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Entrepreneurs' Relief: an update

Entrepreneurs' Relief (ER) is available to taxpayers on the disposal of the whole or part of their business. ER means that you pay capital gains tax (CGT) at a rate of 10% rather than 20%, subject to a lifetime limit of £10 million.

Following the 2018 Autumn Budget, new conditions have been introduced to ensure shareholders benefitting from ER have a minimum economic stake in the company. According to HMRC, 'it is designed to support and encourage investment and means that entrepreneurs can keep more of the rewards when their business is successful'.

Who can claim ER?

ER is available to company directors and employees meeting certain conditions, as detailed later. It is also available to sole traders or partners selling or giving away all or a certain part of their business.

The disposal of 'associated' assets, such as land and buildings used by a company or partnership but owned by an individual, may also attract ER if the individual chooses to leave the company or partnership.

Qualifying company

ER is available on the gains made on the disposals of shares and securities in a trading company or the holding company of a trading group. A trading company is defined as one 'carrying on trading activities whose activities do not include, to a substantial extent, activities other than trading activities'.

Trading activities are those activities which carry on a trade or profession by buying and selling goods or services with a view to making a profit or surplus.

On the other hand, non-trading activities are those undertaken by a company that may invest, for example in properties or shares.

Conditions

In order to qualify for ER, the taxpayer must be an employee or officer of the company and hold at least 5% of the ordinary share capital, and 5% of the associated voting rights.

In addition to the existing tests, a new test is introduced whereby the shareholders must also be entitled to at least 5% of the company's distributable profits and 5% of net assets on the winding up of the company.

However, where the taxpayer cannot demonstrate their entitlement to the profits and assets of the company, a taxpayer can use an alternative test. This is that, in the event of a disposal of the ordinary share capital of the company (i.e. the company being sold), the taxpayer is entitled to 5% of the disposal proceeds.

The above conditions must be satisfied by the shareholders for a period of 12 months until the date of disposal or cessation of the trade. For disposals on or after 6 April 2019, the minimum period throughout which the conditions must be met is increased to two years.

In another change new legislation gives relief where an expanding business raises additional finance by

means of the issue of new shares for cash, but as a result, an individual's shareholding is 'diluted' – falling below the 5% needed to claim ER.

For new investment taking place on or after 6 April 2019, shareholders will be able to make an election, treating them as if they had disposed of their shares and immediately reacquired them at market value just before dilution. To avoid an immediate CGT bill on this deemed disposal, a further election can be made to defer the gain until such time as the shares are actually sold. ER can then be claimed in its current form.

The lifetime limit of £10 million remains intact. Additionally, taxpayers continue to benefit from an annual exempt amount of £12,000 in 2019/20, on which CGT is not due.

Drawbacks

There are situations where shareholders may not be able to claim ER:

- Directors should remain in office up to the date of disposal of their shares to avoid jeopardising an ER claim
- If a company goes from a trading company to an investment company, shareholders of the company will no longer qualify for ER.

If you are thinking of making a disposal of shares in your company, please get in touch to find out if you qualify for ER.

New rules for personal service companies

The 2018 Autumn Budget announced changes to the 'off-payroll' working (or 'IR35') rules, which are set to apply from April 2020. This may affect you if you work on a contract through a personal service company (PSC) in the private sector, or hire or place such workers. Similar rules already apply in the public sector.

The IR35 rules aim to prevent the avoidance of tax and national insurance contributions (NICs), where an individual works for a client through an intermediary (usually a PSC), and the use of the intermediary means that they avoid being taxed as the client's employee.

Currently, responsibility for deciding whether the IR35 rules apply to a private sector contract lies with the intermediary. If IR35 applies, the intermediary also has to account for PAYE and NICs on the fees received.

From 6 April 2020, responsibility for deciding employment status is set to pass from the intermediary to the party engaging the worker. If IR35 applies, the business, agency or third party paying the intermediary must deduct income tax and employee NICs, and become liable for employer NICs.

HMRC has an online Check Employment Status for Tax (CEST) tool to help decide whether the off-payroll working rules apply to any given

contract: www.gov.uk/guidance/check-employment-status-for-tax. The tool can be used by workers, hirers or agencies placing a worker. HMRC will stand by the result, unless a compliance check finds that information supplied was inaccurate.

The service can be used anonymously and will not store any personal details or findings. However, the result can be printed, which is essential. If there are changes to the working arrangement, we would recommend that you run the new details through the check again.

It is important to note that problems regarding employment status do arise in practice, even when the tool is used, and HMRC has stated that it is committed to improving CEST's usefulness.

