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Simplifying taxes

The UK200Group was delighted to be given the opportunity to contribute its opinions to the government's new Office for Tax Simplification (OTS).

When the OTS was set up in July, we got in touch, reminding them of our expert knowledge of tax and accounting issues, particularly regarding small businesses, and were invited to see them.

Two of our members got to meet with officials at the OTS and were able to point out that, while a simpler tax system was desirable, this should not be at the expense of fairness by creating a 'one size fits all' system – the key objective should be to strike a fair balance.

We pointed out that most small businesses have no interest in tax evasion – what they want is certainty that the rules will not keep changing and that they are paying the right amount because the rules are clear.

Specific issues raised included P11Ds - where the same information is often asked for twice on different returns - VAT and the different rules surrounding shares in private versus public companies.

The office appeared very receptive to our points and we got the impression that we were not the first people to raise them. We await with interest what the outcome of the OTS reviews will be.

WINTER 2010

Putting the lid on pensions

Giving tax relief for individual and employer pension contributions has been tax efficient for many years but this is ultimately a costly business for the Exchequer.

The previous Government had passed legislation, due to take effect from 6 April 2011, which could create an income tax charge for certain high earners in respect of pension contributions as a way of clawing back some of the tax relief. For some, 2009/10 and 2010/11 has also involved a tax charge under transitional rules in anticipation of those changes.

The Coalition Government has consulted on an alternative, simpler approach to achieve the same fiscal objective of capping the cost of tax relief on pension contributions. As a result, the Financial Secretary to the Treasury, Mark Hoban MP, has now announced that the annual limit for tax-advantaged pension saving will be reduced from £255,000 to £50,000 from 6 April 2011.

'We have abandoned the previous Government's complex proposals and developed a solution that will help to tackle the deficit but not hit those on low and moderate incomes. We have taken a tough but fair decision.

The Coalition Government believes that our system is fair, will preserve incentives to save and - compared to the last Government's approach - will help UK businesses to attract and retain talent.'

This means that those who are most able to make significant pension savings will still be the primary target group. Where the annual limit is exceeded a tax charge may apply, although measures will be introduced to allow individuals who exceed the annual limit to use up any unused limit from the previous three years. To be able to benefit from this facility, it will also be necessary for the individual to be a member of a registered pension scheme at some time during those earlier years.

Any excess contributions, whether personal or employer provided, will then be taxable. The rate of tax will depend on the individual's personal tax position but will generally be at 40/50%.

Some careful planning may be required for those seeking to make substantial pension provision now or in the future so please contact us for further guidance as to how this may impact on your individual circumstances.



Repair at your leisure

The issue as to whether certain expenditure on buildings is repair or capital in nature is often a source of contention between HMRC and taxpayers. From the business perspective a repairs deduction generally provides immediate tax relief whereas capital expenditure on premises may not qualify at all. Two recent cases in this domain both ended in success for the businesses concerned.

The first case concerned an individual who had income from property lettings and claimed a deduction of £119,002 as repairs and renewals.

One of the properties let had been owned for 30 years and consisted of a house, an outbuilding, garden and grounds. The listed outbuilding had become extremely run down and was becoming dangerous.

The architect concerned confirmed this and stated that, as the building was listed, there was no option other than to undertake a substantial repair scheme. He was concerned that the roof could collapse if there was heavy snow, the point work had perished, the brickwork had been affected by frost, some of the timbers were

rotten and had wet rot, there was no felt under the tiles, the slates had slipped, there was no damp course, an internal partition was required to keep any timber away from moisture and the rafters, doors and windows were in an appalling state of repair.

The plans for the repair scheme were produced to the Tribunal, including photographs of the outbuilding, before and after the work and the consent letters from the council. In undertaking this repair scheme it had also 'made sense' to bring the interior more up to date, including heating, electric power points and water supply, although there were no basins, toilets, kitchen or anything that would allow the building to be anything more than additional living space ancillary to the main house.

The work involved shoring up the structure, grouting, pointing, decorating and replacing windows, doors and roof, keeping exactly to the previous external design apart from a change to the size of a door.

The Tribunal found that the disputed work was one of essential repair. What was very important in this case was all of the factual evidence that the taxpayer was able to produce.

Are alterations incidental?

