

CLIENT NEWSLETTER – SPRING 2010

“ACTIVE ACCOUNTING AND TAX”

Tel: 01480 468931
Fax: 01480 469515
e-Mail: paul@paulahill.co.uk
Web: www.paulahill.co.uk

INTRODUCTION

Alistair Darling gave his third Budget on 24 March 2010. As usual, I will cover the main points in the Budget in this Newsletter and also comment on other matters of current interest. However, given the proximity of the general election, it is at least possible that some of the measures announced by the Chancellor in the Budget will not be able to be included in a truncated Finance Act, which will need to be passed before Parliament is dissolved. We will obviously keep a very close eye on any measures that are left out of the Finance Act and, if necessary, I will prepare a further client alert.

From my perspective there was a little less “smoke and mirrors” than had perhaps been expected, certainly by the press – although the Chancellor’s speech was certainly a pre-election one and extremely upbeat. One “rabbit out of the hat”, I must admit I and I suspect most other professional advisers had not been expecting was an increase in the Entrepreneur’s relief for Capital Gains Tax and a specific announcement of no change in the rate of that tax – see Section **Error! Reference source not found.** below.

This is also an opportune time to comment on further changes to online filing requirements – it now becoming compulsory for many businesses to file VAT returns and PAYE year-end returns online – and from 2011 PAYE “in-year” forms as well. In addition, I comment on the new powers HMRC have taken for themselves over the last few years.

THIS NEWSLETTER COVERS THE FOLLOWING TOPICS:

- **2010/11 Income tax rates and allowances for income of up to £100,000.**
- **Tax increases and withdrawal of allowances and reliefs over £100,000 income.**
- **National insurance contributions in 2010/11 – and beyond!**
- **Corporation tax rates for the year commencing 1 April 2010.**
- **Capital allowances including the “Annual Investment Allowance”.**
- **Other business support measures – including “time to pay” and rates relief.**
- **VAT changes – back to 17½% and a few other changes from the “small print”.**
- **Capital gains tax - two surprise announcements!**
- **Inheritance tax changes and why a will trust for husbands and wives remains good planning.**
- **Stamp duty land tax changes.**
- **Other matters including online filing, national minimum wage, construction industry, HMRC penalties and anti-avoidance measures.**

As I always say, it is only possible for me to comment on some of the matters contained in the Budget and on other current issues. If you are interested or concerned about any other matters that I have not covered in the Newsletter, of course please do not hesitate to get in touch with me to discuss it. To find the information you need, please look under the following headings:

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| 1. 2010/11 Income tax rates for total income of up to £100,000 and PAYE code number problems | 7. Other business support measures – including “time to pay” and rates relief. |
| 2. Tax increases and withdrawal of allowances and reliefs for incomes over £100,000 | 8. VAT matters |
| 3. Can I “avoid” the additional tax in Error! Reference source not found. above? | 9. Capital gains tax - two surprise announcements |
| 4. NICs in 2010/11 and beyond! | 10. Inheritance tax matters and will trusts |
| 5. Corporation tax rates for 2010/11 | 11. Stamp duty land tax changes |
| 6. Capital allowances including the “Annual Investment Allowance” | 12. Other matters incl. online filing, national minimum wage, construction industry, HMRC penalties, anti-avoidance and principles based legislation |

1 2010/11 INCOME TAX RATES FOR TOTAL INCOME OF UP TO £100,000.

1.1 As previously announced at the pre-Budget report in December 2009, for taxpayers with income of up to £100,000, the value of income tax personal allowances, rates and bands for 2010/11 will be frozen at their 2009/10 levels. The personal allowance will therefore remain at £6,475 and the 20% basic rate band at £37,400, meaning that the 40% "higher" rate is reached at total income of £43,875.

1.2 ***PAH Comment: With inflation running at about 3%, this represents quite a considerable "fiscal drag" this year and the opposition parties have not been slow at pointing this out.***

1.3 PAYE code numbers

1.3.1 In the last few months, a considerable number of clients have been in touch with us about their PAYE code number for 2010/11 and many of these have been in error. HMRC introduced a new computer system for PAYE in the Autumn of 2009 and the issue of code numbers for 2010/11 was the first major exercise undertaken by this new system. This upgrade was the first major change to the PAYE computer system since it was first set up in 1985 and there have been a lot of teething troubles.

1.3.2 In making the change HMRC have undertaken the not inconsiderable challenge of moving the basic "unit" on which the system is based from employers/pension providers – with subsidiary records for each employee/pensioner to employees/pensioners, with cross-referencing to a database of employers/pension providers. This recognises the considerable changes in employment demographics over the years, with many people now having more than one employment in a tax year. The new system is also able to cope more easily with taxpayers with more than one pension and with taxpayers with both pension(s) and employment income, both also a much more common occurrence these days and once the system has been fully updated, should result in far less problems.

1.3.3 However, it is fair to say the "data cleansing" exercise undertaken before the system went live was less than satisfactory and the decision to go live was taken at an earlier date than was probably desirable. I think in part this was due to the system already being over a year late and no doubt considerably over budget as well – although I don't know that for certain. What I do know for certain is that the final data cleansing has been up to individual taxpayers and their agents to sort out.

1.3.4 HMRC have advised that the high level of error in the original 2010/11 coding notices that were sent out in January 2010, has meant that although change requests have been logged on their system, the issue of corrected coding notices to individual employees and pensioners is being delayed and sending revised notices to employers and pension companies is taking longer still. Because of this, it may well be the case, particularly if HMRC have been notified of an error since the beginning of March 2010, that they may not be able to process the amendment and issue a revised coding notice to both the employee/pensioner AND the employer/pension provider before the cut off date for an April 2010 payment.

