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Business Matters

The new capital gains tax regime

The 2010 Emergency Budget saw the introduction of key changes to the capital gains tax (CGT) regime, including a new 28% top rate of CGT.

There are now two rates of CGT for individuals – a standard rate of 18% and a higher rate of 28%. From 23 June 2010, the rate of CGT payable on gains realised on or after this date depends on the level of the individual's taxable income and post-22 June 2010 gains for the tax year.

The higher rate applies to gains realised after 22 June 2010 where an individual has total taxable income and gains for the tax year of more than the basic rate band for income tax. For 2010/11 this is set at £37,400. In deciding whether the higher rate applies, no account is taken of any gains realised before 23 June 2010. Where an individual's total taxable income and post-22 June gains are below £37,400 the standard rate of 18% applies. All gains realised before 23 June 2010 are taxed at 18%.

The figure for total taxable income and gains is calculated after taking into account all allowable deductions including losses, personal allowances and the CGT annual exemption. Where Entrepreneurs' Relief applies the effective rate remains at 10%.

An individual can choose to utilise losses and the annual exemption in a way that minimises his or her overall CGT liability. This allows an element of planning for 2010/11 in circumstances where pre-23 June 2010 gains are taxed at 18%, but gains arising after 22 June are taxed at 28%. Clearly it is better to save tax at 28% rather than at 18% and, where the higher rate applies, the annual exemption and any losses should be set against post-22 June 2010 gains first. This is illustrated in the following example:

Example

Jane realises gains and losses during 2010/11 as follows:

April 2010: Loss £5,000

May 2010: Gain £20,000

July 2010: Gain £40,000

Jane has other income, after deducting her personal allowance, of £30,000 for 2010/11. Her total income and post-22 June 2010 gains are £70,000, which will mean that the higher rate will have effect for part of the post-22 June 2010 gains.

To minimise her overall liability, Jane should set the loss of £5,000 and the annual exemption of £10,100 against the July gain of £40,000, reducing it to £24,900. It does not matter that the loss was realised before 23 June 2010 as it was still within the 2010/11 tax year.

Jane's other income is £30,000, leaving £7,400 of the gain to be taxed at 18%. The remaining £17,500 of the gain is taxed at 28%. Her total CGT liability for 2010/11 is therefore £9,832, calculated as follows:

May gain: (£20,000 @ 18%)	£3,600
July gain: £7,400 @ 18%	£1,332
£17,500 @ 28%	£4,900
CGT liability for 2010/11	**£9,832**

Had the loss and the annual exemption been set against the May gain, this would reduce the May gain to £4,900, but increase the portion of the July gain liable to higher rate CGT to £32,600. This would increase her CGT liability for 2010/11 to £11,342. By utilising the exemption and loss carefully the overall CGT liability is minimised.

The failure to align CGT and income tax rates means that capital is preferable to income where the option exists. This should be taken into account in planning strategies.

For further information and advice, please contact us.

Inside this Issue...

The increase in VAT – what you need to know

As announced in the Emergency Budget, the standard rate of VAT is set to rise from 17.5% to 20% on 4 January 2011. It is hoped the additional revenue generated from the increase will help to reduce the UK deficit. The change will undoubtedly have a significant impact on many businesses, with the cost of implementing the new rate expected to cost UK firms millions of pounds in administration fees.

Applying the higher rate

The rate of VAT that businesses charge depends on the date that goods or services are supplied. For VAT purposes this is the date that goods physically change hands (or a service is completed); or payment is received; or an invoice is issued – whichever is the earliest. The rules are modified in certain situations, including when there is a change in the standard rate of VAT.

For any sales of standard-rated goods or services that take place on or after 4 January 2011 businesses should charge VAT at the new rate of 20%. As a consequence, firms currently calculating their VAT using the VAT fraction of 7/47 should use the new fraction of 1/6 from 4 January 2011.

Zero rated supplies, such as basic foodstuffs, children's clothing and books; exempt supplies, such as education and health; and supplies subject to VAT at the reduced 5% rate, such as domestic fuel and power, are not affected by the change.

Anti-forestalling legislation

The Finance (No.2) Act 2010 included anti-forestalling legislation to prevent the 17.5% rate applying to supplies of goods or services that are provided on or after 4 January 2011.

The legislation prevents forestalling by introducing a supplementary charge to VAT of 2.5% on the supply of goods or services where the customer cannot recover all the VAT on the supply, and one or more of the following conditions are met:

- the supplier and customer are connected parties;
- the value of the supply (and any related supplies made under the same scheme) exceeds £100,000. But this does not apply if the prepayment or issuing an advance VAT invoice is normal commercial practice;
- the supplier or someone connected to the supplier funds a prepayment for the goods or services; or
- an advance VAT invoice is issued where payment is not due in full within six months (except hire purchase invoices issued in accordance with normal commercial practice).

The supplementary charge to VAT is due on 4 January 2011 and must be accounted for on the supplier's VAT return covering that date.

