Autumn 2007
Newsletter

RHK RICHARDSON HALL KENNEDY
CHARTERED ACCOUNTANTS & BUSINESS ADVISERS

Inheritance Tax Planning

Lorraine Marley

Due to the recent increases in property values it is vital that consideration is given to tax planning by the majority of homeowners. This is particularly important for married couples. More often than not when a person dies all assets pass on to the surviving spouse. This wastes the nil rate band of £300,000.

Inheritance tax (IHT) may be charged on certain lifetime gifts, on wealth at death, and on certain transfers into and out of trusts. It is payable on death on the assets of an estate where they exceed the 'nil rate band' which, for this year is £300,000 (subject to the inter-spouse transfer exemption).This means that an individual may leave up to £300,000 tax free. Anything in excess of this is taxed either at the lifetime rate of 20% or at 40% for transfers on death.

At RHK we are able to offer comprehensive advice which could save you a considerable amount of inheritance tax. For example, if the nil rate band is wasted this could cost you and your family a maximum of £120,000.

To discuss your personal circumstances please contact Lorraine Marley, RHK's tax planning consultant. Tel: 0191 478 1513.

Lords rule in favour of husband and wife businesses

The long running case of Jones v Garnett (commonly called 'Arctic Systems') which began in 2003, has finally been resolved in favour of the taxpayer. This is good news for the thousands of husband and wife businesses that have faced years of uncertainty.

Background

Geoff and Diana Jones own and run an IT consultancy called Arctic Systems. Like thousands of other couples with similar enterprises, the structure of the business is such that both parties have shares and responsibilities in the company, with one major fee earner (in this case Geoff) and the other partner offering administrative support. Dividends are paid according to their shareholdings.

The case centred on the issue of whether Mr Jones' salary was set at an artificially low level, and whether the dividends received by Diana should have been treated for income tax purposes as those of Geoff, a higher rate taxpayer. HMRC had used an old piece of legislation to argue that the dividends paid to one spouse were really earned by and belonged to the major fee earning partner. This meant a retrospective tax bill of £42,000.

The uncertainty over the case has left thousands of similar businesses concerned that they too could face large and potentially crippling tax demands.

Implications

Although the government has not said that Arctic Systems will be a test case, in practice it will be difficult for the lower courts to ignore the Lords' judgment. Similar husband and wife businesses are therefore highly unlikely to be hit with retrospective tax bills like the ones originally issued in this case.

However, it seems probable that the government will now act to bring in new legislation to close what it considers to be a tax 'loophole'. Arrangements like the Arctic Systems structure may therefore soon become a thing of the past.

Contact us for advice on you particular circumstances.
Tel: 0191 478 1513.

Don't let your business become a statistic - avoid employment tribunals

RHK are hosting an employment law seminar in conjunction with Employment Law Specialists Croner, which will give you an insight into what happens in a tribunal and the legal challenges you could face. Key topics covered:

- discrimination laws
- employee rights
- tribunals
- the cost of getting it wrong

We would like to invite you to attend this free presentation to find out how you might protect your business from costly Employment Tribunal claims.

Date:
Tuesday 16th October 2007

Time:
8.00 am - 10.30 am

Venue:
Lumley Castle, Chester le Street, Co Durham. DH3 4NX

To reserve your place contact Moya Goodyear.
Tel: 0191 478 1513
or Email: mgoodyear@rhk.co.uk

The state pension: should you take a lump sum?

Since April 2005 it has been possible to defer your state retirement pension and, when you do decide to draw it, to take a lump sum or extra state pension in lieu.

If you choose to receive extra state pension, you can get an extra 1% on top of your weekly state pension for every five weeks that you put off claiming. If you defer for one year, for example, this works out as an extra £10.40 per week for every £100 of pension (£540 per annum). This sounds attractive but you will have lost out on receiving £5,200 in pension in the year, so whether you win or lose depends upon how long you receive the extra pension (surviving 10 years will be the approximate 'break even' point).

Somewhat easier to work out is the financial benefit of the lump sum. The lump sum payment is made up of the pension you had put off claiming, plus interest at 2% higher than the Bank of England base rate.

If we assume an annual 6.5% return and an annual pension that would have been payable of £5,200, the lump sum would be:

Years you put off your state pension	Lump sum payment (before tax is taken off)
1	£5,370
5	£30,580

Tax on the lump sum

A pension is counted as taxable earned income when received and a lump sum is counted as income for tax purposes. But the lump sum is not added to the rest of your income to work out your total income for tax. Instead, the rate of tax due on the lump sum payment will be the highest rate of tax paid on your other income, ignoring any of the special rates of tax that apply to interest or dividends.

For example, if you pay no tax because your other income is less than your personal allowance, you will pay no tax on your lump sum; and if your marginal rate of tax is basic rate, your lump sum payment will be taxed at basic rate.