The second case concerned £63,050 incurred by a company on the construction of a control

room to house security equipment. The issue was whether this could qualify as alterations to an existing building incidental to the installation of plant and machinery for the purposes of the company's qualifying activity. If so, then the costs incurred on the construction if not repair expenditure could at least potentially qualify as plant and machinery.

The control room was contained within an existing building already in use by the company and it required substantial alteration to turn it into the control room in question. The existing walls, floors and ceiling had to be strengthened, a floor compatible with extensive computer usage had to be installed, an interlock needed to be fitted, as were fire-proof security doors.

The room was also adapted to render it substantially independent in terms of its facilities. It was provided with washroom facilities, a kitchen and an independent power supply.

In this case, the Tribunal held that there was a close enough link between the costs incurred and the equipment in question and so the majority of the construction costs were allowed.

This is an area of tax which continues to evolve so if you are thinking of any sort of major repair work, please do get in touch before you start to ensure the most tax efficient method.

The seesaw of tax rates

Going up

In the Pre-Budget 2009, the Labour Government proposed an increase in the rates of National Insurance Contributions (NIC) from April 2011. The Coalition Government intend to go ahead with these changes. A further 1% increase will apply to the rates for employers, employees and the self-employed. The employee rate of Class 1 NIC will be 12% and the self-employed Class 4 rate will be 9%. The employer rate will increase to 13.8%. The additional rate of Class 1 and 4 contributions payable which applies once the upper earnings limit is reached will be increased from the current 1% to 2%. This rate only applies to employees and the self-employed. It does not apply to the employer as there is no upper limit on their contributions.

In order to protect those at the lower end of the earnings scale the Government has announced that the primary threshold and lower profits limit will be increased so that those earning below £20,000 should pay less NICs overall as a result of the change.

From April 2011, the Coalition Government will also increase the level before which employers start to pay NICs by £21 per week above indexation. According to the Budget report:

'As a result, the number of employees for whom employers pay no NICs will rise by 650,000.'

For many employers however the 1% rise in NIC rates may represent a significant increase in costs so looking at opportunities to minimize these

costs should be explored. If you have any questions or concerns about the forthcoming changes, please contact us.

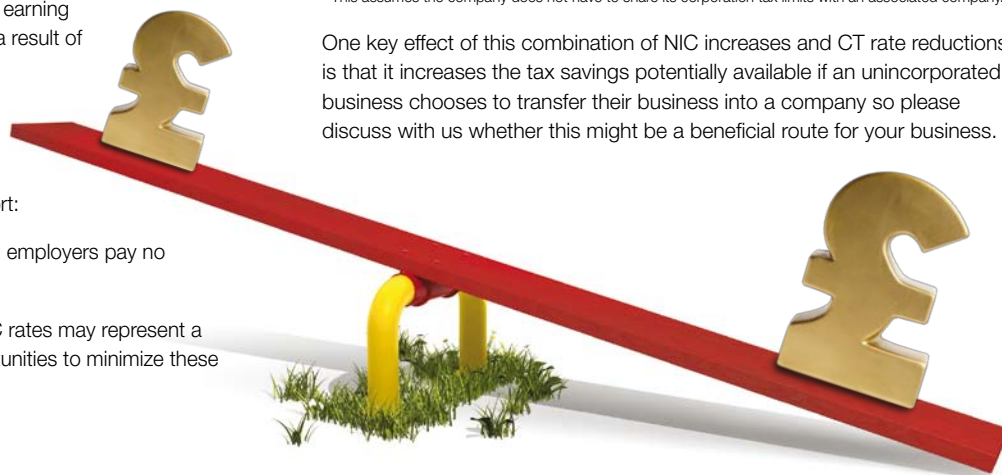
And down

Meantime corporation tax (CT) rates are set to decrease next year as follows:

For a company* on taxable profits	1 April 2010 to 31 March 2011	1 April 2011 to 31 March 2012
First £300,000	21%	20%
Between £300,000 and £1.5 million	29.75%	28.75%
Above £1.5 million	28%	27%

* This assumes the company does not have to share its corporation tax limits with an associated company.

One key effect of this combination of NIC increases and CT rate reductions is that it increases the tax savings potentially available if an unincorporated business chooses to transfer their business into a company so please discuss with us whether this might be a beneficial route for your business.



Is tax exile a realistic option?

