



AAT and ATT Joint Conference Autumn 2013 Sharpen your tax skills

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Remuneration strategies for employers and employees in OMBs

OMBs – general issues

- Fault line in the UK tax system makes companies more attractive than unincorporated structures in most cases
 - So general assumption here that we are talking about companies
- If starting with a sole trade or partnership, we need to consider incorporation issues such as:
 - Goodwill and amortisation for tax purposes (April 2002 rule)
 - Cars in company or not?
 - Property – hold outside or inside the company?

However.....

- Partnerships with corporate members have some appeal
- Diversion of profits to avoid 40% and possibly 45% tax
- But HMRC is attacking this structure, possible as soon as the Autumn Statement 2013
- Condoc. in the summer of 2013
- Watch this space!

Basic OMB remuneration strategies

- No salary - just dividends
 - but no contributions record for benefits
 - Maybe OK if a second business
- Low NIC/PA salary and dividend stripping – especially up to the higher rate boundary
- Reasonable salary and dividend top-ups

Basic OMB remuneration strategies - 2

- Aspects to consider include:
 - PAYE and NIC issues – especially RTI
 - Pension contributions
 - if made by company instead of remuneration may reduce HICBC
 - Student loan repayments
 - Tax credits
 - Possible HMRC challenges?

Example - Gill

- Gill has her own small company
- What is her net disposable income if she:
 - 1 Pays herself £7,500 salary and £12,500 net dividends or
 - 2 Pays herself £20,000 salary?

Gill – option 1

	£
Salary	7,500
Dividend $\text{£}12,500 \times 10/9$	<u>13,889</u>
	21,389
PA (2013/14)	<u>(9,440)</u>
Taxable income	<u>11,949</u>
At 10%	1,195
Tax credit (restricted)	<u>(1,195)</u>
	<u>nil</u>

Gill – option 1

	£
Salary	7,500
Dividend	<u>12,500</u>
	20,000
Tax payable	nil
NIC – payable	<u>nil</u>
Spendable income	<u>20,000</u>
 Cost to company	
Salary – less CT at 20%	6,000
Dividend	<u>12,500</u>
	<u>18,500</u>

Gill – option 2

	£
Salary	20,000
PA	(9,440)
Taxable income	<u>10,560</u>
At 20%	2,112
NIC (20,000 – 7,755) x 12%	<u>1,469</u>
	<u>3,581</u>
Net receipt (20,000 – 3,581)	<u>16,419</u>
Cost to company	
Salary	20,000
NIC (20,000 – 7,696) x 13.8%	1,698
CT relief at 20%	(4,340)
	<u>17,358</u>

Gill - summary

	Option 1	Option 2
Net spendable income	20,000	16,419
Cost to company	18,500	17,358

Are pensions a good investment?

- George is 55 and has his own company
- He is thinking of investing in a pension plan after a long absence from pension saving
- His current personal pension pot is £65k and he hopes to semi-retire at 60
- ISA or pension?
- Company contribute?
- Consider two scenarios: BR and HR taxpayer

George – Issues 1

- ROI on cash ISAs low
 - may be better with shares in current climate
 - funds in an ISA can be accessed if needed
 - funding children's education
 - assistance with kids' mortgage
 - paying for holidays
- 20/40/45% tax relief on pension contributions providing <£50,000 gross (plus unused b/f)
 - company should make contributions to save NIC cost of remuneration (same max applies) to George to allow him to make contributions
 - company tax relief only when contributions paid

George – Issues 2

- Pension contributions exempt benefit if company pays
 - but cannot be accessed until retirement
 - value may not be fully recovered if die ‘early’
 - cannot be passed to next generation on death – but possible survivor’s pension
 - remember contributions to fund for children treated as earnings for tax and NIC from 2013/14
- Low annuity rates mean funds buy ‘small’ pension
 - probably use income drawdown to see if annuity rates improve

Example - Simon

- Simon contributes £240 per month to his personal pension
- He has income for 2013/14 of £55,000
- He is married with two children, and his wife earns £20,000 pa
- What is the value to them of increasing the pension contributions?

Simon 2

Current position		£
Child benefit – 2 children		1,752
Income for HICBC	55,000	
Less: pension 12 x 240 x 100/80	(3,600)	
	<u>51,400</u>	
Restriction 1% for every £100 >£50,000	14%	(245)
		<u>1,507</u>
Additional contributions – say £80pm		
12 x £80 x 100/80	£1,200	
Reinstates 12% of HICBC		210
Tax relief on contributions	£1,200 x 40%	<u>480</u>
		<u>690</u>
Effective saving	690/1,200 x 100	57.5%

Employing family members

- Fine if properly structured
 - and they actually do the work
- Good use of their personal allowances and BR band
- Spousal remuneration – is there a right salary?
- Spousal and other family dividends (Arctic Systems logic)?
 - important to consider rights attaching to shares
 - votes, dividend and net assets on winding-up

The impact of recent case law

- Are dividends still safe?
- PA Holdings Ltd – turning employees into shareholders
- HMRC challenge – PA ultimately lose
 - because ‘scheme’ was totally artificial
 - shares issued, dividend paid, shares cancelled
- But HMRC does not appear to be applying the case to the wider OMB population
- What about ‘alphabet shares’?