Some aspects of the forthcoming change also remain to be clarified, and government consultation is ongoing. The change will affect employing businesses which are classed as 'medium and large businesses', but not 'small' ones; the definition of small will be based on the Companies Act 2006 definition of a small company.

The government has issued a welcome assurance that the change is not retrospective. Where someone starts paying employment taxes under IR35 for the first time, or where a business decides that a worker should come within the rules, this will not automatically trigger an enquiry into earlier years.



Your 2018/19 year end planning checklist



Make use of the annual ISA allowance

Have you made the most of your 'tax-free' ISA allowance for 2018/19? There are several different types of ISA available, including Cash ISAs, Stocks and Shares ISAs, the Lifetime ISA, the Help to Buy ISA and the Innovative Finance ISA. The overall annual subscription limit is £20,000. Payments for the 2018/19 tax year must be made by 5 April 2019.



Utilise personal allowances

Have you made use of the personal allowances available across your family? Individuals within the family are taxed separately, and each is entitled to their own allowances and exemptions. The basic personal allowance (PA) for 2018/19 is £11,850. Making full use of the allowances can help you and your family to benefit from more of your wealth. Contact us for advice.



Consider the Marriage Allowance

If you are married and one partner is a lower earner, have you taken advantage of the transferable Marriage Allowance? Up to £1,190 is available for 2018/19 to married couples and civil partners, where neither pays income tax at the higher or additional rate and one partner earns no more than £11,850. This can help couples to reduce their joint tax liability by up to £238.



Maximise your pension contributions

Have you maximised your contributions into a pension scheme? Tax relief is available on contributions up to the greater of £3,600 and the amount of relevant UK earnings, and subject to an annual allowance of £40,000. Contributions on any excess over this amount will generally be taxable. The allowance can also be tapered for individuals who have income over £110,000 and adjusted annual income over £150,000. Contributions must be paid on or before 5 April 2019 to be applied against 2018/19 income.



Review your remuneration strategy

Have you reviewed your remuneration strategy to establish the right balance between dividends and salary? The Dividend Allowance fell from £5,000 to £2,000 in April 2018. While there may still be potential benefits for a director-shareholder taking a dividend over a salary, the amount of tax saved has been reduced. You may also wish to look at other ways of extracting profit from your business, such as considering incorporation if your business is currently unincorporated, and making the most of tax-free allowances, such as mileage payments for business journeys.

For more information on a range of tax planning tips to consider before the year end, please contact us.



Spotlight on charities

Although charity law varies across the UK, charity governance is very much in the spotlight.



In a recent report, the Charity Commission for England and Wales (CCEW) suggested that nearly 40% of small charities were submitting inaccurate financial information. Small

charities are defined as those with annual income below £25,000, and this category makes up two thirds of those on the CCEW's register. The CCEW is concerned that some of those given the job of submitting a charity's annual return – particularly in the small charity category – are not sufficiently skilled to perform the role accurately.

Annual returns

Against this background, charities registered in England and Wales should be aware of developments regarding annual returns. Returns must be submitted no later than ten months after the end of the financial year and charity trustees must keep the charity's registered details up to date.

From November 2018, the service to update these details changed. All charities must now check and update their details online before they can submit their annual return. Charities will only need to provide missing information the first time they sign in, or when they need to update their charity details. Charities will be able to choose which sections or information to edit and update.

Information required includes all current trustee names, their contact details (including an email address), and details of the charity's UK bank/building society accounts. Bank/building society details will not be available publicly.

From 1 April 2019, full legal names will show to the public and trustees will not be able to use a 'public display' name on the charity register. If, however, this would cause personal danger to an individual, it is possible to apply for a dispensation.

New questions are introduced in the 2018 return, and these can be previewed before signing in. Some questions are optional for 2018, but mandatory from 2019 onwards. They are intended to allay public concerns, for example about high levels of pay in charities: or to highlight possible areas of risk, say in relation to money transfer overseas.

New questions for 2018 include a breakdown of salaries across income bands, and the amount of total employee benefits for the highest paid member of staff. Details of this, however, will not be published on the public register. There are also questions asking about use of professional fundraisers, receipt of grants and contracts from central government and local authorities, as well as questions on safeguarding children and adults at risk.

Overseas expenditure is another area where the detail is being expanded. If a charity has spent money outside England and Wales, it will need to explain if it has transferred money overseas by a means other than the regulated banking system. There are questions about whether controls exist to monitor overseas expenditure, and others asking if the trustees are satisfied that risk management policies and procedures are adequate for the charity's activities and for its place of operations. These are mandatory for returns from 2019 onwards, but optional for 2018.

Questions about income received from outside the UK are also introduced. These include which countries income was from; the value of income by country; the

source and amount of such income, analysed into categories such as overseas governments or quasi government bodies; overseas institutional donors; and individual donors resident overseas. Some of this information will be optional for 2018, but mandatory thereafter.