The introduction of the 50% top rate of income tax and now the increase in capital gains tax on non-business gains to 28% for higher rate taxpayers has caused some individuals to give some passing thought at least to the possibility of leaving the UK completely. Certainly the route into tax exile is a well-trodden one, as was illustrated in the 1970s when tax rates were higher than they are now. However the ground rules have changed and the decision will not be an easy one to take.

In this article we consider the current issues surrounding tax exile and highlight the key areas which must be considered.

It is clear that HMRC have been taking an increasingly close look at a number of individuals who have tried to become non resident. A recent court case has significantly reinforced HMRC's hand and has made it much harder to achieve non resident status. The case concerned an individual who spent the majority of each tax year outside the UK dealing with his many business interests all around the world. His average time in the UK each tax year was well below the 91 days which HMRC have traditionally allowed non residents to spend in the UK in each tax year. The major problem which was identified was the fact that the individual had maintained a substantial property in the UK where his family continued to reside and which he naturally spent time at on his visits back to this country.

The Court has decided that where an individual leaves the UK other than to take up a full time employment abroad they must demonstrate to the satisfaction of HMRC that they have permanently left the country. The court has further interpreted this as meaning that the individual must show that there has been a distinct break in the pattern of their life in leaving the UK. In practical terms this is going to mean having to take very difficult decisions about what to do with the family home and indeed whether or not the whole family needs to move away from the UK. This will obviously have implications for areas such as the education of the children and the economic activity of a spouse or partner.



Assuming that this hurdle is successfully overcome it is important to ensure that visits back to the UK do not exceed the 91 day average. Any day where you are in the UK at midnight counts as a day in the country; so the more visits you make the more you are likely to increase the pressure on your average.

It is possible to become not resident by taking up a full time employment abroad and ensuring that all the duties of that employment are carried out abroad. This employment needs to start immediately on departure from the UK and must last for at least a complete UK tax year. Return visits to the UK must not exceed an average of 91 days in each tax year.

Remember that if you leave any income sources in the UK after you have gone such as an investment property then you remain chargeable to tax in the UK on any income which arises here.

In order to successfully avoid capital gains tax there is a very significant extra requirement. The period of non residence must last for at least five UK tax years from the date of departure otherwise any gains you make whilst abroad will be taxed when you arrive back in the UK.

Please don't forget that the UK only represents half of the issue. The other half is represented by the tax position in the country in which you intend to reside. Whilst there are a few absolute tax havens around the world, most countries have a tax system and careful advanced planning is needed to avoid leaping from a UK tax frying pan into someone else's tax fire.

Pool cars?

A recent case has once again focussed on the rules for pool cars. If an employer provides an employee with a car by reason of their employment, there is usually a tax bill for the employee. However, if the car is a pool car there will be no tax bill for the employee.

The conditions for a car to be regarded as a pool car are:

- the car was made available to, and actually used by, more than one employee
- the car was made available, in the case of each employee, by reason of their employment
- the car was not ordinarily used by one employee to the exclusion of others
- in the case of each employee, any private use of the car made by the employee was merely incidental to the employee's other use of the car in that year and
- the car was not normally kept overnight on or in the vicinity of any residential premises where any employee was residing.

As you might expect, HMRC require clear evidence that these tests are met, especially when, as in this case, the cars in question were high-end cars - a BMW 5 Series, a BMW 6 Series, a Toyota Land Cruiser and a Volvo XC940!

The company had little written evidence, such as a mileage log, to prove that the above tests were met. The employer said that there was sufficient car parking at or near the employer premises. However, the cars were taken home from time to time but usually only where there was a business journey the next morning.

Effectively, HMRC merely said 'prove it'. Fortunately for the employer in this case, the Tribunal found the evidence of the employees to be credible and understandable in this small business. The Tribunal felt that in a small office with a few employees, control of the pooled cars could be achieved without formal written rules although it remains best practice and avoids doubt if those records are maintained.

Two other points are worth noting:

- the company has subsequently changed its policy but did not accept that was an indication of guilt;
- HMRC had carried out surveillance on employees in 2008 but this was not admitted as evidence because it was outside the period covered by the appeals.

On a related matter, statistics released by HMRC show a massive rise in the additional tax that HMRC are finding in relation to employer provided vans, which suggests that this is another problem area.

Of course, good records today keeps the Taxman away! If you would like to discuss these issues in more detail, please do get in touch.



Giving it all away

Individuals who wish to help charities can gain significant tax breaks. With the introduction of the 50% rate and also the rules which withdraw the personal tax allowance for those with adjusted net income over £100,000, the tax benefits of being generous are enhanced.

