

# Tax Times | Autumn 2009

HELP WITH COMPLEX BUSINESS AND PERSONAL TAX ISSUES



“ There's no doubt that the prospect of 50% income tax is worrying some people. In this edition we discuss some of the options available to high earners. ”

# Welcome



Hello again, and welcome to our ninth edition of Tax Times. There's no doubt that the prospect of 50% income tax is worrying some people, so we've included in this edition a few ideas for high earners.

But for most people, the big worry is still coming from the UK recession. How can tax liabilities be managed efficiently when cash flow is so tight? There are ten tips on page 10 which might help.

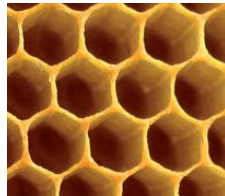
Recession or not, the demand for our tax services continues to rise and we are delighted to welcome Robin Woodhouse to our employer tax team. Robin specialises in helping employers manage payroll, PAYE, NIC and related tax issues effectively. More about him on page 8.

And finally, welcome to our new readers in Guernsey. We hope that you find something useful in these pages, despite the different tax jurisdiction.



**Charles Olley**

Head of Tax Consulting



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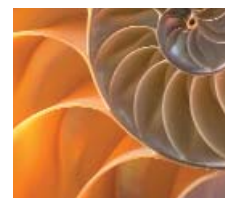
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ADDING SIGNIFICANT VALUE

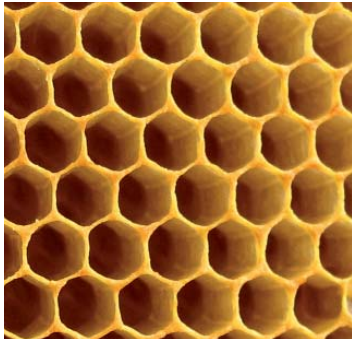
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# Private Client

DEFENDING YOUR FINANCIAL ASSETS FOR THE FUTURE

## Latest tax cases

### Business Property Relief

A number of cases appear to have widened the availability of BPR for inheritance tax purposes. This relief can exempt up to 100% of the value of an asset from Inheritance Tax. In the case of *Brander* (personal representative of the Fourth Earl of Balfour) v HMRC it was found necessary both to establish what the 'preponderance of business activity was' and to look at 'a variety of relevant factors in an attempt to create an overall picture'. In this case even though there was a significant amount of letting income it was held that the management of the landed estate was a trading activity.

### Record keeping

The importance of keeping accurate, timely records cannot be over-emphasised. In the case of *Trainor* the appellant operated a foreign exchange business. HMRC had found a number of errors in the verification and record keeping requirements, as imposed by the money laundering regulations. Warnings were issued and when a third irregularity was found, the department issued £500 penalties.

The taxpayer appealed but the tribunal judge, although agreeing that there had not been money laundering, refused to adjust the penalties, which were regarded as comparatively lenient.

### Employment expenses

It is notoriously difficult for employees to obtain tax relief for expenses paid by them

and not by their employer. However, in the recent case of *CRC v Banerjee* a specialist registrar employed by two NHS Trusts was successful. Her contract contained a training clause which required her to attend courses 'in carrying out the duties of her employment'. She claimed deductions for expenditure incurred in attending educational courses including the associated costs of travel and accommodation. HMRC did not allow the claims.

The registrar was successful before the General Commissioners and HMRC appealed to the High Court. The judge confirmed that attendance at the courses was an objective necessary requirement of the taxpayer's employment and therefore HMRC's appeal was dismissed.

### Income splitting

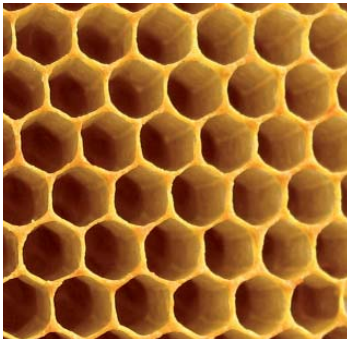
HMRC scrutinises income splitting between husband and wife very closely. In a recent case, *Mr Rockliff* a married retired policeman had his pension paid into a joint bank account with his wife. On his tax return he had declared only one half of the pension, on the basis that the other half should be charged on his wife. Not surprisingly this gave rise to an enquiry by HMRC who amended his return to show the full amount as taxable.

*Mr Rockliff* appealed. He contended that half of the pension income should be apportioned to his wife, because if this was not allowed, it would effectively be discrimination against marriage, since in the event of their possible

divorce, under the pension sharing arrangements, one half of the pension would probably be granted to his wife. She would then be taxed on that half in her own name. If this were the case, divorcees would be treated more favourably than a married couple, contrary to the European Convention on Human Rights.

