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# BUSINESS UPDATE

WINTER 2006

## Welcome

Welcome to the Winter 2006 edition of our newsletter. This issue includes a mix of topical and traditional features that we hope you will find useful.

A recent survey, highlighted by BBC news, suggested that 97% of us leave out enough rubbish to allow at least our name and address to be stolen. Worse still, credit card numbers, bank account details and even signatures are vulnerable too. Identity theft is on the increase and we look at ways of avoiding what can be a very stressful experience.

Controversy was stirred up in the summer over new ways of checking the accuracy of tax returns introduced, on a trial basis, by HMRC. We focus on the different approaches, which have been dubbed 'interventions'.

As new minimum wage rates take effect we point out the common pitfalls that employers may fall into.

We review two crucial capital gains tax reliefs, namely the exemption for the main residence and taper relief.

We hope that you enjoy these and the other topics covered. Please contact us with any comments or for further information.



As most people know, a main residence is exempt from capital gains tax (CGT). This is a valuable exemption and careful planning can make it stretch a little further than you might think.

As you might expect, the property must usually be lived in for the exemption to apply and normally only one home can be exempt at any one time. Married couples and civil partners can only have one main residence between them.

The exemption extends to grounds of up to half a hectare or such greater area as is required for the reasonable enjoyment of the house.

Advice must be taken in each individual case but it follows from case law that:

- there is no length of time for which a property must be

occupied to count as a main residence but clear intention and occupation must be established

- the sale of a part of the garden or grounds for development will usually be covered by the exemption
- a separate wing or building may be covered if it forms part of the occupied residence
- where there are two or more properties, which one is the main residence will depend on factors such as where post is sent, where the taxpayer is most often present and the address at which full council tax is paid.

If the taxpayer has more than one home, they may decide which of those homes is to be the main residence by giving notice to HMRC, usually within two years of acquisition of a second home.

Once established as a main residence the last 36 months of ownership will always be exempt from CGT, even if another home is occupied as the main residence during this time, so giving notice is often advantageous.

For example, a married couple have owned a home in York for two years. They work in Leeds and they buy a second home in that city. They elect for this new home to be their main residence. Exactly four years later they sell the home in York. The York home is exempt for the two years they lived in it and for the last three years of ownership because this period is always exempt provided that the home in question was the main residence at some time. The chargeable gain is apportioned so that, in this case, five sixths of the gain on the property in York will be exempt.

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# Losing your identity!

BBC news recently reported on the massive increase in ID theft and the worrying results of a survey showing that 30% of households had left their credit card details in their rubbish and 73% had left their exact signature.

In 2005 there were 137,000 cases of individual ID theft in the UK. This compares to only around 20,000 in 1999.

## Individual ID theft

This involves the misappropriation of another person's identity usually to carry out identity fraud by obtaining loans or credit and goods and services by deception.

This can have devastating consequences for credit ratings and reputations. Here are some ways individuals can avoid ID theft:

- shred documents carrying your name, address or other details before discarding them. Fraudsters will search rubbish bins and the increased use of paper recycling bins affords the ID thief the luxury of rifling through clean waste
- obtain a credit report regularly and check this for any unexpected activity
- check your bank and credit card statements on receipt and report any unrecognised transactions
- do not give out personal information without being sure

of the authenticity of the requesting body. Never disclose a PIN or an online password

- ignore *all* emails requesting financial information no matter how convincing
- keep documents such as passports, driving licences, birth certificates and marriage certificates in a safe place and preferably not all together
- ensure that your post cannot be intercepted if you live in a flat or similar accommodation.

## Corporate ID theft

Corporate identity theft is also on the increase. Here fraudsters submit forms to Companies House

to change the registered address of a company or appoint new directors. The fraudulently appointed directors could open bank accounts and acquire goods on credit, which are then delivered to the fake registered office.

To help avoid this type of ID theft a company can use the new PROOF service offered by Companies House. This enables specific forms, such as those covering the appointment of directors and a change of registered office, to be filed electronically. Companies House will reject paper versions of those forms. In this way companies can be sure that only they can file the forms to register such changes.

