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WARREN  
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*February 2017* NEWSLETTER

# MAKING TAX DIGITAL

This Newsletter was delayed to await the Revenue's response to their consultation document, which was eventually published on 31st January. As usual they have paid little heed to the fears of the accountancy profession that the new system was being brought in too quickly. Also our concerns that the turnover levels to 'join' were too low, have not yet been addressed.

The Government wish to make the United Kingdom the world leader in making their tax system 'Digital', which effectively means that all information relevant to a person's or Company's tax affairs will be entered onto a separate account, accessible only on a computer or phone screen, for each person or organisation. Some of this financial information will be entered by the tax office themselves, where they already know the figures, such as savings income and wages. Other figures such as income from a business or rents will have to be entered on-line by an individual. This information will have to be entered quarterly, and this is the main difference from the system at present. At the same time they are introducing a 'voluntary' system to pay tax quarterly as well, and Martyn's view is that it wouldn't take a soothsayer to work out that in time this will become compulsory, although no date has yet been fixed.

***So how will all this affect you?*** For those who currently keep their records manually, and wish to continue to do so in the future, we will have to receive all the usual records more regularly for us to submit the quarterly figures to the tax office digitally. For those who already use a computer for their financial records, or wish to change from manual records, it will be possible to upgrade the software and then submit their own figures quarterly. The problem will be knowing what, and what not, to claim for, and consequently either overpaying tax or leaving oneself open to a tax office investigation for underpaying tax, with resulting additional interest and penalties. Many of you will choose to continue to supply us with your financial information once a year as at present. This will be possible because the figures



for first three quarters of a year can be submitted by you, in a fairly basic format, not much more complicated than a VAT return. It is the fourth quarter that the more detailed adjustments have to be made, such as for stock and work in progress movements, debtors, creditors, accruals, prepayments, private use adjustments, Capital allowances and the like. Of course if you wish we can submit all four quarters figures on your behalf.

## ***The time scale for the introduction of the new digital age is –***

April 2018 – Non corporate taxpayers (self-employed & landlords) under the VAT threshold

April 2019 – Non corporate VAT registered firms

April 2020 – Limited Companies

# LANDLORDS

In our Spring 2016 newsletter we listed all the woes that had befallen landlords recently. We have received several requests asking whether incorporation would resolve any of these problems. The answer, as always, is possibly.

*We must first look at some of the advantages –*

- 1. The maximum tax rate on rents in a Company is normally less than half of the top personal rate of tax, and from April 2017 less than even the basic rate of tax.
- 2. Capital gains retained in the Company are taxed at the same low rate as for rents, with, at present, additional relief for indexation, compared with significantly more for individuals who are, or become, higher rate taxpayers.
- 3. In a Company the tax on a Capital gain is not payable until 9 months after the end of the financial year in which the sale took place. After April 2019, individuals pay the tax within 30 days of the sale.
- 4. Interest is fully allowable in a Company, whereas, from April 2017 higher rate tax relief is restricted for individuals. This may not be the advantage that it would appear to be in that the corporation tax relief that it obtains is similar to the basic rate of tax for an individual.

*Conversely we must also look at some of the disadvantages –*

- 1. The first two advantages above only apply if the rental income, or capital gain, is retained in the Limited Company. If the rents or sale proceeds are distributed to the Shareholders there is an element of double taxation in that the profits, having already been taxed in the Company, are then normally taxed again when being paid to the shareholder. For example a higher rate taxpayer would pay additional tax of 32.5% on dividends in excess of £5,000. However if the amounts paid to a shareholder are small, i.e. within their basic rate band and dividend allowance, then there would be no additional tax
- 2. Companies do not obtain an annual



allowance, over £11,000 per individual, against the gain on the sale of properties.

- 3. The corporation tax payable on the sale of a property, followed by either the dividend tax, or CGT if the Company is liquidated, would exceed the CGT payable if the property was held by the individual.
- 4. Residential properties worth over £500,000 may be subject to the Annual Tax on Enveloped Dwellings (ATED), and even if covered by an exemption, forms must be completed annually.
- 5. Individuals can obtain a fixed £1,000 allowance against rents, instead of the actual expenses, if this benefits them.
- 6. Lenders tend to charge a higher rate of interest to Limited Companies, compared with individuals, and just obtaining the finance is more difficult.
- 7. It is also necessary to take into account all the other disadvantages (and advantages) of incorporation.