A deferral could be attractive, therefore, if you expect to remain a higher rate taxpayer when you reach state retirement age because you are continuing to work, but will become a basic rate taxpayer when retired. It may also be appropriate in a number of scenarios where you can reduce your income in the year in which the lump sum is taken.

In summary, an interest accrual of 2% higher than base rate on a pension entitlement before tax is a very attractive return. It gets even better if you can choose which tax rate applies.

Forecasting (sales and) success

Making predictions for future growth should not be limited to those starting up in business. While substantiating the case for finance may be the initial reason for preparing a sales forecast, annually updating your original plans can reap many rewards.

Establishing a sales and marketing plan is the key to setting a sales forecast. Your knowledge of the marketplace or outcomes of market research will help to identify the opportunities for your products and services. Focusing on a 12 to 18 month period, detailed documents can prove unnecessary; often a simple list of realistic key objectives can suffice. Always remember the obvious: customers have to want to buy your products, you wanting to sell them is never enough! The process of recording the sales plan forces you to evaluate the impact of future events on projected sales. Gathering input from the whole team may lead to initiatives and ideas for product development, pricing strategies, or marketing campaigns to your most profitable customers or for your most profitable products. Many businesses use a SWOT (strengths, weaknesses, opportunities and threats) analysis approach to kick-start their thinking.

The next stage is to add numbers to the assumptions in your plan. Calculating monthly sales volumes and values should not prove difficult once a vision for sales has been recorded. Whether a simple spreadsheet or a specialist forecasting package is required will depend on the size and complexity of your business and product mix. Building in 'what if' scenarios is not difficult to do with today's spreadsheets and can provide a clear picture of how different results will be dependent on actions taken. The sales forecast can provide the backbone for a full financial forecast or a cash flow statement where these are required.

Regular monitoring of actual performance in comparison to the forecast enables trends and sales shortfalls to be proactively addressed. Many businesses review their monthly performance and formally revise their sales forecast on a quarterly basis. By the final quarter, your initial predictions can look questionable, so regular reviewing and revising is always recommended.

Don't miss out on the opportunity to use the sales forecast to set targets to incentivise your team. Establishing creative reward schemes can make all the difference between failing, achieving or exceeding your forecast. This can also assist with performance reviews for your team.

The familiar expression 'you cannot manage what you don't measure' is certainly true where sales are concerned. Forecasting can play a key part in measuring your success and helping you to drive the performance of your business. Can you visualise your sales pipeline for the next 12 months? If your plans are not as clear as you would like them to be, we can help so please get in touch.

Making the most of the flat rate VAT scheme

The flat rate VAT scheme can be a very good deal for some small businesses, but not for others. Whether you make or lose money on the scheme largely depends on how unusual your business is compared to others in your trade sector, but there are some other strategies that can be employed.

The flat rate VAT scheme is designed to eliminate the need to record the VAT paid on all your purchases. Under the scheme you simply multiple the total of all supplies made by the business (including the VAT charged to customers) by a flat rate, set according to your main business activity. This is the amount of VAT payable to HMRC. If this calculation produces a lower figure than would result when you subtract the VAT paid on purchases from the VAT charged to customers (the normal quarterly VAT calculation), then you are a flat rate VAT winner. However, to check if you are a winner or loser, you have to keep track of the VAT you pay on purchases, which is what the flat rate scheme was supposed to avoid!

To win with the flat rate scheme you also need to have a relatively low flat rate percentage to apply. The percentage is determined by the trade sector for your business; for example Restaurants must use 12%, while Pubs use 5.5%. If your costs are low compared to an average business in your trade sector, then you are likely to be a flat rate winner.

If your business falls into two or more trade sectors, such as a pub with food sales, you must use the flat rate that relates to the sector which represents the largest part of your business. When joining the scheme, and on each anniversary, you must estimate the mix of sales from your various trade categories for the next year. If you think the mix will change you must adjust the flat rate used accordingly.

In your first year of VAT registration you are entitled to take one percentage point off the flat rate used. If you do not use the flat rate scheme immediately on registration, you will not benefit from the full advantage of the 1% discount. However, many new businesses should hold off using the flat rate scheme for at least one quarter so they can reclaim the VAT incurred on all the one-off start-up costs. It is also worth noting once you have entered the scheme you can still reclaim the VAT you have been charged on single purchases of capital expenditure goods where the amount of the purchase, including VAT, is £2,000 or more.

As you can see this is a complex area. If you have any questions please get in touch with Alison Habebi.
Tel: 0191 478 1513.

Changes to the advisory fuel rates

The advisory fuel rates allow employers to reimburse employees who drive company cars for their business mileage, tax free. For all journeys undertaken on or after 1 August 2007 the rates will increase.

Engine size	Petrol	Diesel	LPG
1400cc or less	10p (9p)	10p (9p)	6p (6p)
1401cc – 2000cc	13p (11p)	10p (9p)	8p (7p)
Over 2000cc	18p (16p)	13p (12p)	10p (10p)

Other points to note about the advisory fuel rates:

- Employers do not need a dispensation to use these rates.
- Employees driving company cars are not entitled to use them to claim a deduction if employers reimburse them at lower rates. Such claims should continue to be based on actual costs incurred.
- The advisory rates are not binding where an employer can demonstrate that the cost of business travel in company cars is higher than the guideline mileage rates.

