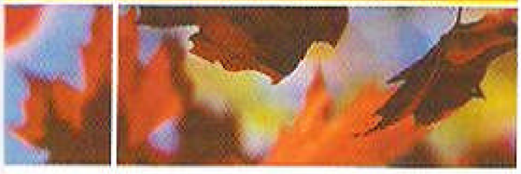
2010 AUTUMN NEWS



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Answer: Tin hats and patience

If that's the answer, the question might be, 'what should we invest in for our dealings with the taxman?'

The Coalition Government has been very straightforward about the financial pain that we will face over the next few years: big cutbacks in public spending and significant increases in tax, particularly VAT and CGT. The Chief Secretary to the Treasury, Danny Alexander, recently announced another aspect of the squeeze – increasing HM Revenue & Customs' budget by £900m, in a time of austerity, so they can chase after £7bn that currently goes missing in the tax system. There will be a 'crackdown on avoidance and evasion'.

We have heard this before. If HMRC use the resources to catch people who are illegally evading tax, good luck to them. But those people are hard to find: it's easier to shake down the ones who are trying to pay the right amount and not a penny more. There are already rumours that they will be looking into the returns of each taxpayer who pays tax at 50% – everyone with an income above £150,000.

Meanwhile, HMRC's routine handling of taxpayers is creaking, even before planned 25% cutbacks in the Department. It can take months to get a reply to a letter. If they want to receive a reply quickly, they have taken to including a red sticker with their enquiry letter so the return envelope stands out in the mountain of mail. This is frustrating for anyone who is trying to comply with their obligations. It's not yet clear whether sticking red dots on all the letters we send to HMRC will achieve a quicker turnaround.

We expect difficult times in dealing with tax. Whatever happens, we will be here to help. •

Rates of change

On 6 April 2010, most tax rates and allowances stayed the same, apart from the introduction of the top 50% rate for people earning over £150,000. On 6 April 2011, personal allowances jump up, NIC rates go up, corporation tax rates come down, the level at which 40% income tax starts comes down, the starting point for employer's NIC goes up... and those are only the main things we know about already.

The combination of effects will be complicated, and a number of tax plans will change. For example, we will have to work out again the best combination of salary, dividends and other ways of extracting profit from a company to balance all the different increases and decreases. Company owners who pay themselves a salary just above the NIC threshold will be able to increase that salary: the corporation tax saving will outweigh a very little extra income tax and NIC.

If you would like to discuss how the changing rates and allowances will affect you, we will be pleased to advise you. •

Buyer beware

'Caveat emptor' is a proverb so old it's in Latin. If you are buying a business, you will want to protect yourself by making the seller promise a long list of things in sale warranties, and agree to pay for another list of indemnities. Give a lawyer a word processor and the clauses multiply.

What happens, then, if the warranties promise that the accounts 'show a true and fair view' and afterwards the target discovers that it owed one of its suppliers £2.4m more than it thought it had? It seems cut and dried – the warranties should protect the purchaser. In a recent case, the court took a different view. There was no way that the vendor or the target could have known about the error, which arose because of problems with the accounting system of a supplier. Accounting standards don't require the inclusion of liabilities you can't possibly know about – so the accounts were 'true and fair' within the meaning of the warranty clause. The vendor was off the hook. •

Milk float

It's good when politicians of all sides agree. Alistair Darling, in his last Budget, announced that there would be no tax charge for five years on the benefit of providing an employee with a van if it was so green that it was not capable of emitting any carbon dioxide at all. Even better, the company will be entitled to a 100% first year allowance for the cost. George Osborne for the Coalition confirmed that this was one policy he would carry forward and implement.

Some cynics suggest that this is just an eye-catching green badge which will not cost much because there are so few zero-emission commercial vehicles available. Even so, a quick search of the internet shows that companies are moving into this market. Five years is a long time: by the end of the tax relief, it may have helped to make a difference to the environment.

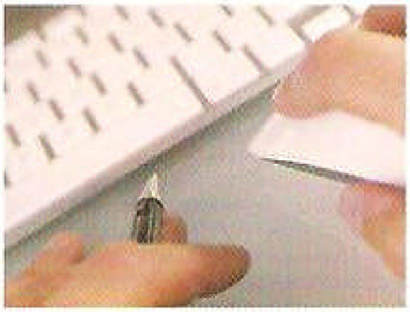
The main problem with these vehicles seems to be that they are so quiet that pedestrians do not get out of the way... •

Online returns

The Government is keen for its departments to use computers to deal with the public – after all, if you can just switch on the machine, you don't have to pay all those people to open the post and read it. So we are increasingly able, or required, to file our tax returns online. Most PAYE and VAT returns now have to go over the internet. From next April, joiner and leaver forms (P45 and P46) will also go online for small businesses. Income tax returns can still be sent in on paper, but the proportion is falling every year.

