Newsletter AUTUMN 2010

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How much CGT will I pay?

Capital gains tax (CGT) has become more complicated following the Budget on 22 June. For gains made after that date, higher rate taxpayers, trustees and personal representatives of deceased estates pay CGT at 28%. CGT at 10% can apply if the disposal qualifies for entrepreneurs' relief.

This mid-year change of rates creates difficulties when calculating the CGT payable for 2010/11. Here's a three-step guide to the problem:

Step 1

First allocate your chargeable gains into those arising before 23 June 2010 (still taxed at 18%) and those arising from that date onwards. To do this you need to identify the exact disposal date for CGT purposes for each disposal. Where a sale is made by contract, the normal disposal date for CGT purposes is the date on which unconditional contracts are exchanged, not the completion date. For conditional contracts, the disposal date is when the condition either lapses or is satisfied.

Different disposal dates apply for deemed gains that arise on the return of a non-resident taxpayer to the UK after an absence of fewer than five years, or in connection with enterprise investment schemes or venture capital trust shares, or where a negligible value claim is made. Complications arise when gains are created by remittances to the UK by non-domiciled individuals, or movements in foreign currency bank accounts. If these circumstances apply to you, please talk to us.

Step 2

Estimate your net taxable income for 2010/11. This is your taxable income for the whole year to 5 April 2011, less your tax-free personal allowances and all tax-allowable deductions. If this exceeds £37,400 (the basic rate limit), the gains you make on or after 23 June 2010 will be taxed at 28%. If your net taxable income is lower than the basic rate limit, deduct that total from the limit. The difference is the amount of your post-22 June gains that are taxed at 18%. The balance of your post-22 June gains will be taxed at 28%. This calculation is made before deducting capital losses, your CGT annual exemption or other CGT reliefs.

Step 3

If you have gains taxed at both 18% and 28%, then you can choose to set your annual exemption and any capital losses against the gains taxed at the higher rate. You should also consider whether to defer or hold-over any particular gain.

Please get in touch with us to discuss how these issues may affect you.

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This newsletter is for general information only and is not intended to be advice to any specific person. You are recommended to seek competent professional advice before taking or refraining from taking any action on the basis of the contents of this publication. The newsletter represents our understanding of law and HM Revenue & Customs practice as at August 2010.

Child trust fund and tax credits

The Government has announced that children born after 31 December 2010 will no longer qualify for a child trust fund account.

Children born between 1 August 2010 and 31 December 2010 will receive a voucher worth £50 instead of £250 as previously, with a top-up of £50 for those on low incomes. The extra £250 currently paid on a child's seventh birthday will cease to be paid where a birthday falls after 31 July this year.

Extensive changes to the tax credits system will also be made from 6 April 2011. The child element of the child tax credit (CTC) will be increased by £150 above the normal inflation increase, but the baby element (£545) will stop. The rate of withdrawal for all tax credits is to be increased to 41p in the pound. Presently, the withdrawal rate is generally 39p, but only 6.67p in the pound for the family element of CTC.

In addition, the level at which the family element of CTC is withdrawn is to be reduced from £50,000 to £40,000.

The exact income level at which no tax credits will be paid depends on personal circumstances, but the Government's intention is that people with incomes of over £50,000 should not in general be entitled to any CTC or working tax credit.

How to defer a capital gain

If you have made a capital gain that will be taxed at the new higher rate of 28%, you might decide to defer it to a later tax year.

This will reduce the tax payable if your future marginal rate of capital gains tax (CGT) is lower, or you have more losses or available annual exemption in that later year.

Where the gain arose from disposing of a business asset used for your trade, you can defer the gain by investing the net proceeds in another qualifying business asset in the period one year before to three years after the date of the disposal.

Alternatively, you could defer your gain by subscribing for Enterprise Investment Scheme (EIS) shares. This acquisition also needs to be made within the same four-year period. But you only need to reinvest the amount of the gain you want to defer, not the net proceeds from your disposal.

You have over five years after the EIS shares are issued to claim the deferral. However, you must pay any CGT due for 2010/11 by 31 January 2012, so in practice your decision period is shorter. Of course you could pay the 2010/11 CGT on time, and then reclaim that tax once your deferral claim is processed.

KEY TAX DATES

Every month

1 Annual corporation tax due for companies with year ending nine months and a day previously, eg tax due 1 July 2010 for year ending 30 September 2009.

14 Quarterly instalment of corporation tax due for large companies (depending on accounting year end).

19 Pay PAYE/NIC and CIS deductions for period ending 5th of the month if not paying electronically. Submit CIS contractors' monthly return.

22 PAYE/NIC and CIS deductions paid electronically should have cleared into HMRC bank account.

30/31 Submit CT600 for year ending 12 months previously. Last day to amend CT600 for year ending 24 months previously.

