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ACCOUNTANTS • BUSINESS ADVISERS

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Accountants ● Business Advisers

END OF THE TAX RETURN

Preparing for digital business records

HMRC believe that a lot of small businesses do not pay the right amount of tax on their profits due to a delay in writing up their accounting records to the end of the year.

To resolve this problem, HMRC announced its intention to require businesses to record their expenses and income digitally, as near to the date of payment or receipt as possible, and update HMRC at least quarterly.

HMRC think that simple accounting software, such as an app on your smart phone, will make this task easy to do. Free software may be available for very simple businesses.

These changes are collectively called Making Tax Digital (MTD) but we suspect it is going to feel like 'making tax difficult' for many businesses.

QUARTERLY REPORTING

Under the existing proposals, from April 2018 most unincorporated businesses and landlords will have to report a summary of their income and expenses to HMRC, within one month of the end of each quarter.

The current timetable envisages that all companies will be making quarterly reports from April 2020. But HMRC have not specified exactly what will be required to be reported by companies or by complex partnerships.

EXEMPTIONS

It is proposed that those with low levels of income (under £10,000 annual turnover or gross rents) will not be required to make quarterly reports to HMRC. Also, slightly larger unincorporated businesses (with turnover of in excess of £10,000 but below a threshold to be decided) will not need to make quarterly reports until after 5 April 2019.

The consultation period for MTD has now closed and HMRC will publish their responses in January 2017. There will be a minimum of one year to adopt any changes and we will advise accordingly at that time.

BE PREPARED

In the meantime, the best way to prepare for this digital revolution is to get into the habit of recording your income and expenses using some form of accounting software. For those taxpayers that already do this there is nothing further to do at this time. The majority, if not all, software providers will accommodate any changes and in any event we will of course be there to assist as and when required.

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EMPLOYMENT TAX ROUNDUP

Changes to benefits in kind in the Autumn Statement

TRIVIAL BENEFITS

From 6 April 2016 a new statutory exemption for trivial benefits came into force. A trivial benefit is a non cash gift to an employee, not exchangeable for cash and worth no more than £50 (though store gift vouchers are permitted). Employers can give as many trivial benefits to their employees as they wish. Each gift is tax free and exempt from NIC, as long as it is not a reward for services and not connected to the recipient's employment contract.

A Company's Directors are only permitted to receive up to £300 of trivial benefits each tax year. That total includes the value of trivial benefits provided to a Director's family members.

SALARY SACRIFICE

Many employers allow employees to pick and choose from a range of benefits such as extra holiday, company car or health insurance. Each employee may be able to sacrifice a part of their salary to receive the benefit, which often results in NIC savings for both parties and a tax reduction for the employee.

From 6 April 2017, most benefits provided by way of salary sacrifice will be taxable on the greater of:

- the amount of salary sacrificed; and
- the value of the benefit for tax purposes.

The employee will face an increased tax charge on the grossed up value of the benefit i.e. the gross salary needed to buy the benefit after tax deductions.

There will be transitional arrangements for cars, school fees and living accommodation, which can stay in place until April 2021 without additional tax charges. Also, the tax treatment of the following four benefits will not be affected:

- pension contributions and associated advice
- childcare vouchers
- cycling to work scheme; and
- ultra low emissions cars.

In all other cases the salary sacrifice arrangements should be reviewed without delay.

QUARTERLY REPORTING FOR AGENCIES

Employment agencies are required to report to HMRC the payments they make to workers they place with third parties, if those workers are not paid under PAYE. This requirement covers any organisation who finds work for an individual, which can include many agencies or intermediaries. One man companies who only find work for their sole Director are, however, exempt.

> This reporting requirement has been in place since 6 April 2015 but many businesses are unaware that they need to report to HMRC at least four times a year, within one month of the end of each quarter. For the quarter to 5 January 2017 the report must arrive with HMRC by 5 February 2017. If the agency has not supplied any workers in the period it must submit a nil report by the same deadline.

The report must be submitted online using a prescribed spreadsheet. HMRC are starting to issue penalties for late reports. These start at £250 for one late report in twelve months, increasing to £1,000 for three or more late reports, then £600 per day for a continued failure to report on time. Please do not ignore any penalty notices you receive from HMRC and do contact us for assistance.

Where your business is involved in finding work for others, we should talk about your reporting requirements.

SQUEEZE ON BUY TO LET LANDLORDS

We summarise the recent changes to property taxation

RESTRICTION OF FINANCE COSTS RELIEF FOR INDIVIDUAL LANDLORDS

This change will restrict relief for finance costs on residential properties to the basic rate of Income Tax and will be introduced gradually from April 2017 over four years. Finance costs do not just include mortgage interest they could also be interest on loans to buy furnishings and fees incurred when taking out or repaying mortgages or loans.

Landlords will no longer be able to deduct all of their finance costs from their property income to arrive at their property profits. They will instead receive a basic rate reduction from their Income Tax liability for their finance costs. They will be able to obtain relief as follows:

For 2017-18 the deduction from property income will be restricted to 75% of finance costs with the remaining 25% being available as a basic rate tax reduction. Over the subsequent three years the direct deduction of finance costs will reduce by 25% each year until 6 April 2020 when all finance costs incurred by a landlord will be given as a basic rate tax deduction.

The overall effect is shown in the table below (assuming basic rate remains at 20%):

There are certain circumstances which allow any excess finance costs to be carried forward to following years.

Please note that these changes do not affect furnished holiday lettings or lettings of non residential property.

As rental profits will be computed without including interest payments, it means residential landlords will have higher overall taxable income. This could push an individual into a higher rate of Income Tax (40% / 45%), reduce their personal allowance (if their income now starts to exceed £100,000), affect their entitlement to child benefit and restrict the amount on which they can claim tax relief for pensions.

