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Newsletter March 2008

Attention on this side of the desk is fixed firmly on the Budget statement expected Wednesday, 12 March. We will be including commentary on the areas of interest to clients in our next newsletter. The current tax year finishes on 5 April. This newsletter includes a reminder on the research and development deadline looming, a comment on Employer Compliance Reviews, a few tax planning pointers for business clients, the treatment of loans for National Insurance purposes, a note regarding certain capital losses that can be set against income, and finally a VAT reminder for owners of property on which there is an election to tax.

Our next newsletter will be published on Thursday 3 April 2008.

[Pass it on!](#)



[Tax Planning](#)



[R&D deadline looming](#)



[Capital losses - disposal of unquoted shares](#)



[Tax Diary March/April 2008](#)



[Website goes live](#)



[An Inspector Calls](#)



[Business tax planning - action before 6 April 2008](#)



[VAT - the election to tax](#)



Pass it on!

If you know anyone who might be interested in our newsletter feel free to forward this copy. If you have received a forwarded copy and would like to subscribe at no charge, just email taxnewsletter@armstrongwatson.co.uk stating "subscription request" in the subject.

Back to top



Website goes live

Whoever you are, whatever you do, whenever you need us... we're with you online

We're delighted to announce that our new website was launched on Monday 11 February. You'll find great time saving tools and inspirational comment on the issues that affect you and your business. Why not make it one of your favourites?

www.armstrongwatson.co.uk

Back to top



Tax Planning

Welcome to our regular section of the newsletter. This section gives a brief description of current "hot topics" and tax saving ideas. If you want a Tax Consultant to contact you about one or more of these please email taxnewsletter@armstrongwatson.co.uk stating which particular idea or ideas you are interested in. Here are a few of our tax strategies, as updated following October's pre budget report. More ideas will be added soon.

Tax efficient cash extraction from companies – makes use of discretionary trusts. Ideal for companies with large cash balances surplus to working capital needs (> £100,000), where the main shareholder or shareholders are considering selling or retiring, or where rewarding key employees is desired. It also offers a cheap mortgage for purchasing buy-to-let properties.

Income tax and NIC savings on car benefits – this is a plan to replicate the positives of employer-provided cars whilst eliminating the income tax and NIC charges. Ideal for fleets of 5 cars or more. Do you provide cash allowances instead of company cars and are you aware of the risks you face as an employer by doing this? If so then our solution is worth considering.

Share options – want to reward key employees with shares in the future? Why not make use of HMRC approved EMI share options. Such options carry income tax and national insurance advantages over unapproved options or outright gifts/sales at an undervalue. The exercise of the options may also bring a substantial corporation tax deduction for the company. An extremely flexible form of employee reward and ideal for a future Management Buy Out team.

Paying tax at 40% on your business profits? – have you considered incorporation? If disclosure is a concern then an unlimited company may be preferable. We also offer an alternative to full incorporation, email to find out more. Now could be a good time to incorporate given the forthcoming changes to capital gains tax as the tax on the sale of goodwill can be minimised. The tax advantages are even better if you commenced trading on or after 1 April 2002.

Employment Taxes (PAYE, NIC, expenses & benefits) are complex and notoriously difficult to administer. HMRC carry out routine inspections and, if they find evidence of non compliance, will seek a settlement covering six years, often on a grossed up basis, to include interest and penalties. The cost, even for a seemingly minor innocent error, can be substantial. Armstrong Watson can carry out a Compliance Review aimed at uncovering areas of non compliance and rectifying them, meaning that risk of a large settlement can be removed, and the inevitable visit from HMRC can be faced with confidence.

Inheritance Tax – Following announcements made in the Pre Budget Report, the second spouse to die can now

benefit from the Nil Rate Band of the first spouse. This was welcome news but there are still many issues to be addressed when drafting your Wills and it is important to ensure that your Wills are efficient for Inheritance Tax purposes and also for Care Home Fee planning purposes. We can assist you in drafting your Will to ensure that it is not only efficient but that your assets pass to your loved ones as you intend. If you have taken advice in the past regarding your Wills, we would also recommend that you have these reviewed again following the changes in the legislation.

Inheritance Tax gifts during life – if you have an estate that will be subject to Inheritance Tax then controlling the growth of your estate is vital to avoid paying too much Inheritance Tax. Every individual can give away up to £3,000 every year (and £6,000 if you haven't used the allowance in the previous year). However, you can also give away your excess income as well, which can restrict the growth of your estate further - although care needs to be taken when considering this option.