## Flattening out VAT

The prevailing argument for persuading small businesses to use the flat rate scheme for VAT is simplicity but a more persuasive argument may be that, for some, less VAT is payable and profit margins increased.

The scheme may be used where the VAT exclusive annual taxable turnover is no more than £150,000 and total turnover (including any exempt supplies or other income out of the scope of VAT) is no more than £187,500. A business may stay on the scheme provided annual turnover does not exceed £225,000.

A business that joins the scheme continues to charge its customers VAT as normal at the rate of VAT applicable (normally 17.5%) and it must continue to issue VAT invoices if the customer is registered for VAT. The customer reclaims the input VAT as normal.

The business then calculates its net VAT liability by simply multiplying its VAT inclusive turnover by the appropriate flat rate percentage found from an industry based table produced by HMRC. The actual amount of output tax on sales and input tax incurred on purchases is irrelevant. The VAT on the purchase of capital assets with a VAT inclusive cost of £2,000 or more can usually be recovered in the normal way.

A recent tribunal case found that a pub, where the larger proportion of turnover was from food sales, should be using the percentage for restaurants rather than the lower percentage applicable to pubs. This shows that choosing the right flat rate for your business is crucial so please contact us for advice.

## Driving at work: the risks



Despite a high proportion of road accidents involving people who were at work at the time, employers often assume that they have little or no responsibility for their staff's safety whilst driving at work.

The reality is, however, that health and safety law applies as much to 'on-the-road' activities as it does to activities in the work place. In all cases where employees drive as part of their work, whether in company vehicles or their own vehicles, the company's health and safety policy should include a section on driving.

Such a policy not only helps to protect employees. It can save costs by reducing insurance premiums, legal fees and claims, and by reducing time off for staff who are injured.

The policy should involve a risk assessment designed to minimise the risk of someone being killed or injured on the road. This will include looking for hazards and considering who might be harmed, such as the driver, passengers or

third parties. The employer should then evaluate the risk and decide what more needs to be done if existing precautions are inadequate. Finally, findings should be recorded and the assessment reviewed to ensure risks are minimised.

The key policy steps of risk evaluation should cover the following:

- **the driver:** considering their competency and qualifications, their health and fitness, their level of training and their awareness of the law, for example, the law on mobile phone use is still regularly flouted
- **the vehicle:** covering the vehicle's fitness for the purpose and its condition
- **the journey:** considering the route, the necessity for the journey, the scheduling of the journey, the prevailing weather conditions and the distance and time allowed.

The Health and Safety Executive have an excellent leaflet containing more information which can be found at [www.hse.gov.uk/pubns/indg382.pdf](http://www.hse.gov.uk/pubns/indg382.pdf)

# Minimum wage compliance



Ensuring compliance with the National Minimum Wage (NMW) is the responsibility of HMRC who operate 16 teams of compliance officers across the UK. They can inspect employers' records, give advice and secure pay arrears. Inevitably, certain types of business tend to attract more attention and among these are the hotel and catering industry, retail trades and, lately, hairdressing.

Typical pitfalls in these and other sectors include: counting tips as part of the wage when not subject to PAYE, not properly dealing with deductions for live-in staff and assuming a trainee, not on an

apprenticeship, is nonetheless exempt.

The NMW rates from 1 October 2006 are £5.35 for workers aged 22 or over, £4.45 for those aged 18 to 21 and £3.30 for those aged 16 or 17.

The new age discrimination laws have brought into question the legality of paying a lower rate to 16 and 17 years olds. However, the government has stated that it is satisfied that this remains valid.

Please contact us for further advice if you are unsure about your responsibilities under minimum wage legislation.

## Mixed blessings of taper relief

Taper relief for capital gains tax (CGT) is now a familiar friend but still it occasionally catches out the unwary. Our emphasis in this article is on taper relief for business assets.