The gifts can be made to existing charities or the individual may want to consider establishing their own charity in order to control the funding of charitable work. There are a number of options available.

Gift Aid

The scheme applies to any donation, whether regular or one-off, and irrespective of the amount. The donor has to give a declaration to the charity which includes a statement that the donor is a taxpayer.

The donor is deemed to have made the gift out of taxed income and the charity can reclaim the income tax deducted. The reduction in the basic rate to 20% threatened to reduce the reclaim by the charity but the introduction of a temporary relief restored the position so that for every £100 donated the charity can currently claim £28.20.

The basic rate band and the higher rate band can be increased by the gross amount of any Gift Aid payments, so that the effect is to give a further relief equivalent to up to 30% of the gross gift.

Carry back of relief

It is also possible to make a claim to carry back a donation so that relief is given in the previous tax year, as long as the donation is made before the tax return for the previous year is submitted and by the following 31 January.

Example

A donation made by 31 January 2011 could be carried back to the 2009/10 tax year provided that the 2009/10 tax return hasn't yet been submitted. However, with a 50% tax rate in 2010/11, a carry back may not give the best result.

Benefit to the donor

Care needs to be taken where the charity may be offering something back to the donor e.g. free tickets for an event. There are specific limits that determine the maximum benefits that can be paid and, if those limits are exceeded, the gift will not be effective for Gift Aid purposes.

Payroll giving

There is no upper limit on the amount of donations under payroll giving. The donor obtains instant tax relief under the scheme

because the agreed donations are deducted from gross pay before tax is applied (although the gross salary is still used for NIC purposes). There is an advantage for the 50% taxpayer in obtaining relief quicker this way than under Gift Aid and the net cost of the donation is lower (a donation of £100 costs only £50 under payroll giving but £62.50 under Gift Aid). However the charity receives only the basic sum.

The scheme is only available to those in employment and requires the employer to be prepared to operate the scheme with the assistance of an agency charity to handle the receipt and distribution of the donations.

Gifts of assets

If you are feeling more adventurous, tax relief is also available for gifts to charities on:

- quoted shares or securities;
- unquoted shares or securities which are dealt in on a recognised stock exchange (e.g. shares traded on AIM);
- units in an authorised unit trust;
- shares in an open-ended investment company; or
- an interest in an offshore fund;
- land and buildings.

Donors are able to claim a deduction in calculating their income for:

- the market value of the investments on the date of disposal; plus
- any incidental costs of disposal; less
- any consideration given in return.

This is a significant tax relief and could mean that a taxpayer say with a large portfolio of stocks and shares could make regular gifts each year and significantly reduce their income tax bill.

So, if you are planning any such donations and would like to maximize your tax position, please talk to us in advance of any gift.



VATs it all about?

Even without the forthcoming increase in the rate, VAT is never easy at the best of times but recent HMRC announcements add to the long list of things to remember.

Reminder about paying VAT by cheque

HMRC have recently issued a reminder about paying VAT by cheque.

Since 1 April 2010 all VAT registered businesses with a VAT exclusive turnover of £100,000 or more, and all newly-registered businesses regardless of their turnover, must submit VAT returns online and pay electronically.

Businesses that are not caught by the above rules can still pay by posting HMRC a cheque but, from 1 April 2010, all cheque payments sent to HMRC by post are treated as being received by HMRC on the date when cleared funds reach HMRC's bank account, not the date of receipt.

So sufficient time must be allowed to enable the cheque to reach HMRC and clear into HMRC's bank account. A cheque generally takes three bank working days to clear.

HMRC have also requested that those paying by post make the cheque payable to 'HM Revenue & Customs only', followed by the nine-digit VAT registration number, and send it with the return using the pre-addressed envelope. In addition, they ask that the cheque is not fastened with paper clips or staples.

VAT errors

If a mistake is identified on a previous VAT return, HMRC may need to be informed or the error adjusted in the next return.

HMRC have found that many of the mistakes separately reported to them could have been corrected by the taxpayer. As there can be a delay of several weeks in processing corrections, HMRC are advising taxpayers to correct the mistake themselves if it is possible under the rules.

HMRC have issued revised guidance on what to do if it is discovered that a mistake has been made.

Please do get in touch if you would like to discuss this or any other VAT matters which may affect your business.