1.3.5 Whilst, they apologise for this, HMRC are insistent that employers and pension providers MUST follow the rules and therefore MUST NOT action a coding change until they receive formal notification of the change directly. In particular, employers and pension providers have been advised they may not action a change based on a revised coding notice issued to an employee or pensioner in advance of one sent to them; **PAH Comment: although it is hard to see how they would ever find this out!**

1.3.6 HMRC expect that the position will improve over the next month or so and corrections to remove coding errors will be able to be made more promptly. They also point out that under the cumulative way in which PAYE operates, any increase in a code will automatically be backdated to the beginning of the tax year, as soon as it is applied.

1.3.7 Where a code is decreased on correction, the same position arises in that the change is cumulative and there is the possibility an individual may suffer a large deduction in one month to backdate the change to the beginning of the tax year. However, in such circumstances HMRC often automatically, and if they don't, we can request them to on your behalf, apply a special code such that PAYE is deducted on a "Month 1" basis, this limiting the change to one month only. In such circumstances, any under-deduction is carried forward to be dealt with

either on your self-assessment return for the year ending 5 April 2011, or if you are not in self-assessment, when your coding notice for 2011/12 is prepared – in about January 2011.

- 1.3.8 ***PAH comment: I must ask all clients to bear with HMRC on PAYE codes, as the new system WILL be much better when it is fully updated, but I appreciate how frustrating it is at the moment.***
- 1.3.9 Coding notices remain an important tax document and as such please can I remind you to send a copy of all coding notices you receive to us – these are dealt with by Claire Jackson in St Ives, as soon as you receive them, so we can check them and make sure the correct or at least a best estimate of the correct amount of tax is being deducted.
- 1.3.10 ***PAH Planning point: As I have mentioned several times in newsletters over the past few years, when it comes to issuing PAYE codes, HMRC are also very "good" at trying to collect tax due on income from other sources through the PAYE system – for example additional tax due on investment income, if you are a 40% taxpayer, or tax due on land and property income; they say they do this to be "helpful" to their "customers" as it simplifies your tax affairs. HOWEVER!, by attempting to collect such tax under PAYE, they are able to collect a proportion of the tax due very nearly TWO YEARS earlier than you would otherwise have to pay it under the self-assessment system. I do not consider this "helpful" and it is our normal practice to request all such adjustments be removed from code numbers; HMRC are obliged to remove this sort of adjustment when we request it. Once we have requested that an adjustment like this be removed, the HMRC system is supposed to keep a note that they should not try to "code out" "other" income in a future year. However, with the new system, this "flag" seems to have been lost and is having to be reinstated. In view of this it will be important for 2011/12 code numbers, due to be issued in January 2011, also to be checked very carefully, to make sure the new system is working properly in this regard.***

2 TAX INCREASES AND WITHDRAWAL OF ALLOWANCES AND RELIEFS FOR INCOMES OVER £100,000

- 2.1 Whilst it is the 50% "additional" tax rate on income over £150,000 that has tended to hog the headlines about the tax increases for the higher paid from 2010/11, the threshold at which these measures begin to bite is really £100,000 in total income from all sources and it is also important to consider pension contributions, which can now have a considerable impact on your tax position.
- 2.2 Where an individual's income exceeds £100,000, the personal allowance will be withdrawn at a rate of £1 for every £2, this meaning there is no personal allowance available for a taxpayer with income over £112,950 (£100,000 plus 2 X £6,475). Where income exceeds £112,950 extra tax of £2,590 will be payable (£6,475 X 40%) and this gives rise to a marginal rate of tax of 60% in the band from £100,000 to £112,950.
- 2.3 The withdrawal of the personal allowance where income is over £100,000 applies regardless of age, but of course a pensioner with income of £100,000 would already have had their personal allowance reduced from the "enhanced" levels only fully available to pensioners with income of under £22,900, which figure is also unchanged for 2010/11, to the "standard" level of £6,475.
- 2.4 Your marginal rate of tax is the additional tax payable if your income increases by £1. The 60% rate arises on the next £1 in the range £100,000 to £112,950, based on the higher rate of 40%, plus a further 40% on 50p = 20p = 20% = 60% in total on the next £1; 50p being the reduction in your personal allowance from £1 extra income.
- 2.5 Those of you who have companies where the profits exceed the "small companies rate" limits, will be well aware of the need, if possible, to avoid high marginal rates of tax and to try to adjust taxable profits/income accordingly, but this is the first time for a considerable period we have had such a high marginal rate of income tax, or a situation where the marginal rate is on a roller-coaster!

2.6 The following table sets out marginal rates of income tax for 2010/11.

Income range	Marginal rate of tax	Income range	Marginal rate of tax
£0 - £6,475	0%	£100,000 - £112,950	60%
£6,475 - £43,875	20%	£112,950 - £150,000	40%
£43,875 - £100,000	40%	Over £150,000	50%

2.7 It is my understanding that the loss of personal allowance is based on gross income before any deductions and that, in particular, any pension contributions paid by an employee, including those paid under a salary sacrifice arrangement, will not affect whether the allowance is withdrawn.

2.8 ***PAH Planning points: I comment on possible strategies for avoiding the effects of these changes, particularly if you need an unusually high level of drawings in one year compared to others, in section 3 below.***

2.9 Dividends

2.9.1 The new additional 50% rate band and the withdrawal of the personal allowance, both have an effect on the extra tax payable where dividends, which continue to be treated as the "top slice" of an individual's income, fall into that band.