We believe that these changes are likely to have a profound effect on the economics of many residential property portfolios. If you think you might be affected please contact us to start planning now for April 2017 and beyond.

	'A' % of costs allowed as deduction	'B' % remaining of costs subject to Basic Rate Tax Relief	'C' Effective tax relief at 20%	Effective Finance Cost Deduction 'A' + 'C'
2017-18	75	25	5	80
2018-19	50	50	10	60
2019-20	25	75	15	40
2020-21 and beyond	0	100	20	20

VAT FLAT RATE SCHEME

Flat Rate Scheme skewered by the Government

Many small businesses use the VAT Flat Rate Scheme (FRS) to simplify VAT reporting and some gain a cash advantage from using the Scheme.

When using the FRS you simply multiply your gross sales (including VAT charged at normal rates) by the FRS percentage for your trade sector. You ignore VAT incurred on purchases, except for capital items costing £2,000 or more. The FRS percentage is set to take account of the VAT likely to be incurred on business expenses.

A business which incurs few expenses, and operates in a sector with a relatively low FRS percentage, will pay out less VAT to HMRC under the FRS, than outside the scheme. This is the cash advantage.

The Government is set to remove this cash advantage from 1 April 2017 by requiring low cost traders to use a FRS percentage of 16.5% of gross sales. This is equivalent to 19.8% of net turnover, leaving almost no credit for VAT incurred on purchases.

You will be classed as a low cost trader if your annual expenditure on goods (not services) is less than 2% of your gross turnover or, if more than 2%, less than £1,000 per year. This will discriminate against businesses who incur VAT on services such as rent, software licenses, IT support, digital journals, subcontractors, and telecoms.

Knowledge based businesses such as consultants, journalists, estate agents and lawyers, may find it uneconomic to use the FRS. If you work in a knowledge based trade we should discuss whether you should withdraw from the FRS from April 2017 or even deregister from VAT.

WORKING FOR PUBLIC SECTOR CLIENTS

If you contract through an agency to work for a public sector body, from 6 April 2017 the agency will have to decide whether the contract falls within IR35 or not. If it does, the payment to your personal company will be subject to PAYE and NIC and no 5% deduction for costs will be made. This change only applies to public sector contracts.

HOW YOUR SAVINGS ARE TAXED

Changes to tax on savings and how it affects you

For many years banks have deducted tax from interest they paid to savers, unless the particular account was designated as tax free, such as an ISA. That default position changed from 6 April 2016.

Now all bank and building society interest is paid without tax deducted but the individual saver is taxed on the interest they receive. However, most taxpayers are eligible to be taxed at 0% on all their savings income, which includes interest, so no tax is payable.

This zero tax rate applies if the savings income falls within the taxpayer's savings rate band (worth up to £5,000 per year) or within their savings allowance (worth up to £1,000 per year). Any savings income which falls outside that rate band or allowance is taxed at the taxpayer's marginal Income Tax rate (20%, 40% or 45%).

Dividends are not categorised as savings income as they are subject to different tax rates and allowances.

How much savings rate band (SRB) you have available depends on the level of your taxable non savings income for the year. Any salary, pensions, trading profits or rent you receive which exceeds your personal allowance, eats up your SRB.

EXAMPLE

Colin receives a pension of £16,000 and savings income of £1,500. After deducting his personal allowance of £11,000, he has £5,000 of taxable pension. This entirely eats up his SRB so he has no SRB band to set against his £1,500 of savings income.

Colin's total taxable income is £6,500 (£5,000 pension plus £1,500 interest) which falls within the basic rate band (up to £32,000). As a basic rate taxpayer Colin is entitled to a savings allowance of £1,000. He deducts this allowance from his savings income of £1,500, leaving £500 taxable at 20%. Colin pays tax of £100 (£500 x 20%) on his savings income.

MARGINAL TAXPAYERS

Higher rate taxpayers are entitled to a savings allowance of £500 and additional rate taxpayers (income over £150,000) are not entitled to the savings allowance.

Taxpayers whose income pushes just over the basic rate band into 40% tax rate will lose half of their saving allowance. Straying over the £150,000 threshold will mean all the savings allowance disappears.

The boundaries between the tax rates can be expanded by making Gift Aid donations or personal pension contributions. We can calculate whether an additional pension contribution or donation will reduce your total tax bill.

CLIENT CORNER

May we all here at Watsons

Escape from transactions

Running payrolls and nominal ledger

Rejoice in the season and generally pledge a

Year ahead of committed endeavour; to

Clients and contacts one and all

Have the best Christmastime, have a ball

Reindeer will soon be on their way

Intrepid travellers hauling their gift laden sleigh

Saint Nick will visit all good boys and girls

Take joy in the moment as the day unfurls

Merriment and excitement fill the air

As families and friends come together everywhere

So **Merry Christmas to all** and a **Happy New Year!**

Wishing you Health, Wealth and Prosperity for 2017!

From all at Watsons

Dates for your Diary

1 January 2017	Due date for payment of Corporation Tax for the period ended 31-3-2016
31 January 2017	Last day to file 2016 Tax Return online
	Balancing payment for 2015/2016 Income Tax/Class 4 NICs due
	Capital Gains Tax payment for 2015/2016
	First Self Assessment payment on account for 2016/2017
2 March 2017	Last day to pay balance of 2015/2016 tax and Class 4 NICs to avoid automatic 5% penalty
March 2017	Budget speech by Chancellor of the Exchequer
31 March 2017	End of Corporation Tax financial year