Talking Tax

DRIVING YOU TO LIFELONG PROSPERITY

Spring 2016

SPOTLIGHT ON UPCOMING CHANGES

Welcome...

As we 'spring' into a new tax year, our latest issue of Talking Tax highlights some changes introduced from April 2016. These include a new SDLT surcharge on second properties, the tapered pensions allowance for higher earners and changes to the benefit in kind rules. We also look at how the new dividend and interest rules could affect your self assessment status and the change in treatment of some distributions on liquidation.

We also summarise the recent Budget announcements, highlight how groups of companies could be caught out by the Apprenticeship Levy from 2017 and look at how Google AdWords might be costing you more than you think.

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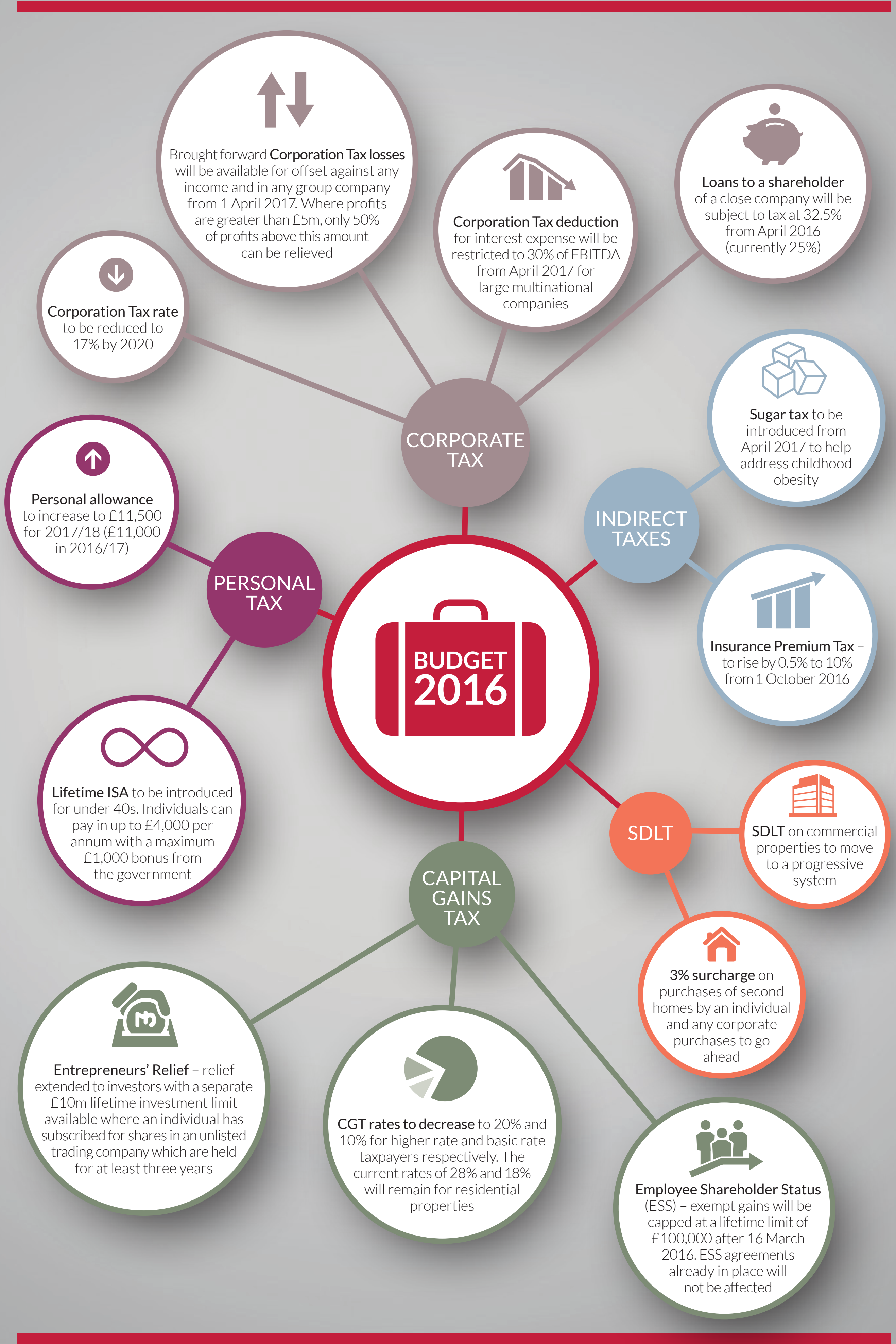