2.9.2 Before taxation is considered, a net dividend paid has to be multiplied by 10/9 to get to the "gross" figure for tax purposes; the difference between these two figures being the "tax credit" on the dividend – 10% of the gross figure.

2.9.3 Where gross dividends, when added as the top slice of an individual's income mean that income is less than the top of the basic rate band – currently £43,875 as mentioned in paragraph 1.1 and the table in paragraph 2.6 above, then no further tax is payable.

2.9.4 Should dividends fall into the 40% "higher" rate band, then tax is payable at 32.5% of the gross amount of the dividend, but the "Tax Credit" of 10% attached to the dividend is then taken into account. In simpler terms, this means that tax at an additional 25% of the net dividend received by you is payable.

2.9.5 Where dividends fall into the additional rate band of income of above £150,000, this extra tax on the net dividend is increased to 36.1% and if dividends fall into the range of total income of £100,000 to £112,950, where as noted in paragraphs 2.4 and 2.6 above the marginal rate is 60% – this rate will be a swingeing 44.4% of the net dividend.

2.10 Pension contributions

2.10.1 I have already mentioned that pension contributions will not be taken into account in determining whether gross income is over £100,000 for the purposes of withdrawal of the personal allowance – see paragraph 2.7 above.

2.10.2 However, the Chancellor has gone a lot further than that and from 2010/11 there will be considerable restrictions on pension contributions tax relief for high earners, whether the contributions are made by the individual concerned, or by their employers. Having said that, tax relief continues as previously for contributions made by individuals where income before pension contributions is up to £130,000 and possibly up to £150,000. Relief will then progressively be withdrawn until for those with income over £180,000, relief for pension contributions will be restricted to 20%.

2.10.3 ***PAH Comment: The availability of 40% tax relief on pension contributions has often been considered for reform, but in recent years the Government has chosen to restrict the amount of tax relief on pension contributions for high earners by establishing a maximum value for the "pension pot" attracting tax benefits, an individual may hold. The changes announced by the Chancellor, initially in the 2009 Budget and now built on, represent a fundamental change in this approach and are considered by many tax professionals to arise directly from the outcry over Sir Fred Goodwin's (Ex RBS!) pension arrangements.***

2.10.4 If an individual has total income, from all sources, of over £130,000, tax relief on pension contributions may be restricted, but if income is in the range £130,000 to £150,000, this will

only apply if the taxpayer's income plus pension contributions made by an employer exceed £150,000. This is essentially an anti-avoidance measure that has been brought in as an afterthought, as after the Chancellor first talked about the restriction of pension contribution relief for high earners in 2009, it was widely talked about that the rules could simply be got around by increasing employer contributions for affected persons.

- 2.10.5 ***PAH Comment: This will require quite a significant change to the information needing to be included on 2011 self-assessment tax returns, with employer pension contributions requiring to be included on an affected employee's personal return.***
- 2.10.6 Where required, the claw back of relief will be achieved by making a "special annual allowance charge" on the individual taxpayer to collect whatever the restriction in the relief may be. As noted in paragraph 2.10.4 above, this "special annual allowance charge" will be tapered for incomes of between £150,000 and £180,000 and as the basis of calculation in this range would take about two pages of Newsletter to set out, I am not including this here – it will however be less than the charge for incomes over £180,000 as set out in paragraph 2.10.7. If you want more details of how the special annual allowance charge is calculated in this range, please give Linda Harrison a call in St Ives.
- 2.10.7 For incomes of over £180,000, the "special annual allowance charge" will be 30% of the pension contributions paid in respect of the individual, including employer contributions.
- 2.11 ***PAH planning point: If you anticipate your income level in 2010/11 may cause you to be affected by the matters set out in this section and would like us to comment in more detail on your individual position, so you can understand the effect on your take home pay, please do not hesitate to contact Kim, me or Linda Harrison for further advice.***

3 CAN I "AVOID" THE ADDITIONAL TAX IN SECTION 2 ABOVE?

- 3.1 ***PAH Comment: It is unclear how long the 50% rate, withdrawal of personal allowances and pension contributions restrictions are likely to be with us. It is also possible, even if the 50% rate were removed in the future, that the other restrictions will remain. When advising on tax matters, the only "safe" course is to advise on the law as it currently stands, but dependent on a your approach to "risk", there are some ways in which money can be withdrawn from a business that will avoid an immediate charge under the new rules set out in section 2 above.***
- 3.2 These strategies are applicable to companies, but not really to sole-traders or partnerships, owing to the entirely different taxable basis of non-corporate entities. It still remains the case that there can be significant benefits from incorporating a sole-trader or partnership making profits of more than, say, c. £30,000 per annum on a regular basis and if you require any further advice on this point, please do not hesitate to get in touch.
- 3.3 Planning for a "big" withdrawal from your business in a few years time
- 3.3.1 Firstly, and I would stress I consider this to be "normal" tax planning, it is important to look as far ahead as you can in your business performance and personal remuneration requirements; by doing so, you can make sure you don't end up paying extra tax "by accident".
- 3.3.2 In the last couple of years or so, following HMRC confirming they did not intend to bring forward new rules on "income splitting", which had initially been proposed following the Arctic Systems case - if you are not familiar with this, please ask, generally, our advice has been that having split income between family members as far as sensible, you should only draw out of your business what you "need" in personal remuneration, to reduce exposure to 40% tax.
- 3.3.3 However, if this means that a company now has significant undrawn profits held within it and, in the next five years or so you think you may want to make a significant withdrawal in one year – perhaps to buy a new property or similar, then advance planning may bring significant benefits.
- 3.3.4 Where profits are available and we are advising on all aspects of your and your business's affairs, we always seek to make sure you use up your basic rate band each year. If the

amount of drawings actually taken by a company's directors/shareholders is less than each of their basic rate limits, we will normally suggest a further dividend be voted at the year-end to bring overall drawings up to this level. An additional dividend of this sort does not incur any additional tax charges for either you or the company and does not have to be drawn from the company in cash at that time. Instead, it forms a loan from you to the company and can then be withdrawn in the future, WITHOUT ANY FURTHER TAX CONSEQUENCES AT THAT POINT. However, whilst there will be some extra tax to pay at the time, building up a loan account due back to you, by voting additional dividends up to an income level of £100,000 for a few years, could result in your being able to avoid section 2 charges, when a big withdrawal of over £100,000 is made in one year.

