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BUSINESS UPDATE

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Clampdown on buy to let property owners

Significant press coverage over the summer indicated that HMRC are intending to target landlords who let property. HMRC denied that there was any specific targeting but advised that they are seeking to encourage compliance, particularly in situations where landlords may have:

- made a capital gain on the sale of let property
- claimed too much tax relief for expenses against their property income
- failed to declare the amount of rent they have received from the let property.

If you have any concerns in this area please get in touch.

Arctic Systems: where next for husband and wife businesses?

With the Law Lords finally ruling in favour of Geoff and Diana Jones in the long running Arctic Systems case, small family businesses might be breathing a sigh of relief. Although HM Revenue & Customs (HMRC) lost the battle, will the government end up winning the war by changing tax law?

The case

Geoff and Diana Jones own and run an IT consultancy called Arctic Systems. Geoff is the major fee earner while Diana provides general administrative support. Like thousands of other couples with similar enterprises, the structure of the business is such that both parties have shares in the company, with profits extracted by way of dividends.

HMRC 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 spouse. Therefore, HMRC argued, the dividends received by Diana should have been treated for income tax purposes as those of Geoff, a higher rate taxpayer. This meant a retrospective tax bill of £42,000.

Following several appeals, the Lords' ruling in favour of Geoff and Diana Jones on 25 July 2007 was final.

The consequences

The uncertainty over the case left thousands of similar businesses concerned that they too could face large and potentially crippling tax demands. Now, husband and wife businesses are highly unlikely to be hit with retrospective tax bills like the one originally issued to the Joneses.

However, following the ruling, Exchequer Secretary to the Treasury Angela Eagle announced the government's intention to introduce legislation to close what it considers to be a tax 'loophole' and end this form of 'income splitting'.

Angela Eagle said: "Some individuals use non-commercial arrangements to divert income to others. That minimises their tax liability, and results in an unfair outcome. It is the government's view that individuals involved in these arrangements should pay tax on what is, in substance, their own income and that the legislation should clearly provide for this."

The government will therefore bring forward proposals for changes to legislation to ensure this is the case."

So it seems likely that following a period of due consultation, new legislation could make arrangements like the Arctic Systems structure a thing of the past.

We will keep you up to date with any changes to the law. If you have any questions regarding your own circumstances please contact us.



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Capital allowances on company cars

For many years the tax system has restricted the annual tax write-off to £3,000 per car for 'expensive' business cars, defined as costing more than £12,000. However, the government is intending to abolish the current restrictions and introduce new rules that will be easier for businesses to administer and will also have a beneficial environmental impact.

The proposals, which are still at the consultation stages, are that:

- the existing 100% first year allowances for cars with CO₂ emissions up to 120g/km be retained
- the general plant and machinery capital allowances pool would be used for cars with CO₂ emissions between 121 and 165g/km
- a new car pool would be introduced with a lower percentage tax write off known as a writing down allowance (WDA), than the general plant and machinery pool for other cars.

As a consequence there would no longer need to be a specific distinction between cars costing more or less than £12,000. This means the £3,000 per annum cap on the WDA for a car would disappear.

In April 2008, the annual WDA available for the general pool would be 20% of the unrelieved expenditure in the pool. So a car costing £40,000 potentially gives a business a tax write-off in the first year of £8,000 rather than £3,000. A further advantage of the pooling concept will be that the business does not have the administrative burden of computing separate allowances for each car.

So what's the catch? Well there is not one necessarily, but there may be if you favour an expensive, highly depreciating car for your business. Under the current system, relief may be restricted to £3,000 per annum, but when the car is sold a significant balancing allowance may be due, giving an additional tax deduction for the 'loss' on the disposal of the car. Under a pooling concept the sale proceeds reduce the unrelieved expenditure in the pool. The business will continue to claim WDA rather than a balancing allowance being given.



Did you disclose?

You may well have read about HMRC's offshore disclosure facility. HMRC obtained details of around 400,000 offshore bank accounts from some of the larger banks. Many of these had not been declared and so HMRC introduced a 'special offer'.

By 22 June 2007 a taxpayer could register their intention to 'confess all' to HMRC, with a full report, and only a 10% penalty on any under-declarations, to be submitted to HMRC later this year.

But what will happen to those who did not register in time?

HMRC say that they will actively pursue those who did not make a disclosure and for whom they hold details. Penalties could be up to 100% of the tax not declared and HMRC have stated that any future penalty is unlikely to be less than 30%.

HMRC will soon start to open enquiries into those taxpayers about whom they have relevant information from the banks. It is still possible to make a disclosure to HMRC, generally via a local tax office, and it is likely that any penalty would be reduced if a disclosure was made, particularly if it was made before HMRC started any enquiry.