Tax on 2nd Properties – if you own a second property you need to be aware that there will be Income Tax, Capital Gains Tax and potentially Inheritance Tax liabilities over the life of the property. We can advise you on the most tax efficient way to hold your 2nd property to achieve your objectives.

Capital Gains Tax - do you own assets which are sitting at a large gain? The Chancellor has back tracked somewhat and is introducing a new Entrepreneurs Relief from 6 April 2008. However, not all assets that qualified for Business Asset Taper Relief will attract this new relief, for example, commercial property let to third parties. As always there are winners and losers so if you are considering any disposals you should seek professional advice. There are also planning opportunities available which can “bank” any reliefs now, without actually disposing of the asset to a third party.

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[Back to top](#)



An Inspector Calls

HMRC recently published their 2007 Autumn Performance Review. Amongst the reams of statistics, covering everything from firearms control to smuggled cigarettes, there is some interesting reading. It is well known that HMRC had substantially increased the resources available for carrying out Employer Compliance Reviews, and this has paid off for them spectacularly. In 2005/6 the yield from this source was £429.9 million. In 2006/07 this increased to £562.6m, a huge leap of almost 31%! The story for 2007/08 is that both numbers of visits and yields from those visits are increasing, and we are certainly seeing this in practice.

The ever complex legislation relating to Employment Tax makes it harder than ever for employers to be fully compliant, yet the penalties for non compliance can be substantial. In view of this it would be worth undertaking a review to ensure the business is as compliant as it can be. At best this will provide a clean bill of health, allowing you to face the inevitable HMRC visit with confidence. However if errors are discovered you will be able to rectify these, thus reducing the likelihood of a large settlement when the Inspector comes calling.

If you would like to discuss this in more detail please click below.

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[Back to top](#)



R&D deadline looming

Time is running out for making claims for Research & Development Tax Relief for older accounting periods.

For accounting periods ending before 31 March 2006, claims must be made by the earlier of 6 years and 31 March 2008. Therefore, all old claims must be made by 31 March 2008.

Armstrong Watson has made successful claims in various sectors such as engineering, manufacturing, IT and pharmaceutical. Most companies know when they are undertaking research but often overlook the development side of R&D.

According to a recent report there is approximately a billion pounds of unclaimed R&D tax relief in the UK. Is some of this yours to claim?

If you want to know more about how this relief works or how to make a claim click on the link below.

[Click here for a call back from our office regarding this article.](#)



[Back to top](#)



Business tax planning - action before 6 April 2008

We have noted below a number of tax issues that you may like to review prior to the end of the current tax year, 5 April 2008 (or 31 March 2008 for companies).

- 1. Capital Allowances.** Clients may be advised to seek our advice before committing to any further capital expenditure before 5 April 2008. As from 6 April 2008 it is likely that new rules will apply to the way in which you are able to claim capital allowances for the purchase of certain qualifying assets. The Government has said it will introduce a new Annual Investment allowance. Essentially from the end of this tax year businesses will be able to write off 100% of their expenditure on plant and other equipment (excluding most cars) up to an annual limit of £50,000. This Annual Investment Allowance will be apportioned in the first year if your year end is not 31 March. For instance if you spend £24,000 on a qualifying asset in April 2008 and your year end is June 2008; one-quarter of the £24,000, £6,000 will qualify for the 100% write down; any balance will be carried forward. This will only affect businesses whose accounting year end straddles 5 April 2008. Because of these changes businesses may be disadvantaged if they commit to capital expenditure before 6 April 2008. If you have plans to acquire assets you may be advised to check out the pros and cons of delaying the expenditure until after 5 April 2008. For companies the applicable dates are 31 March and 1 April as opposed to 5 April and 6 April.
- 2. Benefits in Kind.** Don't forget that if your employees reimburse you for the use of a company asset, or to cover other personal payments that have been made on their behalf, no benefit in kind will arise, and therefore no tax will be due. In most cases reducing taxable benefits in this way will also reduce the National Insurance Class 1A contributions for the business.
- 3. Corporation Tax Rates.** If your taxable profits are likely to take you over the small companies rate, (currently your company can earn up to £300,000 at the small companies rate of 20%, unless you have associated companies which can reduce this entitlement), you could consider bringing forward expenditure to keep your profits under the threshold. The expenditure could be a business expense or capital expenditure.
- 4. Pension contributions.** Tax relief on pension contributions made by the company is only available in the period in which the contributions are actually paid, so if it is planned to increase contributions in respect of the current year, these need to be paid out during the period.
- 5. Directors' bonuses year to 31 March 2008.** Where it is planned to pay directors bonuses out of current profits it is necessary to hold a directors' meeting confirming the decision to do so. This should then be minuted, even if the exact amount of the bonus is to be determined later. In this way the liability for the bonus is created in the current period, and it will be acceptable to provide for the bonus in the accounts. The bonus