BUDGET 2016
CORPORATE TAX
Brought forward Corporation Tax losses will be available for offset against any income and in any group company from 1 April 2017. Where profits are greater than £5m, only 50% of profits above this amount can be relieved
Corporation Tax rate to be reduced to 17% by 2020
Corporation Tax deduction for interest expense will be restricted to 30% of EBITDA from April 2017 for large multinational companies
Loans to a shareholder of a close company will be subject to tax at 32.5% from April 2016 (currently 25%)
INDIRECT TAXES
Sugar tax to be introduced from April 2017 to help address childhood obesity
Insurance Premium Tax – to rise by 0.5% to 10% from 1 October 2016
PERSONAL TAX
Personal allowance to increase to £11,500 for 2017/18 (£11,000 in 2016/17)
Lifetime ISA to be introduced for under 40s. Individuals can pay in up to £4,000 per annum with a maximum £1,000 bonus from the government
SDLT
SDLT on commercial properties to move to a progressive system
3% surcharge on purchases of second homes by an individual and any corporate purchases to go ahead
CAPITAL GAINS TAX
Entrepreneurs' Relief – relief extended to investors with a separate £10m lifetime investment limit available where an individual has subscribed for shares in an unlisted trading company which are held for at least three years
CGT rates to decrease to 20% and 10% for higher rate and basic rate taxpayers respectively. The current rates of 28% and 18% will remain for residential properties
Employee Shareholder Status (ESS) – exempt gains will be capped at a lifetime limit of £100,000 after 16 March 2016. ESS agreements already in place will not be affected

Reducing the administration burden… by putting more people in self assessment

From 6 April 2016, fundamental changes to the taxation of dividends and interest were introduced. HMRC continue to talk about reduced administration for taxpayers, however, these latest changes are likely to result in many more people being required to file a tax return. With the move towards digital tax accounts and quarterly reporting, it is hard to see how tax administration is going to get any easier.

DIVIDENDS

Previously, an individual receiving gross dividends up to the basic rate i.e. £42,385 in 2015/16 (assuming no other income) would not have had a tax liability and would not have been required to file a tax return.

Now, however, the same individual will only be able to receive dividends of up to £16,000 before becoming subject to tax and required to self assess. With a personal allowance of £11,000 and dividend allowance of £5,000, any dividend income above this would be subject to tax at 7.5% for basic rate taxpayers, 32.5% for higher rate taxpayers and 38.1% for additional rate taxpayers.

INTEREST

From April 2016, banks and building societies have begun to make interest payments without deducting tax. Previously, banks withheld 20% tax on interest payments to individuals. Therefore, only higher or additional rate taxpayers would need to pay any additional tax due on interest via a tax return.

The change to pay interest gross is due to the introduction of a new Personal Savings Allowance. This new allowance is set at £1,000 for basic rate taxpayers, £500 for higher rate taxpayers and nil for additional rate taxpayers.

Any taxpayers receiving interest income in excess of the above allowances, and after taking into account any relief under the existing starting savings rate, will need to self-assess to settle their additional tax liability. Therefore, all taxpayers will now have the responsibility of checking the annual interest income they have received and working out whether they have any tax to pay.

As an aside, it should be noted that other companies making interest payments will still need to deduct tax at source, so CT61s will still be required, for example, in respect of payments on a director's loan account.

ADMIN

These changes are mainly likely to affect basic rate taxpayers by bringing them within the self assessment regime and could catch the unwary out, not realising they are now required to file a tax return.

If you come within the self assessment net for 2016/17 you will need to register with HMRC by 5 October 2017 and file your first tax return and pay any tax due by 31 January 2018.

Apprenticeship Levy – implications for groups of companies

A new 'apprenticeship levy' is due to come in from April 2017 and draft legislation has been published. Based on the initial drafting, there appear to be wider consequences for connected companies than anticipated which would leave many being subject to the new levy.

The apprenticeship levy will be charged at 0.5% of the employer's total payroll bill, with a levy allowance of £15,000 available to offset against this. The initial view, therefore, was that any employers with a payroll bill of less than £3 million would not be affected by the new rules.

The legislation, however, as currently drafted provides that, for connected companies, only one company will be eligible to receive the levy allowance. Companies will be treated as connected for the purposes of the apprenticeship levy based on the old associated company rules. Therefore, groups of companies i.e. where one company is under the control of the other company as well as companies under the control of the same individual(s), will be caught.

The group can elect which company receives the allowance but there does not appear to be a provision to transfer any excess allowance to other group companies.

