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HART SHAW
Incorporating Atkin Macredie & Co

Chartered Accountants & Business Advisers

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Money Matters

Tax return pitfalls

As self assessment tax returns for 2012/13 are completed and submitted in advance of the deadline of 31 January 2014, take a moment to reflect on whether you have considered two issues which could require you to complete a self assessment return for the first time, or could lead to an incomplete return being submitted.

The first of these is receipts from PPI claims. These usually comprise three elements; a refund of the mis-sold premiums, a refund of the additional interest incurred on the credit card or loan due to the premiums and compensation interest of 8%. The first two elements for individuals are not usually taxable (unless a tax deduction through a business was originally obtained). The 8% interest is taxable and may or may not have had 20% tax deducted at source depending on the payer. This means that in some cases even basic rate taxpayers may have a tax liability on the interest and higher and additional rate taxpayers will certainly have at least a liability for the marginal rate tax.

The second concerns whether the new High Income Child Benefit Charge applies to you. If you or your partner's income for 2012/13 exceeded £50,000 and one of you is claiming child benefit then this may mean that a tax charge has arisen which needs to be reported.

So please contact us if you are concerned that either of these issues may affect your tax return position so we can properly advise you of the action required.

WINTER 2013

Hart Shaw merges with Atkin Macredie & Co

Hart Shaw is delighted to announce the firm has merged with fellow Sheffield based Chartered Accountants Atkin Macredie & Co.

The merger took place on 1st October 2013 and the Atkin Macredie & Co team have joined Hart Shaw at their offices on the Sheffield Business Park.

Hart Shaw's Senior Partner, Paul Dawson comments: "The merger is fantastic news for both as it allows two already strong firms in the region to grow to the next level.

"As a firm, Hart Shaw has always sought to invest in staff and resources and the merger allows us to accelerate future investment plans for the benefit of all of our clients.

"Bringing both firms under one roof will ensure all clients receive the partner-led service which we pride ourselves on, whilst providing an opportunity for the Atkin Macredie & Co clients to take advantage of the full range of specialist services offered by Hart Shaw."

The merger sees Sarah Brock join as a Partner, adding to the already six strong Partner team at Hart Shaw, with Nigel Oates and Paul Boden joining Hart Shaw as Consultants.

Sarah Brock comments: "It is the right time for us to merge with Hart Shaw. With my fellow Directors at Atkin Macredie & Co coming up to retirement this move provides our client base with security and continuation, as they will still be working with the same people, just under a different banner.

"We have a great fit with Hart Shaw in terms of the type of clients that we service so as far as our clients are concerned it will be business as usual for them. Our clients will benefit from the complete range of services on offer from Hart Shaw. We are bringing our workforce over to Hart Shaw's offices, which is really set up for additional growth in the future.

"I have been a Partner at Atkin Macredie & Co since 1992 and specialise in working with Owner Managed Businesses of varying sizes across the market sectors. I have the experience which Hart Shaw is looking for so the transition will be smooth."

For further information about the merger, please contact Paul Dawson, Senior Partner at Hart Shaw on T: 0114 251 8850 or email: paul.dawson@hartshaw.co.uk.

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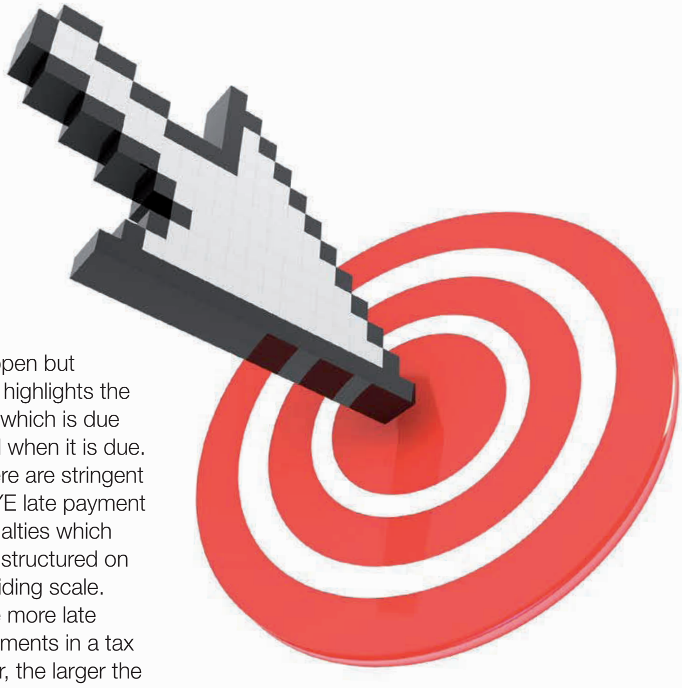
RTI a moving target