The flat rate scheme

Introduced in 2002, the VAT flat rate scheme is designed to simplify VAT for businesses with an annual turnover up to £150,000, tax exclusive. While the rise in VAT will not change the £150,000 threshold, it does affect the flat rate scheme sector flat rates, which have been recalculated. A selection of the new rates is displayed in the table below.

Category of business carried on	Appropriate percentage (from 4 Jan 2011)
Retail of food, newspapers, confectionery	4
Pubs	6.5
Sport or recreation	8.5
Hotel or accommodation	10.5
Entertainment or journalism	12.5
Photography	11
Estate agency	12
Hairdressing	13
Legal services	14.5
Computer and IT consultancy	14.5

A full list of the recalculated sector rates can be found on HM Revenue & Customs' (HMRC) website:
www.hmrc.gov.uk/budget2010/vat.htm

The impact on consumers

The increase in VAT will undoubtedly have an impact on consumers as well as businesses, assuming that retailers pass on the rise. While those goods classed as 'essential' will remain free from VAT, the price of many items will become more expensive. According to some analysts, the 2.5% VAT rise will typically add at least an extra £33 a year to the average consumer's supermarket shop.

If you have any queries regarding the change in the rate of standard VAT, please contact us. We will be delighted to assist you.

Saving for your children's future

If you are a parent, you are likely to want to set aside special savings for your children, whether that means helping to fund a first car, higher education or paying for a wedding. Yet with the Child Trust Fund (CTF) set to be phased out, you may want to review your plans for saving for your child's future.

What's happening to the CTF?

Soon after taking office, the Coalition Government announced that it would restrict payments to the CTF to help reduce the fiscal deficit. From 1 August, payments at birth were reduced from £250 to £50 and from £500 to £100 for children from lower income households. Children will no longer receive an additional payment when they are seven years old and all payments into CTFs, including those for disabled children, will cease from January 2011.

However, if an account has already been opened, family and friends can still invest up to £1,200 a year. As previously, no tax is paid on any income or gains in the account and the Government will not withdraw the money it has already input.

Other options

Despite the demise of the CTF, there are other savings options available, some of which are outlined below. However, it is important to consider the tax consequences, so it is recommended that you seek professional advice.

Income tax

All children have their own personal allowance of £6,475 (2010/11), and parents can make gifts to their children and any resulting income will be tax-free as long as it does not exceed £100 a year. There are tax implications where income exceeds this limit, so investing parental gifts may be advisable. Please contact us for further guidance.

Children's bank or building society account

Setting up an account where the child's name is linked to yours is the simplest way of saving for your child. Known as a 'bare trust', the parent is the trustee and the child is the beneficial owner in respect of interest and capital. The parent has control of the account until the child reaches a specified age, but must apply the funds for the benefit of the child.

Cash ISAs

16 and 17 year olds can invest up to £5,100 in a cash ISA. You may also wish to use your own allowance to save for them and any income or capital gains you receive will be tax-free.

Children's bonus bonds

These are offered by National Savings and Investments (NS&I); the maximum holding per child is £3,000 in each issue (five year investment term). All returns are exempt from tax, and the £100 rule does not apply.

Please note, the above are just some of the available options – for further advice please contact us.

Offshore accounts – where are we now?

Following the end of its New Disclosure Opportunity (NDO), which offered taxpayers a facility to disclose savings and investment income from abroad, HMRC has followed through with its plans to pursue those individuals who it believes have undisclosed income or gains. Here we examine the current situation.

For a number of years HMRC has committed considerable resources to identifying undeclared liabilities hidden in offshore accounts. To this end it has provided a number of disclosure opportunities, initially in 2007 and more recently from 1 September 2009 to 4 January 2010, offering reduced penalties in return for people revealing their undisclosed offshore accounts and liabilities. With the exception of the specialist Liechtenstein Disclosure facility, the disclosure opportunities have now ended.

HMRC is not only interested in any undeclared interest. More importantly, it is interested in any deposits into the account which may represent undeclared sources of income and payments out of the account. It will then seek to establish whether these, in turn, have been invested in income-producing assets in respect of which the associated income has not been declared. The Revenue is also on the look out for evidence of money laundering.

Gathering information

Using its legal powers, HMRC has obtained details on offshore bank accounts from over 300 banks and financial institutions and is now pursuing those individuals who either did not notify their intentions to disclose under the disclosure facility, or made a notification but not a disclosure. Tax officials are also continuing to use their powers to obtain more detailed information on offshore accounts and assets via the European Savings Directive, which exchanges information about interest payable to residents of other EU countries.

When HMRC calls…

As always, honesty is the best policy and where liabilities remain undeclared it is always better to contact HMRC before it approaches you. The penalty regime is more lenient on those who come forward and co-operate than on individuals who seek deliberately to evade. Where an approach is made by letter, again it is advisable to provide the information requested in a timely manner.

