

# NEWSLETTER



## BAXTERS

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## Complex but changing

One of the Government's early actions in July 2010 was to establish the Office of Tax Simplification (OTS) to provide independent advice on how to reduce the complexity of the existing tax system. The Chancellor even stated in his Budget 2011 speech that:

'Our tax code has become so complex that it recently overtook India to become the longest in the world!'

The initial task of the OTS was to carry out two reviews. The first was to list all reliefs, allowances and exemptions applying to businesses and individuals and identify those reliefs that should be repealed or simplified to support the objective for a simpler tax system.

Following the publication of the initial report the Government intends to abolish 43 tax reliefs whose rationale is no longer valid. A minority of redundant reliefs will be repealed in Finance Bill 2011. The other reliefs will be removed after consultation.

The second task was to identify the areas of the tax system that cause the most day-to-day complexity and uncertainty for small businesses and recommend priority areas for simplification. That initial report has resulted in the announcement that the Government will consult on the integration of the operation of the income tax and national insurance systems. This major structural change will take time to properly consider but we will keep you updated on any important developments.

## SUMMER 2011

### Employer Penalties

Employers who fail to pay their PAYE liabilities on time every time and in full may face penalties.

Since 6 April 2010, HMRC have had the right to impose late payment penalties on all employers, regardless of size, who fail to make their monthly or quarterly PAYE payments on time. The payments covered by these rules not only include PAYE but National Insurance contributions, Construction Industry Scheme deductions and Student Loan deductions.

Unfortunately some employers may be blissfully unaware that a penalty may be due as HMRC's approach during 2010/11 has been to issue a warning letter only, and even this has been at their discretion. The receipt or not of such a warning letter is not necessarily an indication that a penalty notice will be levied. In fact HMRC have up to two years after the payment default to issue a penalty notice. The penalties are risk assessed so HMRC may not charge the penalties to all late paying employers. However, HMRC have made it clear that such notices will start to be issued from May 2011.

#### So how do the penalties work?

No penalty will be imposed for the first late payment in a tax year but subsequent breaches may attract penalties from 1% to 4% depending on the number of late payments of PAYE/

NIC etc per tax year. A further penalty of 5% may be charged if any amounts are still outstanding after 6 months and then again after 12 months.

#### Don't owe anything?

It is important to let HMRC know that you have nothing to pay either by:

- completing the online form: [www.hmrc.gov.uk/payinghmrc/payee-nil.htm](http://www.hmrc.gov.uk/payinghmrc/payee-nil.htm)
- sending a signed payslip with the amount completed as "NIL"
- phoning 0845 3667816 with your HMRC accounts office reference and advising them which period no payment is due for.

#### Late returns

2010/11 also saw the demise of the seven days' grace for filing the P35 and P14 end of year returns which have to be filed by 19 May following the end of the tax year. These annual returns need to be filed online by almost all employers. Penalties for late filing of these returns are currently fixed at £100 per month for every 50 employees.

Please get in touch if you want help with payroll issues or you have received a penalty notice which you would like us to check.



# Tax credit errors

In the autumn Comprehensive Spending Review HMRC, like the majority of government departments, were given strict targets to meet over the next four years.

The main headlines were:

- a 15% reduction in costs required before 2015
- £900m to address the tax gap and tackle tax avoidance and evasion, bringing in an additional £7bn per year by 2014/15
- £100m to improve the operation of PAYE
- measures to deliver £8bn of tax credit fraud and error savings by 2014/15
- a five-fold increase in criminal prosecutions
- a new dedicated team of investigators to crack down on offshore evasion and
- improving the scope of in-house debt collection and placing up to £1bn per year of tax to private sector debt collection agencies.

HMRC are starting to make progress in some of these areas and have recently launched a campaign to target suspected fraudulent tax credit claims from the self-employed. According to HMRC, in 2008/09 675,000 tax credit awards (8.9%) had errors relating to income. The potential loss was £145m.

HMRC have been writing to 12,000 self-employed people who are claiming tax credits where they believe that those claims are not genuine or accurate.

This is part of a wider government crackdown and HMRC and the Department for Work and Pensions have published a strategy designed to tackle error and fraud in benefits and credits.

Exchequer Secretary to the Treasury David Gauke said:

‘HMRC is determined to take a tough approach to targeting possible fraud among tax credit claimants. Last year the Government launched radical proposals to reduce the billions lost to tax credit error and fraud every year. These losses are unaffordable and unacceptable.’

HMRC will now use credit reference agencies and data-matching to spot patterns of fraud. The department is also employing additional investigators and are examining each claim in high-fraud areas.’

