



# BAXTERS

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## More Taskforces!

As widely reported in the press the Government have made an investment in HMRC of over £900m to crack down on tax avoidance, evasion and fraud with the aim of raising an additional £7bn each year by 2014/15.

One line of attack by HMRC to tackle evasion and avoidance is the use of taskforces. These bring together various HMRC compliance and enforcement teams for intensive bursts of activity targeted at specific sectors and locations where there is high risk of tax evasion. The first taskforce was launched in May 2011 and according to David Gauke, the Exchequer Secretary:

'HMRC is on target to collect more than £50 million as a result of taskforces launched in 2011/12'.

The most recent campaigns are aimed at:

- The rag trade - expected to recover over £9 million they will target manufacturing, wholesale, retail and textile recycling in the Midlands, North Wales and the North West
- Rental property - expected to recover nearly £4 million in the rental property sector in the South East
- The alcohol industry - expected to recover around £4 million in Scotland.

If you have any concerns that you may be affected by these taskforces please contact us for further information.

## SPRING 2013

### BRC are now up and running

On 1 November 2012, HMRC started a 'new approach to Business Records Checks' (BRCs). The target audience of these checks are small and medium sized businesses.

In the context of income tax, a BRC is a check by HMRC that the records of a business are adequate to allow a taxpayer to submit an accurate income tax return. What is new is a check on records which will be used to prepare a tax return rather than HMRC checking a tax return that has already been submitted.

#### What are adequate records?

This is one of the difficulties. Unfortunately there is no precise answer to this question. For a trading business, the following would be regarded as adequate records:

- a record of all sales and takings, including cash receipts. For example till rolls, sales invoices, bank statements, and paying-in slips.
- a record of all purchases and expenses, including cash purchases. For example purchase invoices, receipts, bank and credit card statements, and cheque book stubs.

#### Why might a business be selected?

HMRC select a number of businesses based on their view which are more likely to be at risk of having inadequate records. The criteria for HMRC's computer driven risk analysis is not known but, for example, a business with a lot of cash transactions is likely to be seen as higher risk.

#### What is involved in a BRC?

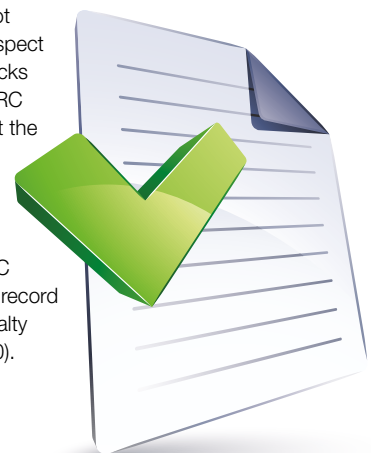
After the selection process the following may happen.

- HMRC will contact the business, initially by letter, advising that the business has been selected for a BRC and HMRC will get in touch, normally by phone, within a few days.
- In the phone call, HMRC will ask approximately 15 questions about the business records to help them determine the adequacy of the records.
- If HMRC decide you are at risk of keeping inadequate records they will state that you need a face to face visit.

#### What action should you take?

If you do receive a letter, we would recommend that you contact us as soon as possible. We can then advise you as to the best course of action.

Please do not take the prospect of these checks lightly. If HMRC consider that the records are inadequate and no changes are made, HMRC may apply a record keeping penalty (usually £500).



# Capital complexity?

The biggest surprise in the Chancellor's Autumn Statement was the tenfold increase in the Annual Investment Allowance (AIA) only months after it was reduced. However, the way the increase is being introduced is not necessarily straightforward.

The AIA provides a 100% deduction for the cost of plant and machinery purchased by a business up to an annual limit which is:

- £100,000 up to 1 April 2012 for companies (6 April for unincorporated businesses)
- £25,000 up to 31 December 2012
- £250,000 from 1 January 2013.

It will revert to £25,000 from 1 January 2015.

So if you incur expenditure on plant from 1 January 2013, you can spend up to £250,000 and get a full tax write off then? Well, not quite.