File accounts with Companies House for private companies with year ending nine months earlier and for public companies with year ending six months earlier.

If the due date for payment falls on a weekend or bank holiday, payment must be made by the previous working day.

September 2010

No key dates

October 2010

5 Deadline to notify HMRC of chargeability to income tax or CGT for 2009/10.

14 Due date for CT61 return and CT payment for quarter to 30 September 2010.

31 Deadline to submit 2009/10 self-assessment tax return if filed on paper.

November 2010

2 Submit employer forms P46 (car) for quarter to 5 October 2010.

December 2010

30 Last day to submit 2009/10 tax return online to have unpaid tax of up to £2,000 collected through the 2011/12 PAYE code.

January 2011

14 Due date for CT61 return and CT payment for quarter to 31 December 2010.

31 Submit 2009/10 self-assessment return online (up to £100 penalty if late).

Pay balance of 2009/10 income tax and CGT plus first payment on account for 2010/11.

February 2011

2 Submit employer forms P46 (car) for quarter to 5 January 2011.

28 Last day to pay 2009/10 tax to avoid automatic 5% surcharge (unless late payment agreed with HMRC).

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The Emergency Budget

The new Chancellor delivered the promised post-election pain.

In the fortnight before the Emergency Budget in June, there were plenty of warnings about the period of austerity and the pain that the country faced. In retrospect, the warnings of gloom and doom were not overdone, at least when a long-term view of the measures is taken. There was some immediate tax pain, but much of it was deferred:

VAT The standard rate of VAT will rise to 20% from 4 January 2011.

Capital gains tax (CGT) The CGT regime became more complicated following the Budget. Now, for gains made after 22 June 2010, only basic rate taxpayers will pay CGT at 18%. Everyone else will pay 28%, although a 10% rate will still apply where the disposal qualifies for entrepreneurs' relief.

Business tax The main corporation tax rate will fall by 1% to 27% from 1 April 2011, further reducing to a 24% rate in April 2014. The small profits rate (formerly small companies' rate) will be cut by 1% to 20% from 1 April 2011. However, the annual investment allowance will fall from £100,000 to £25,000 from 1 April 2012.

Personal allowance and tax bands The personal allowance will rise by £1,000 in 2011/12 to £7,475, but higher rate taxpayers will not benefit because the starting point for 40% tax will be reduced by about £1,500 to claw back the potential tax saving. The starting point for higher rate tax will remain frozen for 2012/13 and then the basic rate band will be frozen for 2013/14.

National insurance contributions (NICs) The planned 1% rise to all the main NIC rates will go ahead for 2011/12. However, the secondary (employer) Class 1 threshold will rise by £21 a week above indexation. The impact of the rise on employees will be limited by increasing the primary threshold by about £25 a week above indexation. The upper earnings/profits limit, above which the NICs rate will be 2%, will *fall* by about £1,500, matching the drop in the higher rate tax starting point.

Pension contribution tax relief The good news is that the Chancellor abandoned the much-criticised 'high income excess relief charge' provisions, which were due to be introduced from 6 April 2011. The bad news is that there will be new restrictions on the amount of pension contribution tax relief. These are set to take the form of a reduction in the annual allowance limit from £255,000 to £30,000–£45,000. As a result of this proposal, 2010/11 may be the last tax year in which you could benefit from full tax relief on a substantial pension contribution.

Pension annuitisation The effective requirement to buy an annuity by age 75 is to be scrapped from 6 April 2011, with interim measures in place now for those who reach age 75 on or after 22 June 2010. The Treasury has made it clear that the changes 'should not incur Exchequer cost and should not create any opportunities for tax avoidance'.

Did you know that the Government has announced that it will bring in regulations to remove the tax charge imposed where a person aged between 50 and 55 transfers his or her pension to another pension provider? From 6 April 2010 the general rule is that only people who are 55 and over can draw their pension without facing an unauthorised payment charge. Those between 50 and 55 are also exempt from the charge if they started drawing their pension before 6 April 2010. However, if they transfer their pension to another provider, they must currently pay the charge. It is this charge that the Government wishes to remove, and the change will be backdated to 6 April 2010.

VAT inspections and the penalty risk

The news that a value added tax (VAT) inspection is due still strikes fear into the hearts of many business owners and managers. If you have been accounting for VAT correctly and kept the necessary records, there should be no cause for worry.

Even if you haven't, there may still be time for us to help put things in order before the VAT officers arrive. Some answers to frequently asked questions follow.

Why and how often?

Inspections are made regularly. The size and complexity of the business or a past record of non-compliance will prompt more frequent visits.

What will VAT officers do?