3.3.5 **PAH Planning point: Accordingly, if you know you want to make a "big" withdrawal in a couple of years time, it would now almost certainly pay to spread that withdrawal over several years, in each year making sure no individual's total income reached £100,000, so that when the time did come for the "big" withdrawal to be made, it is part loan repayment and part income – this not triggering any of the additional charges set out in section 2.**

3.3.6 You will have to pay some additional 40% tax – usually in the form of a further payment of 25% on net dividends (see paragraph 2.9.4 above), based on your self-assessment tax return for the relevant year in which the income is declared and this will be paid earlier than tax on the "big" withdrawal would otherwise be paid, but loss of personal allowance, the special annual allowance charge on pension contributions and 50% tax should be able to be avoided.

3.4 Borrowing money from your company instead of taking income

3.4.1 When the section 2 changes were first announced, there was considerable discussion that an incoming Conservative Government would reverse them at the earliest opportunity. However, as time has moved on I now think, even if the Conservatives do win the election, their room for manoeuvre will be very limited and, as they indicated on 29 March 2010, directed at reducing the NIC increases previously planned for 2011/12, plus some Corporation tax changes that have also already been trailed as possibilities

3.4.2 **PAH Comment: An increase in VAT after the election would leave some more scope, but nobody is talking about that at present!**

3.4.3 **PAH Planning point: If you are willing to take a risk on the section 2 changes only lasting for a few tax years, then taking a loan from a company instead of income is a possibility. A loan does not count as income at the time it is drawn, but you either have to pay interest, or tax based on the fact you do not pay interest. From 6 April 2010 the HMRC "official" rate of interest for such loans is 4% so for a 40% taxpayer the charge on a loan is $4\% \times 40\% = 1.6\%$ per annum.**

3.4.4 **On the basis 40% returns as the top rate of tax in a future tax year, assuming the company has sufficient distributable reserves at that time, you would repay the loan by payment of a bonus or dividend, or it could be written off by the company, whichever is most appropriate for your circumstances and pay the relevant tax due at that time – it would therefore be prudent to put this amount aside so it is available when the tax falls due; we would advise on which is the best approach. The charge you will suffer for postponing this tax payment until the rate is lower is the annual charge on the interest.**

3.4.5 There has always been one significant cashflow drawback to this strategy where the loan is made to a shareholder in a small company controlled by five or fewer person – this is known as a "close" company in the tax jargon. In these circumstances, a deposit of 25% of the loan increase in the company's accounting year has to be paid to HMRC on the normal date of payment of Corporation tax for that period. This deposit is refunded on the due date for payment of Corporation tax for the company's accounting year in which the loan arrangement ceases. In these circumstances, the loss of interest on this money – HMRC do not pay interest on such deposits, also needs to be taken into account.

3.4.6 The HMRC interest rate for "beneficial loans" is commercially based and likely to increase if bank base rates increase – in recent years it has been 4.75% and 6.25% (giving effective tax charges of 1.9% and 2.5 % in those tax years).

3.4.7 The downside risk of this strategy is of course that 40% does not return as the top rate.

3.5 More "aggressive" strategies

3.5.1 There are some more "aggressive" tax strategies promoted by specialist tax avoidance firms available in the market place and we are generally aware of the range of schemes available. If you are interested in considering a more aggressive tax avoidance scheme, please contact me in St Ives to discuss the position in more detail.

4 **NATIONAL INSURANCE CONTRIBUTIONS IN 2010/11 – AND BEYOND!**

4.1 The only significant change to National Insurance Contributions is with regard to the very lowest "threshold" – the lower earnings limit, which is raised from £95 to £97 per week. This is the figure at which an employee can become eligible for certain Social Security benefits, but is of no relevance for any other purpose, including the payment of contributions.

4.2 As far as the payment of contributions are concerned, these commence at weekly earnings of £110 per week, the same as in 2009/10 – this being the equivalent of £475 per month.

4.3 Computerised payroll systems

4.3.1 Although there are no changes to the rates and thresholds on which most PAYE/NIC deductions are based, please do not forget to update your payroll system for 2010/11. The change to the NIC lower earnings limit and other reporting changes for 2010/11 mean that it is not possible to roll over a 2009/10 system to work in 2010/11, even if you have no employees affected by the section 2 changes.

4.4 NICs in 2011/12

4.4.1 All NIC rates are currently due to increase by a full 1% in 2011/12, this includes the additional rate, currently 1% for income over the higher threshold, which is being doubled to 2%. This is probably the one advance announcement most likely to change, as business organisations are united in opposing the increase in Employer NICs, which they describe as a tax on jobs, to 13.8%; it will be very interesting to see what happens to this proposal after the election.

4.4.2 As this newsletter is going to print, the Conservatives have suggested they would remove the 1% increase on the employee's "main" rate and also the increase in the employer's rate, but retain the increase from 1% to 2% in the additional rate for employees earning over £43,875 per annum.