A big change in April 2011 will be the new requirement for all company accounts and tax returns to be submitted electronically – and in a specified format called iXBRL. This system will enable HMRC to analyse and compare information automatically, instead of having to extract it from paper documents and feed it into the computer.

Companies House will also accept



iXBRL accounts in due course, although they are not quite as ready as HMRC. Most small companies will still want to send different things to the two authorities – the taxman wants a profit and loss account, while the rules allow small companies to put abbreviated accounts with only a balance sheet on the public record.

Everyone needs to be ready for the new system in good time. If you want to know what these changes will mean to you and your business, we can advise you. •

Pension proposals

2006 seems a long time ago. Gordon Brown simplified the tax rules for pension schemes, bringing them all under one regime and announcing new limits on savings and contributions that would last for... well, five years. Pensions are such long-term items that it's optimistic to think one set of rules will last. This year and next, they are changing significantly – and we don't even know yet where they are going to end up.

Two years ago we were told that income tax relief for contributions would be restricted to the 20% basic rate for people earning over £180,000 in 2011/12, and people trying to get around that by bumping up their contributions in advance could be caught by an 'anti-forestalling charge'. So this year it's possible to put up to your total earnings (or £255,000, if lower) into a pension scheme, but you might only get 20% relief for it. The charge may affect people with incomes over £130,000 who pay in over £20,000.

The Coalition Government favours keeping 40% relief at least, but restricting the contributions to a much lower level – maybe £40,000. They haven't decided yet, but it seems likely that contributions will be capped after 5 April 2011. If you pay more yourself, you will get no tax relief at all; if your employer pays more for you, you will be taxed on the benefit.

There are problems for people in employer schemes – what if your contract specifies higher contributions as a percentage of your salary? What if you are a member of a final salary scheme, and the increase in your prospective benefits on a pay rise or promotion puts you way over the tax-free limit? These are problems that will affect many people next year.

It's hard to plan when we don't even know the final rules yet. It's wise to understand your pension rights and to take advice on how to maximise them: we will explain how your tax liabilities will be affected once the Chancellor has taken a decision. •

Interest on no tax

If you are late paying your tax, you generally have to pay interest. It's a pain, but you can see the logic. But what if you don't have to pay the tax? That makes no sense – except to the taxman and the courts.

A company sent some goods abroad and zero-rated them. When an HMRC officer checked the records, the company couldn't produce the required evidence that the goods had left the UK. That meant that output tax was due, which could be expensive. Never mind: the taxman said he would be reasonable, as long as the evidence could be found. Relief all round: documents were obtained from the customer and the transporters, and the VAT didn't have to be paid.

HMRC then said they wanted interest from when the sale had been made until the time the evidence was produced. They had been entitled to raise an assessment, and even if they didn't collect the money and repay it, interest ran as if they had. The Tribunal confirmed that this was the law, following a Court of Appeal decision a few years ago.

It's a stark reminder that you must make sure that the paperwork is in order if you are going to zero-rate a despatch or export. At least it's only interest – if you can't produce the evidence at all, you may have to pay the VAT as well. •

VAT rise: be prepared

Everyone running a VAT-registered business should be gearing up for another change in the standard rate on 4 January. At least we should be familiar with some of the problems now, because we had to do the same thing last 1 January.

Remember that there are rules about displaying prices in shops – it's generally not allowed to charge more at the till than it says on the shelf. Last year retailers were given 28 days to change their prices during which time they could adjust the VAT at checkout, but some would prefer not to aggravate their customers. Some will probably choose to put the prices up in advance rather than staying up all night on 3 January.

Remember also that a contract which doesn't mention VAT normally fixes the gross price: if you agree to do something for £11,750, then that's what you must charge. There is a different rule where a rate change intervenes. If you agree the price in December but deliver in January, the supplier will have to account for 20% to HMRC – and the supplier has the option of increasing the price charged to the customer to £12,000. To avoid arguments, it's worth being very clear about pricing around the date of the rate change.

These are just a couple of examples of issues that a rate change produces. We will be happy to go through some of the others with you and make sure that your business is ready. At least we have been told that the rate is supposed to stay at 20% for the rest of the Parliament – as long as the best laid plans don't go astray... •

NIC-free start-ups

One item of 'good news' in the June Budget was the NIC 'holiday' for businesses that commence between 22 June 2010 and 5 September 2013. For the first 10 employees taken on in the business's first year, no employer's NIC will be payable during their first year of employment (up to a maximum of £5,000 in relief per employee).