It is particularly important to bear in mind the following principles:

- you should correct any understatements in your tax affairs whenever you discover them
- it is better to disclose voluntarily, as this reduces the penalty
- it may be possible to negotiate a 10% penalty in any case but it is likely that specialist help would be required.

If you would like to know more about dealing with HMRC please contact us.

Companies Act 2006 - an update

A new Companies Act received Royal Assent in November 2006 and earlier this year the government outlined a timetable for its implementation. Some sections are already effective and the government has indicated that the whole Act will be in force by October 2008. Certain sections of the Act will become effective earlier in October 2007 and in April 2008 and a far clearer picture has now emerged in respect of when the different parts of the Act will be implemented.

BERR (the Department of Business, Enterprise and Regulatory Reform, previously the DTI) has published a number of draft regulations that indicate future implementation dates in addition to the first three Commencement Orders under the new Act. Here we focus on the Third Commencement Order which brings certain provisions into force from 1 October 2007.

Provisions which may affect private companies

- Normally there will be no requirement for an annual general meeting (AGM) or members' meetings, although private companies may continue to hold these if they wish. This means that private companies will generally be able to handle most of their business without holding a formal meeting.
- In the absence of such formal meetings, the default decision-making process for members will now be by written resolution. A simple majority of members will be

required for ordinary resolutions and a 75% majority for special resolutions

- Also as a result of the absence of meetings, in most cases any existing auditor will be re-appointed automatically.
- For the first time the general duties owed by the directors to the company are set out in the Act, although the law is largely unchanged. From 1 October 2007 these duties include: promoting the success of the company, exercising independent judgment, exercising reasonable care, skill and diligence, not accepting benefits from third parties and declaring interests in proposed transactions.
- Also new in statute is a formalised legal procedure which will allow the members of a company to bring an action against directors for a breach of their duty to the company (known as a derivative action).
- As at present non-small companies must continue to produce a 'business review' as part of their directors' report.

BERR has also confirmed that the changes that affect accounts, reports, audits and auditors will apply for accounting periods beginning on or after 6 April 2008.

We will continue to keep you informed about the implementation of the new Act. If you would like to discuss how the Act will affect you and your company in more detail please contact us.

Taking on workers new to the UK

Taking on any new worker can be a time-consuming process with the number of forms that need to be completed. When your prospective employee is from overseas there is even more to do and it is essential to follow correct procedures. You could be fined up to £5,000 for employing someone who does not have permission to work in the UK.

First ask to see an original form of ID that proves the nationality of the applicant, such as a passport, or residence permit. Protect yourself by checking the expiry date, any time limit stamps and endorsements. Do the photo and date of birth match the worker? Take a clear photocopy and double-check the full name on the ID against that shown on other documents presented.

Next check that the individual has permission to work in the UK. Home Office guidance can help with this. While most EU nationals can work freely in the UK, those from the Eastern European countries that joined the EU most recently need to register to work with the Home Office. Keep a copy of your worker's application form until the Home Office has supplied a registration certificate. If the worker's application is rejected you must not continue to employ that person. In addition, workers from Bulgaria and Romania must hold a valid accession worker authorisation document before they can start work.

New EU cash declaration rules

From 15 June 2007 a new European Union (EU) law on travellers declaring cash came into effect. It has been introduced to help combat money laundering.



a penalty of up to £5,000 for failing to comply with the obligation to declare or providing incorrect or incomplete information.

People who are travelling from the UK to a non EU country, or entering the UK from a non EU country, and are carrying the equivalent of 10,000 Euros or more will be required to declare this to HMRC at the place of their departure from, or arrival in, the UK. However, there will still be no declaration required for people travelling between the UK and other EU countries.

The 10,000 Euro limit includes currency notes and coins, bankers' drafts and cheques of any kind, including travellers' cheques. There is

The declaration form will be available at ports and airports and will be produced with a carbon backed top copy so that travellers can keep a duplicate, which HMRC officers may ask them to produce as evidence of having made a declaration. The form will also be downloadable from www.hmrc.gov.uk

Dave Humphries, Head of Criminal and Enforcement Policy at HMRC said: "The declaration system is one means of providing information to assist HMRC in targeting movements of criminal cash more effectively."

Tax implications of an overdrawn director's account

A key fact to get to grips with when you run your own company is that the company is a separate organisation, and the money is not automatically your money. You cannot draw funds from the company bank account, or ask the company to pay for your personal expenses, without some tax and accounting implications.