So, take an example of a group with two companies, each having a payroll of £1 million. Logic would state that there is no apprenticeship levy, as the payroll will be less than £3 million for the group. However, you have to elect which company receives the £15,000 with no ability to transfer the excess. Therefore the "unelected" company, on the basis of draft legislation, will be subject to the levy at 0.5%, i.e. £5,000.

Conversely, if the group had all of its employees in one company, with a total payroll of £2 million, there would be no apprenticeship levy due.

This was not what was anticipated, given that the Government stated it would only affect the top 2% of payrolls. If the rules stand as drafted we would expect all groups of companies to be subject to the levy to some degree, where they have employees in two or more of those companies.

The consultation on the draft legislation closed on 2 March 2016 and revised legislation has since been published. However, as it stands the one levy allowance for connected companies is set to go ahead.

Buy-to-let landlords targeted again

Following the announcements that mortgage interest relief would be restricted to the basic rate of tax for buy-to-let landlords from 2017, the Chancellor delivered a further blow in the Autumn Statement.

From 1 April 2016, second residential property purchases will be subject to a 3% Stamp Duty Land Tax (SDLT) surcharge. Property purchases with a value of less than £40,000 will remain free from SDLT, though all additional property purchases above this amount will be subject to a 3% surcharge going forward (see below table).

Residential property value (£)	Current SDLT rate	New SDLT rate (additional residential purchases)
Up to £40,000	Zero	Zero
Over £40,000 – £125,000	Zero	3%
Over £125,000 – £250,000	2%	5%
Over £250,000 – £925,000	5%	8%
Over £925,000 – £1,500,000	10%	13%
Over £1,500,000	12%	15%

For example the SDLT on a second property purchase of £265,000 would now be calculated as follows:

3% on the first £125,000 = £3,750

Plus: 5% on the next £125,000 = £6,250

Plus: 8% on the remaining £15,000 = £1,200

The total SDLT due, therefore, would be £11,200.

This is compared to £3,250 under the current rules (2% on £125,000 plus 5% on £15,000) – in this case, an increase in tax due of almost £8,000.

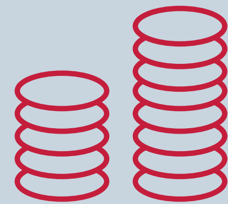
Some key points to note on the new surcharge include:

- Married couples/civil partners will be treated as a 'unit' and can only own one residence between them with any second purchase being subject to the higher rate.
- Unmarried couples will be able to own one property each (but not jointly) before being subject to the higher rate.
- For joint purchases, if one of the purchasers already owns a property the 3% surcharge will apply to the entire transaction regardless of how small an interest that purchaser has in the new property.
- Mixed use property (e.g. part residential, part commercial) purchases will not be subject to the additional 3% SDLT.
- If selling the main residence and purchasing another within 36 months the higher rates will not apply. If the main residence has not been sold at the point of purchase, the higher rate will apply but a refund can be claimed if the previous main residence is subsequently sold within 36 months.
- The first purchase of a residential property by a company will be subject to the higher rates to reduce the risk of avoidance of the 3% rate.

The surcharge is expected to raise £625m in additional taxes in 2016-17 and is being introduced to try and dampen the buy-to-let market so that more people have the opportunity to become home owners.

On top of the introduction of the surcharge, from April 2017, the SDLT filing and payment date will be shortened from 30 days to 14 days.

MVLs next on HMRC's hit list?



New rules were introduced from April 2016, to tax certain distributions on a wind up as income rather than capital. This legislation was introduced following a consultation on company distributions published in December 2015.

INCOME DISTRIBUTIONS ON A WIND UP

Under the new rules, a distribution on wind up will be treated as income rather than capital where all of the following are met:

- immediately before the winding up, the individual has a share holding of 5% or more;
- the company being wound up is a close company (e.g. owned by five or less participators or controlled by any number of participators who are directors);
- the individual receiving the distribution, or a connected person, carries on a trade or activity similar to that of the company being wound up within two years following the distribution; and
- the main purpose or one of the main purposes of the winding up is the avoidance or reduction of a charge to income tax.

For companies with significant reserves, a tax rate of 32.5% or 38.1% could be due on a liquidation distribution taxed as a dividend under the income tax rules. This is assuming that the new £5,000 dividend allowance has been used against real dividends and that the individual receiving the dividend is a higher rate taxpayer.

Compared to the tax rates if treated as a capital gain of 10% (where Entrepreneurs' Relief is available) or otherwise 20%, this could result in a significantly higher tax bill.

The taxpayer will be required to self assess whether the new rules apply and there are currently no procedures in place to apply to HMRC for clearance to obtain certainty.

WILL HMRC STOP THERE?

