

Talking Tax

Guiding you to lifelong prosperity

Introduction

Welcome to the latest edition of Talking Tax, the newsletter from Hazlewoods tax team.

In this edition we have articles focusing on a selection of areas of taxation that have been, and continue to be, changing. Improvements to the Enterprise Investment Scheme were announced in this year's Budget but were subject to State Aid approval. This has now been granted and the article inside summarises the changes.

Although the previous Government's plan to abolish the beneficial tax treatment for furnished holiday lettings did not come to fruition, the coalition Government has made changes and more are on the way. We explain the rules and some of the pitfalls to watch out for with the forthcoming changes.

Other articles focus on why you don't need to be afraid of trusts and why 'green' cars are becoming more and more attractive.

You will know from previous editions that our tax team has been expanding with many key appointments in recent years. We have managed to get as many of the team as we can in the same place at the same time and there is a photo of almost the whole team on the back page.

Contents:

The holiday goes on

Trusts don't have to be complicated

You can have any colour you like as long as it's green

Axa Denplan - A step too far?

Enterprise Investment Scheme enhancements given the green light by Europe

For key tax dates visit www.hazlewoods.co.uk

The holiday goes on

A couple of years ago the Labour Government was planning to remove the tax breaks given to furnished holiday lettings (FHLs). Thankfully with the change of Government came the news that the tax treatment of FHLs would continue, although from 6 April 2011 there has been a change to the rules and further changes are due from 6 April 2012.

If you own a holiday property or properties this article considers what the new rules mean for you and how you can **ensure your property retains its beneficial tax status**. But before looking at the new rules it is worth having a recap of the rules in place before 6 April 2011.

Continued on page 2



HAZLEWOODS

DRIVING LIFELONG PROSPERITY

Where were we?

In general if you were involved in the 'commercial letting of furnished holiday accommodation' you could benefit from some of the tax treatments afforded to traders. These tax breaks included:

- Loss relief - including sideways loss relief against general income and terminal loss relief
- Capital allowances
- Landlords Energy Saving Allowance (LESA)
- Profits qualifying as net relevant earnings for an individual's pension contributions
- Certain Capital Gains Tax reliefs (including Entrepreneurs' Relief, business asset roll-over relief and relief for gifts of business assets)
- It is also possible that FHLs will qualify for Inheritance Tax Business Property Relief. However this will depend on the specific circumstances and types of services you provide with the holiday accommodation.

To qualify for the beneficial tax treatment you would have to be able to show that the property was let commercially with a view to making a profit. HMRC would expect a profit to be made within five years of starting to let the property. The other qualifying conditions were:

- The property had to be in the UK or another country in the European Economic Area (EEA). Before the 2009 Budget the property had to be in the UK, but the change to include the EEA is retroactive, so if you had a furnished holiday home in the EEA prior to 22 April 2009 you can still make a claim, subject to the normal time limits.

- The property had to be available for commercial letting as holiday accommodation to the public for at least 140 days a year.
- The property had to be commercially let for at least 70 days a year.
- The total period of 'longer term occupation' must not be more than 155 days during the relevant period (a period of 'longer term occupation' is a period of letting to the same person for longer than 31 consecutive days).
- The property must be furnished.

What's new?

From 6 April 2011 losses can only be carried forward and relieved against income from the same FHL business.

What's coming?

Perhaps more significantly, from 6 April 2012 the qualifying conditions are changing so:

- The property must be available for commercial letting as holiday accommodation to the public for at least 210 days a year (increased from 140 days); and
- The property must be commercially let for at least 105 days a year (increased from 70 days a year). There is, however, a two year period of grace if this is the only condition not met.

The trap to watch out for

Of the three changes (one implemented and two more on their way in 2012) the biggest problems are likely to come from the property

needing to be let commercially for at least 105 days a year. It's important to remember that the two year period of grace will only apply if this is the only condition that is not met. So if a property is not available for commercial letting for at least 210 days a year from 6 April 2012 it will not be a FHL immediately from that date.

