Talking Tax

DRIVING LIFELONG PROSPERITY

Autumn 2017

SPOTLIGHT ON THE FUTURE

Welcome...

With the snap general election in May, changes in the world of tax were put on the back burner somewhat. This included a large number of clauses from the 2017 Finance Bill being axed. We have since heard though that those with an April 2017 commencement date will still be introduced as planned.

One welcome announcement is the delay in the Making Tax Digital (MTD) timeline until 2020 for most taxes. This seems a wise move given recent glitches with HMRC's online filing system which we look at in further detail, along with the new proposed timetable for MTD.

In other news, we are pleased to announce that we are proud winners of the prestigious Tolley Tax Awards 2017 for Tax Practice in a Regional Firm. This is a fantastic achievement for our firm and independent recognition of the great work our tax team consistently produces.

INSIDE

HAZLEWOODS
DRIVING LIFELONG PROSPERITY

Family Investment Companies

In our last issue of Talking Tax we looked at the changes to the taxation of residential property from April 2017. This included the restriction of relief on mortgage interest costs to the basic rate of tax for landlords.

We have been working with a number of our clients to assess the impact of these new rules. In some cases, it could render their property business to be no longer viable with effective tax rates of over 100% of the rental profits.

One option we have implemented for some clients is the transfer of the properties to a company. This has also provided the opportunity for our clients to look at the succession of the property business to the next generation. Using a family investment company (FIC) as an alternative to a trust to hold the properties could result in inheritance tax (IHT) savings.

WHY USE A FAMILY INVESTMENT COMPANY?

An FIC is formed as a limited company which is a well known and understood vehicle and, with currently low corporation tax rates, it can be more tax efficient than holding investments or properties directly.

An FIC tends to have different classes of shares with different rights attached to each class. This allows the properties to be passed on to the next generation whilst retaining some control. For example, the parents may have the voting rights in the company but only a small percentage of the capital rights, the majority held by the children.

Any growth in the value of the company would be sheltered from IHT as the children would own the capital rights.

The company will receive full corporation tax relief for interest charges on the property mortgages, however, on transferring the properties to a company it may not always be possible to obtain as favourable rates as when held personally.

WHEN A FIC MIGHT NOT BE THE WAY TO GO

Some points to consider:

- There could be significant SDLT and/or capital gains tax charges on transferring the properties to a company. In some cases these can be mitigated, but this would be dependent upon the facts and circumstances of the existing property business.
- On transfer to the company there could potentially be an IHT charge if the properties are gifted in and there is a reduction in the value of the parents' estate. This would depend on the specific facts, however, and in some cases an IHT charge may be avoided on transfer.
- The ongoing costs of operating via a company should be considered including;
  - annual filing obligations and costs;
  - potential charges under the ATED regime (Annual Tax on Enveloped Dwellings) which applies for residential properties held by a company with a value of £500,000 or more, although there is an exemption for rental properties; and
  - overall tax cost of operating via a company with corporation taxes and income tax on distribution.
- As mentioned, the loan interest rate offered by the banks may not be as preferential when held by a company.

NOT JUST PROPERTY

An FIC does not just have to be established to transfer in property. In fact, due to the upfront taxes which may be levied on transferring properties into a company, the typical structure is to establish a company funded by cash which the company then invests.

Funds are extracted by way of repayment of the loan and any growth in the company again accrues mainly to the children's shares, limiting the IHT exposure for the parents.

HMRC software errors affect self-assessment filings

Errors in HMRC's self-assessment software are leading to online tax returns for the 2016/17 tax year either being rejected or tax being overstated. As a result, some taxpayers might be required to file their tax returns on paper rather than online.

THE ISSUE

HMRC's software for 2016/17 tax returns has not been updated to correctly calculate the tax due with certain combinations of income and utilising the various savings and personal allowances in the most favourable way. This also includes the new £5,000 dividend allowance introduced in April 2016.

If you are using a third party software to submit your tax return and your income falls within one of the exceptions detailed below, the tax return may be rejected at submission. Although the tax due calculated by the software is likely to be correct, an error in HMRC's code is resulting in a different (and higher) tax liability and because of the difference in calculation the return will be rejected.

