

TCP UPDATE

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the newsletter of tcp chartered accountants

10 the triangle ng2 business park nottingham ng2 1ae
t (0115) 986 2411 f (0115) 986 2412
e info@tcp.uk.com w www.tcp.uk.com



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Alistair Darling presented his second Budget on Wednesday 22 April 2009. Having acknowledged the depth of the recession, he hinted that the Budget measures would enable the UK economy to begin to grow 'by the end of the year'.

Our round up highlights the key budget headlines likely to affect you and your business.

- From 6 April 2010 there will be a 50% top rate of tax for those with taxable income over £150,000 and in the following tax year the government has also announced its intention to restrict tax relief on pension savings for this group.
- A phased reduction of personal allowances for those with income over £100,000 is also due to impact from 6 April 2010.
- The amount which can be invested in an 'ISA' account the tax free savings vehicle is to increase by £3,000 to £10,200.
- The ability to use trade losses through relief in earlier years by both an unincorporated business and a company has been enhanced.
- There is a temporary additional capital allowance on plant expenditure which may benefit those with higher levels of spending on plant and machinery.
- Extension of the furnished holiday lettings scheme to properties in the European Economic Area is to apply but the scheme is to be abolished completely from April 2010.

Please contact us for further advice on any matter which may affect you.

Bowled over by benefits

The knowledge that you are getting the most out of your hard earned profits may provide as much of a boost as the prospect of sunshine and warm summer breezes. Whilst a key consideration might be maximising the cash at your disposal for the minimum tax cost - are you optimising your benefits?

Dividend extraction has reigned supreme in recent years for small companies as a means of providing cash to director shareholders and may also now be the most cost efficient for other companies under current tax rules and rates. Its advantage over remuneration generally is that there is no national insurance cost. This fact currently outweighs the other key matter that dividends do not attract corporation tax relief. But what about remuneration which benefits from obtaining tax relief for the business and has no national insurance cost?

The need to extract cash is always going to be an essential component for living requirements but the provision of tax free benefits by a company to directors and employees has certain merit, worthy of fresh consideration. Like dividends, tax free benefits are not subject to national insurance for either the employee or the employer. Yet the company should obtain a tax deduction where provided as part of a commercial remuneration package. It also has flexibility as different types of benefit can be provided for different individuals. Furthermore, unincorporated businesses can also participate in respect of their employees. This could be a valuable motivational incentive at a reduced cost.

Even where benefits are not income tax free and so attract employer national insurance there are still favourable reasons for considering their provision. Firstly, there is still no employee national insurance.

Secondly, the cost to the employer of providing certain benefits to employees is cheaper than each individual employee buying the benefit out of post tax wages.

Clearly if the overall aim is to minimise tax and NI cost overall then the benefit provided needs to be tax free and some examples of such benefits include:

- a mobile phone for personal and business use (restricted to one per employee from 6 April 2006)
- free car parking at/near place of work
- contributions to registered pension schemes
- health checks and eye tests
- business mileage paid at HMRC's approved rates
- nursery provision up to £55 a week per parent
- permanent health insurance

To obtain tax and national insurance favourable treatment on benefits, it is essential that their provision is structured correctly. If this is an area of interest to you please contact us for further information.



Settle for nothing less

You may remember the case of Arctic Systems. It involved a company owned jointly by Mr and Mrs Jones. Whilst Mr Jones did most of the day-to-day work and generated most of the company's profit, the dividends were paid out (in accordance with the shareholdings) equally to Mr and Mrs Jones.

HMRC attempted to assess the dividends received by Mrs Jones on her husband, using a piece of tax legislation often referred to as the 'settlements' legislation. In order for these rules to apply, three conditions are necessary:

- a settlement exists ie an arrangement, understanding or plan;
- there is a tax advantage to what has been done, sometimes referred to as 'bounty' – in particular, whether this was an arrangement which the taxpayer would have entered into with someone with whom he was dealing at arm's length; and
- the person who created the settlement (or their spouse / registered civil partner or minor children) retains some sort of interest in it.

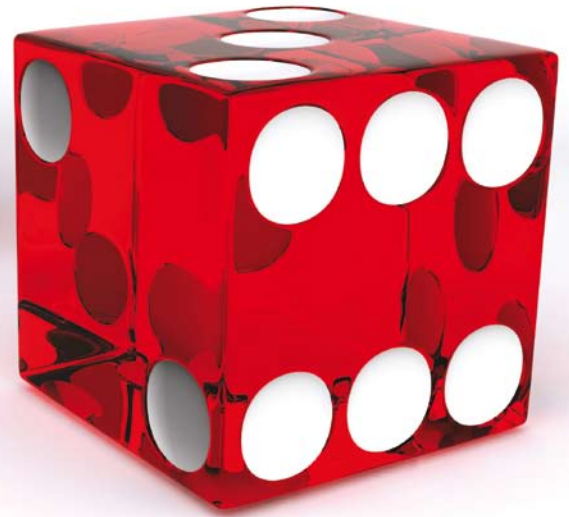
In the Arctic case, the judge held that all of these conditions applied. However, there is an exemption from the rules for inter-spouse transfers, provided that the transfer is not just a right to income. This exemption ultimately protected Mr and Mrs Jones.

