2010 **SPRING NEWS**

HEYWARDS

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We can't go on like this…

The Conservatives' billboard campaign for the General Election promises to "cut the deficit, not the NHS". The details of how this will be done have not yet been spelled out: Mr Osborne says that he would like a look at the books before he can be sure what needs to be done. On the other hand, Mr Darling's Pre-Budget Report in December set out how he proposes to bring public borrowing down if Labour is re-elected. There are painful tax increases ahead, but even so the deficit will take years to correct. It seems likely that there will be even more cuts to public spending as the economy struggles out of recession. The Conservatives' slogan – "we can't go on like this" – suggests they want to put the country's finances straight sooner, but if they want to reduce the deficit faster they surely cannot follow their tax-cutting instincts.

Mr Darling will confirm his plans in more detail in the Spring Budget, and no doubt Mr Osborne will give us more details as the general election approaches. While they argue it out, the rest of us will have to cope with the rules they produce. This newsletter highlights some things that you might consider now to pay less tax, or to keep clear of the traps and pitfalls of Britain's increasingly complicated tax system. The Government may be about to change, but we will still be here to advise you. ●

The name is Bond

Not James Bond – Investment Bond. Bonds are "wrappers" which fund managers use to parcel up their products to sell to the public. Like any investment, they can go up as well as down, and like most investments, they have been having a rocky time over the last couple of years. This has highlighted one of the differences between bonds and straightforward investment in shares – the tax treatment of gains and losses.

The glossy brochure will probably explain the tax treatment somewhere, but it often isn't at the front and it often isn't easy to follow. In general, bonds are chargeable to income tax, not to CGT. If the funds are invested in the UK, it's assumed that there will be some UK tax on the money while it's invested, so any gain is only charged to higher rate income tax – currently still the difference between 40% and 20%, but rising soon potentially to 50% less 20%. However, if you choose the time of encashment carefully, it's often possible to reduce this tax charge.

If the money is invested offshore, any gain will usually be charged to income tax in full (20%, 40%, 50%) when the bond is cashed in, because it's assumed that there has been no UK tax in the meantime.

That's if there is a gain – what about losses? If you are unlucky enough to have picked the wrong moment to buy your bond, the tax system has no sympathy for you. You cannot set a loss against your other income, nor even against your gains – so profits can be taxed at 40% and losses are usually not relieved at all.

If you have any bonds that you are thinking of cashing in, it's worth checking first what the tax consequences will be. And if you are thinking of buying one, check out the tax position. We will be happy to advise you. ●

Pension problems

Since last April there have been special rules to catch attempts to get around the restriction of pension tax relief from April 2011 for those earning over £150,000. If you pay extra contributions now to beat the change, you may suffer an extra tax charge.

There were changes to these rules in December so that contributions paid by employers can be caught, and people on incomes of £130,000 – previously £150,000 – can be affected. If you have an income around that level, or have had in the last two years, and you want to pay extra contributions totalling more than £20,000 in the year, discuss it first with us. We'll check whether you might trigger the tax charge. ●

Flat rates aren't flat

If you use the VAT Flat Rate Scheme, the VAT you paid during 2009 should have been less than it was in 2008 – the flat rates changed when the standard rate was cut to 15%, although they didn't all drop by the same amount. Now the standard rate has gone back up, so have the flat rates – but not always to the place they were before. It's important to make sure that you are using the right rate, and that you deal with the change of rate correctly – if you collect debtors in January and February who were charged 15% VAT in November and December, you should use the 2009 flat rate in working out what you pay to HMRC.

The FRS is supposed to be simple. If you are finding the change of rates anything but, we can help. ●

Tax dot com

HMRC increasingly want to deal with taxpayers over the internet – then they can cut costs by replacing people with machines. Looking for positives, filing returns electronically can save time and increase certainty – as long as HMRC's computer is working and not overloaded by the demand on 31 January (the system crashed one year), the envelope can't get lost in the post and you know it's arrived.

Firms with 50 or more employees now have to e-file in-year PAYE forms, and nearly all will have to do so for their 2009/10 annual returns. Most VAT returns will go the same way from April 2010. Corporation tax e-returns are coming in 2011. If you aren't sure how you will comply with these new rules, we can advise you. ●

Moving goalposts

Before personal pensions were introduced in the 1980s, tax-advantaged pension schemes couldn't pay out until your 60th birthday – unless you were in a job where people generally retire earlier, such as a sports player. In a fit of optimism about the future, the 1988 rules allowed people to take the benefits from pension policies at 50 – although building up a fund large enough to retire by that age has been a challenge for most people.