Unfortunately, the matter has not been resolved as the question of whether national legislation was incompatible with the Human Rights Convention was not within the tribunal's jurisdiction. The tribunal judge considered that the matter would have to go to appeal for a decision to be made. Whether a formal appeal is launched remains to be seen.

Do not hesitate to contact one of our tax consultants, or your usual Price Bailey contact if you wish to discuss how any of these cases may be relevant to you.



# Private Client

DEFENDING YOUR FINANCIAL ASSETS FOR THE FUTURE

## The 50% income tax rate is coming!

### What can you do to avoid it?

**As all high earners in the UK will be only too well aware, income tax rates will increase significantly on 6 April 2010, when a new top rate of 50% will be introduced, and the personal allowance for those with income over £100,000 will be phased out. What can be done?**

#### Using your spouse

Many married couples have their home in joint names, but often other assets are "his" or "hers". If that leads to capital and income inequality, one spouse could end up in 50% tax territory with the other on the breadline. Careful reorganising of capital assets, so that income arises in the right place has to be done before income arises, so now is the time to consider moving capital assets about. Don't wait until the end of the tax year.

Usually there is no capital gains tax, inheritance tax or stamp duty to worry about when assets pass between spouses, but you should certainly check with us first.

But if the asset is no more than a right to earned income, for instance shares in a personal services company, the tax man is likely to use his anti avoidance armoury to ensure that the person who

earns the money is the person who is taxed. So transferring entitlements to income will not work.

#### Joint assets

In many cases it will not be commercially desirable, or possible, to transfer shares in a company to a spouse, perhaps because of a shareholders agreement or pre-emption rights in the company's articles. Joint interests may then be a possible solution. As a rule, the first named gets the votes and legal rights, the second named shares only the beneficial interests. So dividends paid on shares owned jointly get shared equally for tax purposes. This may enable efficient use of allowances and basic rate tax bands.

#### Retain to exit

Can you afford to leave your income in your company? If so, why not leave it there to be taxed at corporate tax rates rather than personal tax rates? You may then eventually collect it at capital gains rates (which will surely always be lower than income tax rates, even if the 18% sounds too cheap to last), or maybe when income tax rates are on the way back down again.

#### Accelerate your income

Why not accelerate your income, by bringing forward salary rises, bonus payments, proposed dividends etc? The precise acceleration mechanism will vary from case to case and our teams can advise you on what might be suitable in your circumstances. Of course, you will have to pay the tax sooner than would otherwise be the case, but remember, tax for the high earners is going up 25%. That's a big price rise.



If cash is available at low cost, that's potentially a big saving.

### Take loans not pay

At the time of going to press, it's possible to borrow money from a UK close company with only a basic rate tax charge of 25% that falls on the company and a benefit in kind charge that works out at about 2% pa. Taking into account the full rate of underlying corporation tax, this adds up to an effective rate of tax of 44% for the first year plus 2% per annum thereafter. This will compare favourably with the effective rate of tax for a salary of 56.6% and for a dividend of 54%, but you need to take care. Might you be called on to repay your loan? There's a big difference between a loan and a dividend that's nothing to do with tax.

### Don't forget tax efficient savings

Have you made full use of tax efficient savings vehicles? ISAs, VCTs, EIS and life policies all

have some tax breaks. Now is a good time to review your investment portfolio for tax efficiency. Don't wait until after the new rate starts to bite.

### Pension Contributions

Pension contributions remain one of the most tax efficient ways of saving. However, the Finance Act 2009 introduced yet another raft of contribution rules, so there is even more reason to plan ahead. Now not only will overfunding incur unexpected tax charges, but so will over contributing by those earning over £150,000.

### Only 5 ways to save income tax

There are only five ways to save income tax:

- Think ahead - nothing happens without planning
- Minimise your taxable income
- Maximise your reliefs, allowances and reductions

- Calculate it properly
- Avoid the tax traps

Call your usual service team or contact one of our tax consultants for help. That's what we are here for.

## Time limits for tax claims

Note for your diary that the time limits for making tax claims are reducing according to the following table:

Claims for the Year:	Must be made by:
2003/04	31/01/2010
2004/05	31/03/2010 – (currently nearly 6 years)
2005/06	05/04/2010
2006/07	05/04/2011
Thereafter	Four years





# Corporate

ENABLING, GUIDING AND OPTIMISING BUSINESSES

## Prepare for VAT rate increase

From 1 January 2010 the VAT rate will increase from 15% to 17.5%. The rate of VAT chargeable is determined by the time of the tax point. If a tax point for a supply is prior to the rate change the existing rate of 15% may be used.