These changes mean some additional work

for charities, and may require changes to financial systems to capture relevant detail.

Please do not hesitate to contact us for further advice.

From 1 April 2019, full legal names will show to the public and trustees will not be able to use a 'public display' name on the charity register.

Tax Round-up

The new Welsh rates of income tax

6 April 2019 sees the introduction of the new Welsh Rates of Income Tax (WRIT), which will be payable by individuals whose main residence is in Wales.

Currently, all income tax from Wales is paid to the UK government. From 6 April 2019, a proportion of that income tax will be paid directly to the Welsh government. The UK government will reduce the basic, higher and additional rates of income tax by 10p for Welsh taxpayers, and the Welsh government will set the three WRIT. These will then be added to the UK rates.

The Welsh Assembly has agreed the government's proposal to set the first WRIT at 10p, meaning that for 2019/20 Welsh taxpayers will pay the same income tax as those in England and Northern Ireland.

Income tax will continue to be collected via PAYE and self assessment. However, Welsh taxpayers will have a new 'C' prefix added to their tax code.

The personal allowance and tax rates on dividends and savings income will continue to be set by the UK government for all UK taxpayers, regardless of where they live in the UK.

Taxpayers are being advised to ensure that they keep HMRC informed of any change of address.

Making Tax Digital for VAT – exemptions and deferrals

Making Tax Digital for VAT (MTD for VAT) is set to come into effect from 1 April 2019 for businesses whose turnover is greater than the current VAT registration threshold of £85,000. However, there are deferrals and exemptions to this as listed below.

Firms that fall into the categories below are exempt from MTD for VAT:

- Businesses run by practicing members of a religious society or order with beliefs incompatible with the regulation's requirements
- Businesses subject to an insolvency procedure

- Those satisfying HMRC that, for reasons of age, disability, remoteness of location or for any other reason, it is not reasonably practicable for them to use digital tools to keep business records in order to submit returns.

Furthermore, HMRC's MTD for VAT guidance was updated in October 2018, outlining a significant deferral of the initiative for a small group of taxpayers with 'more complex' requirements. They will be given an additional six months to prepare for MTD for VAT, and will therefore not be mandated to use the system until 1 October 2019.

The deferral applies to: not-for-profit organisations that are not set up as a company; trusts; VAT divisions; VAT groups; local authorities; public corporations; and traders based overseas. Public sector entities required to provide additional information on their VAT return, those who must make payments on account, and annual accounting scheme users are also covered by the deferral.

Tax Tip

Forming a limited company

If you are self-employed you may want to consider forming a limited company. A limited company can be an effective way to shelter profits, especially if immediate access to them is not required.

Profits paid out as salaries, dividends or bonuses are often liable to the top tax rates, whereas profits kept in the company will be taxed at 19%.

Funds retained by the company can be used to buy assets or provide for pensions, both of which can be eligible for tax relief.

We can help you set up a company – please contact us for more information.

Reminders for your diary

March 2019

- 1 New Advisory Fuel Rates (AFR) for company car users apply from today.
- 3 5% late payment penalty on any 2017/18 outstanding tax which was due on 31 January 2019 and still remains unpaid.
- 19 PAYE, Student loan and CIS deductions are due for the month to 5 March 2019.
- 31 End of corporation tax financial year.
End of CT61 quarterly period.
Filing date for Company Tax Return Form CT600 for period ended 31 March 2018.
Last minute planning for tax year 2018/19 – please contact us for advice.

April 2019

- 1 Making Tax Digital for VAT is introduced. Most businesses must comply from their first VAT return period starting on or after 1 April 2019.
- 5 Last day of 2018/19 tax year.
- Deadline for 2018/19 ISA investments and pension contributions.
Last day to make disposals using the 2018/19 CGT exemption.
- 14 Due date for income tax for the CT61 period to 31 March 2019.
- 19 Automatic interest is charged where PAYE tax, Student loan deductions, Class 1 NI or CIS deductions for 2018/19 are not paid by today. Penalties may also apply if any payments have been

made late throughout the tax year.

PAYE quarterly payments are due for small employers for the pay periods 6 January 2019 to 5 April 2019.

PAYE, Student loan and CIS deductions are due for the month to 5 April 2019.

Deadline for employers' final PAYE return to be submitted online for 2018/19.

May 2019

- 3 Deadline for submitting P46(Car) for employees whose car/fuel benefits changed during the quarter to 5 April 2019.
- 19 PAYE, Student loan and CIS deductions are due for the month to 5 May 2019.
- 31 Deadline for forms P60 for 2018/19 to be issued to employees.