*In addition there are three further disadvantages if transferring properties, already owned, into a limited company –*

- 1. Whether the properties could be classed as a 'business'. The classification of a 'business' then permits the transfer of the properties without incurring Capital Gains Tax on the gain when transferring the properties. The definition of a business would be letting several properties and actively managing them, carrying out virtually all the functions associated with letting (collecting rent, obtaining and vetting new tenants, enforcing tenancy agreements and maintaining the property). This category permits properties to be transferred to a Limited Company with a



section 162 roll-over of the Capital gains tax, although as the base cost of the shares is reduced it is in effect only a deferral of the tax, which would materialise when the Company was sold or liquidated. The scale of activities is generally considered to require at least ten hours of work per week. This requirement to have a business, as compared to a trade, is only relevant to obtain CGT incorporation relief. It has no relevance to Business Property relief (IHT), Entrepreneur relief (CGT) or offsetting losses (IT), all of which requires the business to also qualify as a trade, which is exceptionally hard, if not impossible, to achieve for property rentals.

■ 2. The second disadvantages of transferring property to a Limited Company is that under s.53 FA 2003 there may be Stamp Duty payable on the market value of the property transferred, together with legal fees. However, under Sch. 15 FA 2003, partnerships, in certain limited circumstances, can transfer properties without Stamp Duty.

■ 3. Finally incorporating an existing rental business would involve refinancing all the properties which were previously on personal mortgages. This may prove to be expensive, with the probability of being unable to match the terms of a personal mortgage, and possibly incur early repayment penalties.

## EMPLOYERS

### Same rules for all

The same rules now apply to tax expenses and benefits regardless of how much the employee earns and whether he or she is a director. The old £8,500 threshold was abolished from 6 April 2016. Since that date, employees who were previously P9D employees are taxed on any benefits in kind that they receive in the same way as for P11D employees. This means that benefits such as company cars and private medical insurance are now taxable if the employee earns less than £8,500.



### No more P9Ds

As a result of the changes, 2015/16 is the last tax year for which P9Ds are required. From 2016/17, where an employee has received a taxable benefit in kind, you will need to use form P11D to tell HMRC about that benefit, unless you have opted to tax it through the payroll.

### Payrolling for 2017/18

Although it is now too late to start payrolling for 2016/17, looking ahead to next year, if you want to deal with some or all of the taxable benefits that you provide through the payroll instead of reporting them to HMRC on form P11D after the end of the tax year, you need to register to do so by 5 April 2017. Speak to Ken regarding what benefits can be payrolled and whether payrolling is for you.

### New exemption for deductible expenses

A new exemption replaced the dispensation regime from 6 April 2016. It is available for expenses which would be fully deductible if the employee met the expense from his or her own pocket. Items such as business travel qualify. The exemption, which applies to qualifying paid and reimbursed expenses, is given automatically. Unlike the old dispensations, you no longer need to apply.

### Trivial benefits

The long-awaited exemption for trivial benefits came into effect from 6 April 2016. Broadly, a benefit is trivial if the cost of providing it is £50 or less. Benefits that count as 'trivial' can be ignored and do not need to be reported to HMRC. Items such as a bunch of flowers sent to an employee on her birthday or a bottle of wine given to employees at Christmas may pass the 'trivial' test. However, for directors and employees of close companies, the trivial benefits exemption is capped at £300 per individual per year.

## GET YOUR AFFAIRS IN ORDER HMRC campaigns

HMRC are currently running a number of campaigns to encourage taxpayers who have undeclared income to come forward and bring their tax affairs up to date in return for lower penalties. In particular, campaigns are available in respect of let property, second incomes and credit card sales. If you have income from any of these sources which you need to tell HMRC about, please talk to us as to how you can get the best possible deal under the available campaigns.

## Other undeclared income

If you have undeclared income and gains from a source not currently covered by an HMRC campaign, speak to Martyn about making a disclosure. HMRC deal more favourably with people who come to them, than with those who wait to be found out.

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This newsletter deals with a number of topics which, it is hoped, will be of general interest to clients. However, in the space available it is impossible to mention all the points which may be relevant in individual cases, so please contact us for personal advice on your own affairs.

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**Martyn J. G. Warren**

*Chartered Accountant* - mw@awgw.co.uk

**Kandy Pitrola**

FCCA, FMAAT, ATT - kp@awgw.co.uk

**Simon Jeremy**

FCCA, BA (Hons) - sj@awgw.co.uk

**Nick Metallinos**

AFA - nm@awgw.co.uk

**Ken Rock**

kenrock@awgw.co.uk

**Lorraine Clutterbuck-Jones**

lcj@awgw.co.uk

**Gail Kurowski**

*Administration & Company Secretarial* - gail@awgw.co.uk

**Debbie Lawes**

debbie@awgw.co.uk

**Amrit L Bhardwaja**

*Consultant Bsc, FCCA, PGCE, Dip IFR* - ab@awgw.co.uk