Conversely, if you are using HMRC software to submit your tax return it will let you submit but, as a result of the errors, the tax calculated may well be overstated by up to £1,000 with no obvious mechanism to rectify.

WHO MIGHT BE AFFECTED

Two groups of individuals who could potentially be caught out by the HMRC glitch when trying to submit their 2016/17 tax returns:

1. In some cases the HMRC software is not allocating the £5,000 starting savings rate to the taxpayer, which could result in their tax liability being overstated by up to £1,000. Those affected appear to be individuals with non-savings income of less than £16,000 and savings income which is not covered by the personal savings allowance.
2. Up to £280 of additional tax could be charged for additional rate taxpayers with dividends in excess of the dividend allowance. The software incorrectly allocates the £5,000 dividend allowance, taxing more dividends at the 38.1% additional rate.

ACTION TO TAKE

HMRC had, somewhat frustratingly, confirmed that they will not be correcting the errors until the 2017/18 filing. Instead, they have issued an exclusions list from online filing including the above cases.

It appears though that several versions and over 15 pages later, they may have conceded and are likely to update their software later this year for some of the errors.

For early filers and all others affected, a paper return will need to be filed. The deadline for a paper return is 31 October 2017, however, HMRC have confirmed that they will extend this to the online filing deadline of 31 January 2018 for those specified cases.

To avoid an automatic late filing penalty, HMRC also advise that a 'reasonable excuse' claim should be submitted along with the paper return. If you think you might be affected, however, it might be worthwhile holding off from filing to see if the issues are resolved and avoid having to file a paper return.

These issues, along with the time to rectify, support that the decision to delay the Making Tax Digital timetable was a wise move!

SDLT and MDR – confused already?!

Stamp Duty Land Tax (SDLT) is payable on the purchase of properties; the amount paid and applicable rate depends on the value of the property. Sounds simple, right?

Unfortunately, it is not always quite as straightforward as multiplying the purchase price by certain rates, particularly when there is more than one property being purchased. In addition, the introduction of a 3% surcharge on the purchase of second homes has complicated matters further.

THE BASICS

SDLT is calculated in bands so, for residential property, 0% on the first £125,000 of consideration and 2% on the next £125,000 etc. (see tables for further details).

STAMP DUTIES

RESIDENTIAL PROPERTY	SDLT RATE#
Up to £125,000	Zero
Over £125,000 to £250,000	2%
Over £250,000 to £925,000	5%
Over £925,000 to £1,500,000	10%
Over £1,500,000	12%
Over £500,000 if bought by a non-natural person (e.g. a company)*	15%

* 15% rate applies to the entire consideration, subject to certain exemptions.

\# 3% surcharge applies for additional residential property purchased by an individual or any purchases by a company, trust or partnership, where chargeable consideration exceeds £40,000.

NON-RESIDENTIAL OR MIXED USE PROPERTY	SDLT RATE
Up to £150,000	Zero
Over £150,000 to £250,000	2%
Over £250,000	5%

However, where the 3% surcharge applies this is calculated on the entire purchase consideration.

Example: Fred purchases a second home for £250,000.

The SDLT charge would be £10,000 calculated as:

£125,000 x 0%
£125,000 x 2% = £2,500

Plus the 3% surcharge on the whole consideration:

£250,000 x 3% = £7,500

MULTIPLE DWELLINGS RELIEF

Multiple Dwellings Relief (MDR) 'does as it says on the tin' – it is a relief, which is available on the purchase of more than one residential property. Essentially, it works by calculating the mean price of the properties purchased, working out the SDLT charge on one property and then multiplying by the number of properties purchased.

Example: A block of three flats are purchased for £900,000.

Under the normal calculations, the SDLT charge would be £62,000

Calculated as:

£125,000 x 0%
+ £125,000 x 2% = £2,500
+ £650,000 x 5% = £32,500
+ £900,000 x 3% = £27,000 (SDLT surcharge)

With MDR, the mean value of the properties would be £300,000 (£900,000/3) and the SDLT charge would be £42,000 calculated as:

£125,000 x 0%
+ £125,000 x 2% = £2,500
+ £50,000 x 5% = £2,500
+ £300,000 x 3% = £9,000 (SDLT surcharge)

The SDLT charge would therefore be £14,000 per property and £42,000 in total when applying MDR. This is a saving of £20,000.

