its benefits. Income is often moved around to maximise the use of personal allowances and tax rates bands and alphabet shares have been used to help fund children through university.

In 2022, with increasing household costs, alphabet shares now have further possibilities. We could pay dividends to our children who are over 18 and living at home, who then use that income to pay rent, with parents claiming rent-a-room relief to avoid paying tax on that income.

### *Reclassifying shares*

Alphabet shares are best set up when the company is first formed but it is feasible to issue them during a company's trading life.

We could engage the services of a company secretarial agency to reclassify ordinary shares that are currently in issue to become 'A' shares with the same full voting and capital rights as they had before reclassification. The difference is that dividends are now independent of all other class of shares. The secretarial agency would then create a new class of 'B' shares and schedule a bonus issue of these shares to the parents. These shares would have full voting and capital rights but independent dividend entitlement from any other class of shares. The B shares are then gifted to the children who are 18 or over with any gain covered by gift relief as this is a gift of shares in an unquoted trading company.

Typically, the fee charged by the secretarial agency would be in the region of £250 to £300.

### *Example*

Andy and Jane each own 50 ordinary £1 shares in their trading company and are both directors of the company. Each draws a salary of £12,500 and take dividends of £37,500 per annum (£3,125 per month). The couple could withdraw more money from the company but are keen to avoid higher rates of tax. They are also aware that their child benefit for their 14 year old twins would be reduced if they had income in excess of £50,000.

Their third child, Rob, is 18, and about to start an apprenticeship at a local plumbing company.

A secretarial agency is appointed to redesignate the existing ordinary shares into ordinary 'A' shares. A new class of 'B' shares is created, with both 'A' and 'B' shares ranking equally in respect of votes and capital rights. Dividends can be declared independently of each class of share. A 1 for 2 bonus issue of 'B' shares is made.

After the bonus issue both Andy and Jane each own 50 'A' shares and 25 'B' shares. They both gift 5 of their 'B' shares to their 18 year old son, Rob.

The couple are aiming to pay £6,000 to Rob so that he can pay £4,000 into a Lifetime ISA. The remaining £2,000 will help him pay his rent of £275 per month for living at home.

For Rob to receive an annual dividend of £6,000, the 'B' shares must pay a dividend of £600 per share. Andy and Jane would then also receive £12,000 each so they would need to reduce their 'A' dividends from £37,500 to £25,500 to stay within the basic rate band.



### *Practicalities*

A gift claim is prepared (HS295) for each gift of shares by Andy and Jane, for the parties to sign. This gift will be declared on their Self Assessment return.

Using Rent-a-room relief, qualifying rental income is tax free up to £7,500. Rob's rent is well below this and so is tax free income for his parents. Andy and Jane could charge more rent and it would still be tax free. They could consider using this in the future for their twins.

Rob has an annual dividend of £6,000 per annum, of which £4,000 would be taxed at 8.75%. Remember the first £2,000 is covered by the dividend allowance. However, he has £5,000 per annum building up in his Lifetime ISA. That is the £4,000 plus the £1,000 government bonus.

### *Settlements legislation*

The settlements legislation is in point where there is a bounteous gift of income and the settlor still has an interest in this income.

In our example, Andy and Jane do have an interest in this income as some of the dividend is paid back to them as rent. However, as the shares have capital and voting rights, it would be difficult for HMRC to argue that pure income has been shifted. The gift that was made was of capital and income. If we stripped the shares of capital and voting rights, there could be an issue.

*Article contributed by Dean Wootten*