There are three main points to note. The first two have always been a feature of AIA:

- there is no AIA on some plant – the main exclusion being cars
- the AIA limits may need to be shared with other businesses which are under common ownership
- if the accounting period of the company straddles 1 January 2013, there are special rules being introduced which may restrict the AIA to a much lower figure in the straddling accounting period.

Where a business has an accounting period that straddles the date of change the allowances have to be apportioned on a time basis.

## Example

A company has a 12 month accounting period ending on 30 June 2013 (which started on 1 July 2012). The AIA will be £137,500 (£25,000 x ½ + £250,000 x ½).

However, for expenditure incurred before the 1 January 2013, new legislation will be introduced to limit the maximum figure available. The maximum allowance will be the AIA that would have been due for the whole of the accounting period to 30 June 2013 if the increase in AIA had not taken place. This would have meant that the company would have been entitled to £25,000 for the 12 month period and so this is the limit for the six months to 31 December 2012.

On 1 January 2015, the AIA will revert back to £25,000. This will mean that the same company will have an AIA in later periods as follows:

Accounting period to 30 June 2014	£250,000
Accounting period to 30 June 2015	£137,500

## Tips

*The main point to appreciate is that expenditure incurred after 31 December 2012 may give a full tax write off but expenditure incurred before the 1 January 2013 may not give this result. In the example, if the company had spent £40,000 in the first six months of the accounting period relief would be limited to £25,000. The company can spend £112,500 (£137,500 - £25,000) in the six months to 30 June 2013.*

*If the company is planning capital expenditure in excess of this figure, then it may pay to defer the expenditure (or part of the expenditure) until after the end of the current accounting period as the full £250,000 AIA may be available. In the example above, the company could spend £250,000 in July 2013.*

The special rules are published as draft legislation and so some of the detail may change. Please contact us if you are about to incur a significant amount on plant so that we can best advise you.

# Running your business as a company - time to reconsider?

For many people running a business through the medium of a limited company makes sense due to the income tax and National Insurance savings that can be made. But for some people whose business has become very small, perhaps because they are winding down their workload, the extra administrative costs of running a company may not be appropriate.

So is it easy to transfer the business from a company back to individuals? The short answer is no due to the tax costs of the transfer. This has to be viewed from two perspectives:

- the potential corporation tax charge for the company of disposing of any premises and goodwill to its shareholder(s) and
- the tax position of the recipient shareholder(s).

Goodwill for example is a key issue as the transfer of the business by the company is, without any relieving provisions, a disposal at market value. If the original cost to the company is nil (as it often is), the market value is a gain/profit which is chargeable to corporation tax.

So the Government has introduced draft legislation which may make the transfer easier for a small business. This will relieve the tax charges on the

company when certain assets are transferred to the shareholder(s) who will run the business as an unincorporated business.

There are limits to the assets in the company qualifying for this relief. It will not be available if the combined value of goodwill and any premises which are owned by the company (and from which the company trades) exceed £100,000. If the trading premises are owned by the company this limit is likely to be exceeded but the premises may already be in the direct ownership of the individual(s) so this aspect of the problem is removed. However, it should also be noted that business goodwill can be very difficult to value. Caution is required before taking this route.

## Shareholder position

The proposals do not extend to cover any specific relief from tax charges for the recipient shareholder(s). This means that the transfer of the goodwill and other assets of the business will be treated as a distribution to the shareholder at market value. Income tax or capital gains tax may be payable by the shareholder(s) as a result. However,

the following will help to minimise tax charges arising:

- where a distribution of assets is classed as income, there will be no additional tax charge to the extent that the distribution is within the basic rate band and
- where the company is wound up (which is likely) so that the distribution is capital, the capital gains tax annual exemption might be available to cover some or all of the capital gain.

If you are interested in disincorporating your business do please talk to us. We can advise you whether use of the new relief is appropriate for you but we may also be able to show you that continuing to run your business as a company saves you tax.



# Enterprising employees

On 8 October 2012 the Government announced its intention to introduce a new 'employee shareholder' employment status. Individuals adopting the status will receive between £2,000 and £50,000 of Capital Gains Tax (CGT) exempt shares. They will have to give up certain employment rights in exchange for shares in the employer company.