If owned for two years or more, the gain on a business asset may be reduced by up to 75% before it is charged to CGT. The rate of taper is 50% if the asset is owned for more than one year but less than two.

However, the usage of the asset must be considered throughout any ownership period since 1998 to determine whether the full 75% relief is due.

The most common examples of business assets include: assets used in self-employed businesses such as land and buildings and goodwill; all shareholdings in unquoted trading companies; shareholdings held by employees of quoted trading companies and property which is let to a trading business or trading company.

It is tempting to assume that assets used wholly for business purposes for the last two years of ownership will attract the full 75% taper. The following scenario may seem unlikely but it helps us to illustrate that this is not always so.

Richard bought a property on 1 August 1998. He let this for one year (not to a

trading business or trading company) and then he occupied 60% of the property for his own trade and let the rest. After two years he expanded his business and took over the whole property in which he traded for five more years until he sold it on 1 August 2006 making a gain of £72,000.

For each distinct period we must consider the extent of business use.

| Year  | % of business use | % of non-business use |
|-------|-------------------|-----------------------|
| 1     | 0%                | 100%                  |
| 2 - 3 | 60%               | 40%                   |
| 3 - 8 | 100%              | 0%                    |

The gain of £72,000 is treated as arising on a business asset for 6.2 years out of 8 (1 x 0.0 + 2 x 0.6 + 5 x 1.0) which gives £55,800. The remainder of the gain, £16,200, is treated as a non-business asset. The rate of taper for each part depends on the qualifying period of ownership which, in this case, is 8 years and will therefore be 75% for the business part of the gain. The rate of taper for a non-business asset owned for 8 years is 30%. The chargeable gain is £25,290 (£55,800 x 25% + £16,200 x 70%).

As you can see, these rules are complex. Please ask us for more information if you are considering sales of assets.

## Personal computer use

Almost everyone makes personal use of a work computer by sending private emails or doing the weekly shopping even though this may be limited to break times.

Private use by an employee of an employer provided asset is subject to a tax charge but, until recently, computers were specifically exempt from this charge. Any other asset is only exempt if the private use is 'not significant'.

The exemption for computers was removed in the last Budget. It therefore becomes important to know how this 'not significant' condition is to be applied to their use. HMRC have issued helpful guidance with practical examples.

Where a computer is provided by an employer because it is necessary for the employee to be able to carry out their duties, it is highly unlikely that any private use will be significant. In the examples given, where the sole reason for supplying the computer is to enable the employee to carry out an essential part of their work, HMRC conclude that private use is 'not significant' and no tax charge arises. This is so even where there is substantial private use. The same principle applies where a broadband internet connection is provided.

HMRC guidance states that the employer must document the private use policy. If the cost of private use is not recovered by the employer, this must be for commercial reasons (for example because recharging is impractical) rather than an intention to reward the employee.

Documentation of the policy could be in employment contracts or employees could be asked to sign a statement acknowledging the policy.

Please contact us if you would like more specific advice on complying with this guidance.



# Powers of intervention

In an effort to reduce the time and cost of enquiries, HMRC have promoted some new ideas for identifying errors that may have been made on self assessment tax returns.

Trials of these interventions, as they have been called, began in July this year. Essentially they involve a lighter touch than with a full enquiry and they will usually start with a letter to the taxpayer. This will be followed by an examination the nature and depth of which will depend on the perceived risk. The six methods of intervention are:

- **record keeping review:** during a 'live' accounting period a visit is made to examine record keeping procedures concentrating on cash sales, drawings and wages

- **risk review:** profiles developed for particular trades are compared with selected taxpayers and, if there appears to be a risk of error, a questionnaire is issued to obtain a measure of the actual risk that exists

- **self-audit:** possible errors in specific entries on the tax return are pointed out by letter, telephone or personal visit and the taxpayer is encouraged to make amendments where necessary

- **telephone contact:** a trained officer contacts the taxpayer by telephone to explain why HMRC considers that an error has been made and to give advice on making a correction

- **correction challenge:** where they have good quality information that an error has been made, HMRC will correct a

return, ask for an explanation of why the error was made and ask for payment of the extra tax

- **health check:** a target population, where past compliance work indicates a risk of error, is contacted, advised of the risks and given assistance to put any matters right.