What the future holds

HMRC is continuing to devote considerable resources to tackling the problem and will come down particularly hard on those who use offshore accounts to evade tax. Legislation introduced by the Finance Act 2010 increases the penalties which may be charged for evasion linked to offshore accounts. From the appointed day, the maximum penalty (currently 100% of tax understated) is increased to 150% where the non-compliance arises in a jurisdiction that has agreed to share information with the UK but does not automatically do so. It climbs to 200% for non-compliance arising in a jurisdiction which has not agreed to share information. Thus, the penalty is higher if the account is in a country where it is more likely to stay hidden from HMRC.

HMRC has considerable information gathering powers at its disposal and ignoring requests is likely to make matters worse in the long term. The advice of an experienced professional can be invaluable and may remove a lot of the associated stress, particularly if matters are complex and negotiations are protracted.

Emergency Budget Round-Up

The 2010 Emergency Budget announced a series of sweeping changes to the tax system, which are likely to have an impact on the majority of UK taxpayers. The changes to CGT and VAT are detailed in the previous pages, but what were the other key announcements?

Personal allowance

With the aim of protecting lower earners from the squeeze, the income tax personal allowance will rise to £7,475 in April 2011, removing around 880,000 people from the requirement to pay any income tax. However, higher rate taxpayers will be prevented from reaping the benefits of the changes by means of a reduction in the basic rate limit for 2011/12.

National insurance contributions (NICs)

Employers will see an increase in the threshold at which they start to pay national insurance contributions, which will rise by £21 a week above indexation. In addition, qualifying new businesses in targeted areas of the UK will enjoy a national insurance 'holiday' of up to £5,000 for each of the first 10 employees hired within the first year of business.

Corporation tax

Corporation tax will be reduced to 27% from April 2011, with a further series of 1% cuts taking place each year until the rate reaches 24% in 2014. The small profits rate will also be cut from 21% to 20% from April 2011.

Small business finance

In a bid to improve access to finance for small businesses, a new Enterprise Capital fund of £37.5 million is being introduced, and the Enterprise Finance Guarantee will also provide £200 million of additional lending until 31 March 2011.

Pensions

The Government has announced plans to review the pension system, with a view to accelerating a rise in the state pension age to 66 for men, and phasing out the default retirement age. The link between the state pension and earnings will be restored, and pensions will rise by the highest of the increase in average earnings, prices or 2.5%. The requirement to buy an annuity (or otherwise secure an income) by the age of 75 is to end from 2011/12. In the interim the age has been increased to 77 for those who had not reached 75 before 22 June 2010.

Office of Tax Simplification is launched

As announced in the Emergency Budget, the Government has launched its new Office of Tax Simplification (OTS), with the objective of streamlining the UK tax system and reducing compliance burdens on both businesses and individual taxpayers.

The body has been set up to analyse tax reliefs, allowances and exemptions, and to conduct a review of business taxation with a view to reducing its complexity. The organisation has been requested to produce two reports – the first a review of all 400 reliefs in the tax system to identify those that should be repealed. The second report will look at reducing complexity for smaller businesses and finding alternative legislative approaches to the IR35 rule.

A final report with recommendations will be submitted to the Chancellor ahead of the 2011 Budget.

For more advice on how the Coalition Budget measures could affect you and your business, please contact us.

Web Watch

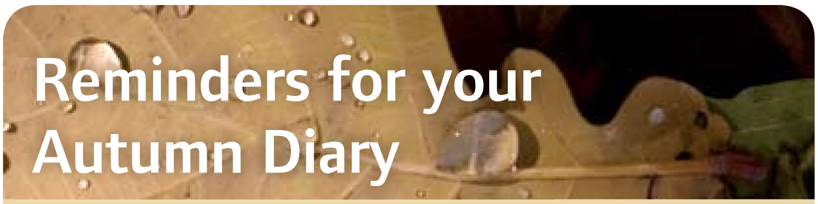
Essential sites for business owners

http://yourfreedom.hmg.gov.uk
Government website offering businesses and individuals the chance to put forward their views on specific laws and regulations.

www.payontime.co.uk
Information for UK businesses on late payment legislation and good payment practice.

www.hm-treasury.gov.uk/ots.htm
Details on the new Office of Tax Simplification, an independent body set up to advise the Government on simplifying the UK tax system.

www.retirementreform.org.uk
Website of the Centre for Retirement Reform, a think tank which has been set up to facilitate reform of the UK pensions system.



Reminders for your Autumn Diary

September

30 End of CT61 quarterly period.

October

1 Due date for payment of Corporation Tax for period ended 31 December 2009.

5 Individuals/trustees must notify HMRC of new sources of income/chargeability in 2009/10 if a Tax Return has not been received.

14 Due date for income tax for the CT61 quarter to 30 September 2010.

19/22 Quarter 2 2010/11 PAYE remittance due.

31 Last day to file 2010 paper Tax Return.

November

1 Please ensure you are retaining your documents for the 2011 Tax Return.

2 Quarterly submission date of P46 (Car) for quarter to 5 October.