If you have any concerns about tax credits, please do get in touch.

# Getting the VAT job done with the right tools

HMRC toolkits are issued to help taxpayers and agents to file accurate returns. They focus on common problem areas for both direct taxes and more recently VAT. VAT toolkits issued so far include such areas as Input VAT, Output VAT and Partial Exemption.

As well as covering specific technical areas the toolkits emphasise the need for better record keeping. This is critical as penalties may be incurred for filing incorrect returns (including VAT) particularly if documentation is not available to support the figures in the returns. The rest of this article examines some of the key issues outlined in the recently issued VAT toolkit on Output VAT. Further areas are considered in the toolkit itself.

## Output VAT problems

Outputs are often incorrectly accounted for on occasional, miscellaneous and incidental transactions, including on deemed supplies. For example, deemed supply occurs when the business gives away gifts to one person costing more than £50, or a series of gifts to the same person, or puts goods or assets to non business use. Output VAT must be charged by the business to itself on the value of these transactions. This is commonly seen in the calculation of the fuel scale charge for supplies of fuel for private motoring, but many taxpayers seem unaware of the need to calculate the tax on other such supplies.

## Not a pool car

There have been several recent Tribunal cases which illustrate the dangers of the tax rules on what are generally known as pool cars. Pool cars are tax efficient as there is no taxable benefit. However, as always, there is no such thing as a free lunch.

The conditions for a car to be regarded as a pool car and so tax free are:

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

In the first case, HMRC carried out an Employer Compliance Review and found that the company had provided the taxpayer with vehicles for several years. The taxpayer claimed that the vehicles were pool cars but no one else was available to use

For businesses using the flat rate scheme, using incorrect percentages and incorrect turnover figures are common problem areas. This is especially going to

be an issue for VAT returns spanning the change in the standard rate of VAT on 4 January 2011. The new flat rate percentages must be applied to turnover from 4 January 2011. Businesses must ensure they use their new flat rate percentage, rather than just adding 2.5% to their old flat rate percentage. A revised table has been issued for this purpose. This can be accessed at [www.hmrc.gov.uk/vat/start/schemes/flat-rate.htm#sa](http://www.hmrc.gov.uk/vat/start/schemes/flat-rate.htm#sa)

Other errors regarding output VAT include incorrect zero rating of exports outside of the EU and dispatches to other EU countries. These supplies can only be zero rated when supporting documentation to prove movement of goods is held. For EU dispatches, the customer's VAT number must be obtained and quoted on the invoice for zero rating to apply.

So finally, if you would like any help in calculating output VAT or any other aspect of VAT please do not hesitate to contact us.



them as staff that needed cars for official use had other pool cars available.

The Tribunal found that the vehicles were not pool cars and that:

‘...the Appellant's lack of fiscal knowledge had caused him to fall foul of (the rules) which in his case became penal causing him to become liable to a car benefit charge based on the £51,000 list price of the cars which amounted to £9,156 per year. The independent dealer value of the cars having regard to their age was some £6,000 for each car meaning that the Appellant could have bought the cars for less than the tax arising on the car and fuel benefit.’

In the second case, a Mercedes Benz CD320CDI, owned by the company of which the taxpayer was a shareholder and director was claimed a pool car.

The taxpayer stated that the Mercedes was kept in a steel container at the factory and that it was never taken home. It was also only used to visit customers. However, there appeared to be no mileage log. The Tribunal found that the taxpayer failed to provide satisfactory evidence to show that all five conditions were met.

The message is clear – the key to tax free success is to ensure all conditions are considered and in particular, proper records maintained. Please do get in touch if you would like to discuss this area further.

# Let's go Real Time - the future of PAYE

In July 2010 HMRC issued a Consultation Document looking at major reforms of the PAYE system using real time information. You may have read or heard about elements of the system but we thought that we would try to dispel a few myths.

The project consists of two separate elements:

- Real Time Information (RTI) would collect information about tax and other deductions automatically each time employers ran their payroll. This information would be submitted automatically to HMRC at the same time employees were paid.
- Centralised Deductions (CD) would build on RTI by moving the responsibility for calculating and deducting tax, national insurance and student loan repayments from employers to the electronic payment system.

It appears that the Government have decided to proceed with a phased introduction of RTI with a pilot beginning in 2012 and then implementation from April 2013. It also appears that CD will only be considered once RTI has been fully introduced and this seems unlikely before 2015.