5 **CORPORATION TAX FOR THE YEAR COMMENCING 1 APRIL 2010**

5.1 The "small companies" rate of Corporation tax will remain at 21% for 2010/11, the proposed increase to 22% having been deferred for a further year. However, unless there is a further postponement or change of direction by a new Government, the rate is currently planned to increase to 22% from 1 April 2011.

5.2 Where an accounting period for a company covers more than one "fiscal year" – the name for each year commencing 1 April for Corporation tax purposes, then profits for the company's accounting year in total are time apportioned and the appropriate rate of Corporation tax applied to each portion.

5.3 The "full" rate of Corporation tax for profits in excess of £300,000 (divided by the number of associated companies if required) remains at 28% and therefore the marginal rate on profits over £300,000, but less than £1.5 million, or the appropriate lesser figures taking associated companies into account, will remain at 29.75%.

5.4 In one of a daily increasing number of pre-election announcements, the Conservatives have suggested that they would cut the small companies rate of Corporation tax to 20% and the main rate to 25%, but at the expense of abolishing the Annual Investment Allowance – see under Capital Allowances in section 6 below.

- 5.5 As with the income tax changes set out in section 2 above, given the election will not now be until May 2010 at the very earliest, any changes are unlikely to be brought in until 2011.

6 CAPITAL ALLOWANCES INCLUDING THE "ANNUAL INVESTMENT ALLOWANCE"

- 6.1 In one of two surprise announcements, the other one being in respect of capital gains – see section 9 below, the Chancellor doubled the value of the Annual Investment Allowance (AIA) to £100,000 from April 2010.
- 6.2 Under AIA, expenditure on fixed assets qualifying for plant and machinery allowances up to this level will be eligible for 100% tax relief in the year of purchase. At the same time, the 40% first year allowance on expenditure in excess of the AIA limit is withdrawn.
- 6.3 Where an accounting period overlaps the date of change, the new and old rates of AIA will be time apportioned to get to the allowable figure for a particular business.
- 6.4 Plant and machinery expenditure not qualifying for AIA will remain eligible for 20% writing down allowance (WDA).
- 6.5 ***PAH planning point: The planning point here is not what to do now, but what to do before 31 March 2011 if the Conservatives win the election. As noted in paragraph 5.4 above, they may well reduce AIA in exchange for a reduction in the rates of Corporation tax. In that case, planning plant and machinery expenditure to make sure it takes place before rather than after 31 March 2011 would be sensible.***
- 6.6 Please also remember that with the introduction of AIA, a new "pool" of expenditure for capital allowances that only attracts 10% writing down allowance was created and the definition of plant and machinery restricted so that more expenditure has to be placed in this lower WDA pool.
- 6.7 There is also a slightly obscure new rule about the use of AIA in a property business, by which we can only assume they mean a furnished holiday letting (FHL). This would appear to be an attempt to reduce losses carried forward and we will be considering this on an individual basis as we prepare client's 2010 self-assessment tax returns including the last year in which FHL can be treated as trade; we will advise further at that time.
- 6.8 ***PAH Planning point: If you need any advice on the allowances you may be able to claim on specific capital expenditure, please do not hesitate to contact Linda Harrison in St Ives.***

7 OTHER BUSINESS SUPPORT MEASURES – INCLUDING "TIME TO PAY" AND RATES RELIEF

7.1 Time to pay arrangements – the Business Payments Support Service

- 7.1.1 This originally temporary arrangement is to be extended for the term of the next parliament – a proposal I cannot see being controversial in any way and therefore I expect it to be included in the Finance Bill.

7.1.2 To quote from HMRC's publicity:

"If you are worried about being able to meet tax, National Insurance, VAT or other payments owed to HM Revenue & Customs, or you anticipate that payments becoming due will cause you problems, you can call our business payment support line on **0845 302 1435**. The line will be open Monday to Friday 8 am to 8 pm, Saturday and Sunday 8 am to 4 pm.

This support line is intended for new enquiries only, if you have already been contacted about an overdue payment or if you already have a payment arrangement with HMRC please call the

original office that contacted you, who will be ready to discuss payment arrangement options and explain how to avoid legal action being taken”.

- 7.1.3 As noted in my September 2009 newsletter, the major change to the HMRC penalty regime in 2010/11 is "in-year" penalties for late payments of PAYE and NIC, although it is perhaps more uncertain than when I wrote in that newsletter as to "how" this is going to work. Despite this change, where a time to pay arrangement is in place, although interest will be charged, there will be no penalties or surcharges.
- 7.1.4 ***PAH Planning point: It is therefore important that if at any time from now on, you are unable to make the full amount of any tax payment, including a monthly payment of PAYE/NICs, that you contact the Business Payments Support Service IN ADVANCE!***
- 7.1.5 In the original publicity, when calling the service, you were asked to have to hand your tax reference number, details of the tax that you are having or will have trouble paying and basic details of your business's income and outgoings. In practice, certainly immediately after the original launch of the service back in November 2008, no questions were ever asked about your business's economic position, but more recently we have found these questions are being asked, particularly where a second or further postponement is being requested. Indeed, in cases where a very large amounts is being asked to be postponed (although we understand this is currently only in respect of amounts of more than £1 million), the business is now required to obtain a report from a qualified insolvency practitioner that they are a going concern and will be able to make the payments they are proposing.
- 7.1.6 ***PAH Comment: I think these additional questions are being asked because HMRC has become aware, as I commented in my September 2009 newsletter, that there is some evidence of businesses using the service to replace bank overdrafts, at probably a lower interest rate. A specific question that has been asked on one occasion recently was just that, was the business using its full bank overdraft facility and therefore the business payments support service was really a lender of last resort – as had been the original intention.***
- 7.1.7 ***PAH Planning point: Please make sure you have thought about these issues and your cash flow requirements over the period you are asking for postponement, before you call the service. If you need any assistance in drawing up cash flow projections, please do not hesitate to get in touch.***
- 7.1.8 ***PAH further comment: I still don't think the Treasury, or HMRC for that matter, "gets" the difficult relationship that many small businesses have with their bankers at present. In addition, I don't think they have realised that having got used to being able to spread tax payments, small businesses will find it difficult to save up for the next payment when still paying off the last and that this will continue for some time to come. I would value evidence from clients as to how the service is operating practically, as this is a key tenet of Government policy and if - I stress I hope this is not the case, it becomes more difficult to access the service as time goes on, it is important tax agents get that message back to HMRC and the Treasury at a senior level, via the contacts the professional bodies have, as soon as possible.***
- 7.2 Business rates
- 7.2.1 To quote the "red book" – the full detailed budget statement :
- "To provide help with the fixed costs of starting and running a small business, the Government will fund a temporary increase in the level of small business rate relief, so that eligible small businesses occupying properties with rateable values of up to £6,000 will pay no business rates for one year from October. In addition, small businesses benefiting from the rate relief taper (rateable values up to £12,000) will receive significant reductions."
- 7.2.2 ***PAH Comment: I assume this measure has only recently been thought of and the delay to October is a practical one to enable information to be sent out – rates bills for 2010/11, having already been sent to businesses.***