It is probably fair to say that the biggest change to the PAYE system has gone quite well for those employers that prepared for it. The technology seems robust and there have been no 'crashes' of the system. However, it is also clear that many smaller employers have not really started to get to grips with RTI.



HMRC also know this, which explains the announcement that the temporary relaxation of the new rules for businesses with fewer than 50 employees has been extended until April 2014. The effect of the relaxation means that a small business paying employees is permitted to submit only one report under RTI a month, rather than all the reports which may be required. However, this is all a bit of a red herring, as HMRC has previously announced that there will be no penalties for late filing of RTI returns for 2013/14, provided that the employer has submitted the final report of payments made to employees by 19 May 2014. What does appear clear, though, is that the gloves will be off from April 2014 when late return penalties will be levied, although the level of penalties has yet to be announced.

In a second development, HMRC now appear able to process requests for annual PAYE schemes. HMRC are keen to emphasise that annual schemes only apply where:

- ALL the employees are paid annually in the same month and
- the employer is required to pay HMRC annually.

This reduces the number of RTI returns required from 12 to only one.

Finally, it has always been clear that the RTI system is not directly linked to the HMRC system that records PAYE payments. Over time this will happen but RTI highlights the tax which is due and when it is due. There are stringent PAYE late payment penalties which are structured on a sliding scale. The more late payments in a tax year, the larger the percentage penalty applied to the aggregate of the late payments. The first default in any year is disregarded altogether. The remaining defaults trigger a penalty of 1%, 2%, 3% or 4% depending on their number. A 4% penalty is payable if there are ten or more defaults during the tax year. The penalties can be large and HMRC also have the power (although it has not started yet) to impose interest on the late paid PAYE. The moral is clear - ensure that PAYE is paid on time before the chickens come home to roost.

There are many PAYE related issues that occur, so if we can be of help with these or any other matters, please do not hesitate to contact us.

Mixing it up

HMRC issued a consultation document 'Partnerships: A review of two aspects of the tax rules' earlier this year. We are currently awaiting further response from HMRC and possibly draft legislation at some point in Finance Bill 2014.

This article outlines the potential scope of these changes and how these might affect you.

Salaried members of LLPs

An LLP (limited liability partnership) is an alternative corporate business vehicle that gives the benefits of limited liability but allows its members the flexibility of organising their internal structure as a traditional partnership. The LLP is a separate legal entity with liability for the full extent of its assets but which accords its members the benefit of limited liability. However, for tax purposes, the LLP is usually taxed as though it were an ordinary partnership with its individual members taxed on their profit share on a self-employed basis.

Individual members are taxed as a self-employed member even if their role in the LLP would ordinarily mean that they would be regarded as being in an employer-employee relationship. They may, for example, bear no risk within the LLP and enjoy a fixed salary which they are guaranteed to receive. HMRC are concerned this results in an individual member receiving a more favourable treatment in respect of their income tax and National Insurance Contributions (NIC) position compared to an employee of the LLP (or any other business) on similar terms.

From 6 April 2014 the proposals will prevent members of an LLP benefitting from the default position of self-employment status if the reality is that their terms of engagement amount to an employee-employer relationship. As a result, the salaried member will be liable to both PAYE and employee Class 1 NIC. Additionally, the LLP will have to pay employer NIC at 13.8%. These rules will apply where specific conditions apply.

Profit and loss allocation schemes - all partnerships

The principal arrangements under the microscope are where partnerships with mixed members or partners i.e. individuals and companies arrange the allocation of profits and losses in such a way that a tax advantage is obtained. Typically this means the allocation of sometimes substantial profits to corporate members that will pay a lower rate of tax rather than to an individual member. A corporate member may pay a 20% rate of corporation tax whereas an individual member may have an income tax rate of 40% or 45%.