A tax point is created at the earlier of:

- receipt of money
- date invoice is issued, or
- delivery of goods or completion of service

If your customers cannot recover VAT charged it will be beneficial to create a tax point prior to the rate change. So, for goods to be supplied or services provided after 1 January 2010 you may consider invoicing or collecting payment before that date. This will also benefit your cashflow.

If a business makes continuous supplies of services, there are special rules for rate changes. Broadly, it may account for VAT at 15% on the part of the supply made before 1 January 2010 even when the normal tax point occurs after that date. This is optional, and the normal tax point rules may be applied if preferred. There is anti-forestalling legislation for more aggressive VAT planning, but for practical purposes, this will not affect normal business transactions.

Don't forget that rate change will also affect business which use the Road Fuel Scale Charge, and those which operate the Flat Rate Scheme.

## The Reverse Charge on services received from overseas

Normally, the supplier of a service is the person who must account to the tax authorities for any VAT due on the supply. However, in certain situations, the position is reversed and it is the customer who must account for any VAT due. This is known as the 'Reverse Charge' procedure. Generally, the reverse charge must be applied to services which are received by a business in the UK VAT free from overseas.

### Accounting for VAT and recovery of input tax

Where the reverse charge procedure applies, the recipient of the services must act as both the supplier and the recipient of the services. On the same VAT return, the recipient must

- account for output tax, calculated on the full value of the supply received
- (subject to partial exemption and non-business rules) reclaim this VAT as input tax
- Include the full value of the both supplies on the VAT return

The effect of the provisions is that the reverse charge has no net cost to the recipient if he can attribute the input tax to taxable supplies and can therefore reclaim it in full. If he cannot, the effect is to put him in the same position as if had received the supply from a UK supplier rather than from one outside the UK so as to avoid distortion of trade by businesses which cannot recover all of their VAT cross-border shopping.

The reverse charge will become more common after 1 January 2010 because the place of supply rules change on that date so that more services will be VAT free when supplied cross border. This is good news and will reduce the amount of overseas VAT which businesses incur (which cannot be reclaimed on a UK VAT return). So, although apparently "going round in VAT circles" the Reverse Charge is actually rather useful.



## VAT Groups – Pros and Cons

VAT groups are not only useful for reducing paperwork, but are very beneficial for VAT planning.

If you are considering VAT grouping companies (or LLPs) you will find the following points helpful:

### Pros

- Only one VAT return per quarter – less administration
- No VAT on supplies between VAT group members. No need to invoice or include supplies on VAT return
- May improve partial exemption position if exempt supplies are made between group companies
- May improve input tax recovery if taxable supplies are made to a partly exempt company
- May provide useful planning opportunities/convenience at a later date

### Cons

- All members of the group are jointly and severally liable for any VAT due
- Only one partial exemption de-minimis limit for group
- Obtaining all relevant data to complete one return may cause delay and the potential to miss filing deadlines
- A new VAT number is issued
- Assessments can be raised on the representative member relating to earlier periods when it was not the representative member and even when it was not a member of the group at that time

- The limit for voluntary disclosures of errors on past returns applies to the group as a whole (rather than each company having its own limit)
- The payments on account limits apply to the group as a whole. This applies to a business whose VAT liability is more than £2million pa.
- May detrimentally affect partial exemption position if a partly exempt company makes taxable supplies to a fully taxable company

### Don't forget VAT Bad Debt Relief!

In the current climate it is vital for businesses to maximise available tax relief. Remember that if you have not been paid by a customer for a supply made over six months previously ensure that Bad Debt Relief is claimed on the VAT!

This works both ways – if you are six months late paying a supplier, you have to repay the input tax.

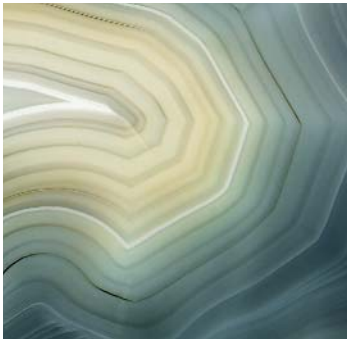
## Do you employ engineers or scientists?

Don't forget you could qualify for research and development tax credit!

Research and Development (R&D) tax credits were introduced in April 2000 for companies which qualified as small and medium enterprises (SMEs) and extended to large companies in April 2002.

From 1 August 2008 the rate of qualifying cost enhancement for SME companies is 175% (previously 150%); and for "large" companies from 1 April 2008, the relevant enhancement rate is 130% (previously 125%). The rate of relief available to SMEs is now highly attractive and with our continued success in making claims for our clients, the Price Bailey message on R&D is simple; "If you employ engineers or scientists then you are likely to be carrying out R&D without even realising it and may be missing out on this valuable relief".