The period of grace

The two year period of grace enables an election to be made for the FHL rules to continue to apply even though the actual lettings do not meet the 105 day requirement. This means businesses only need to meet the thresholds once every three years.

Action

If you have a furnished holiday let, but you do not let it commercially for at least 105 days per year, you should consider your options to ensure you are not negatively affected by the new rules, for example:

- Can you change your letting strategy so you do meet the 105 day limit?
- If you don't ever plan to let your property for 105 days per year, you could consider selling it whilst you still benefit from the 10% Capital Gains Tax rate available under Entrepreneurs' Relief.

If you would like to talk through your options or would like more information about FHLs please give Nicholas Smail a call on 01452 634800 or email him at nicholas.smail@hazlewoods.co.uk

Trusts don't have to be complicated

Many people think of trusts as being for other people and not for them. There can be many reasons for this, including the worry that a trust will be administratively time consuming, complicated and costly. But trusts don't have to be complicated and can be a very useful and cost efficient tool for saving Inheritance Tax (IHT).

A trust is simply a way for a person to pass on the benefit of assets to other people without the other people owning the assets outright. Trusts also allow for a huge amount of flexibility. For example if you are setting up a trust for your grandchildren and you know you want them all to benefit equally, this can be written into the trust deed. However, if you want the grandchildren to benefit according to their circumstances you can give the trustees discretion to pay out income according to need.

In this article we run through a few practical



ways trusts can be used to help your family save money.

A simple trust

With the cost of private and university education rising many families are looking at ways to ensure the children continue to get the best education they can. If you are the parent of young children for whom you pay school fees (or will in the next few years) it would be better for IHT purposes for one of the children's grandparents to set up a trust to pay the school fees.

The benefits of doing this would be fourfold:

- 1 It removes the money from the grandparent's estate thus reducing the potential IHT due when they die.
- 2 It also improves your IHT position because the money by-passes your estate thus reducing the potential IHT when you die.
- 3 A Capital Gains Tax deferral can be achieved on relevant assets.
- 4 It is income tax efficient for all parties.

IHT saving

Assuming the grandparent is not able to benefit from the assets in the trust the grandparent can put up to £325,000 (the annual IHT exemption) of assets into trust without incurring an IHT charge, so long as they have not made other gifts in the previous seven years. A couple could, therefore, place £650,000 into trust without there being an IHT charge.

Capital Gains Tax saving

If the assets transferred into trust would normally be chargeable to Capital Gains Tax (CGT), the person putting them into trust can claim for the gain to be held-over into the hands of the trustees. This means that there will be no CGT charge until the trustees sell the assets.

Income tax saving

The trust pays tax at the same rates as an additional rate taxpayer, so income tax is levied at 50% and CGT at 28%. However, if the income is distributed to the children (eg when paying school fees), the children will be able to reclaim much of the tax that the trustees have paid. The trust could instead be set up so that the income goes automatically to the children, in which case the trust does not pay any income tax at all.

This means that instead of the grandparent paying tax at 40% or even 50%, income generated by the assets in trust can be used to meet the costs of a child's education, with tax at 0% on the first £7,475 in 2011/12 per child, and then 20%. If the child has any other income this will affect the tax rate.

This is a very practical example of how a trust can be used. If your children are too old to need help with school fees this idea could be used equally well for a grandparent to help a grandchild buy their first car or put a deposit down for a house.

A more sophisticated trust

Trusts can also be used in a more sophisticated way to save IHT. However, although the tax ideas behind them are complicated, they are not necessarily difficult to implement and administer. One idea is using pilot trusts.

A pilot trust is not a specific type of trust in itself, so it can have any of the normal provisions, but we normally use a Discretionary Trust, as they are very flexible and protective. It is a trust set up during your lifetime with a small amount of money (usually £10) which can be added to, either in your lifetime or on your death by a legacy in your Will.

