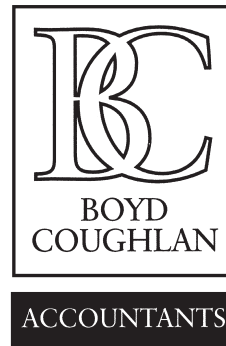
2008 AUTUMN NEWS



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Fasten your seat belts

The financial world seems to be falling apart so quickly that it is hard to imagine what will happen next. We were shaken last year by what happened to Northern Rock: the Americans seem to be doing everything larger than the UK as usual, with bigger catastrophes and bigger rescue packages. The Stock Market behaves like a yo-yo and politicians blame "the credit crunch" as if a force of nature outside all human control had taken over the world's economy. It's enough to make the Chancellor's hair turn white.

Meanwhile, life goes on: what does all the turmoil mean for you and your finances? The media can spread panic about investments that are safe – the scare-stories may then become self-fulfilling prophecies. For example, bank deposits were protected up to £35,000, and this has now been increased to £50,000 – but even so, some savers were withdrawing their money from HBOS on rumours that the bank was in trouble.

Even if the roller-coaster seems to be outside anyone's control, there are still things that individuals can do to help their own situation. It's important to understand how your finances are affected – for example, if you have a fixed rate mortgage deal that is coming to an end, what will happen then? If you have buy-to-let investments that may have fallen in value, what does that mean? If you want an objective second opinion on your finances, we will be happy to help.

Meanwhile, we are hoping that Mr Darling is too busy with the big picture to think of any new taxes to impose in his Pre-Budget Report later in the year – but don't bet on that. ●

Rock bottom

Those people who had deposits in Northern Rock should not have suffered any losses. Those people who owned shares in the "credit crunched" bank were not so lucky. The bank was taken into "temporary public ownership" by the Government, and any compensation to shareholders is to be considered by an independent valuer. HM Revenue & Customs have said that the nationalisation triggers a disposal at a loss for CGT purposes. If the shareholders get compensation, that will be taxed in the year in which it is received.

Anyone who was awarded shares in the demutualisation of Northern Rock in 1997 will feel that they have lost money because the shares were worth something and they have been paid nothing – but the shares came with no cost for CGT purposes, so there won't be an allowable loss.

If you held shares in Northern Rock – or in any other company that has been brought down by the economic slowdown – we will be happy to advise you on how you can obtain relief for the losses you may have suffered. ●

Overtaxed, over here?

The dust is settling on the changes Mr Darling announced last year to tax for foreign domiciled people who live in the UK. They have in the past been allowed not to pay UK tax on foreign income and gains as long as they leave the money overseas. In 2008/09, anyone who's been tax resident here for 7 of the last 10 years will have a choice: pay tax on income and gains as they arise, or pay a flat rate charge of £30,000. It's easy to work out that "normal" tax will be cheaper on foreign income up to £75,000 – at 40%, the result will be less than £30,000.

There's an important exception: if your foreign income and gains total less than £2,000 in a year, you can still leave the money offshore and off your UK tax return. Between £2,000 and £75,000, you will need to declare it. Above £75,000, you need to think about it – or think about leaving the UK, which some have threatened to do.

The Government has also closed down a number of other loopholes that have been exploited in the past by foreigners living here in order not to pay the normal rates of tax. It remains to be seen whether this will bring in any more cash, or whether it will lead to that money leaving the country altogether.

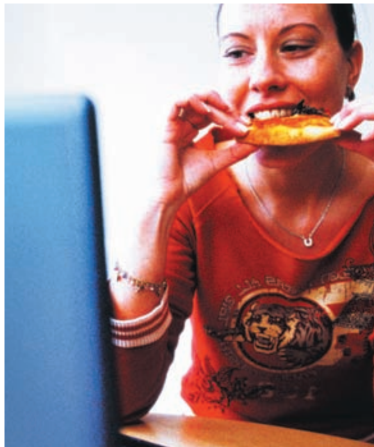
These rules are new and complicated and the details have many catches in them. The one thing that is certain is that anyone who has in the past relied on the remittance basis of taxation – paying tax in the UK only on bringing the money here – needs to look closely at what they do from this year on. We will be happy to discuss the issues if you are affected. ●

Counting the days

Part of this year's crackdown on "foreigners not paying their fair share of tax in the UK" is a change to the way non-residents count the number of days they spend here. Tax exiles can generally visit the UK for up to 90 days a year without putting their tax advantages in jeopardy, and up to now the taxman has very generously ignored days of arrival and days of departure. Someone who arrived on Monday and left on Friday would only count 3 days.

