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Registered to carry on audit work in the UK and Ireland by the Institute of Chartered Accountants in England and Wales.

HART SHAW

Chartered Accountants & Business Advisers

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Money Matters

PAYE: How are you coping with RTI?

The new Real Time Information system is now in operation.

Is your business up to speed with the changes to how PAYE operates?

Employers are now burdened with a range of legal obligations when it comes to paying employees, and complying with the large number of payroll regulations is a challenge.



So let Hart Shaw take the strain and help you to avoid any penalties.

For more information please contact Sue Farrell on T: 0114 251 8850 or email: sue.farrell@hartshaw.co.uk.

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Loan attack

In many close companies (essentially owner managed companies) director shareholders have a current account with the company. This is often used to credit salary and dividends and to charge personal bills and draw down funds for personal use. In some cases this account becomes overdrawn during the accounting period and this is treated as an advance or loan. The company must then make a payment to HMRC if the advance made in the accounting period is not repaid within nine months of the end of the accounting period.

The amount of this corporation tax, often referred to as s455 tax, is 25% of the loan. Where the tax is paid over then the company may have to wait some time for a repayment as the tax is not then repayable until nine months after the end of the accounting period in which the loan is repaid. A loan or advance to an 'associate' of a shareholder, such as a relative, is also included for this purpose as if the loan had been made to the shareholder.

HMRC changes

HMRC have become concerned about the way in which some close companies have been arranging these loans in a way that seeks to avoid the tax. Whilst not necessarily accepting that all such arrangements work, HMRC want to ensure that some of the arrangements are definitely caught by the tax charge and therefore intend to make some changes which will have effect from 20 March 2013 once ratified.

One change proposed is to put beyond doubt that the charge applies where loans or advances are made via intermediaries such as Limited Liability Partnerships, partnerships and trusts. The charge will apply where at

least one participator in the close company is a member, partner or trustee.

Another change is to prevent the practise of avoiding the payment of the tax charge by repaying the loan before the tax is due (nine months after the end of the accounting period) and then effectively withdrawing the same money shortly after. This change may also prevent refunds of the 25% tax already paid where loans are redrawn shortly after.

The long established procedure of declaring a dividend or granting of a bonus which is equal to the amount outstanding will still remove the tax liability.

It is essential however that the amounts are cleared properly and, in the case of a dividend, in compliance with company law.

There are other changes proposed in this area which are not covered here so please contact us for assistance to help you to ensure that s455 tax is not payable.



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Contribution to childcare costs

The Government has announced a new scheme for tax free childcare for working families. Once fully up and running, the tax free childcare scheme will be worth up to £1,200 per child, and so will save a typical family with two children under 12 years old up to £2,400 a year.

The scheme will be phased in from autumn 2015 and will ultimately be open to around 2.5 million families with children under 12. For the first year of operation, all children under 5 will be eligible initially opening the scheme to 1.3 million families.

To be eligible, families will have to have all parents in work, with each earning less than £150,000 a year and not already receiving support through Tax Credits or Universal Credit. They will receive 20% of their yearly childcare costs up to £6,000 per child.

The new scheme will extend support compared to the current system of Employer Supported Childcare (ESC). ESC is offered by less than 5% of employers and is used by around 450,000 families. It provides an income tax and National Insurance Contributions (NICs) exemption equivalent to basic rate tax relief for childcare vouchers and directly contracted childcare. These alternatives will be closed to new entrants as the new scheme is introduced. Existing members of these schemes can however choose to remain in their current scheme. Alternatively ESC recipients may choose to move into the new scheme if they wish but will not be able to receive both. Further, the tax exemption available for workplace nurseries will continue, where offered by employers.

For parents who currently receive childcare support through Tax Credits and in due course Universal Credit, the Government will increase childcare support to improve work incentives and ensure that it is

worthwhile to work up to full time hours for low and middle income parents. At present, through the childcare element of Working Tax Credit, households where each parent works 16 hours or more already receive support for 70% of their childcare costs up to a weekly cap of £175 for one child or £300 for two or more.

The Government will shortly consult on the detail of the new scheme, including details on how employers can continue to play a role in supporting their employees with childcare costs within the new system. We will keep you posted of key developments in the run up to when the new scheme is implemented.



State Pension - the next phase

Late last year in December 2012 saw the 70th anniversary of the publication of the Beveridge report. This document which ran to 300 pages became the model for the welfare state. Indeed, the anticipation concerning its publication led to a reportedly mile long queue outside the Government Stationery Office on 1 December 1942 to get hold of a copy. Entitlement to a basic non means-tested contributory retirement pension was central to Beveridge's vision of a universal social insurance scheme.

Seventy years on, much has changed:

- the Office for National Statistics projects that 36% of people born in 2013 will live to become centenarians – in the 1940s only a minority of men survived to 65
- the number of women in work has seen a 50% increase – in 1948 only around four out of ten women were in paid employment
- the number of divorces that took place has risen from 11% of the number of marriages in 1948 to about 50% in 2012
- the labour market has become a lot more diverse – over a third of those working today are either self-employed or in part-time work.