Pilot trusts can be used in a very simple way to take Death in Service Benefits (DISB) from pension funds. If you have a DISB of, say, £300,000, you can request that on your death, it is paid into a pilot trust that you have set up in your lifetime for the benefit of your spouse and children. After your death, they can have access to those funds very flexibly without the value being included in your spouse's estate for IHT. If it is set up correctly, there will be minimal administration.

Multiple pilot trusts

There are also ways to use multiple pilot trusts to mitigate IHT on much larger sums of money.

If you take a long-term view of asset protection and IHT minimisation and you are planning to leave a large amount of money on trust after your death (there could be many reasons for this), using a number of pilot trusts is a good option. There are two ways to do this.

Set up trusts in your lifetime

You can set up any number of trusts in your lifetime, such that each trust will have its own nil rate band. In the first option, although you cannot avoid the IHT charge on death, you can avoid ongoing IHT charges in the trusts after your death, whilst retaining some measure of control and protection. For example, if you have

£2m of non-business assets that you want your adult children to benefit from without adding to their own IHT issues, you could set up a number of pilot trusts in your lifetime so that the £2m of assets could be split between them on your death. In this example, seven pilot trusts would ensure each held less than £325,000 of assets so avoiding the 10 year charge. The administration can be combined, so need not be complicated.

Set up pilot trusts every seven years

Another way to use pilot trusts (which could avoid the charge on death as well) is to set up individual pilot trusts every seven years and rather than just putting in £10, transfer cash of the nil-rate band (currently £325,000). Whilst you or your spouse retain an interest in the trust, its value remains in your estate. However, if you have a large amount of cash (or non-business assets that have small gains) that you think you may need access to for some time, this could be the answer. You and your spouse could both set up trusts every seven years, still have access to the capital if you need it and take the income, but once you are at the point where you know you will not need it or all of it, you can remove yourselves from benefit. If you both live more than seven years from that date, all of those trusts are in an IHT free "pot" for your family, and you have paid no IHT to get it into trust. Because each of the trusts was set up at seven year intervals with cash equal to the nil-rate band it enables you to benefit from several nil-rate bands, whereas if you just put the cash into trust when you knew you did not need it you would only be able to gift up to the nil-rate band IHT free.

These pilot trusts require thought before implementing as the planning does have to be tailored to the needs of the donor.

If you want to talk about how we can help you save IHT speak to Tom Woodcock on 01242 237661 or email him at tom.woodcock@hazlewoods.co.uk.

Don't forget to use your IHT exemptions

Each year you can make the following gifts from your estate without any IHT implications:

Gifts to UK domiciled spouse	£Unlimited
Gifts to non-UK domiciled spouse	£55,000
Gifts to charities	£Unlimited
Annual gifts (can be carried forward one year)	£3,000
Small gifts to different people	£250
Gifts on marriage	
- by parent	£5,000
- by remoter ancestor	£2,500
- by other	£1,000

Axa Denplan

- A step too far?

Following the European Court of Justice (ECJ) ruling in Axa Denplan, Adam Lloyd, VAT Director, asks whether HMRC's subsequent Business Brief goes beyond the ECJ's interpretation of "debt collection".

Background

Denplan is a plan operated by Axa, whereby dentists provide a fixed amount of care to dental patients in return for a fixed monthly fee. Patients enter into a contract with the dentist but this contract states that payments will be made to Denplan. A direct debit mandate is accordingly set up between Denplan and the patient.

Each month Denplan "will seek to collect the payments due from patients' bank accounts...". Once received, Denplan then deducts its own fees and transfers the net credit to the dentist.

Denplan argued that its services were exempt under Article 13B(d)(3) of the EU 6th Directive (namely "transactions, including negotiation, concerning payments, transfers, debts but excluding debt collection and factoring"). HMRC's argument was that the services were administrative in nature and the case was referred to the ECJ.