The normal tax and National Insurance rules attaching to shares acquired by reason of employment will apply, including corporation tax relief and no stamp duty payable on issue. The shares will be valued according to their unrestricted market value at the time they are awarded and the company would have to buy them back at a reasonable value on surrender.

## In exchange

The rights that will have to be given up will include employment rights for unfair dismissal in some cases, certain rights to request flexible working and training and statutory redundancy entitlement. Additionally 16 weeks' notice of the intention to return early from maternity or adoption leave (compared to 8 weeks' notice for other employees) will have to be given.

Employers can choose to operate this new employment status. All types of shares will be eligible for use and will take effect as part of a contractual arrangement between employer and the employee. Companies of any size will be able to use this status.

If you are interested in discussing this further please contact us for further information.

# And more enterprising incentives!

The Enterprise Management Incentive (EMI) scheme is an approved statutory share option scheme. A qualifying share option scheme offers employees (known as 'granting the option') the opportunity to purchase shares at a later date, generally at the market value prevailing at the date of the original offer. When the shares are actually purchased, this is known as exercising the option. As EMI is a tax advantaged scheme this generally means there is no income tax or National Insurance liability when the options are granted nor when the shares are exercised and the shares acquired. Instead, on a disposal of the shares any profit made is charged to capital gains tax which would probably be at the 28% rate in many circumstances. The scheme is intended to help qualifying trading companies recruit and retain key employees and is available where a company's gross assets do not exceed £30 million.

In Budget 2012 the Government announced its intention to relax the Entrepreneurs' Relief (ER) rules for capital gains tax in so far as they affect EMI shares so that they can easily qualify for the relief on a disposal by an employee of the company. This would mean that any resulting gain will be taxed at 10% as long as certain conditions are met.

## ER before the changes

The current ER rules require that throughout the period of 12 months immediately preceding the disposal:

- the claimant held a minimum 5% of the ordinary shares in the company and
- the company was a trading company or the holding company of a trading group and
- the claimant was an officer or employee of the company or one of the trading group companies.



## Comment

*In many cases employees with EMI acquired shares would not qualify under the 5% minimum ownership rule. In addition ER is only available on shares owned for 12 months and ignores the time the option is held. In many option situations, shares are sold shortly after acquisition.*

## The proposed changes

Legislation will be introduced in Finance Bill 2013 and will apply to eligible shares acquired on or after 6 April 2012 that are disposed of on or after 6 April 2013.

- The requirement that the person must hold a minimum of 5% or more of the ordinary share capital in the company will be removed.
- Additionally, the 12 month minimum holding period requirement will include the period the option is held.

The impact of this is to further enhance the tax advantages of the EMI scheme to promote such schemes to small and medium sized enterprises.

If you would like to discuss if the EMI would be of value to your business and the conditions which need to be satisfied to implement such a scheme please contact us for further advice.

# Family pension plans

An individual has an annual pension contributions limit for tax relief purposes. The limit applies to contributions whether made by the individual or by another person such as an employer. From 2011/12 this allowance was reduced from £255,000 to £50,000 and will reduce to £40,000 from 2014/15 onwards.

Some employers not only offer pension plans to their employees but also make contributions to a registered pension scheme for family members as part of their employees' flexible remuneration package. However, in response to the lower annual allowance limits placed on the individual employee from 2011/12 these types of arrangement have been used to side step the new rules for employees who would have faced an income tax charge on contributions in excess of the £50,000 limit.

Currently whether payments are made to the employee's own scheme or that of a family member, as long as the contributions are made

to a registered pension scheme and are within the annual limit for each individual then no tax charge arises. The effect is that the employee is exempt from income tax and National Insurance (NI) on the employer's contributions into a family member's pension scheme. In other words, these contributions do not count towards the £50,000 limit for the employee, thus avoiding the income tax that would otherwise be due on the employee for contributions in excess of the limit.

## Changes ahead

With effect from 6 April 2013 employees will no longer enjoy exemption from income tax

and NI on such contributions into a family member's pension scheme. Employers will have to report such payments in line with other employee benefits and the payment will be subject to employer NI.