From 6 April 2008, a day is counted if the person is in the UK at the end of the day, unless they are a passenger in transit to somewhere else. There are some detailed and complicated rules about that, so if you are one of those who has to keep a record of your days in the UK, we'll be happy to explain to you what's changed. ●

Home office



The electronic age has made working from home much more common. No commuting, no parking problems, no boss breathing down your neck, permanent dress-down Friday. This may or may not lead to greater productivity, but more and more people are spending part of their working lives in the house.

The tax question is then whether the cost of running the house becomes a deductible expense for tax. The rule is that the employer can reimburse extra expenses without the employee becoming taxable: but what is extra? For example, an employee may need a broadband connection in order to work from home – but if the employee already has one, the employer taking over the bill would create a taxable benefit because there would be no extra cost.

For several years the taxman has been prepared to allow a measly £2 a week to be paid by the employer to the employee tax-free without having to justify the amount. This covers the likely extra costs of heat and light which arise from being in the house rather than being in the employer's premises. From April 2008 this has gone up to £3 a week. Bear in mind that this does require that the employee works from home some of the time – you cannot simply pay everyone £3 a week tax-free!

You can also pay and claim larger amounts if you are able to justify them. For example, the provision of equipment that is necessary for the employee's job will not create a taxable benefit. If you work from home, or employ people who do, we will be happy to discuss ways of making the arrangement tax-efficient. ●

Trust in money

There's an old saying – probably thought up by a lawyer – "don't put your trust in money, but do put your money in trust". The idea is that someone you trust – maybe that lawyer again – can take decisions about your money while you aren't able to, possibly after you're gone, in accordance with your wishes and instructions. It used to be possible to save a great deal of tax by using trusts, too – the trustees might pay a lower rate on income, gains and gifts than the person who put the money in or the people who were intended to benefit in the end.

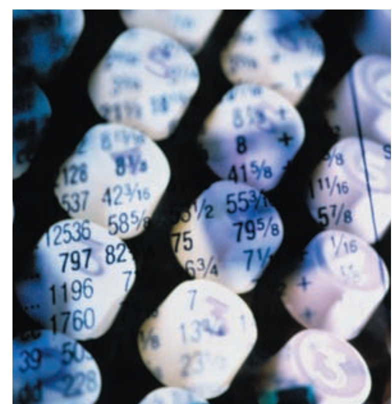
The tax advantages of trusts have been whittled away over the years and they are now not nearly so favourable. There are still plenty of non-tax reasons for having trusts, but the tax problems should make people think about whether to change their arrangements. An unusual one recently hit the courts: a man had set up a trust during his lifetime with the long-term idea that the National Trust would get a great deal of the money. Within a year of his death, the trustees followed his wishes. A gift to the National Trust is usually exempt from inheritance tax at death – but because of the unusual way in which this money reached the charity, 40% IHT was due.

If you have any involvement with trusts – whether you are the beneficiary or the settlor of a current trust, or you've put one in your will – it's worth looking at them again to make sure they do what you want them to and don't have any tax catches in them. We'll be happy to help. ●

Code breaking

Many people will have noticed that their PAYE code has recently gone up, probably by 60. This will probably have increased their take-home pay in September. This is the result of the Government's U-turn following the abolition of the 10% tax band in April. In May the Chancellor announced that everyone's tax allowances would go up in order to compensate the lower-paid who would be worse off without the starting rate. It has taken HM Revenue & Customs several months to get all the paperwork in place to put that increase in allowances into effect.

The first payslip after the change will have an extra increase in net pay because some of your PAYE deducted in earlier months will be repaid. After that it will settle down again to a slightly higher net amount than was being received earlier in the year. ●



Should know better

There's a certain satisfaction in seeing a tax dispute between HM Revenue & Customs and one of their own Inspectors. That seems a no-win situation for the individual – get a little tax relief and lose all prospect of promotion, or fail to win the argument and show that perhaps you don't know enough about tax. She lost.

It's a common argument: she had agreed with her employer that she could work from home for two days a week. So she had an office at home and an office in London, and she claimed that travelling between the two was a tax-deductible expense. If you travel between two different workplaces, that normally qualifies for a deduction.

The Appeal Commissioners didn't agree with her. Travelling from home to work is "ordinary commuting", and there's no deduction for that. Even though she had an office at home, it was still her home – so travelling from there to another "permanent workplace" was still commuting.

There was also nothing special about her job that turned the travel into part of her duties. There is an old case about an anaesthetist who was allowed the cost of journeys to hospitals when he was on call because he gave instructions on the phone before setting out – he was actually on duty from the moment he was summoned. The Inspector was simply going to the office. It's important to deduct travelling expenses when you can, and not to when you can't.