Not a great deal more has been heard of these rules until the end of last year, when HMRC were successful in applying the rules to two slightly different situations.

The first case concerned a husband's waiver of dividends on 9,999 shares with the effect that dividends were paid to his wife, who held one share. The company did not have the distributable reserves to enable dividends to be paid in respect of all of the issued shares; if that were to have happened, the company would have needed some £300m of reserves!

The second case involved a company owned by a husband and wife which issued shares to each of their three minor daughters. HMRC argued that the dividends paid to the three daughters until they each reached 18 constituted income arising under a settlement.

HMRC won both of these cases, so it is important to note that the settlements legislation is not dead. If you have any concerns about these rules, please do not hesitate to contact us.



How to avoid being a winner in the HMRC lottery

Many books have been written about how to improve your chances of winning in the National Lottery or how to improve your chances of backing a certain winner in the 2.30 at Chepstow. This article is about how to avoid winning the HMRC lottery and therefore avoid the prize of having a Tax Inspector crawling all over your business.

HMRC investigations of any kind are costly in time and even more costly in the emotions they engender and the distraction they cause in the running of your business. So is it possible to avoid them?

The honest answer is that no one has absolute immunity from investigation. There is always a small random element in the choice of cases for enquiry but there are a number of basic things that you can do to help improve your position.

The number one priority is to have an impeccable record of submitting all tax returns on time. This applies not just to the personal self assessment or the corporation tax return but also covers your employer returns such as the P35, the P11Ds and any regular VAT returns that you have to make. Regular delays in submission signal to HMRC that there may be control issues and put the accuracy of basic business records under scrutiny.

Number two is to always ensure that your returns are accurate and complete. HMRC have a wide range of information gathering powers and receive large amounts of information from third parties about amounts that might be paid to you. The omission of interest credited to bank accounts from returns is common and is a regular reason for HMRC to start an enquiry. Information is also obtained about commission payments and a wide range of other matters.

Number three would be to look at your business accounts when they have been prepared and try to explain any significant changes from the previous year. HMRC will look at trends in accounts and also compare them to results from other traders in your line of business. Marked differences will cause alarm bells to ring. Consider providing explanations when the return is submitted that might prevent

questions being asked. Look for the reasons for significant changes in turnover and gross profit rates - they are real favourites of HMRC. There may be a very good reason why things have changed - make sure the Inspector knows. Only a few years ago your Tax Inspector would have been in an office probably no more than 20 miles away from you. Today it is more likely that your Tax Inspector will be many hundreds of miles away from you and he will have absolutely no knowledge of the trading conditions you are facing - so tell him!

Cash businesses are always high on HMRC's suspect list and extra vigilance is needed here but HMRC know that people being paid by direct bank transfer can arrange for money to disappear as well.

Dramatic changes in turnover / gross profit rates will really ring alarm bells when drawings taken from the business or remuneration paid seem to be insufficient to meet perceived living expenses. Remember that the Inspector has only the return on which to make a judgement and some background information may help make the difference.

If you are a sole trader or in a partnership, perceived inadequate adjustment for private matters such as motor expenses, or goods taken for own use, may prompt an enquiry.

Major changes in any other significant expenses may also need to be explained and you should always ensure that your stock or work-in-progress at the year end has been given some careful thought.

HMRC have new powers from April 2009 which will alter the way in which they carry out investigations. They also have a new penalty regime that will inevitably mean that the level of penalties charged where tax has been lost due to negligence or deliberate action on the part of the taxpayer will increase. You don't want to be involved in helping an Inspector get practical experience of how the new powers work! Various tax returns will be prepared over the coming months so give some careful thought to what goes in them.

Reduce your business rates

Many businesses pay more business rates than they need to because they don't realise they could claim a discount through the small business rate relief scheme (SBRR). This scheme has been poorly promoted by the billing authorities, but it is worth applying for relief as you could reduce your rates bill by up to 50%.

It is the size of the property occupied that determines the discount not the size of the business. Generally business properties in England with rateable values of less than £15,000 (£21,500 in Greater London) qualify for some discount. However, where one business occupies several properties, the SBRR will only apply to one main property and then only if the total rateable value of all the properties occupied is less than £15,000 (with each property having a rateable value of less than £2,200).