ECJ Ruling

The ECJ goes into the detail of Denplan's service, highlighting certain characteristics in particular:

- it "consists, in particular, in transferring information to the third party's bank calling for the transfer of a certain sum of money from the third party's bank account to the service provider's bank account";
- "meanwhile, the service supplier sends to its client a statement of sums received and contacts third parties from whom it has not received transfer of the sums requested";
- "Denplan is responsible for the recovery of those debts and provides a service of managing those debts"

The ECJ concluded that the service as described above is a transaction within the meaning of 13B(d)(3) as it has the "effect of transferring funds and entails changes to the legal and financial situation". However, because Denplan is responsible for the recovery of the debt and the management of those debts, its service also falls

within the definition of debt collection as described above and is therefore excluded from the exemption.

The ECJ therefore ruled the services to be VATable.

HMRC Business Brief

Following the judgement, HMRC released its Business Brief setting out how it intends to apply the judgement. However, the Business Brief appears to go beyond the criteria set out in the Denplan case. While the Business Brief refers only to "debt collection" it does not define this in any way other than "collecting payments from the person owing them for the benefit of the entity to whom they are owed." What it does not say is that the ECJ concluded that Denplan is engaged in debt collection because it is "responsible for the collection of the debt and provides a service of managing those debts".

Furthermore the ECJ makes specific reference to the fact that Denplan requests payment from the customer's bank ("the service.....consists, in particular, in transferring information to the third party's bank calling for the transfer of a certain sum of money from the third party's bank account to the service provider's bank account"). There is no stipulation in the Business Brief that such an action is instrumental in the creation of a debt collection service.

In essence, the ECJ concluded that Denplan was responsible for the collection of the debts and that, combined with the fact that Denplan requests payments, leads it to be excluded from the exemption. At no point are these criteria mentioned in the Business Brief.

As a slight aside, the Business Brief does state that

core exempt services such as "the settlement of payments between bank accounts" are not affected, which leaves rather a large grey area.

This means that HMRC may well attack businesses involved in finance. However if their attack is based on the contents of the Business Brief and not the actual ECJ ruling speak to us because you may be able to fight it.

Conclusion

In fairness, no one predicted the ruling (or at least the reasoning behind the ruling) that was passed down. However, HMRC's Business Brief does appear to push the definition of debt collection beyond that described by the ECJ. The Brief says that if a business is "collecting payments from the person owing them for the benefit of the entity to whom they are owed" then the service is taxable debt collection. However, the ECJ stipulates the characteristics of such services as:

- calling for the transfer of money;
- sending a statement of sums received and contacting third parties from whom it has not received transfer of the sums requested; and
- being responsible for the recovery of those debts and providing a service of managing those debts.

If a business's services do not include these there is a strong argument that they do not fall within the meaning of debt collection as set out in the Denplan case, despite what the Business Brief might say.

Businesses who are potentially affected by the ruling and / or the Business Brief should contact Adam Lloyd on 01242 237 661 or adam.lloyd@hazlewoods.co.uk.



Visit Our New Website!

www.hazlewoods.co.uk



Tax Investigations Service

Last year's Comprehensive Spending Review reallocated £900 million to HMRC's enforcement team. The team has been targeted with raising an extra £7 billion per year through tackling both tax avoidance and tax evasion. Combine this with Danny Alexander's recent announcement that more than 2,000 tax inspectors are to be recruited, the additional powers of inspection given to HMRC and the new penalty regime it is likely to mean that tax enquiries will become **more complex and expensive**.

Our Tax Investigations Service enables you to claim the cost of our fees should you suffer an HMRC enquiry or other type of investigation.

Tax enquiries can take several years to settle, incurring significant professional fees along the way. We believe that our Tax Investigations Service provides our clients with low cost, but valuable, peace of mind at a time when it is most needed.

If you are already covered by the service or are going to apply, make sure you do so by Monday 31 October. If you would like more details or an application form please contact Margaret Wilkinson on 01242 680000 or email: margaret.wilkinson@hazlewoods.co.uk.

Enterprise Investment Scheme enhancements given the green light by Europe

The Enterprise Investment Scheme (EIS) helps smaller high-risk trading companies raise finance. It does this by offering a range of tax reliefs to investors who subscribe for shares in qualifying companies.