Don't hesitate to contact our R&D Specialist, James Doggett, on 01223 507632 for an initial no obligation discussion on whether your company's activities may qualify for R&D relief.



# Consulting

ADDING SIGNIFICANT VALUE

## Walking the tightrope between recession and recovery

In tough economic times, employers need to seize every available opportunity to streamline their employment costs. But they must also be geared up for business when the economy recovers.

Flexibility and tax efficiency can be the key, says a Price Bailey employment tax specialist. In conversation with Robin Woodhouse, Tax Times unlocks the opportunities available to employers.

### **TT: You've recently joined PB from a Big 4 Firm. Was it a culture shock?**

Yes, but a pleasant one. We're big enough to have top quality specialists in all areas but local enough to be really close to our clients. And we're a very close-knit team, so it's a much more collaborative and client focused environment than I've been used to.

### **TT: You're an employment tax specialist, what are the biggest challenges facing employers in the recession?**

It's a balancing act between reducing employment costs and retaining skilled workers. Making redundancies in a downturn, only to recruit and re-train in a recovery, is expensive and disruptive. So the key is to reduce the cost of employing people without losing them or cutting their pay.

### **TT: How can employers achieve that balance?**

By being more flexible and tax efficient. Employers pay 12.80% national insurance (NICs) on employees' taxable pay and benefits. But many items that employees buy could be

provided tax free by their employers, often with the added benefit of corporate discounts. Valuable items such as childcare, staff canteens, bicycles or workplace car parking can be given as tax free benefits instead of taxable pay, saving the employee tax and the employer national insurance.

### **TT: And this principle also applies to pension contributions?**

Yes. Employee contributions into a company pension scheme are allowable for tax but not NICs. So if the employer pays them, and the employees take a corresponding reduction in contractual gross pay, the employer saves the NICs.

### **TT: We have heard of some employers paying business travelling expenses on the same basis?**

There are two issues here.

First, in April this year, HMRC published generous flat rate meals allowances that employees on qualifying business journeys can receive, tax free, without having to provide receipts. For employees engaged on overseas travel these rates are extended to include accommodation. This represents a significant reduction in the employer's admin burden.

Secondly, an employee engaged on a temporary detached assignment or secondment could consolidate these tax-free allowances

into their package with a corresponding reduction in taxable pay to achieve overall savings in tax and employer NICs.

### **TT: Is there any risk attached?**

Not if it's done properly. The key to this, and any other so-called "salary sacrifice" arrangement, is to ensure that the changes are correctly reflected in the employee's terms and conditions so that the contractual gross pay is legitimately reduced for tax and NICs whilst enhancing the overall net value of the remuneration package.

Employees must also be reassured that their pre-sacrifice gross pay value will be retained as a benchmark for pay-related items such as overtime, bonuses and mortgage applications so they will not be worse off.



**Robin Woodhouse**  
Senior Manager

## Summer brings good news on employee share schemes for international business

The European Union has agreed that the UK can continue the popular Enterprise Management Incentives (EMI) – the tax-favoured employee share option scheme for smaller and/or entrepreneurial companies regime – at least until 2018. There had been some doubt about whether the generous tax break afforded by the EMI regime offended the EU's rules about allowable state aid. The European Commission has recently ruled that the EMI regime does not offend these rules– good news indeed for those operating in an increasingly international business context.

Secondly, the Government is extending the categories of company that can be eligible for the EMI regime. Previously, a company has had to be mainly UK-oriented to qualify. From April 2010 this will no longer be the case. This means that UK companies with predominantly overseas business or foreign companies with only slender UK connections are more likely to be eligible for the EMI regime.

While having significant overseas business is not always a problem, this is a welcome extension of the EMI regime. It is to be hoped that this extension will better enable smaller employers to recruit or retain highly skilled staff.

## EBT IHT – OMG!

### Employee Benefit Trusts

The taxman is not keen on EBTs that are used primarily for the benefit of owner-managers and has recently made this very clear.

During the summer the taxman slipped out a spotlight about EBTs, announcing that he is going to use the rules about Inheritance Tax to attack those EBTs where the owner manager is a potential beneficiary of the trust. He will do this by getting the owner-manager(s) to fill in an Inheritance Tax return each time that the company makes a contribution to the EBT.

This will be no fun for the individuals concerned – either in filling in the right form in the right way at the right time or in making any necessary inheritance tax payment on time.

We think this is likely to be the first broadside in a more determined effort to stamp out EBT abuse.

