Tax Briefing

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What we know about MTD

The government is determined to push ahead with Making Tax Digital (MTD), which will require businesses and landlords to use accounting software to make quarterly reports of income and expenses to HMRC. This reporting will apply for accounting periods starting on and after:

- 6 April 2018 for businesses and landlords who pay income tax;
- 1 April 2019 for VAT reporting; and
- 1 April 2020 for all companies and for partnerships with turnover of £10m or more.

Those with low levels of sales or rents will be exempt from making quarterly reports, but the government hasn't confirmed what this minimum turnover threshold will be. Businesses with turnover up to another, also as yet undetermined, threshold will be able to delay quarterly reporting for another year. Quarterly reporting will be compulsory for all other businesses and landlords, but penalties for non-compliance won't be imposed for a year.

If your turnover is less than the VAT registration threshold (£83,000 from 1 April 2016), you are permitted to complete just three lines on your tax return regarding your accounts: total income, total expenses and resulting profit or loss. These three lines will be all you need to report quarterly under MTD. HMRC has promised that free software will be available to businesses in this category, if they have no employees.

Where your turnover is higher than the VAT threshold you will be required to submit totals of around fifteen categories of expenses, plus sales income for each quarter. The software to do this will not be free.

VAT reporting won't be combined with MTD quarterly reporting until at least April 2019, so until then you will need to submit VAT returns in addition to your quarterly MTD returns.

To finalise your accounts with HMRC you will have to send HMRC a final period statement by ten months after the end of your accounting period end. A business with a 31 March year end will have to submit a year end statement by the following 31 January, as is the case now on a self assessment tax return.

You will be permitted to use spreadsheets to record day-to-day transactions, but to make MTD reports the data will have to be transferred into MTD-compliant accounting software. We can discuss how your accounting systems may need to change to prepare for MTD.

Revised cash basis

Reporting income and expenses under MTD will be easier for businesses who draw up their accounts using the cash basis. This is a basic form of accounting which suits certain small unincorporated businesses.

Currently, in order to use the cash basis you must be a trading business, not a limited liability partnership or property investor, with turnover not exceeding the VAT registration threshold (£83,000). »

» You must switch to a traditional accruals basis of accounting once your turnover exceeds twice the VAT threshold (£166,000).

The entry and exit thresholds for the cash basis will increase to £150,000, and £300,000 respectively, on 6 April 2017. However, other restrictions remain, including a block on setting losses against the trader's other income and a £500 cap on the amount of interest which can be deducted per year.

Property businesses

Individual landlords will be expected to use a special form of the cash basis from 6 April 2017, where their annual rental income does not exceed £150,000. If you don't want to use this cash basis for your property business, you will have to opt out by checking a box on your tax return.

All individual landlords (not companies) who let residential property from April 2017 will have restrictions imposed on the amount of interest and finance charges they can deduct each year. These restrictions will equally apply to landlords using the cash basis. However, cash basis landlords will be subject to an additional restriction. The deduction for interest and finance charges will be proportionally reduced if the total value of the outstanding mortgages connected to the property business exceeds the market value of the let properties at the end of the year.

Long-term implications of child benefit

Child benefit is paid to parents of young children in the UK, if they claim it. Some higher earning parents don't claim the benefit, as they know it will be clawed-back as a tax charge. However, not claiming child benefit can disadvantage both the parent and the child in the long term.

Claiming child benefit, whether it is actually paid or not, ensures the parent receives national insurance (NI) credits for periods when they aren't working or claiming job seekers allowance, whilst the child is under twelve.

To receive the full state pension, the parent needs to have paid NI, or received NI credits, for 35 tax years. The NI credits from child benefit help plug the gap in the NI record which may be created when one of the parents stays at home to care for the child. Both parents need to build up a complete NI record, as the new flat-rate state pension is not paid based on a spouse's NI contributions.