When you do take money from the company, that payment has to be treated as:

- salary - which must be taxed under PAYE and is subject to national insurance when it is made available to you; or
- dividends - which must be approved by the members and be paid out of the existing profits of the company; or
- a loan - which does not create an immediate tax charge but may do so if the total amount borrowed exceeds £5,000 at any point in the tax year.

The legal rules covering transactions with directors including loans have historically been complex. The new Companies Act 2006 introduces some much needed simplification into this area. In this article we focus on the tax implications of such transactions, of which there are currently no plans to simplify.

A loan may be made up of cash drawings, but also the value of personal expenses that the company has paid for on your behalf. To avoid these expenses being treated as benefits in kind, or as salary payments, and creating high tax and national insurance charges for both you and the company, the company may 'lend' you the value through your director's account in the company's books, to repay the expense incurred. This loan can quickly lead to an overdrawn director's account.

When you borrow more than £5,000 there will also be a benefit in kind charge on the basis that you have had an interest-free loan. You will be required to pay tax on the interest you should have paid on the loan, which is calculated at 6.25% per annum. This tax charge applies where you borrow more than £5,000 for any period; whether five months or five years.

A loan made to a director should be cleared within nine

months of the company's year end. If you do not do so the company must pay an extra corporation tax charge equivalent to 25% of the amount of the loan. That tax charge will be set-off against the next corporation tax payment due after you finally repay the loan. The tax charge on the company is in addition to the benefit in kind charge on you personally.

The tax issues are complex and we recommend you contact us for advice before extracting funds from your company.



More pay and leave for parents



The rules for maternity pay and leave are complex, and things may become even more complicated for employers as they become more generous for mothers and their partners.

The current rules

Currently mothers whose babies are due on or after 1 April 2007, and who satisfy minimum pay and length of service criteria, are entitled to a year off work, nine months of which is paid as Statutory Maternity Pay (SMP). The first six weeks of SMP are generally paid at 90% of their average weekly earnings. The remaining 33 weeks are normally paid at £112.75 a week.

The proposals

The government proposes to increase the payment period for SMP to a year, which will match the leave period. They also propose that, if the mother and father wish, six months of this pay and leave period may be transferred from the mother to the father as Additional Paternity Leave (APL) and pay.

Currently fathers are entitled to a maximum

of two weeks Statutory Paternity Pay which for most claimants is paid at £112.75 a week.

The government has entered into a consultation process with interested parties on the introduction of APL and pay for fathers. Although the consultation period will have closed before this newsletter reaches you it is unlikely that the government will have been able to issue its response or further guidance. We will keep you informed of developments.

Part of the problem with the introduction of APL and pay is that it could potentially involve two employers, the mother's and the father's. The consultation focuses on the administration of the scheme and includes:

- procedures for the notification by the father and mother to the father's employer that he intends to take APL and pay
- the proposal that notification will not have to be made to the mother's employer. This is the government's preferred approach recommended in the consultation as the involvement of both

the mother's and father's employers was thought to be too administratively burdensome

- the notice period required to allow employers to plan for the employee's absence
- the procedures to be put in place where the mother's and father's circumstances change and they want to amend the proposed leave dates.

The government has stated its intention to keep the APL and pay scheme as straightforward as possible for both employers and employees.

Implementation

The government's goal is to bring in APL and pay at the same time as extending SMP from 39 weeks to 52 weeks, which they hope to achieve by the end of this parliament. This will mean that both parents could choose to take an equal amount of paid leave. The earliest proposed date that APL and pay will be implemented will be for babies due on or after 5 April 2009.

Lasting Power of Attorney

From October 2007 individuals will be able to make a Lasting Power of Attorney (LPA) which will enable them to nominate individuals to make decisions on their behalf regarding their health and welfare, as well as their finances, should they lose mental capacity at some point in the future. There are also provisions for individuals to state their wishes regarding potential medical treatment that they may be offered in the future. The new

LPA replaces the previous system of Enduring Powers of Attorney (EPA) which only covered financial matters. The change has come about as a result of the Mental Capacity Act 2005.

After October 2007 it will no longer be possible to create an EPA although those already in existence will remain legally binding. Under the LPA system it will be possible to appoint an attorney either for personal

welfare or property and affairs purposes, or for both. It will not be possible to convert existing EPAs into LPAs.

To be legally binding an LPA needs to be registered with the new office of the Public Guardian as soon as it is created. Under the system of EPAs the attorney only needed to be registered when the individual was believed to have lost mental capacity. An LPA must also be 'certified' by someone

who has known the individual for two years.

Once certified and registered, the attorney has the authority to act in accordance with the terms of the LPA. The attorney does not have the power to act for the individual unless they lose mental capacity. Third parties, such as banks or doctors, will need to see a copy of the document before they will accept an attorney's instructions.

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