7.3 Other measures

- 7.3.1 The Chancellor also talked about increasing bank lending to business, particularly from the publicly owned banks – RBS (including NatWest) and Lloyds, but whilst a fair proportion of this was to be allocated to small and medium sized businesses (SMEs), the definition of what is an SME includes businesses of up to £25 million turnover and 250 employees.
- 7.3.2 ***PAH Comment: Whilst it might not be used internationally, I feel it would be very useful for a new class of business – perhaps called micro businesses, say with turnover under £500,000 or with less than ten employees, to be identified as a class to which specific support might be given. It remains to be seen how much of the lending referred to above will be directed to these businesses.***
- 7.3.3 There is also to be a banking adjudicator to intervene if an SME feels bank lending has been unfairly turned down, but I am concerned that the time and bureaucracy I believe is likely to attach to this process will mean it will not be an effective remedy for "micro" businesses.
- 7.3.4 As always, and my apologies for sounding slightly cynical, but this point does come up every year – HMRC will seek to reduce burdens on business of complying with its requirements. Having said that, it is fair to say, they are making some strides to make sure information needs only to be given to HMRC once and after it has been given it can be shared amongst all HMRC departments that may have to use it – examples are changes of address and a simplification of the multiple registration processes that currently face new businesses.

8 VAT MATTERS

8.1 Standard rate

- 8.1.1 Please remember the standard rate of VAT returned to 17½ % from 1 January 2010. If you use a spreadsheet and/or formulae to work out the output VAT on VAT inclusive process, for sales from 1 January 2010, the fraction to use is 7/47^{ths}.
- 8.1.2 If by any chance you have already completed a VAT return inaccurately, based on the old fraction of 3/23^{ths}, please recalculate the figures and include the additional VAT on your next return, even if your return has not been picked up in one of the statistical checks that HMRC do – these being part of the reason why net of VAT sales and purchases figures are required in boxes 6 and 7 on the return.
- 8.1.3 ***PAH warning: If you have calculated VAT wrongly and do not correct it, if HMRC find out about this, before you tell them, correcting the figures on the next return being sufficient "telling" in this context, as well as demanding payment of the tax plus interest from the original due date, we fear they could seek a penalty of up to 60% of the tax due, on the basis this was a deliberate misstatement of tax.***

There has been some talk on tax websites that with the general publicity attaching to the change back to 17½ %, a failure to deal with this would always initially be determined by HMRC to be "deliberate" and it would be up to you to defend the position and claim it was a genuine mistake or a lack of reasonable care – this latter claim still leaving you open to a possible penalty of 30% of the tax due.

- 8.1.4 If you have any queries on change back to a standard rate of 17½ %, please do not hesitate to contact us.

8.2 Turnover threshold

- 8.2.1 The turnover threshold is increased to £70,000 with effect from 1 April 2010; this remains the highest threshold in the EU – by far!
- 8.2.2 If you are reviewing turnover on a monthly basis, you are required to register if your rolling 12 months turnover to the end of March is over £68,000, but from April 2010, this figure is increased to £70,000.

8.2.3 The deregistration threshold is similarly increased and stands at £68,000 from 1 April 2010.

8.3 Private use scales

8.3.1 The scale charges for private use of cars where private petrol is provided have been increased. I am only aware of two clients who now use this form of adjustment and they have already been sent details. However, if you would like a copy of the new figures, please contact Lesley Knell in St Ives and she will be pleased to send one to you.

8.4 EC Sales lists for services

8.4.1 If required, these need to be first completed for the calendar quarter to 31 March 2010 and may require to be submitted by 14 April 2010 to avoid penalties, if you need help, please ask soon!

8.5 Other VAT matters

8.5.1 There are a number of technical matters, but the only one of general interest is that from an unspecified date in the future, under an EU ruling, certain Royal Mail services, in particular "Parcelforce" services, will be subject to VAT.