The claim also creates a dormant NI record for the child: at the age of fifteen years and nine months, they are allocated an NI number. Where child benefit hasn't been claimed, the individual needs to apply for an NI number before they can work, open an ISA or receive a student loan.

To avoid these difficulties, the child benefit should be claimed as soon as possible after the child's birth. Where the parent expects that the benefit will be clawed-back as a tax charge, they should tick a box on the claim form to receive a nil payment. They can reverse this at any time; however, a benefit claim can only be back-dated for up to three months.

Paying the ATED charge

Where a company owns, or partly owns, residential property worth £500,000 or more, it must pay the Annual Tax on Enveloped Dwellings (ATED) charge each year in April or apply for relief from that charge.

The amount due for 2017-18 varies from £3,500, for properties worth up to £1m, to the maximum of £220,350, for properties worth £20m or more. The ATED is payable to HMRC by 30 April each year and applies in addition to council tax charged by the local authority.

When the property is acquired during the year, the charge must be paid within 30 days of the acquisition date. For a new build, the company has 90 days to pay from the date the local council issues a completion notice.

Properties which are commercially let, held for development, used by a charity or used to house employees may all qualify for an exemption or relief from ATED. In those cases, the company must submit an ATED relief declaration form by 30 April. Late forms will trigger penalties.

HMRC can easily check which companies own residential properties by searching the Land Registry.

How to deregister for VAT

It's good practice to step back and review your business at least once a year. Ask yourself where you expect your sales to come from in the next twelve months. If your projected annual turnover is less than £81,000 (excluding VAT), you may want to consider cancelling your registration.

To do this, pick a date from which the deregistration will take effect, such as the last day of the month or quarter. This can't be any earlier than the day on which you apply to HMRC to deregister. You won't be able to reclaim VAT on anything you buy after the deregistration date, so it pays to plan the date carefully.

If you have ceased to trade, you can deregister from the day you stopped trading, even if that was before you told HMRC.

You can cancel your VAT registration online, or by completing a form VAT7, which needs to be signed and posted to HMRC. We can help you with this.

Claim VAT on pre-registration costs

When you register your business for VAT, you can reclaim the VAT you paid on stock or assets acquired in the four years before the date of registration, if you still hold those assets on the registration day. You can also reclaim VAT incurred on services purchased for business purposes within six months before registration.

Suppose that you bought a new van for £24,000 (including £4,000 VAT) to use in your business on 1 December 2013. You register your business for VAT on 1 March 2017 and still own the van at that date. You can reclaim the full £4,000 of VAT you paid when you bought the van, although by March 2017 the van is over three years old.

HMRC had been arguing that the VAT reclaimed on assets such as your van should be reduced to reflect the reduction in the asset's value between its purchase and the VAT registration day. This has been shown to be the wrong approach: all the VAT can be reclaimed.

If you reclaimed only a proportion of the VAT incurred on the purchase of assets acquired before becoming VAT-registered, you can amend your claim to recover the full amount, if less than four years have passed since your initial claim. It's worth checking your old receipts to see if there is additional VAT you can reclaim.

VAT flat-rate changes

Businesses who use the VAT flat-rate scheme (FRS) can't reclaim VAT on most purchases, but they can keep a small slice of the VAT they charge to customers. If the business has limited input costs, the VAT retained will more than compensate for the input VAT they can't reclaim.

From 1 April 2017, such limited cost traders who use the FRS will need to perform a few more steps before completing each VAT return.

Step 1: Work out what has been spent on goods, as opposed to services. Goods are generally anything physical, but supplies of electricity, gas and water are treated as goods. Publications received in paper form are goods, but electronic publications are services. Professional advice and subscriptions are services.

Step 2: Remove from the list of goods any capital items; expenditure on food or drink consumed by the owner or employees; and motor fuel and parts. Taxi businesses can include motoring expenses.