Now the age is changing again: from 6 April 2010, the minimum retirement age moves up to 55. Anyone aged between 50 and 55 at present has the opportunity to cash in a policy – taking a tax-free lump sum and starting to draw a pension – before 6 April, but if they don't, they will have to wait until their 55th birthday. Maybe in five years it will go back up to 60, and retirement will continue to disappear over the horizon.

Some people may want to take advantage of this now, but the rate of annuity that can be achieved at such a young age is usually very low. Pension fund values have taken a hammering over the

last few years, and we can only hope that they will recover further in the next few – this may not be a good time to crystallise the value by cashing in the benefits. But it's important to know that the opportunity is there, and it's going away for a few years. ●

Silver and gold

If you lose your job, a golden handshake could be the silver lining. Traditionally the first £30,000 of a pay-off has been regarded as tax-free – but don't count on it, because the taxman usually wants a slice of the whole thing.

The exemption applies if the payment is purely "for losing the job" – damages for the employer's breach of contract in sacking you, or a wholly unexpected thank you to compensate you for the shock. If you have the right to the payment in your contract, then it's taxed in full as pay.

Even if you don't obviously have the right, HMRC may try to read it in. For example, if you have the right to three months' pay in lieu of notice, but your employer just pays you the cash to go immediately, they will look for anything that indicates the employer has a choice between these two routes. If so, it's paid under the contract, and it's taxable.

There have been recent cases in the Tribunal which show that this is a live issue in a recession, and the decision can go either way. If you are on the receiving or the paying end of a golden handshake, we can advise you on what the likely tax treatment will be. ●

Doctor, doctor…

There have now been two "disclosure opportunities" for people who have salted away undeclared money in foreign bank accounts to come forward and put their affairs in order with HMRC by paying any outstanding tax and a reduced penalty. Now HMRC have announced a "tax health plan", offering the same idea to doctors. The offshore arrangement came about because HMRC obtained a great deal of information from banks about customers who had foreign accounts – now it seems that they have required insurance companies to give them details of payments made to doctors, and they reckon they can scare large numbers into coming forward by giving the impression that "they know everything". To take advantage of a reduced penalty offer, the doctor has to declare an intention to make a disclosure by 31 March and provide the full details by 30 June.

HMRC seem to suspect everyone of hiding their money – the medical profession is a surprising target, and accountants are wondering where the next "last chance offer" will come. If you have nothing to hide, you have nothing to fear – except possibly the inconvenience of HMRC asking questions. If you think that you may not have told them everything, it's important to put the record straight before they come knocking – whether you are a doctor, a baker or a candlestick-maker. We can advise you. ●

Flapjack flash

Jaffa Cakes were the subject of a famous VAT dispute: chocolate cake or chocolate biscuit? The court decided that they were cakes, because – seriously – cakes go hard when they are stale and biscuits go soft. After an adjournment to allow the evidence to go stale, it was found to have become hard.

Why does it matter? Cakes are zero-rated for VAT, but chocolate biscuits and "confectionery" are standard rated. Another argument recently came before the Tribunal. Asda ran a competition for people to design new products, and a retired wrestler came up with a bar containing a variety of seeds. The judges thought it was tasty and the company marketed it as a "flapjack bar", even though flapjacks traditionally are made of oats and contain other ingredients that weren't included in this product. HMRC may have suspected that it was called a flapjack because they decided back in the 1970s that flapjacks are cakes, not confectionery, so they aren't charged to VAT. Cereal bars are usually taxed as sweets.

The Tax Tribunal had to discuss the weighty question "what is a flapjack?" and decided that these seed bars didn't fit the description. VAT was due. Although this must be light relief for the judges – and a tasty snack between other cases – it highlights the difficulty of applying the VAT rules if you are a retailer. How can you tell what's VATable and what's not? Usually you follow what the supplier does – if they charge VAT, so do you. But if you want to discuss the correct liability of your stocks, we'll be happy to talk – over a cup of tea and a biscuit. ●

Reverse the charges

Does anyone reverse the charges on the telephone any more? In VAT, a reverse charge is something quite different – if a UK business buys services in from a foreign supplier, it has to account for VAT as if it both sold and bought the supply. That's to level the playing field – a UK supplier would have to charge UK VAT, so you can't avoid it just by going to someone overseas.