9 CAPITAL GAINS TAX - TWO BIG SURPRISE ANNOUNCEMENTS!

9.1 ***PAH Comment: In the run up to the Budget, there was feverish discussion amongst tax professionals as to whether there would be an increase in the rate of capital gains tax (CGT) – currently 18%. The reason for this is that there is now up to at least a 32% and if entrepreneur's relief is available, a 40% difference between the marginal rates of income tax and capital gains tax. The argument is that with such a difference, the desire to change income into capital, such that it is taxed at a much lower rate, becomes irresistible and a plethora of new avoidance schemes designed to do just this can be expected, this in turn leading to more anti-avoidance legislation and an even more complex tax system.***

9.2 However, what do tax professionals know!, in the first surprise announcement, the Chancellor has decided not to increase the rate of capital gains tax this year. Like all other allowances, the tax-free amount is frozen and will remain at £10,100 for 2010/11.

9.3 The second surprise was a doubling to £2 million in the amount of lifetime gains eligible for entrepreneur's relief, which gives an effective capital gains tax rate of 10% on such gains. With the speculation on the rate of CGT, there was also speculation entrepreneur's relief would be abolished or at least scaled back, but exactly the opposite has occurred.

9.4 ***PAH further comment: Whilst these two announcements are of course welcome, they do not fit any pattern in tax policy that I and many others can ascertain. In my opinion it cannot be good for the country as a whole if tax policy is unclear and I hope having got the election out of the way, whoever is in power will have the guts to set out a sensible policy covering the whole of the next parliament – to give business a chance to fully recover, knowing the tax it will pay on that recovery.***

10 INHERITANCE TAX MATTERS AND WILL TRUSTS

10.1 In line with other tax allowances and thresholds, the inheritance tax (IHT) nil rate band will be frozen at £325,000 for 2010/11. In addition, the Chancellor announced it would remain frozen at that rate until 2014/15, but it is unclear why this announcement has been made at this point.

10.2 Following the major change to IHT a few years ago now, such that a surviving spouse or civil partner can have the benefit of any unused nil rate band of their partner, there has been a lot of comment that "old" nil rate band planning, including the use of will trusts to make sure the nil rate band on the first death was not lost if the whole estate was otherwise bequeathed to the surviving spouse, is no longer relevant. Whilst this is true for IHT purposes, there are other considerations that may mean this planning is still valuable.

- 10.3 Over the last few months, one of the areas that the political parties have been seeking to make capital on is how to fund care for the elderly, and no doubt we will hear more about this in the run up to the election. However, whichever party is in power, one thing that is clear is that there is not a bottomless pit of State funding and however it is done, individuals will almost certainly continue to have to bear a proportion of their own non-medical care costs.
- 10.4 ***PAH Planning point: In these circumstances, certainly to date, and I don't believe either main party is proposing a significant change, an individual's assets are taken into account in assessing the contribution they have to make to their own care. Accordingly, whilst it may no longer be of benefit to exclude assets from the estate of a surviving spouse for IHT purposes, it may be of considerable importance to reduce the contribution to care costs.***
- 10.5 If you would like any further advice on these matters, or to discuss IHT and capital tax planning in more detail, please do not hesitate contact either Kim or me.

11 STAMP DUTY LAND TAX (SDLT) CHANGES

- 11.1 There are two significant changes to SDLT – the removal of the 1% charge on properties worth between £125,000 and £250,000 in respect of a purchase by first time buyers and the introduction of a new 5% charge on residential properties of over £1 million.
- 11.2 The first change has immediate effect and lasts for two years, which it should be noted end on 24 March 2012 exactly! The effective date for SDLT is normally the date of completion and it will be important to ensure this occurs before 24 March 2012 if you are eligible for this relief.
- 11.3 Various commentators have pointed out that one difficulty with this relief will be policing who is entitled to it, as the land registry in the UK no longer has records of previous owners of properties and the definition of a "first time" buyer also excludes someone who has owned property overseas, where land ownership records are often virtually non-existent.
- 11.4 ***PAH Comment: In the same vein as my comments on capital gains tax in section 9 above, it would have been helpful for the Government to have given notice of this proposal much earlier, to enable private individuals who are able to claim the relief not getting "caught out" between two different reliefs for SDLT. It is only last December that the extension the 0% band for SDLT up to properties worth £175,000 was removed and here we have another relief – if you had bought a property in the intervening three months, but could have claimed the new relief, you would really have cause for anger at there being no coherent policy to support purchasers of eligible properties.***
- 11.5 Although the relief for first time buyers comes in immediately, the new SDLT rate of 5% for purchase of residential property over £1 million is deferred and will come into force where the effective date for SDLT is on or after 6 April 2011.
- 11.6 The Conservatives have already indicated they would be unlikely to reverse this change.

12 OTHER MATTERS

- 12.1 Online filing - VAT
- 12.1.1 Online filing for VAT will become compulsory for traders with annual turnover in excess of £100,000 per annum, with effect from the first return period commencing after 1 April 2010.
- 12.1.2 I expect this requirement will be extended to all traders with effect from 1 April 2011 or possibly 2012 and would therefore recommend that even if you are not obliged to file online you consider doing so.
- 12.1.3 ***PAH Planning point: We are able to assist with registration for online filing and in the actual online filing of VAT return information you have prepared. We have a fixed price menu for this work; please contact Kim or me for details.***

12.2 Online filing – PAYE

12.2.1 With effect from this year, 2009/10, tax year-end PAYE returns have to be submitted online for virtually all employers; returns submitted manually will no longer be accepted.

12.2.2 From 2011, in addition to all tax year-end returns having to be submitted online, all in-year documents – e.g. forms P45 for starters and leavers and form P46 for starters without a form P45, will also have to be submitted online.