Alternatively, where losses are incurred the arrangements are such that the losses are allocated to the individual member who will obtain relief at a higher rate of tax!

There may, of course, be sound commercial reasons for having a company as a member of the partnership. However, HMRC has seen an increasing number of such arrangements where it considers profit sharing ratios are artificial.

The proposed changes to the rules are intended to deter arrangements that exploit the tax treatment of mixed member partnerships. Subject to specific conditions being met, HMRC would be able to counteract the arrangements and allocate all or part of the profits that have been allocated to the corporate member to individual members with a restriction in tax relief in the case of losses.

The consultation document states that these rules would apply with effect from 6 April 2014 in relation to profits and losses that arise on or after that date.

As you can see these are fundamental proposals which could impact on you. We will keep you informed on any developments in this area and how they may affect you.

It's all about the records

6 April 2013 saw the start of a brand new way of determining the UK tax residence status of individuals. Known as the Statutory Residence Test (SRT) it provides a series of tests which, when correctly followed, will enable a definitive answer to be given to the question 'Am I resident in the UK?'

The tests cover a wide range of issues including:

- days spent in the UK
- employment or business activities both in the UK and in other countries
- the existence of a home, whether in the UK or overseas
- the residence of a spouse or live-in partner and
- availability of accommodation.

This article cannot consider the detail of the rules but we can supply you with more information on the likely application of the rules to your situation.

What is clear is that anyone wishing to claim non-resident status should be aware that such a claim will require evidence to support it. In the absence of sufficient evidence, HMRC will be entitled to reject the claim and regard the individual as UK resident which may have significant, adverse consequences. We understand that keeping detailed records can be a bit of a pain especially when coping with a modern business life which is hectic and stressful. However, finding that you have a significant tax bill because HMRC will not accept a claim for non-residence could be a very high price to pay for not spending just a few minutes each day recording some basic information.

What records?

There is no set list of records but we consider that the following evidence would be the minimum that is likely to be required by HMRC.

All individuals should keep records to show their movements in and out of the UK and in other countries. The minimum requirements will be to record:

- days when you were in the UK at midnight
- identify any days where you were in the UK at midnight but only because circumstances beyond your control meant that you had to remain in this country
- identify also any days when you were in the UK at midnight but were simply in transit on to another country (provided you did not have any business in the UK during your transit period)
- days when you were in the UK during any part of the day but not at midnight
- if you were not in the UK at midnight, where were you?

If you have a home overseas (you don't have to own it) you will need to record all the days on which you were present in that home in each tax year. HMRC may wish to see evidence to justify why you think a particular property should be regarded as a home for this purpose.

Individuals who are working either as employees or as self-employed individuals in their own business should have copies of any employment contracts or contracts for their services and will also need to have records of:

- the hours spent working in the UK on any day
- the hours spent working overseas each day
- days when you were on annual, sick, or parenting leave from your work overseas.

The list looks formidable but can be reduced to a basic spreadsheet. Armed with that information it will be possible to give advice on your residence status for UK tax purposes. Without it the advice would be very provisional and the position could well be challenged by HMRC.

Exiting the family business efficiently

Imagine this scenario. Mother and father have been running their business as a company for many years. Some of the children are taking more responsibility in the business and it is time perhaps for the parents to let the children take control. The parents would like the profits which may have been accumulated in the company to be paid out to them if it can be done tax efficiently.

Both these objectives can be achieved by using tax legislation which gives favourable tax treatment to an individual when a company purchases some of its own shares.

In broad terms the steps are:

- The next generation is given some shares in the company. This may be a minority holding say 30% of the company and may be done several years before the parents want to relinquish control. No tax charge should arise for the parents or the children due to the availability of tax reliefs where it qualifies as a trading company.
- Sometime later, when parents want to retire, the company buys back their shares. If done correctly the proceeds received by the parents will be taxed as capital receipts for the sale of their shares (rather than subject to income tax). Entrepreneurs' Relief may be available where both the individual and the company meet certain conditions so the tax charge is only 10% on the receipts less the original cost of the shares.
- Under company law, the company will cancel the shares with the effect that the shares held by the next generation are the only shares in issue. This means they now own 100% of the company.