If you would like to discuss your company car policy please contact us.

28 days holiday on the horizon

Earlier this year the government proposed to increase the minimum statutory holiday entitlement from the current 20 days (including bank holidays) to 28 days (bank holidays inclusive). The 28 days equates to 5.6 weeks for an employee working a normal five day week.

Following consultation with interested parties some amendments have been made to the original proposals. The main change is delaying when employees will be entitled to the full amount of additional leave.

The initial increase from 4 to 4.8 weeks, or 20 to 24 days for an employee who works a five day week, will come into effect on 1 October 2007, as originally suggested.

The second part of the increase, which was due to take effect from 1 October 2008, is delayed to 1 April 2009. This increase will be from 4.8 to 5.6 weeks. This will increase the holiday entitlement of an employee who works a five day week, from 24 days to 28 days leave.

The government has also amended the proposals to enable employers to pay employees for the additional holiday entitlement (the additional 0.8 weeks or 4 days) until 1 April 2009. This is a temporary measure to ease the transition.

The increased leave entitlement includes bank holidays, so employees who already receive four weeks leave plus bank holidays will not be automatically entitled to an increase.

Increases from October 2007 and April 2009 will be calculated proportionally depending on when the employee's leave year starts. The Department for Business, Enterprise and Regulatory Reform (DBERR) propose to make an online calculator available to assist employers in calculating entitlement.

In the meantime an example of how the increase in entitlement should be calculated has already been issued by the DBERR:

'If your leave year started in April, you work a 5 day week and you currently receive 20 days including bank and public holidays, you will be entitled to 2 additional days from October 2007 to March 2008.'

These proposals relate to England, Wales and Scotland. The Department for Employment and Learning in Northern Ireland is in the process of making proposals for Northern Ireland.

Drive safely

What is a sensible driving policy for your business and do you legally need to have a policy?

Businesses that employ five or more people must have a driving policy as part of their health and safety requirements.

The law requires employers to carry out an assessment of risk and to enforce a policy to minimise any potential risks identified. The policy should cover driving for work purposes but not an employee's ordinary commuting journey to and from home and their normal workplace. The policy should cover not only those driving work vehicles such as LGV, PSV and company cars but also employees using their own cars for work purposes.

Why is a policy important?

- There are an estimated three million company cars on the roads and roughly one in three will be involved in an accident each year.
- Company drivers who drive more than 80% of their annual mileage on work-related journeys have in excess of 50% more accidents involving injury than similar drivers who do no work-related mileage.
- Every week around 200 road deaths and serious injuries involve someone at work.
- About 300 people are killed each year as a result of drivers falling asleep at the wheel. About four in ten tiredness-related crashes involve someone driving a commercial vehicle.
- Work-related road accidents are the biggest cause of work-related accidental death. Between 800 and 1000 people are killed annually in work-related road traffic accidents compared to approximately 250 fatalities due to other accidents.
- Business drivers have collision rates that are 30% to 40% higher than those of private drivers.

What should your policy include?

You should first carry out an assessment of areas where there are potential hazards and the risk level these pose to employees. Where particular risk areas are identified these should be investigated to see if alternative arrangements or procedures can be put in place to effectively manage safe driving. A health and safety policy covering work-related road safety should be issued and enforced. Some of the points which employers should consider including in a safe driving policy for employees are:

- take regular breaks if travelling long distances
- be particularly vigilant if travelling early or late in the day, as at these times drivers are more likely to be tired or sleepy
- always observe speed restrictions
- carry first aid equipment
- have regular sight tests
- always carry details of the procedures to follow in case of emergency
- not to use mobile phones when driving unless a legal hands-free kit is used.

For detailed guidance on what to include in your policy the Department for Transport has set up a new area on their website, 'Driving for Work', which contains practical guidance to help businesses comply with their legal obligations. Visit www.dft.gov.uk

HMRC target buy to let landlords

Over recent months many media outlets have reported that HMRC are intending to target landlords who let property.

HMRC's concern appears to be two-fold. The buy to let market has expanded massively over the past ten years and many landlords who buy to let property attempt to sort out their tax position themselves, which can lead to misunderstandings and errors in a complex area.

Particularly common problem areas with buy to let properties include:

- claiming too much tax relief for expenses against property income
- failing to declare the amount of rent received from the let property
- failing to declare a capital gain on the sale of let property.

However, HMRC have responded with a press release; stating that they were not planning a tax crackdown but that:

'HMRC is planning to take a concerted approach to helping landlords of all descriptions (not just in the buy to let market) to understand and comply with their tax obligations in what they recognise to be a complex area … to ensure that the correct amount is paid.'

Crackdown or not … we'll let you decide!

RHK

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