If you want to discuss what's allowable, we aim to understand the rules better than this Inspector. ●

Money for nothing

In 2004/05 the Government introduced incentive payments to encourage small employers – those with fewer than 50 employees – to make their annual PAYE returns online. The first two years qualified for tax-free payments of £250. The payments go on for another three years – £150, then £100, and just £75 for 2008/09. After that we are all supposed to have grown to like the system anyway so we will stick with it without having to be paid.

The Revenue were surprised that some people set up a large number of very small employers to take advantage of the system. The Government hurried through legislation to prevent payments to people who did this, but that only took effect on 8 April 2005. Did this mean that the scheme would work for 2004/05 if you got your returns in before that date?

An individual who set up 500 companies, which claimed to have paid £1 gross each to him as their director, applied for payments for 2004/05 and the following two years. He appealed against the Revenue's decision to refuse, but the Appeal Commissioner did not think his scheme was effective: the "pay" of £1 gross with 22p of PAYE did not represent a real movement of cash. As a result, the companies had paid no salary, so they were not required to make PAYE returns and were not entitled to the incentive payments.

For those people who really have employees, the incentive payment has been a sensible boost that has encouraged use of online filing – which, for small employers, can be simple and efficient. It was always likely that such a blatant abuse of the Government's generosity would not be allowed to work. The April 2009 returns are the last to enjoy the benefit – if you aren't using the system yet, we can help. ●

Last call?

Remember that the deadline for filing "paper" tax returns for 2007/08 has been moved forward to 31 October 2008. If your return is filed by that date, HM Revenue & Customs are committed to telling you how much to pay by 31 January 2009.

If you miss that deadline, you can still file a return online up to 31 January 2009. The Revenue's website crashed on the last deadline date because too many people were trying to use it at once, so it's better not to leave it until the last minute (even if they did extend the deadline because they admitted it was their fault).

If you send in a paper return after 31 October, you will be charged a £100 penalty – but that will be cancelled if all the tax due is paid by 31 January. You – or we – will have to calculate the liability to make sure that it is paid, because the taxman won't promise to do so in time.

If you have underpaid up to £2,000 and you want the underpayment to be dealt with in next year's PAYE code rather than "on the nail" on 31 January, you have to file your online return by 30 December. ●

Divvy up

It's standard tax planning for someone running a small company to make sure that they take out part of the earnings as a dividend. Dividends are generally taxed more favourably than salary in the hands of the shareholder-director. If you take a regular amount out of the company as salary, you have to account for PAYE tax and National Insurance through the year – if it's paid out as dividends, you settle up the tax through self-assessment and there's no NIC.

There is a catch, though: dividends can only legally be paid out of the company's profits. If the company hasn't got any profits – current year and brought forward in reserves – it isn't allowed to pay dividends. If you draw money out when there aren't profits, it can't be a legal dividend – you either have to call it salary and deduct PAYE, or you are liable to pay it back to the company.

The starting point for measuring available profits is last year's annual accounts. If they haven't got enough in to pay the current dividend, you need some interim accounts that will give a reasonably accurate picture – they don't have to have all the adjustments you'd make for final accounts, but they should show that there's enough profit to justify the dividend. In a recent case, a director was held to be liable to repay some dividends because he had received professional advice that the company didn't have any reserves – after that, distributions became unlawful, and he should have known.

If you use dividends to extract earnings from your company, it's important to be able to justify the amount you pay. We can advise you on what's needed. ●

Stamp duty holiday

The Government has announced a one-year holiday from Stamp Duty Land Tax for houses bought for up to £175,000. Normally the tax is charged at 1% on the whole value of any house which costs over £125,000, so this relief can save up to £1,750.

Unfortunately, if the house you are buying costs more than that, this doesn't help you at all – you'll still pay 1%, 3% or 4% on the full purchase price. This help is targeted at first time buyers rather than at the whole of the troubled housing market.

The purchase has to be completed by 2 September 2009 to qualify for the exemption. ●

Cash on delivery

If you import goods into the EU, you may have to pay import duty and VAT – that's what the red channels at ports and airports are for. If the goods arrive in the post, the sender may have attached a customs declaration and the postman will collect the duties for the taxman before handing your parcel over.

There is a lower limit below which they don't bother – if the cost of goods in an individual parcel is below £18, there's no duty and no VAT to pay. That's why you might find that a single order coming from outside the EU arrives in several packages – CDs, for example, are likely to cost less than £18 each.