FURTHER SAVINGS TO BE HAD?

On close inspection of the legislation, the additional 3% surcharge may not apply on certain multiple dwelling purchases.

In our above example, even if the individual did not own a residential property before the purchase of the block of flats they would still be liable to the 3% surcharge on the whole consideration.

There is an exception, however, for purchases of dwellings with self-contained annexes, or outbuildings that are also dwellings if they equate to less than one third of the total price paid. Examples could include a house with a self-contained granny annexe or a farmhouse which also has a cottage on the same plot. Bear in mind though this exemption would only apply where the purchaser does not already own a residential property or if they are purchasing this property to replace their main residence. In all other cases the 3% surcharge would still apply.

SIX OR MORE DWELLINGS

There is another option to consider when six or more properties are purchased together in one transaction. In this case it is possible to treat the purchase as a commercial one and apply the non-residential rates. The highest rate for non-residential property is 5% compared to 12% for residential purchases so the savings can be significant. The 3% surcharge will also not apply as it is not classed as a residential purchase.

Suppose that our earlier example was instead for the purchase of six flats for £1.8million. This leaves you with three different ways to calculate the SDLT payable. We will not bore you further with the calculations but it could bring about three very different results i.e.

1. Following normal rates and rules - £183,750
2. Claiming MDR - £84,000
3. Electing as commercial and applying non-residential rates - £79,500

In this case, therefore, it would be more beneficial to elect to treat the purchase as a commercial purchase with savings of over £100,000 compared to calculating under the normal rates for residential purchases.

CRYSTAL CLEAR?

Calculating the SDLT charge is not as simple as multiplying a few numbers together and there are ways to minimise your bill. The legislation is complex and detailed and it is advisable to speak to a tax professional to ensure that you are taking full advantage of any reliefs and minimising your liability as far as possible.

Helping to protect and enhance your wealth

Although we have been offering cross service support to our entrepreneurial family clients for many years now, we thought it was time to consolidate our offering and shout about what we can do.

The core aim of the Family Office is to help families protect and enhance their wealth. By bringing together key advisers it ensures we all work together to meet the family's objectives, needs and aspirations. This joined up approach means that the tax and investment aspects are all included in the decision making process at the outset to give the best results for the family.

Our services are tailor made for each family to reflect your individual circumstances, working with existing advisers or introduce others who can help as needed.

WEALTH MANAGEMENT

As mentioned, the best way to protect and enhance family wealth is to take a holistic view considering all potential implications when making any decisions. Bringing our financial planners and tax experts together to advise on wealth management helps to achieve this.

Succession planning to pass down wealth to future generations whilst maintaining the required cash flow to carry on with your desired lifestyle is another key area of wealth management. Assisting with cash flow projections as well as minimising taxes as far as possible is part of our core service.

We can also advise on charitable giving, whether this is to existing charities or a family charitable trust, and advise on how the tax benefits can be maximised.

FINANCIAL PLANNING

Providing independent financial advice and investment management services tailored to your specific needs is the key focus of our financial planners. We will create an investment portfolio based on your specific aims, objectives and risk profile. We can also help with retirement planning, inheritance tax and succession planning, all whilst protecting your family wealth.

To manage your current and future financial position, cash flow modelling is a key part of our service, to ensure that you can continue to afford your lifestyle on a day-to-day basis and in years to come.

TAX

There are the general compliance obligations which everyone has to meet such as filing of accounts and tax returns and we can of course help with this. Long term planning for you and your family, however, is where significant value can be added by our tax experts. Evaluating your exposure to capital gains tax, will also give you the opportunity to assess the potential impact on your cash flow, so that you can prepare accordingly.

We can advise on; structuring of family investments and finances to ensure tax efficiency; the use of trusts; inheritance tax planning and assisting with deceased estates.

If you would like further information or advice please visit our website: **http://bit.ly/hazlewoods-main** or contact a member of our Family Office team;

Nick Haines on **01242 237661** or nick.haines@hazlewoods.co.uk;

Nicholas Smail on **01242 680000** or nicholas.smail@hazlewoods.co.uk.