Over the last 70 years since then, successive governments have attempted to keep pace with this social and economic change building on top of the Beveridge model. However many people do not have any idea as to what they will receive when they retire due to the complexities of the system as a result of these continual changes. Furthermore increasing dependence on means-tested benefits etc, which in effect compensate for the long-term decline in the relative value of the basic State Pension has compounded this complexity.

The Government had previously announced in the 2011 Budget that it intended to simplify the State Pension scheme so that it would provide a simple, contributory, flat rate support above the level of the means-tested Guarantee Credit. In the 2012 Budget it was confirmed that a

single tier pension would be introduced early in the next Parliament. In addition, because of the increases in longevity the State Pension age will be increased in the future.

The devil is in the detail...

The single tier reforms will restructure the State Pension into a simple flat rate amount from 2016 at the earliest. Those over State Pension age when the reforms are implemented will continue to receive it in line with existing rules. The single tier pension will:

- be set above the basic level of means-tested support. The amount in current terms is around £144 weekly but may well alter nearer implementation
- replace the State Second Pension, contracting out and out-dated additions, such as the Category D pension and the Age Addition. The Savings Credit element of Pension Credit will also close to pensioners reaching State Pension age after the implementation of the single tier pension
- require 35 qualifying years of NIC or credits for the full amount, with pro-rating where 35 years is not achieved. A minimum qualifying period of between seven and ten qualifying years is also being considered
- be based on individual qualification, without the facility to inherit or derive rights to the state pension from a spouse or civil partner and
- continue to allow people to defer claiming their state pension and receive a higher weekly

state pension in return. The deferral rate will be finalised closer to the planned implementation date. It will no longer be possible to receive deferred state pension as a lump sum payment.

Transition to the new regime

The transitional regime will:

- translate an individual's existing NIC records into a simple single tier starting amount to be known as the 'foundation amount'
- value an individual's NIC record using single tier rules. Where an individual has previously been contracted out of the additional State Pension, a deduction will be applied and
- as a safeguard, the Government will check to see if the rules of the current system would give a better outcome. The higher valuation will then become that individual's foundation amount.

For those with a foundation amount which is more than the full level of the single tier pension, likely to be older people with many qualifying years and who have not spent significant periods contracted out of the additional State Pension, these people will receive the difference between their foundation amount and the full single tier amount as an extra payment on top of the full single tier weekly amount.

We will keep you posted of any further developments.

A package of benefits

The potential 'feel good' factor that arises from the prospect of better summer weather could be likened to the satisfaction of getting the most out of your hard earned profits. Whilst a key consideration might be maximising the cash at your disposal for the minimum tax cost - are you optimising the potential of tax free benefits or even making use of value for money taxable benefits?

From a cash perspective dividend extraction as a means of providing cash to director shareholders continues to be generally tax efficient for all sizes of company under current tax rules and corporation tax rates. Its advantage over remuneration is that there is no national insurance cost. This fact currently outweighs the other key matter that dividends do not attract corporation tax relief. But what about the type of remuneration which benefits from obtaining tax relief for the business and has no national insurance cost?

The need to extract cash is always going to be an essential component of extracting profits for living requirements but the provision of tax free benefits by a company to directors and employees has certain merit, worthy of fresh consideration. Like dividends, tax free benefits are not subject to national insurance for either the employee or the employer. Yet the company should obtain a tax deduction where provided as part of a commercial remuneration package. It also has flexibility as different types of benefit can be provided for different individuals. Furthermore, unincorporated businesses can also participate in respect of their employees. This could be a valuable motivational incentive at a reduced cost.

Even where benefits are not income tax free and so attract employer national insurance there are still favourable reasons for considering their provision. Firstly, there is still no employee national insurance. Secondly, the cost to the employer of providing certain benefits to employees is cheaper than each individual employee buying the benefit out of 'net of tax' wages.

Clearly if the overall aim is to minimise tax and national insurance cost overall then the benefit provided needs to be tax free and some examples of such benefits include:

- a mobile phone for personal and business use (restricted to one per employee)
- free car parking at/near place of work
- contributions to registered pension schemes
- health checks and eye tests
- business mileage paid at HMRC's approved rates
- nursery provision up to £55 a week per parent (depending on whether basic, higher or additional rate tax payer)
- permanent health insurance
- interest free loans provided the total does not exceed £5,000 (to be increased to £10,000 from 6 April 2014).

To obtain tax and national insurance favourable treatment on benefits, it is essential that their provision is structured correctly. If this is an area of interest to you please contact us for further information.

Timely or costly?