## RTI

With RTI, employers paying employees electronically would send HMRC details of employees' pay, the deductions of tax, NIC and student loan repayments and information about employees' identities.

The information would be produced automatically by the payroll system at the point of making the payment and would be sent to HMRC via the electronic payments system as part of the payment instructions.

HMRC think that this could simplify the processes when people change jobs, with no need to complete a P45/46 but with a notification through the new electronic system. Individuals changing jobs in the year would be more likely to pay the right amount of tax. It could also do away with end of year information. Access to real time data would also improve the benefits and tax credits

system, with better administration and reductions in fraud, error and overpayment.

The basic process would be:

- most employers would be required by regulation to use the Bacs system to transmit RTI information with payment instructions;
- a common standard will be used for the transmission of RTI data at all stages of the payments infrastructure from payroll software through banking interfaces and Bacs submission software to the Bacs system itself;
- smaller employers (fewer than 50 employees) who do not pay their employees via Bacs will initially be able to submit RTI from their software, or via an agent, using an internet channel through the Government Gateway.

Employers would still need to issue payslips to their employees and issue P60s at the year end.

## CD

The basic concept is that HMRC would construct a central calculator to work out the correct deductions of tax, national insurance and student loan repayments from an individual's pay. The employer would send the gross payment through the electronic payment system to the central calculator where the deductions calculated by HMRC would be made automatically. The resulting net payment would then be sent to the individual's bank account and the deductions would be paid directly to the government.

As employers would no longer be responsible for the tax, they would not need to operate tax codes.

Obviously, things are in their infancy and there will be a lot more information to come in future months. We will keep you fully informed of developments.



# Minimizing IHT by maximising relief

Agricultural Property Relief (APR) is an important relief for landowners as it reduces the value charged to Inheritance Tax (IHT). During lifetime it is available to relieve a charge that might arise on a gift to trust. At death it has the effect of providing IHT relief on both estate assets and reducing any additional charges on lifetime gifts. The rate of relief is frequently 100% although some tenanted land only secures 50% relief to the owner. It is also necessary that the owner either occupied the property themselves for the purposes of agriculture for the two years prior to a transfer or that the property was occupied by someone else for the purposes of agriculture in the seven years prior to transfer.

A significant change in the scope of APR has been made following pressure from the EU. The relief used to be limited to property in the UK, Channel Islands and the Isle of Man but is now extended to property situated in the European Economic Area. This relief is effectively backdated although time limits mean that the earliest year which may now benefit is the tax year 2007/08.

The property must fall within the definition of agricultural property. Bare land used for agriculture qualifies without restriction. Problems can arise where a claim is made for APR in respect of buildings, especially residential buildings on the farm. The requirement is that the buildings must be occupied for the purposes of agriculture and must be of a character appropriate to the agricultural property.

A recent case has held that a property left unoccupied because the farmer was in hospital and then a nursing home could still qualify because all his effects were still in the property and he was playing an active role in the business almost up to his death.

The issue of large residences claimed as farmhouses remains a problem area and one in which HMRC are likely to take an interest. It is clear that HMRC expect to see that the farming operations are controlled from the house and will then consider whether its character is appropriate. This will involve looking at the physical size of the house and its relationship to the farm. A large property with a small area of farmland may struggle to qualify for relief. HMRC accept that the issue is a question of fact in each case.

## Agricultural purpose

Assuming that the property qualifies as agricultural property it must still pass a test of being used for agricultural purposes. These are not comprehensively defined in legislation, apart from one or two exceptions such as the breeding of racehorses on a stud farm which is given specific legislative approval. However other common farming activities do qualify and HMRC also accept that seed and tree nurseries and growing grass for turf all qualify. On the other hand, occupation for livestock other than for food for human consumption does not qualify. Neither does sporting rights nor the use of land for purposes other than agriculture such as grouse moor. Schemes to preserve habitat for wildlife will generally qualify if it is managed in the right way.

This relief and other IHT reliefs may be available on lifetime gifts as well as on your estate so if you would like us to review their availability please do not hesitate to contact us.

# Funding not to be taken for granted

Obtaining finance to help start, grow or develop a business can be a difficult task. However, grants and other financial support may be available to help the business realise its potential.

Grants are contributions awarded to businesses or individuals to assist with specific projects or activities. These can be obtained from a number of different types of body which include government departments, local development agencies, local authorities or councils and charitable organisations.

Investment in growth is a key objective of the current Government. Grants and other methods of support, therefore, are still available to both new and established businesses in spite of spending cuts on the whole.