If you are a fully taxable trader for VAT, it doesn't matter a great deal because you can recover in Box 4 the figure you put in Box 1 of your return. So on a UK purchase you pay £11,750 to your supplier and claim £1,750 back in Box 4; on a foreign purchase you pay £10,000 to the supplier and put £1,750 in Box 1 and Box 4, netting off to nothing. It matters if you can't recover VAT in full – then Box 1 is bigger than Box 4 and the difference has to be paid to HMRC as a cost.

Recently an organisation which helps to defend doctors against negligence claims landed in hot water over this. It used foreign lawyers for some of the cases, but it didn't account for the reverse charge because it thought the doctors themselves were the lawyers' clients – if anyone should be dealing with it, it would be the doctors. When HMRC looked into it, they decided that the organisation engaged the lawyers, and it was liable for £5m in back tax which it couldn't recover. The doctors' premiums may be going up this year as a result.

If you buy in services from abroad, and you aren't sure how to deal with them – or if your supplier wants to charge you foreign VAT – we will be happy to advise you. ●

Ready set ECSL

From 1 January 2010, new rules have applied to many services provided by UK businesses to foreign customers and by foreign suppliers to UK businesses. One of the key changes is a wholly new requirement to provide HMRC with an analysis of sales by customer – an "EC Sales List" – showing the foreign VAT registration numbers, where you treat supplies of services as "outside the scope of UK VAT" because the customer is a business registered elsewhere in the EU.

The first report of services is due in April, and there is no lower limit below which you don't have to provide it – if you sell any services at all to EU business customers, you are likely to have to file a return. If you want to be sure that you are ready for the new reports, or you are not sure which services are still chargeable to UK VAT, we will be happy to help.

If you are selling goods to EU business customers, you will already be used to EC Sales Lists, but you will now have to provide them much quicker – if your despatches are more than £70,000 a quarter, the return becomes a monthly chore to be done within 14 days of the month end (on paper) or in 21 days (online). ●

No difference

From the boss's point of view, employing people can be a minefield – they have so many rights. The workers may see it differently if they need the protection of the law. One area in which European law continues to expand worker protection is non-discrimination. Everyone has a right to be treated equally, regardless of race, gender, religion or disability.

In a recent case, a woman claimed that she was discriminated against by her employer – a law firm – because she had a disabled child. The firm argued that the law didn't apply, but the European Court and the Employment Appeals Tribunal have agreed that it does – an employee should be protected from "discrimination by association" if they are connected with a disabled person, even if they are not disabled themselves.

That doesn't necessarily mean that the employee will win when they argue about the facts. She will still have to prove that the firm treated her differently from someone who had to care for a non-disabled child. If the employer can show that it would have applied the same treatment to anyone taking time off to look after someone else, regardless of the background of that person, then the claim for discrimination will probably fail.

It's all about being fair to everyone – but it's often hard to see how to achieve that. ●

Excuses, excuses

When HMRC want information, they usually start just by asking. If that doesn't work, they send a Notice (with a capital N) demanding it. If the taxpayer doesn't comply, they can charge stiff penalties. These can be cancelled if the trader has a "reasonable excuse" for not answering.

In two recent cases, companies pleaded that they had relied on their accountant to respond – it was the same accountant, and he was overwhelmed with 50 enquiry cases on the go at once. One of the companies won their appeal: the information was complicated and it was reasonable to rely on the accountant, even if he was snowed under. The other company could have provided the answers itself, because the questions were straightforward. The penalty was confirmed.

The main thing is, if you get a request from HMRC – especially if it's a formal Notice – you need to deal with it promptly. We will help – not all advisers are submerged under that many enquiry cases! ●

I want my lawyer

If an employer wants to discipline someone, or possibly sack them, it is essential to follow the proper procedure. Otherwise the worker can claim unfair dismissal and compensation. A couple of recent cases have considered whether "the proper procedure" includes allowing the employee to have a legal representative at any disciplinary hearing. Under the ACAS Code of Practice on Disciplinary and Grievance Procedures, a worker only has the right to be accompanied by a colleague or a trade union representative. The employer might feel that the presence of a lawyer would raise the stakes and require them to incur the cost of bringing their own professional adviser.

The Court of Appeal said that the employee would have the right to a lawyer if the allegation was so serious that it was effectively a criminal charge, even though it was being dealt with as a disciplinary matter. The case concerned allegations that a doctor had acted improperly with a patient, and that could lead to him being struck off and unable to practice at all. In those circumstances, fairness required that he should be allowed legal representation. It won't apply in every disciplinary case – but it may be hard to tell when the employer can refuse. ●

A grey area

Age discrimination in the workplace was outlawed by the Employment Equality (Age) Regulations 2006. However, it is still open to employers to require workers to retire at the "default retirement age" of 65. That is obviously discriminatory: yesterday you were fine in the job, today you must go for no reason other than it's your birthday.