should then be finalised and paid out within 9 months of the year end to secure a corporation tax deduction for the payment.

These are just a few of the possible planning issues that you should take a look at before 5 April 2008. Please contact us if you need to clarify any issue prior to a 31 March year end.

[Click here for a call back from our office regarding this article.](#)



[Back to top](#)



Capital losses - disposal of unquoted shares

If the conditions set out below apply, it may be possible to set off a loss on the disposal of certain shares in unquoted, trading companies, against the other earnings of the disposing shareholder.

In order to qualify:

- The shares disposed of must form part of the ordinary share capital of the company.
- The claimant (or spouse/civil partner) must have subscribed for the share.
- The company must be a qualifying trading company.
- The shares must not be listed on a recognised stock exchange - listing on the AIM market are not considered "quoted".

Any loss relief computed will be limited to:

- A transaction made at arms length for full consideration.
- A distribution in the course of liquidation or winding up.
- A negligible value claim. (When shares have no value)

The relief can be claimed:

- For the tax year in which the loss occurred.
- Or, the preceding tax year.

This relief provides a measure of compensation for shareholders who invested in companies, and have lost money when the company was subsequently sold or wound up.

Also bear in mind that losses of this type, set against other capital gains in the same year, will save capital gains tax at 18% after 5 April 2008. (If the proposed changes to CGT are carried through in the forthcoming Finance Bill.) If those same losses are set off against other income in 2008-2009, as suggested in this article, the tax savings at income tax rates could be 20% - 40%.

[Click here for a call back from our office regarding this article.](#)



[Back to top](#)



If you are considering exercising an option to tax over a business property then you need to be aware that this can sometimes be a commercial inconvenience.

Certain businesses those, for example, in the financial sector which may only have exempt income or small businesses which are not registered for VAT will be less likely to rent premises where they will be charged non-recoverable VAT on their rent.

In addition the sale of business property over which an option to tax has been exercised will attract VAT at the standard-rate of 17.5% thus making it unattractive for purchasers who are not registered for VAT.

Once exercised you will normally only be allowed to apply for a revocation of the option to tax if, within 3 months of the effective date, you have not put the option into practical effect by:

- Charging rent or receiving any payments on which you should have accounted for VAT or
- Recovering input tax in relation to the land and buildings as a result of the option, disregarding any input tax that you would have been able to recover under the normal partial exemption rules and
- The land or building has not been acquired or disposed of as a transfer of a going concern.

Once the initial 3 month period has passed, or you have put the option to tax to practical effect, you cannot request permission to revoke the option to tax until 20 years or more have passed.

You may like to note that the first options to tax were granted in 1989, 20 years ago next year. If there would be an advantage for the option on your property to be revoked, you may like to find out when the election was granted. To do so you should email to option to tax unit at optiontotaxnationalunit@hmrc.gsi.gov.uk

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Back to top



1 March 2008 - Due date for corporation tax due for the year ended 31 May 2007.

19 March 2008 - PAYE and NIC deductions due for month ended 5 March 2008. (If you pay your tax electronically the due date is 22 March 2008)

19 March 2008 - Filing deadline for the CIS300 monthly return for the month ended 5 March 2008.

19 March 2008 - CIS tax deducted for the month ended 5 March 2008 is payable by today.

1 April 2008 - Due date for corporation tax due for the year ended 30 June 2007.

19 April 2008 - PAYE and NIC deductions due for month ended 5 April 2008. (If you pay your tax electronically the due date is 22 April 2008)

19 April 2008 - Filing deadline for the CIS300 monthly return for the month ended 5 April 2008.

19 April 2008 - CIS tax deducted for the month ended 5 April 2008 is payable by today.

Click here for a call back from our office regarding this article.



Back to top



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