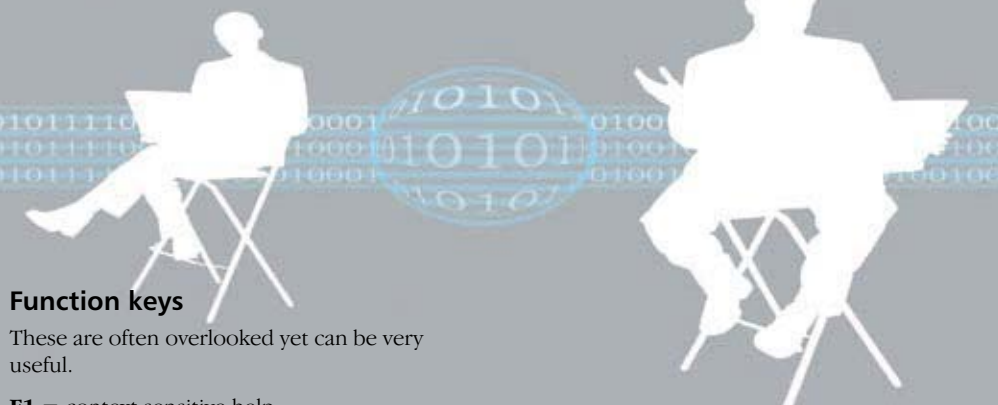
The trials are voluntary and the taxpayers chosen will need to consider whether it is in their interest to take part. HMRC's website states that a decision to opt out of the trial 'will not automatically result in an enquiry'. However, the website makes clear that the risk of error still exists and a number of taxpayers must expect an in-depth investigation.

The process has been criticised for a lack of consultation and because some letters sent out to taxpayers, as part of the trials, imply wrong doing and sometimes refer the taxpayer to highly complex tax rules on the HMRC web site. This has caused confusion and worry.

HMRC should give us advance warning of an intervention but, if you are contacted by them, please get in touch with us immediately so that we can discuss your approach thoroughly.

## Handy hints for Sage

In the IT tips feature this time we concentrate on Sage accounts. Sage released version 13 of their Line 50 accounts program in August although, in a concession to the superstitious, they have called this 2007!



### Function keys

These are often overlooked yet can be very useful.

**F1** = context sensitive help.

**F2** = for the Windows calculator.

**F3** = brings up line items on invoicing or orders.

**F4** = brings up a list from which to select a record e.g. a nominal code or an account reference.

**F6** = repeats the previous line entry when entering transactions. This is especially useful where many similar invoices are being entered which might have the same description or nominal code.

**F7** = inserts a line in any data entry screen.

**F8** = deletes a line in any data entry screen.

### Active searching

Active search, in version 7 onwards, speeds up data entry by revealing a list of common entries that match what has been typed.

Most people find this useful when searching for an entry from a pre-defined list, such as a supplier reference or a nominal code. Without this help you need to know your account references and codes well to find them quickly.

Active search also works on the 'Details' field when entering invoices, journals or bank transactions. Sage retains a list of previous entries made in this field and searches this to look for a match. Some users find this distracting and it can result in inappropriate details being accepted.

By default, active search is enabled when Sage is first installed but it can be switched off.

From the menu bar select 'Settings' and then 'Company Preferences', Select the Parameters tab. In the list under 'Others' uncheck 'Display Active Search Popup'.



## Brainteaser

86 people have booked to go on holiday in TANZANIA,  
89 have booked for AUSTRIA and  
47 have booked to go to FRANCE.

**How many have booked to go on holiday in Brazil?**



"Here's a letter from the Inland Revenue about going to prison if you don't respond before yesterday."

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