Scotland and Wales have slightly different small business discount schemes as those regional Governments set their own levels of business rate. Northern Ireland does not have a business rates system, as it still uses the old domestic rates system that has its own hardship scheme.

All business properties pay rates according to their rateable value multiplied by a set multiplier, which is 48.5p for 2009/10. The English SBRR applies a lower multiplier (48.1p for 2009/10) to qualifying properties, plus the following additional reductions:

Rateable value of building	Relief given
Less than £5,000	Lower multiplier, then 50% reduction in resulting figure
£5,000 - £9,999	Lower multiplier, then 1% reduction from 50% for every £100 of rateable value above £5,000.
£10,000 - 14,999 (£21,499 in London)	Lower multiplier only

Example

Your office has a rateable value of £5,500. You are sent a business rates bill of £2,668 (£5,500 x 0.485) for 2009/10. You apply for the SBRR and receive a refund of £1,213, calculated as follows:

Rateable value at lower multiplier rate:	£5,500 x 0.481	£2,645
Discount for value less than £5,000:	50%	
Reduced by 1% x (£5,500 - £5000)	5%	
Final discount for small property	45% x £2,645	£1,190
Final business rates for 2009/10		£1,455
Original rates bill		£2,668
Reduction achieved:		£1,213

You need to apply for the SBRR from the billing authority that collects your business rates, but you only have to complete one form to cover all the years from 2007/08 to 2009/10. A new claim will be required from April 2010. The extended deadline for claims for these years is now **30 September 2010**.

Vacant properties

If your business property is vacant you can claim an exemption from business rates, but only for restricted periods, known as permitted void periods. From 1 April 2008, the permitted void period is six months for industrial properties, and three months for other commercial properties. Full business rates are due on all empty properties when the permitted void period comes to an end, subject to any SBRR reductions due. However, for just one year from 1 April 2009 all empty properties with a rateable value of less than £15,000 are fully exempt from business rates.

The war on wages

The National Minimum Wage (NMW) rules have been around for some years. Whilst the rules have not really changed since they were introduced, the Government has become increasingly concerned that many businesses do not pay the required rates:

- workers aged 22 and over - £5.73 per hour
- workers aged 18-21 - £4.77 per hour
- workers aged 16-17 - £3.53 per hour

HMRC are the organisation tasked with policing the rules and the government has made funding available to do this. However, HMRC cannot visit every business in the country, so they have adopted a programme of targeted enforcement. This is designed to work with employers and workers to address issues and concerns about the NMW and to produce guidance in order to assist employers in meeting their obligations. Business sectors chosen under this new programme so far have been hairdressing, childcare providers and the hospitality industry.

From 6 April 2009, a new automatic penalty will be levied on employers where HMRC find NMW arrears. The penalty is 50% of the total underpayment (for periods starting on or after 6 April 2009) but there is a minimum penalty of £100 and a maximum penalty of £5,000. The penalty must be paid in addition to any arrears owed to the workers. The most serious cases of non compliance may be tried in a Crown Court and subject to an unlimited fine.

The Department of Business Enterprise and Regulatory Reform are providing a decision making tool to enable employers to check whether an individual is eligible for the NMW, and if so at what rate. Where there has been an underpayment of the NMW, the tool will also help employers calculate the arrears that are due to a particular worker in respect of a specified pay reference period.

For further information, please see www.berr.gov.uk/whatwedo/employment/pay/index.html

Change in intestacy rules in England and Wales

Where a person dies intestate (ie without having left a Will) the law prescribes how the estate of the deceased is to be divided. The rules are different around the UK with England & Wales, Scotland and Northern Ireland all having different provisions.

For deaths on or after 1 February 2009 the limits to be used in England & Wales have changed. Under the new limits where the deceased leaves a spouse (or registered civil partner) and children, the surviving spouse will receive everything up to £250,000 plus all personal possessions. Anything remaining is divided equally with one half going to any children of the deceased and the other half being left so that the surviving spouse receives the income and on their death the capital passes to the children.

Where the deceased leaves a spouse but no children, the spouse will now receive the first £450,000 plus personal possessions. Anything above that will be split equally with one half to the spouse and the other half to the parents. If there are no parents there is a specified order of relatives to consider. If there are no relatives still alive the surviving spouse will take the whole estate.

If there is no surviving spouse (or registered civil partner) but a surviving unmarried (unregistered) partner, they are entitled to absolutely nothing under the intestacy rules. Where the deceased has children they would take the whole estate. If there are no children the estate would pass to the parents etc of the deceased.

It is vital that if you want to direct where your estate will go that you make a valid Will to achieve that.



Keeping on the right side of the law

Dividend extraction is frequently the right move when withdrawing profits from a company for tax efficiency but you need to ensure that you have considered the legal aspects as well.

A company can only make a distribution by way of a dividend out of profits available for that purpose.