Step 3: Compare the allowable expenditure on goods with the total sales including VAT for the quarter. If the value of this expenditure amounts to 2% or more of sales and is at least £250, complete the VAT return using the FRS percentage for the trade sector normally used.

Step 4: Where the value of the allowable expenditure on goods is less than 2% of turnover, you must use an FRS percentage of 16.5%. This means the financial benefit of using the FRS is effectively removed.

You may want to opt out of using the FRS from 1 April 2017 and use normal VAT accounting instead. If your sales for the next twelve months are expected to be less than the deregistration threshold (currently £81,000), you may also consider deregistering from VAT. Let's discuss your options.

Marginal tax hit for Scots

The Scottish Parliament has proposed that the threshold for 40% tax will be held at £43,000 for 2017-18. In the rest of the UK, this 40% threshold will increase to £45,000 as shown in the table below.

2017-18	Scotland	Rest of UK
Personal allowance tax free	11,500	11,500
20% tax on next	31,500	33,500
40% tax applies from	£43,000	£45,000
Class 1 NIC at 12% up to	£45,000	£45,000
Class 4 NIC at 9% up to	£45,000	£45,000

The power to alter national insurance contributions has not been devolved to Scotland, so the Class 1 and Class 4 NIC thresholds won't align with the 40% income tax threshold for Scottish taxpayers in 2017-18. This will create a 52% marginal rate (40% tax + 12% NIC) for Scottish taxpayers on employment income between £43,000 and £45,000.

The Scottish income tax bands do not apply for capital gains, savings income or dividend income. This means that Scottish taxpayers will have to perform two separate tax computations to work out their entitlement to the savings allowance, the correct dividend tax rate or the capital gains tax rate. In practice those calculations should be performed by tax software.

As an employer, you need to follow HMRC's instructions to apply tax codes. The PAYE codes for Scottish taxpayers should include a prefix 'S'. Check that your tax software is using the correct tax bands for 2017-18 if your payroll includes Scottish taxpayers.

NMW traps

The national minimum wage (NMW) always increases in October, right? Wrong. This year the new rates of NMW apply from 1 April 2017. This is on top of the last compulsory pay rise for those aged under 25, which applied from 1 October 2016. The current and new hourly rates are below.

It is crucial to know which of your employees is entitled to each rate of the NMW, and from what date. All working time must be paid, including training, overtime, and queuing for security checks.

For miscalculating NMW payable, HMRC can impose a penalty of up to 200% of the underpaid amount. In addition, you must make good the unpaid wages to your worker.

Where you underpay wages by £100 or more across your workforce, HMRC can include your business on a 'name and shame' list of employers. That list doesn't explain that the underpayment was due to an innocent mistake, even if it was.

We can help you check that your NMW calculations are correct.

For pay periods starting after	25 and over	21 to 24	18 to 20	Under 18	Apprentice
1 April 2017	£7.50	£7.05	£5.60	£4.05	£3.50
1 October 2016	£7.20	£6.95	£5.55	£4.00	£3.40

Levies and charges for employers

April brings the new Apprenticeship Levy and a new Immigration Skills Charge. Both are potentially payable annually and are designed to encourage employers to train the staff they need, rather than to recruit skilled workers from abroad.

Employers with annual payroll costs of £3 million or more will have to pay HMRC an additional 0.5% of their payroll as the Apprenticeship Levy. That money will go into a digital apprenticeship fund, which the employer can access from 1 May 2017 to pay for training and assessment for new apprentices. Arrangements in Scotland, Wales and Northern Ireland may be different, as education and training is a devolved issue.

Employers who do not pay the Apprenticeship Levy will be able to use the digital apprenticeship service to choose training providers and to advertise apprenticeship vacancies.

The Immigration Skills Charge only applies where permanent skilled workers are recruited from outside the European Economic Area. It is set at £1,000 per year per worker, with exemptions for graduate trainees. This charge is payable to the Home Office, not to HMRC.