In our view, an EBT remains a valuable planning tool for an Employer, but only when its focused on Employees and not the business owner.





# Small Business

INFORMING, DEVELOPING AND SUPPORTING SMEs

## MPs

You will recall that MPs were heavily criticised for abusing tax law when flipping homes and claiming expenses. Where did they go wrong?

### Flipping homes

Despite the media furore, the tax side of the flipping homes is acceptable planning, well within legally acceptable behaviour. The technique is well described in the HM Revenue & Customs manuals. Certain individual MPs forced to pay tax in such situations may well feel aggrieved.

If you have more than one home, talk to us about your rights to flip.

### MP's expenses

The expenses claims are however a different matter. A taxpayer is entitled to make expense claims in a tax return as part of the compliance process. If an honest mistake is made it has to be corrected and perhaps a penalty is payable. But the claiming of an expense is simply a matter of tax compliance.

Claiming for an expense that you know is not allowable for tax is however very different. The dishonesty makes it Evasion which is unacceptable. So those MPs who knew they shouldn't have been claiming certain expense payments as tax free cannot complain at the public anger: they may yet have to face far worse. But those who did so in ignorance have nothing to fear. Strangely in this instance ignorance of the law could well be a decent defence.

## Managing tax in a recession

There are various ways Price Bailey's tax specialists can help you and your business in the recession.

Uncomplicated, sensible tax planning could result in significant reductions in tax payable or even cash inflows.

If you think you need to consider any of the following then we would urge you to contact one of our specialists:

1. Using tax losses
2. Small business rate relief / rural rate relief
3. Writing down overvalued assets
4. Consider the type of entity through which you trade – sole trade, partnership, company
5. Use your spouse
6. Reduce employee costs without reducing headcount
7. Watch for tax overpayments on projected profits
8. Making the most of, or accelerating, tax reliefs e.g. R&D spend
9. Deferring VAT payments or perhaps register for VAT
10. Talk to HMRC

## Unannounced VAT visits

### New powers and penalties

We hope that you never receive an unannounced visit, since these are carried out where HMRC suspects wrongdoing. There are new penalties for obstructing officers, but this does not mean that HMRC has carte blanche to do whatever they wish.

If you receive such a visit, our practical advice is;

- Ask for formal identification and request sight of the Visit Notice
- Buy time in order to prepare. Requesting that the officers "go for a coffee" for half an hour should not be considered obstruction, although care should be taken
- Contact us immediately
- Be circumspect in replying to questions, specifically in the time before help arrives (HMRC do not have to wait for an advisor before they start their visit)

Unannounced visits may herald serious proceedings. Price Bailey has experience in assisting in such situations.

## HMRC harmonises interest rates on late payments of tax

At last, HMRC's interest rates for late payment of tax and refunds have all been harmonised. From 29 September 2009 (rent day), you need to remember only three rates, which are:

- Late payment of quarterly corporation tax instalments 1.5%
- Late payment of all other taxes 3%
- Overpayments ½%

The official rate of interest for beneficial loans remains at 4.75%.





# Small Business

INFORMING, DEVELOPING AND SUPPORTING SMEs

## Business Assurance – Needed now more than ever

There are many potential disasters which can affect any business and it is sensible to insure against them. But we often overlook the most valuable asset of all – our people!

### Shareholder Protection

What happens if a shareholder dies? Can the others buy out the family? What do the family actually get if they cannot? A policy would ensure that:

- The deceased shareholder's family receive a capital gains tax free sum
- The remaining shareholders get the shares and full control of the business
- The overall financial position of the business is unaffected
- The overall financial position of the continuing shareholders is unaffected

Please note, similar cover can be provided for partnerships.

### Key Person Cover

Are there key individuals within the business, the loss of whom would:

- Reduce profits?
- Impact on confidence and the ability to raise finance?
- Cost a significant amount to replace?

A policy can be arranged to provide positive cash flow to help the business survive. When trading is difficult it is important to keep control of costs but equally it makes it more difficult for a business to survive any setback. We can help by reviewing any arrangements to ensure that the level of cover is appropriate, premiums are competitive and the arrangement is properly set up. In this way you minimise the cost but maximise the benefit!

## Contact us

For specific advice contact your usual client service team or contact the tax helpdesk on +44 (0)1223 507630 or email [taxhelpdesk@pricebailey.co.uk](mailto:taxhelpdesk@pricebailey.co.uk).

### Pre-Budget Report Summary

The much publicised and eagerly awaited 2009 Pre-Budget report will be presented in November 2009. Please continue to check [www.pricebailey.co.uk](http://www.pricebailey.co.uk) for updates including a summary report.

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