Are there any problems? Yes there are but we are here to help manage the process.

Playing by the rules

There are rules in company law which must be dealt with. If the rules are not followed, the effect can be that the purchase of shares is an invalid purchase and unfortunate consequences may follow.

There are also tax rules to follow. The two keys matters to establish are:

- that the company is a trading company for the purposes of Entrepreneurs' Relief. This enables the proceeds from the sale of shares to the company to qualify for a 10% tax rate.
- that the purchase of shares is for 'bona fide commercial reasons'. A clearance procedure is available upon application to HMRC.

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And finally there are financing issues. What if the company has insufficient cash to pay for the shares in one go? This can trigger all sorts of problems for the unwary but it is possible in many cases to resolve the issues.

A recent dispute between an individual and HMRC has recently ended up before a tax tribunal. One of the two shareholders wanted to exit the company as there was disagreement as to the running of the company. £120,000 was paid by the company for the purchase of his shares. The individual expected a capital gains tax bill at 10%. HMRC assessed him to income tax as the shareholder had only owned the shares for four years (one of the conditions for capital treatment is that the shares are owned for at least five years).

He was able to remove the income tax bill at the tax tribunal on the basis that the distribution was unlawful as the company had not complied with a number of company law requirements. The tax tribunal agreed that the £120,000 was not a valid distribution. However, this did mean that the £120,000 paid to him had to be returned to the company. The consequential effect is that the company is instead treated as having lent him the money which triggers off other tax consequences for the company (and him).

And he has to pay the costs of his professional advisers and other costs...

Oh dear. Do please talk to us so that we can guide you through the minefield to a safe 10% tax bill.

Successful giving has rules too

Many people make donations of unwanted clothes and other goods to charity shops. If you have done this in recent years you will almost certainly have been asked by the staff in the shop if you want to Gift Aid your donation. This may come as a bit of a surprise because you were of the opinion that Gift Aid applied only to gifts of money! Actually you were quite right - Gift Aid is only applicable to gifts of money. This does not mean that what the charity shop is asking you to do is to take part in some tax avoidance scheme but there are some misconceptions on both sides about what is actually happening here.

What HMRC have been prepared to do is to accept that if the charity shop is actually selling goods on behalf of the donor, and the donor is prepared to allow the shop to retain the cash proceeds then those cash proceeds can be subject to a Gift Aid claim. That of course helps the charity and can help the donor if they are a higher or additional rate taxpayer. Unfortunately it is clear that many volunteers in charity shops do not understand the system and that could lead to some problems for the charity concerned.

HMRC recently updated their guidance to charities on how to deal with these matters. The guidance is on the HMRC website at www.hmrc.gov.uk/charities/guidance-notes/chapter3/sectionf.htm. It is strongly recommended that if you are involved with a charity shop that you look at this detailed guidance and ensure that your procedures are compliant with it. Failure to do so could mean that HMRC take action to recover any tax wrongly claimed.

The guidance makes it very clear that what is happening in these situations is that the shop is selling the goods as agent for the donor who can actually do what they like with the proceeds. The shop should make clear to the donor the implications of the Gift Aid process.

Charity shops are being given different ways in which they can operate the Gift Aid scheme. There is not space in this article to cover all the details but the essential processes are:

- the donor gives a Gift Aid declaration when they donate the goods
- the shop marks the goods so that they can be identified as coming from the donor
- the shop will normally advise the donor of the net sale proceeds before a Gift Aid claim is made unless one of two methods (helpfully referred to as Method A and Method B) are used.

Method A involves the charity writing to the donor only where the total sums donated in a year exceed £100. Method B will be used where there is a trading company running the shop and replaces the limit with £1,000 as an annual sum. In both cases the details of the scheme must be explained to the donor at the time they donate the goods and the shop must have procedures in place to be able to track the sale of the goods and record the amounts for each donor so that letters can be sent out if those limits are exceeded. If a donor asks for details of the sums actually received by the charity so that they can make a claim for higher rate relief, then that information must be supplied to them.

Given that sales in charity shops are now approaching £1billion annually there are clearly significant benefits to charities in seeking Gift Aid but those benefits will be lost if basic procedures are not followed. The message from HMRC is to take the time to get the procedures right and the benefits will flow.