The VAT officer will begin by discussing your business before asking to examine your business records. Sometimes, they may ask to view business premises and any goods stored there. Occasionally, the officer may take details of supplies made by or to you to check their treatment in your customers' or suppliers' records.

And when it's over?

A visit may result in no further action at all. However, if the VAT officer considers that you have failed to keep correct or adequate records, or discovers a mistake, this should be explained to you clearly, as should the reason for and the amount of any adjustment to your VAT payable. Your right to disagree with or appeal the adjustment should also be made clear.

How can we help?

If you advise us in good time of a forthcoming visit, we can arrange a quick health-check of your records and systems (this is something we advise you to have regularly, in any case). If you would like us to attend during the visit, and/or answer questions on your behalf, we can do so.

If, despite everything, the officer finds a default, the potential penalties depend on the nature of that default. No penalty will be charged if you have a reasonable excuse, although what is 'reasonable' is quite narrowly defined. With our help, penalties should not arise. If they do, we shall seek to have them mitigated to the greatest extent possible in the circumstances.

Did you know that new businesses set up in some parts of England on or after 22 June 2010 can claim exemption from paying employer's class 1 NICs for the first ten employees hired in the first year of trading? The idea is to help boost employment. The exemption will apply for the first 52 weeks of employment, and will be capped at £5,000 per employee. The employees' NICs will still have to be paid. The scheme is expected to start in September 2010 and run for three years. Businesses established in London, the east and south-east regions of England will be excluded, as will certain businesses in grant-supported sectors.

Choosing how to own business property

It can be difficult to decide whether to buy a business property in your own name or within your company, which will use the property for its trade. If the cash for a purchase is available for either route, the decision will turn on the tax implications.

Personal purchase

If you buy the property, you can receive commercial rent for leasing it to your company. The rent is free of national insurance contributions, so represents a tax-efficient way of extracting funds from your company. The rent paid should be fully tax deductible for the company.

If your spouse or civil partner pays tax at a lower rate than you, holding the property in your joint names can reduce your family's total tax bill. Your partner's portion of the rent becomes taxable at a lower rate.

The property need not be held on an equal basis. You need to inform HMRC of each person's holding using form 17, and declare the relevant proportion of the rents on your own tax returns.

Any gain on the sale of the property after deduction of the annual exemption (£10,100 in 2010/11) may be taxed at 18% or 28% in your hands. Companies pay tax on gains at 21% or 28%, reducing to 20% and 27% from April 2011. The company cannot deduct the annual exemption, but it can claim indexation allowance, which reduces the gain by the effect of inflation. If the company sells the property, the proceeds will be trapped within the company, and may incur another tax charge when you extract them.

If you do not charge a full market rent for the property, you may be able to claim entrepreneurs' relief on any gain made on disposal. This reduces the rate of CGT to 10% on a gain of up to £5 million per taxpayer, but it only applies if the property is sold in association with your withdrawal from the business and the disposal of some of your company's shares.

Corporate purchase

Holding the property in the company allows the full value of the property to be sheltered from inheritance tax (IHT). If you hold the property personally, only 50% of the value escapes IHT. If you're faced with this choice, let us know and we will be able to help.

Offsetting property losses

Where an individual lets property, the profit or loss is calculated just like for any other trade (there are different rules for companies). All expenses, including interest paid on loans used to fund the property business, are deducted from the rental income. If the expenses exceed the income the result is a loss.

This loss can generally only be set against future profits from property. However, where some of the loss relates to capital allowances, that part of the loss may be set against the taxpayer's other income in the same or the next tax year. All the loss may be deducted from other income if the property is commercially let as furnished holiday accommodation (FHL).

Using capital allowances

Capital allowances can be claimed for expenditure on equipment and certain fixtures used in the property business, but not where the equipment is used within, or attached to, residential property that does not qualify as FHL.

Capital allowances are normally given at 20% of the cost each year, or 10% for fixtures that qualify as 'integral features'. However, where expenditure (excluding cars) falls within the annual investment allowance (AIA), 100% of the cost is deducted in the year of purchase. The AIA is capped at £100,000 per year.

Integral features

Landlords of commercial properties often spend large amounts on refurbishing their buildings. Where that expenditure is incurred after 5 April 2008 in the following categories, it qualifies as integral features, and may fall under the AIA cap:

- Electrical systems, including lighting;
- Cold water systems;
- Space or water heating systems;
- Powered ventilation and air-conditioning systems;
- Lifts, escalators and moving walkways; and
- External solar shading.

A 100% cost deduction under the AIA can create a significant loss, which is available to set against the landlord's other income. However, where the loss is generated by using the AIA after 23 March 2010, and there was a plan to avoid tax deliberately through the use of the loss, the taxpayer may be barred from setting-off the loss against their other income. In this case the loss will only be available to set against future profits from property.