As part of the consultation on the new legislation highlighted above, HMRC also asked for comments on other company distributions on a wind up that are currently treated as capital. This included where either the company has retained profits in excess of the company's commercial needs or a 'special purpose company' is set up for separate projects of the same trade.

It would appear difficult to see how HMRC could determine what constitutes excess profits in order to be able to tax these as income, however, there has been talk of reintroducing close company apportionment rules which were repealed in the late 80's. Effectively this operated by notionally distributing undistributed reserves to the shareholders of a close company and subjecting them to an income tax charge.

Using separate companies for joint ventures on different projects with different partners is a common operating structure. The new rules introduced as highlighted above could prevent such commercial arrangements from being treated as a capital distribution on liquidations going forward.

WHAT'S NEXT?

As part of the consultation HMRC also explored other distributions taxed as capital including:

- repayment of share capital which has been increased by way of a share reconstruction; and
- purchases of own shares.

Although HMRC said within the consultation document that they have "no current plans to introduce any further changes to the distribution legislation" we would not be surprised if they do look to introduce further restrictions in the future.

If you think you might be affected by the new rules or would like to discuss your operating structure based on the potential changes ahead, please get in touch with your usual tax contact.

VAT AND GOOGLE ADWORDS: HOW MUCH ARE YOU ACTUALLY PAYING FOR "PAY PER CLICK"?

"Pay per click" is widely used by businesses across the UK. Where Google invoices another business outside the Irish Republic, they do so without VAT from their office in Dublin. However, what is not so widely known is that UK businesses may be required to account for the VAT at the UK rate (20%) through the 'reverse charge' legislation, which applies to most supplies of services received from suppliers based outside the UK.

VAT REGISTERED BUSINESS

If you are a VAT registered business making only VATable supplies, the process is straightforward. You are treated as though you are both the supplier and the customer and include the equivalent of both the input and output VAT on your VAT return. The effect is therefore cost neutral.

If a partially exempt business receives supplies which are subject to the reverse charge, they will need to account for the full value of the output tax, but may only be able to recover at best a proportion of the corresponding input tax, depending on the result of the partial exemption calculation.

UNREGISTERED BUSINESS

If your business is not registered for VAT but you receive supplies which should be subject to the reverse charge process, then you need to add the value of those supplies to your other VATable turnover to assess whether the VAT registration threshold (currently £82,000) has been breached. If so, you would need to register for VAT with HMRC.

TAX SIMPLIFICATION REACHING OUT TO BENEFITS IN KIND

On 6 April 2016 we welcomed in a new tax year and with it some new rules intended to simplify the benefits in kind (BIK) regime. The tax cost of these new rules is minimal to the Treasury, but the main objective is to cut the administrative costs of reporting for both businesses and the Treasury. The key areas of change are:

VOLUNTARY PAYROLLING OF BIK

Employers are now able to tax certain benefits through the payroll. By doing so, this will remove the requirement to report the benefits on a P11D form. Employers can choose which benefits they would like to payroll, with the exception of vouchers, living accommodation and loans which are not covered by this new regime. This could potentially negate the requirement to complete P11D forms for a number of employers.

For the 2016/17 tax year employers must have registered to use this service by 5 April 2016 and their payroll software must have the capability to collect the correct amount of tax. HMRC's 'Basic PAYE Tools' software is not suitable for this.

During the recent Budget, the Chancellor announced that from 2017/18 it will also be possible to voluntary payroll non-cash vouchers.

TRIVIAL EXEMPTION

Under a new statutory exemption, if an employer provides a benefit to its employees, the benefit is exempt from tax as employment income providing all of the following conditions are satisfied:

- the cost does not exceed £50;
- it is not cash or cash vouchers (high street vouchers are ok);
- the employee is not contractually entitled to the benefit; and
- the benefit is not provided in recognition of their employment duties.

There are no restrictions on the number of trivial benefits which can be provided in one year for employees, however for directors of close companies the total value of benefits which can be treated as exempt trivial benefits are capped at the annual exempt amount of £300. If the employer is a close company employing members of the office holder's family, they too are subject to the annual cap of £300.

ABOLITION OF DISPENSATIONS

Previously an employer had been able to request a dispensation from reporting certain benefits and expenses to HMRC. Dispensations became obsolete with effect from 6 April 2016 with new legislation introduced to cover the payment of business related expenses.

Nearly all expenses and BIK previously covered by a dispensation will now be automatically exempt and will not need to be reported to HMRC nor included on a P11D. In some cases approved HMRC scale rates can be used for reimbursing employee expenses rather than the actual costs incurred. These rates will still apply under the new exemption. If, however, you would like to apply a bespoke scale rate, agreement will need to be obtained from HMRC.