The improvements to EIS announced in Budget 2011 have received State aid approval from the European Commission. This means that the following changes can go ahead:

- Raising the income tax relief given under EIS from 20% to 30%, backdated to April 2011.
- Increasing the thresholds for the maximum size of qualifying company to fewer than 250 employees (currently fewer than 50

employees) and gross assets of no more than £15m before investment (currently £7m);

- Increasing the maximum annual investment in an individual company to £10m (currently £2m); and
- Increasing the annual amount an individual can invest under EIS to £1m (currently £500,000).

This is good news because it means that more businesses and individuals can benefit from EIS.

If you would like to talk about EIS or other tax incentives available for people who invest in smaller companies speak to Ruth Dooley on 01452 634800 or email her at ruth.dooley@hazlewoods.co.uk

Last chance to win an all-new design iPad 2

This year's prize for letting us have your tax return information in plenty of time is an iPad 2 and smart cover. To be in with a chance of winning let us have your tax return information and postcard entry by **Monday 31 October**.



You can have any colour you like as long as it's green

We have mentioned many times before in this newsletter about the tax incentives available for energy efficient or 'green' cars. We don't plan to go through all the benefits of having a green car here, but it is interesting to note that the car manufacturers do seem to be catching up with the idea.

Gone are the days when you had to buy a Smart car to achieve tax savings. Nowadays if you want a car that you can claim a 100% first year capital allowance on and that only gives rise to a 10% benefit in kind on the list price of the car, your choices include (but are not limited to) the cars detailed in the table:

Before buying or leasing your next car it is worth looking at the car's CO2 emissions figure and checking the tax implications of the purchase. If you would like advice please call Kirsty Lightowlers on 01242 237661 or email her at kirsty.lightowlers@hazlewoods.co.uk.

Toyota iQ 1.0 VVT-i (petrol)
Mazda 2 1.4 (diesel)
Skoda Octavia Estate 1.6 TDI (diesel)
Peugeot 107 Facelift 1.0 (petrol)
Ford Fiesta 1.6 Duratorq (diesel)
Volkswagen New Golf 1.6 TDI (diesel)
Renault Modus 1.4 dCi (diesel)
Citroen DS3 1.6 HDi (diesel)
Honda Insight 1.3 IMA (petrol hybrid)

For a complete list, visit www.direct.gov.uk



Hazlewoods Tax Team



Services

We provide specialist advice in all areas of tax including the following:

- Business structuring
- Employer services
- Inheritance Tax and estate planning
- Partnership Tax services
- Tax Investigations
- VAT
- Corporation Tax
- International Tax services
- Owner Managed Businesses
- Personal Tax
- Trust Tax
- Stamp Duty and SDLT mitigation
- Transactions, planning and support
- Capital Gains Tax planning

Hazlewoods Tax Team

Gloucester Office:

Windsor House
Barnett Way, Barnwood, Gloucester, GL4 3RT
Tel: 01452 634800 Fax: 01452 371900

Cheltenham Office:

Windsor House
Bayshill Road, Cheltenham, GL50 3AT
Tel: 01242 237661 Fax: 01242 584263

Staverton Office:

Staverton Court
Staverton, Cheltenham, GL51 0UX
Tel: 01242 680000 Fax: 01242 680857

www.hazlewoods.co.uk

This newsletter has been prepared as a guide to topics of current financial and business interest. We strongly recommend you take professional advice before making decisions on matters discussed here. No responsibility for any loss to any person acting as a result of this material can be accepted by us.

Hazlewoods LLP is a Limited Liability Partnership registered in England with number OC311817.
Registered Office: Staverton Court, Staverton, Cheltenham, Glos. GL51 0UX

A list of LLP partners is available from each office.
Registered as auditors by the Institute of Chartered Accountants in England & Wales.
Hazlewoods LLP is authorised and regulated by the Financial Services Authority.

Hazlewoods is a
member of **HLB** International.