The idea of a boost of up to £50,000 in the start-up period of a business is attractive, but it's quite hard to get the maximum. The business has to be genuinely 'new' – you can't close down and reopen in order to save NIC. You have to be based outside London and the South East, because the move is supposed to 'rebalance the economy' in areas that need more private sector jobs. And it's the first 10 employees who qualify, not the 10 that you would choose because their NIC is the highest.

All right, it's complicated, but it's a gift horse and we shouldn't look it in the mouth. If you are thinking of setting up a new business outside the 'excluded region', we will be happy to advise you on how to make the most of this relief. •

On yer bike tax

In 1999 the last Government introduced a tax exemption to encourage people to cycle to work. If an employer lends a bike to an employee who uses it mainly for work – including, for this purpose, commuting – there is no taxable benefit. It's supposed to encourage people to leave the car at home and get healthy.

As usual, the taxman looks at these incentives after a few years and takes the cynical view that they are being twisted to save tax. First, employers are lending the bike to the employee for a short time and then selling it at a knock-down second-hand price. HMRC have recently revised their guidance on what will be accepted as the market value of a bike at the end of a loan arrangement – if it's sold too cheaply, a tax charge may arise.

Second, employers have not just loaned bikes for nothing. They have agreed 'salary sacrifices' with employees – at its simplest, the worker takes a salary reduction of £600 for a year and the employer loans a £600 bike for a year. If it's done properly, there are savings in income tax, NIC and VAT which the employer and employee can share between them. HMRC have recently announced that they believe that these schemes are not always set up properly. If they aren't, the tax advantages may be lost.

To add another uncertainty, the European Court of Justice has recently heard a case about a different sort of salary sacrifice scheme – for retail vouchers – and ruled that the employee was in reality paying for the benefit. If that was applied to the bike scheme, it would mean the employer would have to account for VAT on the salary forgone. HMRC have not taken that line up to now.

Salary sacrifice arrangements do save tax if they are done well. If you have one that you want to check for punctures, or you are interested in road-testing one, we can advise you. •

For your health?

Several cases have recently been heard by the European Court on what seems to be science fiction. Companies are extracting stem cells from the umbilical cords of newborn babies and storing them for future medical use – after all, the way that technology is advancing, stem cells may be able to cure anything in a few years' time. Any loving parent would want to make sure these wonderful things will be available if they are needed...

That appears to be the sales pitch. The ECJ had to consider whether the companies were providing VAT-exempt healthcare services. The judges decided that there wasn't a close enough link with any healthcare – the stem cells might be used in the future, but they might not. The child might never need the sort of treatment the cells would make possible; and science might not invent a use for the cells by the time the child needed them. In essence, the companies were selling hope – and hope is VATable. •

Gains fallout

The changes to CGT in the June Budget were not as bad as some people expected – the 28% rate is still well below the higher income tax rates at 40% and 50%, and the annual exemption was unchanged at £10,100. This year's calculations are complicated because gains realised up to 22 June will only be taxed at 18%, but the higher rate will apply after that to higher rate income tax payers.

Plenty of people realised gains before the Budget in order to take advantage of the lower rate, figuring that paying 18% on 31 January 2012 would be better than paying a higher rate later. The reverse applies to people who claimed to defer gains from an earlier year – when the charge is triggered after 22 June 2010, they may find they are paying 28% tax rather than the lower rates that would have applied if they'd never claimed the relief. This can happen with gains attached to Enterprise Investment Scheme shares or to loan stocks after a takeover, on replacement of business assets and in a number of other situations.

At least it appears that the rate of CGT will stay where it is for the remainder of this Parliament – George Osborne said so to a Parliamentary committee in July. That means we know where we stand and can make plans.

If you want to know what CGT you might pay on your assets, we will be happy to advise you. •

Not good enough

If you don't pay your VAT on time, you suffer default surcharge, which is expensive. A company recently appealed, arguing that the management had done all that a reasonable trader could, but they had been fooled by a newly-hired accountant who wasn't as competent as they had thought.

They had taken references, provided training and even arranged for a handover period while the retiring employee showed the new man the ropes. It was not enough, and VAT returns were not filed. The board only discovered what was (or wasn't) going on when HMRC served a winding-up notice on a group company.

The Tribunal ruled that the board had relied too much on someone who was not known to be reliable. They had noticed some failures – management accounts were late – and they should have looked for other problems as well. They had to pay the surcharge and misdeclaration penalties.