Eligibility for grant funding can be dependent upon your location, business size and industry sector. Some areas, for example, are eligible for government funding through schemes to improve local social deprivation or unemployment.

Grants or other support can be obtained to provide funding for a diverse range of purposes. Some key types of support include:

- **Investment in capital to create new jobs or safeguard existing ones**  
Government grants have previously been available for investment in business through various grants. Grants within this remit are often still offered at a local level.
- **Investment in environmentally friendly assets**  
0% loans of £3,000 to £100,000 are available from the Carbon Trust.
- **Activities stimulating regional development**  
Regional development agencies, often distributing European funding, offer a range of grants to businesses to develop their local area.
- **Investment in innovation, research and development**  
Government grants are available to small and medium sized businesses for the research and development of technologically innovative products and processes. Grants are often made which cover a proportion of costs directly attributable to the activities.
- **Employment and training**  
A number of different types of grant are available ranging from those helping with additional costs incurred in employing disabled employees, to those helping with training and staff development expenditure.

## Applying for a grant

The exact nature of the application will differ dependent on the type and source of funding being applied for. Formal application will normally be preceded by discussion with the funding body. The application is likely to then require completion of the relevant paperwork in addition to a sound business plan, as the overall pot for funding is often restricted.

Monies received will often require match-funding and performance criteria to be met, with a potential claw-back where funds are not used for their designated purpose.

The process of obtaining grant funding can be daunting due to the detailed information requirements of the application but we can assist with the process, or in preparation of a business plan.

So if you are thinking about applying for grant funding, please contact us to help you secure the best outcome.

# Short life not short thrift

Some unwelcome capital allowance reductions are set to come into operation from April 2012 but it's not all bad news.....

## First the bad news

The Annual Investment Allowance (AIA) provides 100% relief on qualifying plant and machinery expenditure but it is to reduce from £100,000 to just £25,000. Further, the main writing down allowance (WDA) which applies generally to any expenditure in excess of the AIA in the current period (or brought forward from previous accounting periods) will reduce to 18% annually from the current rate of 20%. This means lower tax relief on expenditure in the period of acquisition and delayed relief in later years for both unincorporated and corporate businesses.

## But it gets better

One way of obtaining more capital allowances earlier is to make a 'short life asset (SLA) election'. This facility has been available for many years but the 2012 changes and an announcement in Budget 2011 has put the SLA back on to centre stage.

Up until now it has been possible to make a SLA election on most assets with an expected useful life to the business of four years or less from the end of the accounting period of acquisition. Fast moving technology like computers would be a good example of a potential SLA. However, cars are specifically excluded from SLA treatment. Such an election means that the asset is placed into a single asset pool for capital allowance purposes. Initially it is eligible for the same allowances (AIA and WDA) as would have applied if placed in the main plant pool. However, on disposal, where there is an unrelieved balance of expenditure, an extra allowance can be claimed. This equates to writing off the whole cost of the asset over its economic life to the business. In fact, a SLA election should only ideally be made on assets which are likely to lose value quicker than they receive tax relief. This is because where assets hold their value well this could result in a clawback of some or all of the tax relief given.

Many small (and possibly medium too!) businesses have not found it advantageous to make SLA elections on additions since April 2008 due to the availability of the AIA. Most small businesses found that the AIA covered their additions in full, thus full tax relief was obtained in the year of

acquisition. The AIA reduction from April 2012 makes the SLA election more attractive to a wider range of businesses.

## And better

The lifetime period for SLAs has been extended to eight years from the end of the accounting period of acquisition for additions on or after 1 April 2011 for companies or 6 April 2011 for the self employed. This makes it more useful as it means more assets could benefit from SLA election.

### Example

A business purchases qualifying plant for £100,000. It has an estimated business life of 6 years and no scrap value.

- If acquired in the year to 31 March 2012 it would be totally relieved by the AIA and a SLA election would not be worthwhile.
- If acquired in the year to 31 March 2013 and no SLA election is made then total allowances over the 6 year period would be £77,200 comprising the £25,000 AIA and £55,200 WDA over the 6 years. Further tax relief will continue to be obtained in future years after the asset has gone!
- If instead a SLA election had been made on this asset acquired in the year to 31 March 2013, the shortfall still unrelieved in year 6 could have been claimed meaning an extra £22,800 overall.

## The best for last

This would be worth a minimum £4,560 in tax saving (based on the current basic rate of income tax excluding any national insurance saving or alternatively the small company corporation tax rate) and significantly more for individuals and companies subject to a higher rate of tax.

If you would like any advice on these changes, or capital allowances in general, please do not hesitate to get in touch.