Do the hokey cokey

Clauses to be included in Finance Bill 2017 appear to be following the lyrics of the well-loved party song 'The hokey cokey'. Trying to keep up with what's 'in' and what's 'out' has been a challenge.

IN

The draft Finance Bill 2017 was set to turn into the longest Act in history with over 750 pages. This included clauses set to come in from April 2017 including:

Deemed UK domicile rules where non-domiciled individuals would be deemed to be UK domiciled for all UK tax purposes once they have been resident in the UK for 15 out of the last 20 years.

Corporate interest relief restrictions – on top of the already long list of restrictions for interest relief on corporate debt, new rules for the largest companies to restrict interest deductions in excess of £2million to 30% of 'tax EBITDA' (net income adjusted for certain items including tax).

Corporate loss restrictions – new provisions to relax the rules in relation to carried forward corporation tax losses enabling more flexibility for the offset against other profits of the company. In addition, a 50% cap for utilisation of carried forward losses in excess of £5million will apply.

OUT

With the snap general election in May taking over, parliament ran out of time to debate many of the Finance Bill clauses. As a result over 600 pages were axed quickly going from one of the longest Bills to something quite paltry.

For some time we were left in 'limbo' as April came and went, but we were none the wiser whether we should be applying the new rules or not.

IN

Just before the summer recess, an announcement was made that the clauses set to come in from April 2017 would still be introduced and still effective from that date. Although the draft legislation for these clauses has been released, the Finance Bill is still awaited following the summer recess.

OUT

The Making Tax Digital clauses included in the original Finance Bill will not be making the cut as detailed in our article below.

AND SHAKE IT ALL ABOUT...

Fortunately, it looks like this is where the song comes to an end as the updated draft legislation as currently released has no material changes to the original principles.

The clauses will not be set in statute, however, until the new Finance Bill has been released and subsequently reaches Royal Assent, so there is still a chance we could be doing the hokey cokey again.

AN EXERCISE OF TRUST

MORE ONLINE TALK...

The talk of online filing continues with HMRC launching their online Trusts Registration Service for all complex estates and trusts with UK tax liabilities.

This service replaces the paper form 41G which was previously used to notify HMRC of new trusts. Any paper forms submitted to HMRC will now be rejected.

As well as notifying HMRC of new trusts using the new online service, all trusts previously notified to HMRC via the paper form will also need to be registered.

The first deadline is 31 January 2018 for existing trusts and 5 October following the tax year in which a new trust is created or, if later, starts to make income or chargeable gains. There will be an annual requirement to notify HMRC of any changes (or not) by 31 January each year following.

The service was launched in June 2017 but tax agents have not yet been granted access. We understand that this will be any day now though.

For complex estates and trusts, completion of the register could be a time consuming process. The information to be supplied includes:

- details of trust assets, addresses and their values; and
- the identity of the settlor, trustees and beneficiaries.

10-YEAR CHARGES

Since March 2006, most assets held in trusts have been deemed to be 'relevant property' including, shares, property and money. For inheritance tax purposes a tax charge is crystalised when the assets are transferred out of a trust to a beneficiary and on each tenth anniversary from the date the trust was set up.

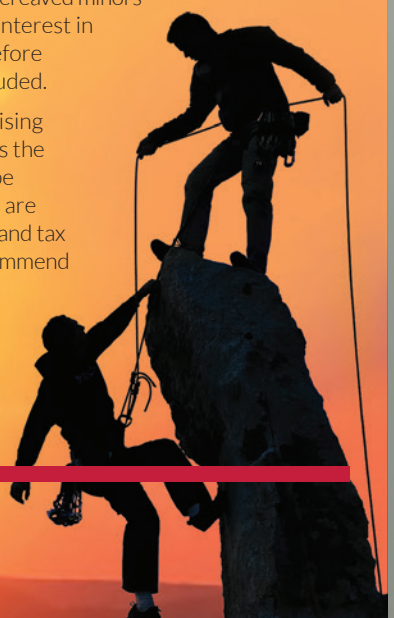
Over ten years on, the first of these periodic charges have been realised and the trustees will be responsible for calculating and paying the tax charge. The return and tax should be paid within six months of the 10-year anniversary date.

The amount payable is based on the value of the trust assets on the day before the anniversary date, less any available nil rate band (currently £325,000) and multiplied by a set percentage (currently 6%).