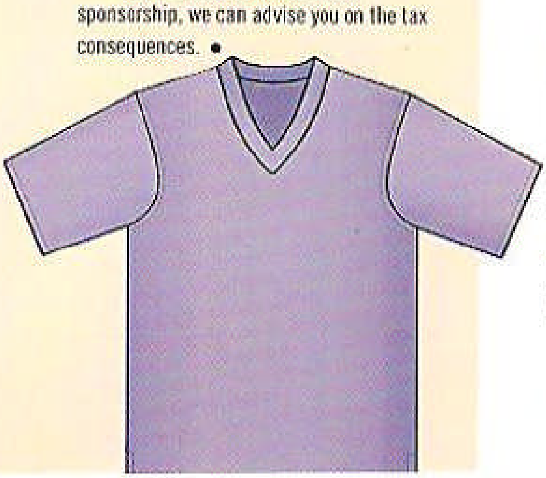
It's a reminder that the management has to take full responsibility for VAT failings, even if the day-to-day work is delegated to someone else. You need to keep an eye on them and follow up any signs of trouble. •

Name on the shirt

Sports sponsorship: a business expense, or a rich man's fancy? It depends, of course. The trouble is that a great deal of sponsorship starts with a love of the game or the club, and the business case – if any – has to stand on that. If the business case is strong enough, though, the company can deduct the expense for tax.

HMRC recently argued about £1.1m paid by a fishing company to support a local rugby club. The advertising benefits would have cost about £10,000 at the club's published rates. Not surprisingly, the Tribunal ruled that the payments were not 'wholly and exclusively for the trade' – they might promote the business, but they were much more to do with the controlling director's love of his club.

If you are interested in sports sponsorship, we can advise you on the tax consequences. •



Do not go gentle

The statutory default retirement age will be abolished on 1 October 2011. This means that employers will no longer automatically be able to dismiss 65-year old employees on the grounds that they should retire: age discrimination legislation will apply.

A recent Court of Appeal case examined a dispute between partners in a law firm. The partnership deed provided for retirement at 65, and one of the partners objected – he wanted to carry on. Employment law doesn't apply to partners, but the judges ruled that the statutory age provided a reasonable benchmark to use. More important, though, were the firm's reasons for the policy – to encourage retention of junior employees by providing opportunities for promotion, to help with business planning, and to improve employee relations by having a non-confrontational reason to move people on. When the statutory limit has gone, this type of justification will become the only way to back up a compulsory retirement decision.

It will be important for anyone who currently retires employees at a set age to think carefully about their policy as October 2011 approaches. •

Untangled web

A company with 'small profits' – up to £300,000 a year – pays a lower rate of corporation tax. At the moment it's 21%. The rate then rises to 29.75% until profits reach £1.5m, when the 28% rate applies. All three rates are due to drop by 1% on 1 April 2011.

If two companies are 'associated' with each other, these limits are divided between them. That means that highest rate of CT will be paid if either makes more than £150,000. If there are more associates, the limits get cut again and again.

For years, this has applied to companies owned by the same married couple (or by civil partners). Other close relations could avoid association of their companies if there was no 'commercial interdependence' between the businesses, but husband and wife could run completely different trades and still suffer the disadvantage.

From 1 April 2011 the rules are changing. Companies will only be associated for determining their CT rate if they are closely linked by financial, economic or organisational factors. That may still catch many of those who are associated under the current rules, but it's worth looking at.

If you and your close relations are involved in running more than one company, we will be happy to advise you on whether you can pay less corporation tax from next April. •

In black and white

It's important to file accounts on time to avoid Companies House penalties. It's particularly annoying if a set of accounts is submitted at the last minute but rejected for a minor mistake – there's no grace period for resubmitting. One of the most basic instructions is that they want everything in black ink on matt white paper – they are keen that their photocopying and scanning needs to produce legible results. So if you use glossy paper or sign the accounts in blue, you may find the accounts coming back to you. •

Car conundrums

If you have a company car, you pay income tax and your employer pays NIC on the taxable benefit. The rule originally only applied to so-called 'higher paid employees' – the threshold of £8,500 was brought in when that was a reasonable salary. Now it's less than the minimum wage.

In a recent case, a husband-and-wife company provided the wife with a £32,000 BMW and nothing else. She worked as the company secretary, and used the car for deliveries as well as private motoring. HMRC accepted that her overall level of pay – just the car, on which the taxable benefit would be less than £8,500 – was not excessive, and she had the car in her own right. Even so, they were entitled to charge Class 1A NIC on the company because it was not 'normal commercial practice' for such a car to be given to a secretary.

Two other cases were about 'pool cars'. If a car is only used for business motoring, is not kept overnight at an employee's home and is not habitually used by a single employee, no-one is taxed on the benefit of providing it. HMRC were not convinced in either case that the conditions were met, but the Tribunal accepted one of the two appeals. Even though the two vehicles were unusually expensive for pool cars, and even though there were only six employees, the company had done enough to show that it met the conditions.

For most people, the company car rules work in the normal way. If you think your circumstances might be different – particularly if you think you could escape the charge by using a pool car arrangement – we will be happy to go over the conditions with you. •