If you would like to discuss this further or require any advice regarding pension planning please contact us for further information.



# Simpler tax for the smaller business?

The Chancellor is to proceed with proposals to make the tax system simpler for the small unincorporated business with an optional simplified cash basis. The scheme is not available to companies but is available to general partnerships.

Where a business has a turnover up to the VAT limit (currently £77,000) it will be able to calculate its profits on the simplified cash basis rather than full accruals accounting basis. In addition, it will not have to distinguish between revenue and capital expenditure. This means that capital expenditure on asset acquisitions will generally be deductible when paid with certain exceptions such as cars and premises. A business will be able to continue to use this basis until its turnover reaches twice the VAT limit (currently £154,000).

All unincorporated businesses will be able to claim a range of expenses on a flat rate basis rather than having to identify actual amounts spent. This facility will be available whether or not the simplified cash basis option is used. Flat rate allowances to be available include:

- **Cars, vans and motorcycles**

For cars or vans the rate for the first 10,000 business miles is 45p, after which the rate reduces to 25p. For motorcycles the rate is 24p. These rates are mandatory for users of cash basis.

- **Business use of a home**

Provided certain conditions are satisfied, the following monthly rates will be allowed:

Business use in a month	Deduction
25 hours or more	£10
51 hours or more	£18
101 hours or more	£26

The new rules are not quite as simple as the Government would have us believe. Whilst the actual accounting treatment may be simpler it will still be necessary to have regard to tax rules for the deductibility of some expenses.

One negative point is that there will be no facility to relieve a trading loss against other personal income. Rather it will have to be carried forward for relief against future trading profits.

If you think this may be of interest to you and require further information then please do get in touch.



## Boxing with National Insurance

A recent case concerning the structure of a motor expense policy demonstrates the importance of understanding how the tax and National Insurance (NI) law is constructed when considering alternative expense and other remuneration strategies.

Cheshire Employer and Skills Development Limited (formerly Total People Limited) was engaged in the provision and placement of apprentices and other trainees with employers and the supervision of their training. The company employed training advisers who were required to visit the employers and the trainees at their place of work.

Motor expenses were paid to the employees as necessary but most of them were paid to the training advisers.

The staff handbook provided two options for the payment of travel expenses:

- a cash entitlement of 12p per mile plus a lump sum or
- mileage expenses of 40p per mile (the statutory rate at the time).

However, in practice, the staff likely to perform extensive business travel, were not given the option to elect for the 40p rate. The lump sum entitlement was the only option for employees travelling at least 2,500 miles per annum. The level of the lump sum was set according to salary and was paid by monthly instalments and the contracts of employment did not show the lump sum as part of salary. Increases in the lump sum payment were not linked to increases in salaries and were at a much lower level and occurred less frequently.

The company claimed a refund of NI which it considered it had wrongly paid in respect of the lump sum payments. HMRC refused to make the repayment.

### Round 1 to the taxpayer

At the First Tier Tribunal (FTT) the company argued that the payments were not earnings but were relevant motoring expenditure and therefore exempt from NI. The Tribunal agreed with the company as there was no link between any increase in salary and the increase in motoring expenses. HMRC had argued on the basis that there was a contractual entitlement to the lump sum, the amount paid differed depending on the grade of the employee rather than the grade of the car and that there was no correlation between the amount paid and the distance travelled. HMRC then appealed.

### Round 2 to HMRC

The Upper Tier Tribunal (UTT) established that there was no link between the payment and the use of the vehicle and agreed with HMRC that the payments were not relevant motoring expenditure and were emoluments of employment liable for NI.

### And the final decision...

The company appealed to the Court of Appeal on the basis that the FTT had not made an error of law in reaching its conclusion on the earnings point. If it had not made an error of law, then the UTT had no jurisdiction in overturning the decision. The Court of Appeal decided that the FTT had not made such an error and the company's appeal was allowed.

If you have any concerns regarding any aspects of your remuneration and expense policies please contact us for further advice.