12.2.3 **PAH Planning point: We are able to provide full and partial payroll services for clients and should be pleased either to undertake all payroll work for you on a bureau basis, or to prepare and file online documents from information you produce. Again, please contact Kim or me for details.**

12.3 National Minimum Wage

12.3.1 Based on current data, the standard rate for the national minimum wage is expected to increase by 2.2% to £5.93 per hour from October 2010. The rates for younger workers have not yet been announced.

12.4 Construction industry

12.4.1 In early March 2010, the Government published a summary of responses to a consultation document on "*false*" (my emphasis) self-employment in the construction industry. The preamble to this includes the following:

"The Government is committed to tackling this issue and given that there is broad recognition of the problem of false self-employment, continuing with the status quo or legislating the current case law tests are not viable options".

12.4.2 More work will now be done to refine and develop tests of self-employment specifically for the construction industry and whilst it is also pleasing to note that change will not be rushed through, it does seem a legislative approach is likely.

12.4.3 The paper also states that the Government recognises the effect that the economic downturn has had on the construction industry and intends that change will only be made when the industry is in a stronger position.

12.4.4 ***PAH Comment: Having said all that, when the change is made, it looks likely that the clinching test in many cases will be that the self-employed contractor has to supply not only all tools and equipment, including large plant, but also ALL materials used by him for his work on the construction site, this probably means the complete end of the labour only subcontractor.***

12.5 HMRC penalties – getting returns in and paying tax on time

12.5.1 Over the past few years quite substantial penalties for late filing of returns have been introduced and the opportunity taken to standardise penalties across taxes. The first Finance Bill after the election is expected bring the remaining taxes that currently have separate legislation within the standardised regime – this including VAT and excise duties – except for tax credits.

12.5.2 I set out more information on HMRC Powers and Penalties in both my December 2008 and September 2009 newsletters, which are available on our website at www.paulahill.co.uk if you do not have a copy to hand. If you would like an emailed or hard copy of either of these past newsletters, please contact Andrew Coates in St Ives and he will be pleased to send them to you.

12.5.3 The message from HMRC is clear – if you do not get returns in on time AND pay the tax due on time – there will be penalties, but.....

12.5.4 if you cannot pay the tax on time, to avoid a late payment penalty or surcharge you should apply to the Business Payments Support Service, before the tax is due for payment - see paragraphs 7.1 above.

12.6 HMRC penalties – taking reasonable care

12.6.1 Even if you get all your returns in on time and pay the tax shown as due on them, you could still suffer a penalty if you have not taken "reasonable care" in the preparation of the returns.

12.6.2 As has also been mentioned in previous newsletters the concept of "reasonable care" is new and we are still not quite sure what HMRC think it means – other than "getting it completely right". HMRC have confirmed that an individual taxpayer or business can demonstrate reasonable care themselves by using an agent such as us to perform work on your behalf. You will appreciate that we also have to take reasonable care in our work for you and that is why we undertake certain processes in our work – so we can demonstrate this to HMRC if required.

12.6.3 If you have any queries on the current HMRC penalties regime, please do not hesitate to contact Kim, Linda or me.

12.7 Anti-avoidance rules and principles based legislation

12.7.1 The budget has strengthened the rules relating to the "Disclosure of Tax Avoidance Schemes" (DOTAS rules) and HMRC are clearly looking to change the focus of their resources from routine compliance – much more of which can now be done through computer analysis of online submissions, this reducing the population of "ordinary" returns selected for more detailed manual checking, to closing down the more imaginative avoidance schemes.

12.7.2 There is specific mention in the Budget documents to the use of "principles based legislation" in several complex areas. The idea of this is to set out in general terms what legislation is designed to achieve and rely on the courts to find against avoidance schemes that, even if they do not break the letter of the law, are against the "principles" set out in the legislation.

12.7.3 The Government have used a similar, but not quite identical, approach once before, with regard to employment income. Back in December 2004, they made some announcements of principles with regard to taxation of employment income and where schemes have subsequently been discovered to breach those principles, have enacted retrospective legislation to outlaw the schemes from inception – effectively saying – "we told you we would not put up with this, so hard luck!"

12.7.4 With regard to particular current avoidance schemes, paragraph 5.63 of the Budget report states:

"The Government also announces future action to tackle the use of intermediaries, with the purpose of avoiding, deferring or reducing liabilities to income tax and NICs or avoiding restrictions on pensions tax relief. The Government will consider options for tackling these avoidance arrangements with the intention of introducing any necessary legislation to take effect from April 2011."

12.7.5 This paragraph would appear to be specifically directed at avoidance schemes involving vehicles such as employee benefits trusts (EBTs), different forms of which have become much more commonplace in the last few years. The good news is that by specifically mentioning this now, it may well be an indication they think many current schemes do work and are just trying to frighten off people from taking up new schemes between now and next April.

12.7.6 ***PAH Comment: As a number of clients do have schemes involving EBTs, we will be keeping a close eye on any pronouncements on this issue and will provide further information as soon as it becomes available.***

Our business grows mainly by referrals and we are always looking for new clients. I should appreciate it if you could let me know of any colleagues, customers or associates who may be interested in the way we do business. Thank you.

PAUL HILL

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Please contact:

<p>Paul Hill</p> <p>Paul A. Hill & Co 3 Bull Lane ST IVES Cambs PE27 5AX</p> <p>Tel: 01480 468931 Fax: 01480 469515</p> <p>Email: paul@paulahill.co.uk</p>	<p>Kim Upton</p> <p>Paul A. Hill & Co. Suite L8 South Fens Business Centre Fenton Way, CHATTERIS Cambs PE16 6TT</p> <p>Tel: 01354 694111 Fax: 01354 692291</p> <p>Email: kim@pahcochatteris.co.uk</p>
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