Real Time Information (RTI) which has been compulsory for virtually all employers from April 2013 requires employers operating PAYE to report information on employees' pay and deductions in real time to HMRC. The key change under RTI is that payments made to employees are reported in year on or before the date each payment is made. In the past this information was generally not submitted until after the end of each tax year. Employers will continue to pay over to HMRC the sums deducted from their employees under the PAYE system monthly or quarterly.

What about penalties?

In this first year of operation, there are no new penalties introduced over and above the rules already in existence. The existing rules are not covered in detail here but essentially penalties for a late return only impact if the information required is not with HMRC by 19 May following the end of the tax year. If you require any assistance on this please do not hesitate to contact us. This article instead focuses on outlining the basis of the proposals for new penalties which will apply from 6 April 2014.

HMRC are introducing a penalty regime for RTI which is designed to encourage compliance with the information and payment obligations, whilst ensuring those who do not comply do not gain a significant advantage.

Late filing

In essence penalties will apply to each PAYE scheme, with the size of the penalty based on the number of employees in the scheme, so that different sized penalties will apply to micro, small, medium and large employers. Each scheme will be subject to only one late filing penalty each month, regardless of the number of returns due in the month. There will be one unpenalised default each year with all subsequent defaults attracting a penalty. Penalties will be charged quarterly, and subject to the usual reasonable excuse and appeal provisions. Regulations will be used to set the penalty rates.

What about late payment of tax?

Some changes will also be made to the current late payment penalty regime which is based on the number of late payments relating to each tax year.

HMRC envisage notifying defaults monthly and charging penalties quarterly to most employers.

From October 2013 employers will receive electronic notices telling them when they have incurred a filing and/or payment default but HMRC do not intend to introduce automated penalties before April 2014. There is also a current intention to apply interest to late payments from 6 April 2014.

It is important to be aware of these proposals to ensure that your business does not suffer from the charges and we will be happy to discuss how we can assist.



Guaranteeing relief

Many owner managers provide guarantees to lending institutions for loans made to their companies but is tax relief available when that guarantee has to be honoured? A recent case demonstrates how tricky this question can be because of how tax rules are structured.

The taxpayer was a director of a property trading company and made payments under a guarantee given to the bank which had lent money to the company. Immediately prior to the Tribunal hearing, HMRC accepted the company was carrying on a trade. This is critical to obtain tax relief when loans become irrecoverable and guarantees have to be paid out.

The bank made loans to the company and the taxpayer was a guarantor of the loans. The loans were used to acquire two flats, each with a view to selling them on at a profit. The interest payments exceeded the rents received for every accounting period that the company existed and the shortfall was made up by the taxpayer. The majority of the interest payments were paid directly by the taxpayer to the bank and the amounts owed by the company to the taxpayer resulted in credits to his loan account.

In June 1994 the bank demanded immediate payment of the outstanding balance. The letter stated that:

'... the event of our not receiving such repayment we shall proceed to exercise our rights under any security we may hold.'

The company was dissolved in March 1995.

The taxpayer claimed loss relief for the loan and interest payments he had to make under the guarantee.

HMRC argued that loss relief was not available at all because the loan was irrecoverable at the

outset and so did not become irrecoverable. They also said there was no evidence that repayment was demanded by the bank under the guarantee which is essential to get tax relief.

The taxpayer argued that the bank loans were not irrecoverable from the outset and the payments had been made under the guarantee.

The decision

The Tribunal held that the documentary evidence available showed that a commercial lender had been prepared to lend money to a company which had bought two properties, which did not indicate that outstanding amounts on those loans would be irrecoverable at the outset:

'In our view it was only when it became clear the property would be disposed of at a loss that sums paid in respect of interest on the loans would be known to be irrecoverable. We therefore do not agree with HMRC's submission that the loss relief claim should be denied on the grounds that the outstanding amount had not become irrecoverable.' As to whether the payments had been made under the guarantee, the Tribunal held:

'We think it is for the appellant to establish that the payments were made under the guarantee but there is inadequate evidence before us to reach that conclusion. We accept the appellant may genuinely have been motivated to make the payment in the knowledge that if there was a shortfall he would be pursued for it under the guarantee but this cannot answer the test posed

in the legislation which we think is an objective one.'

Whilst the position as to who was obliged to pay what to who was not clear, the Tribunal accepted that the payments amounted to there being a loan between the taxpayer and the company which was reflected in the directors loan account with the company. The taxpayer was therefore entitled to his claim for the outstanding amount of the loans he made to the company.

What relief then for the allowable loss?

Once established such losses can however only be used against capital gains and not income. This is in contrast to losses on the disposal of shares where an individual has subscribed for the shares in a qualifying trading company. Such losses on shares can instead be relieved against income (subject to a maximum from 2013/14 depending on individual circumstances) which generally means relief is available earlier and often at a higher rate of tax.

How we can help?

You can see that the way in which capital and financing structures operate can affect the tax relief you may obtain so please contact us to review what is most suitable for your circumstances.