If more than one trust has been set up on the same day, the value of the other trust will also need to be included in the calculation.

Not all trusts are subject to the 10-year charge with bare trusts, trusts for bereaved minors and disabled persons, and interest in possession trusts set up before 22 March 2006 being excluded.

As we see more charges arising it is clear that in some cases the trustees, who may simply be family members or friends, are unaware of their reporting and tax obligations. We would recommend that professional tax and, as appropriate, legal advice is taken to understand specific requirements.



MAKING TAX ~~DIFFICULT~~ DIGITAL – DELAYED AT LAST

The government has confirmed that the timetable for Making Tax Digital (MTD) has been delayed, after considerable pressure from professionals and taxpayers.

With the general election resulting in the MTD provisions being axed from the Finance Bill and the pilot project behind schedule, it is no surprise, but a very welcome one, that the timetable has been pushed back.

Under the original timetable, businesses with turnover above the VAT threshold (currently £85,000) would have been required to maintain digital accounts and provide quarterly reports to HMRC for income tax purposes from April 2018. This was set to extend to all businesses and landlords with turnover above £10,000 from April 2019.

Under the new proposals, MTD will not come in until 2019 and then only for VAT purposes. In reality, this should have minimal impact as most businesses above the VAT threshold already have a quarterly reporting requirement.

For other taxes including income tax, national insurance and corporation tax, a commencement date has not yet been set in stone. We do know, however, that there will be no requirement to keep digital accounts or provide quarterly updates for these taxes until April 2020 at the very earliest.

In addition, the government has now advised that MTD will be voluntary for smaller businesses i.e. those below the VAT threshold.

For now we can breathe a sigh of relief and hope that the extra time will help lead to a smoother transition rather than Making Tax (more) Difficult!

BREXIT AND THE CUSTOMS UNION

There has been a lot of talk regarding what happens when the UK leaves the EU and what changes it will really bring. Nowhere will it be more keenly felt than in how the UK trades with our international partners.

Since the single market was introduced in 1993, the UK has enjoyed barrier free access to the EU member states for trade. In those 24 years since its creation, the UK goods trade to that market has grown to some £466bn, and a number of UK industries have embraced the ability to move goods around the EU for the purposes of sale or manufacture. Indeed, industries like car manufacture rely on the ability to build parts or source from third party manufacturers based around the EU and have it all arrive 'just in time' for final manufacture as a core part of their model. A return to the pre-1993 border checks would invariably hamper their, and many others, plans and methods.

As it stands, the negotiations for the UK's divorce from the EU are still very much under discussion and are likely to be so for some time. Nevertheless, UK companies still need to consider what implications there may be for them, if only for the purposes of planning for consistency or contingency purposes. Companies operating under long term contracts or on a rolling basis need to be able to ascertain the regulations that will come into force, or at least have a range of options available to meet whichever set of rules come about. And this doesn't only affect companies who trade with the EU; the UK's free trade program stems entirely from its membership within the EU. When we leave, those current free trade agreements around the world fall away too.

Much has been made of the comments that 'no deal is better than a bad deal' attributed to Mrs May, and that the fall-back position of World Trade Organisation (WTO) rules will ensure we can continue to trade with the world whilst we negotiate our own free trade agreements with new trading partners. However, we must also consider that the UK's membership of the WTO exists as part of its membership of the EU, and so there are still question marks regarding our standing in that organisation.

Where does all this leave the UK trader? With a lot of uncertainty is the first point, but this does not help with making the transition to the post-Brexit world any easier. Clearly, the changes will affect the commercial aspects of business, and may well make current supply chain models inefficient or redundant. Sales to EU business customers will potentially become more expensive as they lose their ability to reverse charge the VAT liability and self-credit the input tax; so new distribution models may need to be considered. However, the most crucial part of the changes for any business that trades outside of the domestic UK market is to recognise that they are coming. We may not yet be able to dial down on the specifics, but we are able to identify, analyse, map and consider the tasks we already have and so be aware of what may need to be amended. With lead times for customs simplifications taking up to nine months and readying for things like Authorised Economic Operator status applications taking in excess of a year, now is definitely the time to be thinking about 2019.

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