The organisation Age UK challenged this principle in the courts, but a judge upheld it – for the moment. The government allows this specific discrimination as an exception to the general rule "to protect the integrity of the labour market" – taking away the retirement age suddenly could create significant difficulties for employers and employees alike, particularly in younger groups who would find fewer jobs available to them.

The judge considered that the government's promise to review the position soon – in 2010 – meant that the current rule was acceptable. It seems likely that the law will have to change, and people will be allowed to keep going until they want to leave or are dismissed on other grounds – but the idea of a compulsory retirement age may be phased out gradually. ●

Blessed are the givers

Gift Aid has been a great success since it was introduced in 1990 to allow tax relief for single gifts to charity. It's easy: make a gift, give your name and postcode, and the charity gets a bonus from the taxman. What could be simpler?

For a basic rate taxpayer, it really is that simple – sign and forget it. You pay basic rate tax to the taxman, who hands it on to the charity. If you pay at 40%, though, remember that you can claim more relief through self-assessment – you don't have to pay the top rate on money that you've given to charity. It's a little more complicated – you need to record what you've given so you can put it on your tax return. You give £80 to the charity, which claims back £20 (in theory – at the moment it gets a small bonus on top), and then your own tax is reduced by £20.

If you happen not to be a taxpayer this year, you have to be careful. The Gift Aid declaration says that you will pay enough tax to cover the amount the taxman passes on for you – so if you give a charity £80 and sign, the charity will claim £20 from HMRC, and HMRC will expect you to be paying at least £20 in tax that year. If your income drops but you carry on making the same regular donations, this can catch you out – although it's not clear how rigorously HMRC police it, because matching up the names would be a huge exercise. They pick up some regular givers who stop paying tax, for example because they go abroad for a spell but still pay charitable covenants.

If you've made Gift Aid donations, do keep a note for the tax return. And if you realise that you haven't been claiming the higher rate relief, you can go back to previous years – 2004/05 is still open until 31 January 2011. ●

A lofty idea

If you pay a builder to convert your loft into a room, everything you pay is VATable – if the builder is respectable. The builder may use individual sub-contractors to do plumbing and plastering who are too small to be VAT-registered – so the builder's costs are not VATable, but all the sales are chargeable.

A company came up with an ingenious idea to get around this – instead of contracting to build the loft, it offered to organise the project. The client contracted individually with Tom, Dick and Harry for all the work, and only the "management fee" carried VAT. Not surprisingly, the taxman didn't like it, and persuaded the Appeal Tribunal that it didn't work – the real supply was the normal one, and the company should have charged VAT on everything.

Now the High Court judge has sent it back for the Tribunal to think again. He ruled that the signed contracts are the starting point in deciding who does what for VAT. If the Tribunal thought "the real supply" was something else, it would have to base that more clearly on the evidence. This trader hasn't won yet, but he has a second chance to persuade the Tribunal to cancel an assessment for more than £1m of VAT that he didn't think he had to collect from his customers.

This was an ingenious idea, but the dispute is a reminder of two things if you use a cunning plan to reduce your tax – you have to be prepared to argue with the taxman, and you have to make sure that you will win on the evidence. ●

Unpleasant discoveries

When you have filed your tax return, you hope that's the end of that. The taxman has a year to raise routine questions, and then it ought to be done and dusted. Unfortunately, it isn't that simple – HMRC still have the right to ask for more tax if they make a "discovery" by 31 January 5 years and 10 months after the tax year. They can't use this power if the return contained enough information for them to appreciate what had happened when it was submitted, but if it didn't, the taxpayer has no protection.

In a recent case, the taxpayer treated an "offshore bond" – fully taxable at 40% – as if it had been a UK investment, only taxable at higher rates of income tax. The Tribunal agreed that this was an innocent error, but there hadn't been anything in the tax return to alert the Inspector. The law was complicated, but the taxpayer should have recognised that and taken advice to be sure that the return was correct. The extra tax had to be paid.

It's important not only to check that the numbers in a tax return are as accurate as possible, but also to think whether any words should go with them to try to get protection against discovery. "Hoping the taxman never finds out" is not a safe strategy. ●