Whilst this potentially removes a large proportion of the reporting requirement, employers should continue to maintain detailed records of expenses and benefits.

REMOVAL OF £8,500 THRESHOLD FOR TAXATION OF BIK

Those employees who earn at a rate of less than £8,500 per annum have historically been exempt from tax on certain BIKs. From 6 April 2016 this no longer applies and all employees will now be subject to tax on BIK, where applicable, irrespective of their level of income. However, new measures will mitigate against some of this for lower paid ministers of religion and home care workers.

The P9D form has now been scrapped and any benefits will need to be reported on the P11D unless they are dealt with under voluntary payrolling.

The correct treatment of BIK can be a complex area. The above changes do not exempt employers from reporting any and all BIK; the onus is still on the employer to ensure the correct treatment is applied.

Even if your business makes only VAT-exempt supplies nevertheless the reverse charge supplies still count as a taxable supply for VAT purposes. If the value of the reverse charge supplies is such that the business is required to register, it will have to account for 20% VAT as output tax on the reverse charge supply, but because the business is exempt, it is unable to reclaim the corresponding input tax.

For example, an insurance broker (exempt supply for VAT) spends £100,000 on Google AdWords. The business is required to be registered for VAT due to the reverse charge legislation and they must pay over the additional 20% on its purchases subject to a reverse charge (£20,000). As the business is exempt, it is unable to include the £20,000 in its input tax claim and so Google AdWords has cost the business a total of £120,000.

WHAT TO DO IF YOU HAVEN'T TREATED YOUR SUPPLIES CORRECTLY UNDER THE REVERSE CHARGE LEGISLATION.

If you have not paid the correct amount of VAT, there may be penalties and interest due. If you are in this position, prompt disclosure to HMRC can help to mitigate penalties. If you are unsure about how this affects your business, please contact Julian Millinchamp in our VAT team who would be happy to advise on your business's individual requirements. As noted above, reverse charges will affect most business to business supplies from outside the UK, not just Google AdWords.

ENTERPRISE INVESTMENT SCHEME – THE NEW PENSION?

New rules which come into effect from April 2016 of this year will significantly restrict the tax relief higher earners can obtain on their pension contributions. The rules introduce a tapered annual allowance whereby individuals will lose £1 of their annual allowance for every £2 they earn over £150,000, subject to a minimum annual allowance of £10,000. This in effect means that any individual with earnings in excess of £210,000 will only be able to contribute £10,000 into a pension in any year and still receive tax relief on their contribution.

This has meant many higher earners are looking at what other tax efficient savings options there are available to them, to compensate for the huge reduction in their pension contribution allowance.

One such investment opportunity which is attracting much attention is the Enterprise Investment Scheme (EIS).

The EIS was originally introduced in 1994, and its aim is to encourage investment into small unquoted companies through a series of tax reliefs.

These reliefs include:

- 30% income tax relief on any contributions into EIS funds, subject to a maximum investment of £1 million per year.
- The ability to defer the payment of an existing Capital Gains Tax liability through investment of the gain into EIS qualifying shares.
- Almost all investments into these schemes qualify for Business Property Relief at 100% meaning that there is no Inheritance Tax liability on these shares, providing they have been held for two years.
- All monies held within EIS funds should grow tax free.

Investors often approach EIS funds with caution, due to the higher risks involved with investing in such small companies. However, in more recent times, many EIS fund managers have attempted to mitigate many of the risks involved.

This can be achieved in a number of ways. For example, some funds have assets backing the investment, including property and technology, whilst other investment funds have a clear predetermined exit strategy, meaning there is a known clear plan for the fund not reliant on other unknown factors.

With over 40 EIS funds currently available, it can be very difficult for investors to decide which is the most appropriate fund for them. Hazlewoods Financial Planning use a series of research and analytical tools to filter funds to help recommend the most appropriate ones to clients.

Please contact Kyle Nethercott on 01242 682141 or kyle.nethercott@hazlewoods.co.uk should you wish to discuss this in more detail.

MEET THE TAX PARTNERS

NICK HAINES
01242 237661
nick.haines@hazlewoods.co.uk

TOM WOODCOCK
01242 237661
tom.woodcock@hazlewoods.co.uk

RUTH DOOLEY
01242 680000
ruth.dooley@hazlewoods.co.uk

DAVID CLIFT
01242 680000
david.clift@hazlewoods.co.uk

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

www.hazlewoods.co.uk / @Hazlewoods_Tax

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