The customs duty limit is going up to £105 from 1 December. Some people have suggested that this is a good reason to delay your Christmas internet shopping until the last minute. HM Revenue & Customs have pointed out that the VAT limit is still only £18 – so if you buy stuff for £100, there won't be any customs duty to pay, but the poor postman will still have to ring your doorbell and collect the VAT.

No, it doesn't make sense – but we didn't write the rules! ●

P&P&VAT

There's no VAT on stamps, is there? So why should I pay VAT on "postage and packing" charges? It's one of those catches of the VAT system that gets traders into trouble – if you charge someone £20 plus £2 for sending it to them, the VATman reckons you've simply charged £22 for the thing itself, and it's all one for VAT. If the £20 is VATable, so is the £2. Separating the charge out and calling it "postage" makes no difference.

The good thing about this is that you don't have to charge VAT if the item is zero-rated – books, children's clothes, and some kinds of food can be sold by mail order without triggering any VAT charges. If you are worried about when you have to add VAT to recharged costs, we can advise you. ●

VAT went wrong?

If you discover an error in your VAT accounting, you have a choice: if the effect of the mistake is no bigger than a set limit, you can make a correction in the current VAT return and not tell HM Revenue & Customs about it, or you can make a "voluntary disclosure". If the error is bigger than the limit, you have to tell them.

For many years the threshold for disclosures has been £2,000. This has been put up to £10,000, or 1% of the turnover on the return up to £50,000. So if Box 6 of the current return has £3m in it, you can correct an error of £30,000 without separate disclosure.

The limit applies to the net VAT effect of errors you discover in a period, not to the periods that they come from. So if you find that 2 years ago you underpaid £100,000 of output tax, but in the same checking exercise you discover that last quarter you overpaid £91,000 of output tax, you correct both mistakes as a single £9,000 current quarter adjustment.

The advantage of making the correction through the accounts is that there is no interest on an underpayment. It's treated as if the original return was correct at the lower figure, and the current return is correct at the higher figure. Of course, you can't take advantage of that deliberately – that would be dishonest, and there are penalties for that. But it's a useful rule for accidental errors. The most important thing is that any mistakes have to be dealt with under one rule or the other. If you have found something wrong and you don't correct it, that's also likely to be penalised. If you need to make any VAT corrections, we will be happy to help make sure you comply with the rules. ●

Po-Ta-To, Poh-Tah-To

When is a crisp not a crisp? When it's a Pringle. The courts have in the past ruled that a Jaffa Cake is a chocolate cake, not a chocolate biscuit, so it shouldn't have any VAT in it. Now a judge has had to consider whether Pringles are "potato crisps or similar products made from the potato or from potato flour". If so, they would be VATable.

A VAT Tribunal reckoned that they were made of potato flour because it was the largest single ingredient at 42% – and, in spite of the manufacturer's protests that they are completely different from ordinary crisps, they were "similar products". The High Court disagreed. The judge said that "made from the potato" surely meant that there had to be nothing much else apart from spud in the product. 42% wasn't enough, so Pringles are VAT-free.

The downside is that the case reveals the second largest ingredient to be… fat. ●

Nobody's perfect

Suppose you enter into a deal where disputes might arise. To make life simpler you agree in the contract that disputes are to be settled by the decision of a named expert, whose ruling will be final. What if you then think that the expert has made a mistake?

In a recent case, one of the parties was convinced that the expert was biased against him, so he went to court to try to have the expert's ruling struck out. The judge held that the point of the expert clause was to resolve disputes: as long as the expert had come to an honest answer to the questions put to him, his decision was binding even if it could be shown to be wrong. In this case, there was no evidence that he actually was biased or had ignored the evidence, so his decision stood.

A dispute resolution clause can save you going to court – but bear in mind that you might not like the expert's ruling, and you are likely to be stuck with it. ●

Discrimination

It's well known that an employer is not allowed to treat an employee less favourably because the employee is disabled – that's discrimination, and it's wrong. The employee is likely to be due compensation. But what about a woman who claimed that she was harassed by her employer because she had to look after her disabled son? The UK law appeared to protect the disabled person, but not someone who had to care for them.

The European Court of Justice has confirmed that European law requires "associated discrimination" to be outlawed as well. An able-bodied person should not be discriminated against because of someone else's disability. That means that the employer has to give reasonable consideration to requests for flexible working and treat them no less favourably than such requests made by other workers. It's also important to make it clear that workplace jibes and harassment are unacceptable, or the employer could become liable for allowing the actions of other workers. ●

This newsletter is written for the benefit of our clients. Further advice should be obtained before any action is taken.