These profits are defined as its accumulated realised profits not previously utilised, less its accumulated losses not previously written off.

In order to determine whether a dividend payment may be made, the Companies Act 2006 requires justification of the distribution by reference to relevant accounts.

Relevant accounts are the company's last accounts prepared in accordance with the Companies Act 2006, interim accounts or initial accounts. Both interim and initial accounts must enable profits, losses, assets, liabilities, share capital and reserves to be determined.

An unlawful dividend is any distribution made by a company to its shareholders that breaches the rules on dividends.

The law is very specific in this area and a minor technical breach of them will lead to an unlawful dividend. The most likely example of a breach is insufficient profits to make a distribution at a particular date.

The consequences of such a breach in the law render the shareholders liable to repay the dividend to the company if at the time of distribution they knew or had reasonable grounds to suspect it was unlawful.

Should an unlawful dividend be distributed, directors are considered to be 'in default' if they permit or fail to prevent the breach. This can lead to a liability that the directors have to pay personally.

For dividends to be valid, certain other procedures need to be followed, so please contact us for further advice.

Changes to the State Pension

The State Pension is still a fundamental part of peoples' retirement plans. Over the last two years a number of changes to the basic State Pension have been announced. These include:

- increasing the basic State Pension in line with earnings, rather than prices, which means it should rise more quickly each year than it does now. This change will happen from 2012 at the earliest and by 2015 at the latest and will also apply to people currently getting their State Pension or who reach State Pension age before 6 April 2010;
- both paid and credited National Insurance Contributions (NIC) will count towards the basic State Pension in the same way;
- reducing the number of qualifying years needed for a full basic State Pension to 30 for people who will reach State retirement age on or after 6 April 2010;
- any number of qualifying years will give an entitlement to at least some basic State Pension;

- replacing the system of Home Responsibilities Protection with a weekly NI credit for people caring for children or severely disabled people and converting past years of HRP into years of credits.
- changing the way the State Second Pension (S2P) builds up, so that it will provide a simple, flat-rate weekly top-up to the basic State Pension; and
- increasing the State Pension age for both men and women from 65 to 68 in stages between 2024 and 2046.

It is not unknown for errors to occur due to difficulties linking national insurance contributions with pension records. However, there is an easy way to check your current pension entitlement – ask for a pension forecast. If you would like to know more about the changes or ask for a forecast, visit www.pensionservice.gov.uk

All change...for the holiday express

You may be aware that statutory holiday entitlement for all employees whether full, part time, shift, agency or casual, has been enhanced from 1 April 2009.

The legal minimum under the Working Time Regulations 1998 (as amended) has increased from 4.8 weeks' paid leave each year to 5.6 weeks (capped at 28 days) for a full time worker. Any days off for public or bank holidays count towards a worker's statutory holiday entitlement as long as it is paid leave. Many workers already get contractual leave which is more than 28 days so if that already applies to your staff this aspect of the changes does not affect you.

The other key change is that it will no longer be possible to make payment in lieu of statutory holiday.

Holiday entitlement in excess of the statutory rules is governed by employment arrangements and could therefore be carried forward or paid depending on the terms of your employment contracts.

Some of the frequently asked questions published by Acas are covered below to assist you on these important changes.

Do I need to inform my employees about the increased holiday entitlement?

Yes. You need to inform your employees in writing of their increased holiday entitlement from

4.8 to 5.6 weeks per year. You do not have to issue a new contract of employment but could notify employees using pay slips.

How is a part time worker's holiday entitlement calculated?

Part time workers are entitled to the same holidays as full time workers, calculated on a pro rata basis. For example, an employee who works four days a week is entitled to 22.4 days' paid holiday - their normal working week multiplied by 5.6.

An employee only works during term time. How much extra leave will they get?

You need to work out how many hours the employee works on average over the whole year. For example, if the employee works 40 hours a week for 40 weeks of the year, they work a total of 1,600 hours a year. This works out at 34.48 hours a week over 46.4 weeks of the year (the 5.6 weeks of statutory holiday entitlement are excluded from the average working week calculations). The employee's holiday entitlement is 5.6 weeks x 34.48 hours a week = 193.09 hours holiday for the year.

How do you manage part days?

Holiday entitlements for some employees who work part time may be made up of part

days - for example, 22.4 days for someone working four days a week. An employer can manage these part days by:

- taking the part day off a day's shift (an employee leaves early or comes in late)
- rounding the time up to the nearest full day (the time cannot be rounded down)
- paying the employee for the part day owed.
- carrying the part day forward to the next holiday year.

The Department for Business Enterprise and Regulatory Reform provides relevant links to help you work out your holiday entitlement in addition to other useful guidance. It can be found at www.berr.gov.uk/whatwedo/employment/holidays/index.html However do contact us if you require any other assistance.