Other dividend issues

- Distributable profits – and proof of consideration
- Frequency of payments – monthly too frequent?
- Voting a dividend quarterly – could be to the DLA, then drawdown
 - interim (directors) v final (shareholders)
- Killing the DLA with a dividend
- Right paperwork

Case study- Alphabet shares

- Gerry and Frances started a small manufacturing business in the 1980s. Despite the ups and downs in the economy, it has quietly thrived.
- They have adult children, a son and a daughter, who are employed in the company and 5 employees.
- They want to make their children shareholders, but to be able to pay dividends to them differentially (Gerry and Frances are quite comfortable and the children have minor children of their own).
- Will this work?

Directors' Loan Accounts and current accounts

DLAs and DCAs

- The terms are sometimes used interchangeably
- Does it matter?
- Here for our analysis, we use DCA for a day-to-day account to deal with personal expenses that are intended to be cleared with a dividend, or an account to vote remuneration into
- DLA is used for a proper loan – one way or the other

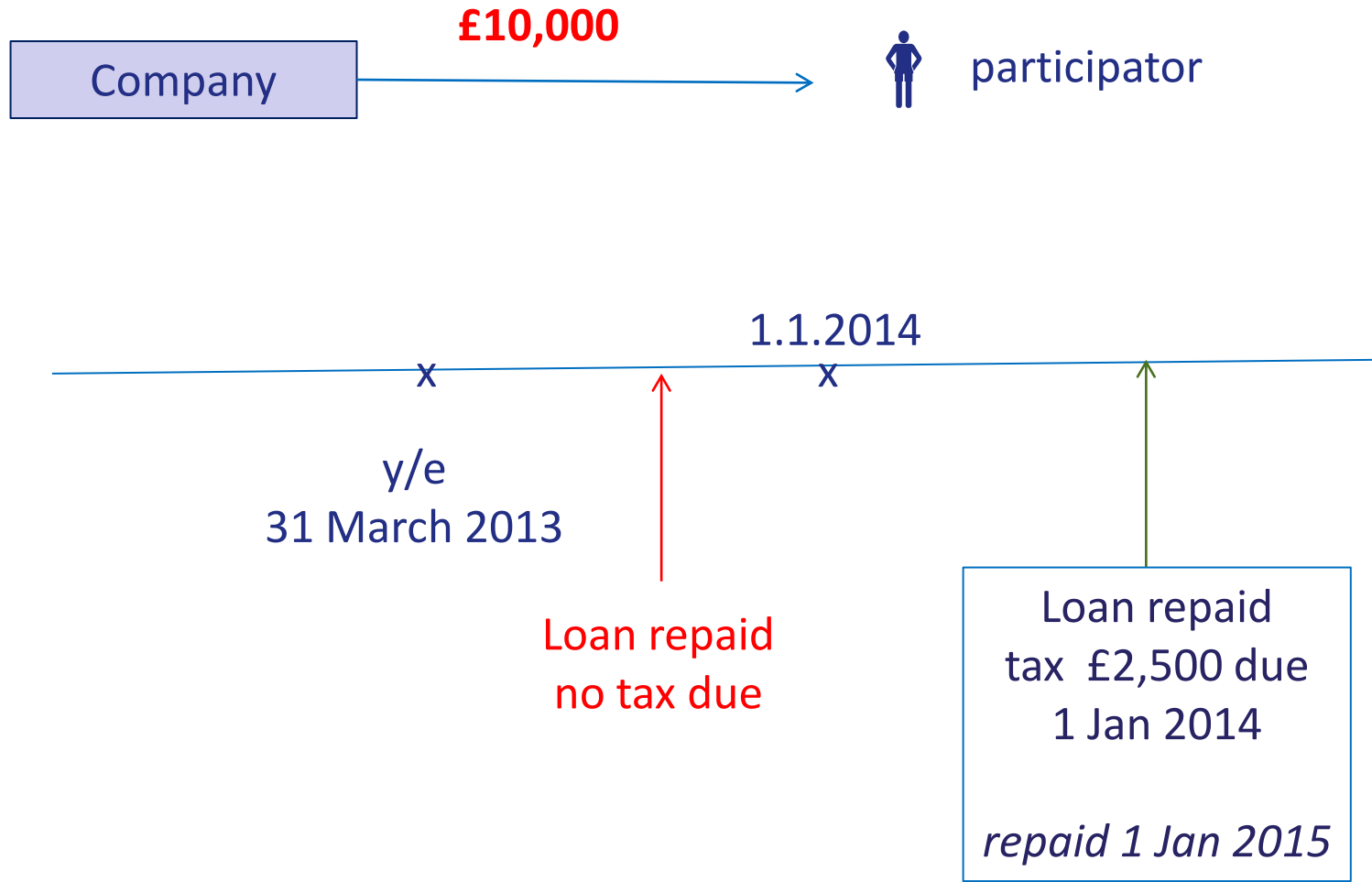
HMRC's view...

- “A director's loan account can include:
- Cash payments other than your salary or dividend
- Expenses that you may have paid for using company funds that are actually for personal use
- Money withdrawn for your personal use - for example, to renovate your home, pay school fees or personal Income Tax”
- So, interchangeable!

Loans by close coy to participators

- S455 CTA 2010 charge applies unless individual
 - owns <5% of shares, and
 - works full time for company, and
 - loan <£15,000
- or loan made in normal course of lending as part of business of company

Loans to participators – s455 charge



Loans to participators - 2

- Partial repayment triggers proportionate reclaim for coy
- Loan w/off - company recovers outstanding s455 tax
 - but no CT deduction for amount w/off
- Individual liable to IT on amount written off
 - taxed as distribution
- No IT/NIC for w/off on death of shareholder
- Don't forget BLK if interest free and n/e £5,000
 - increasing to £10,000 next year

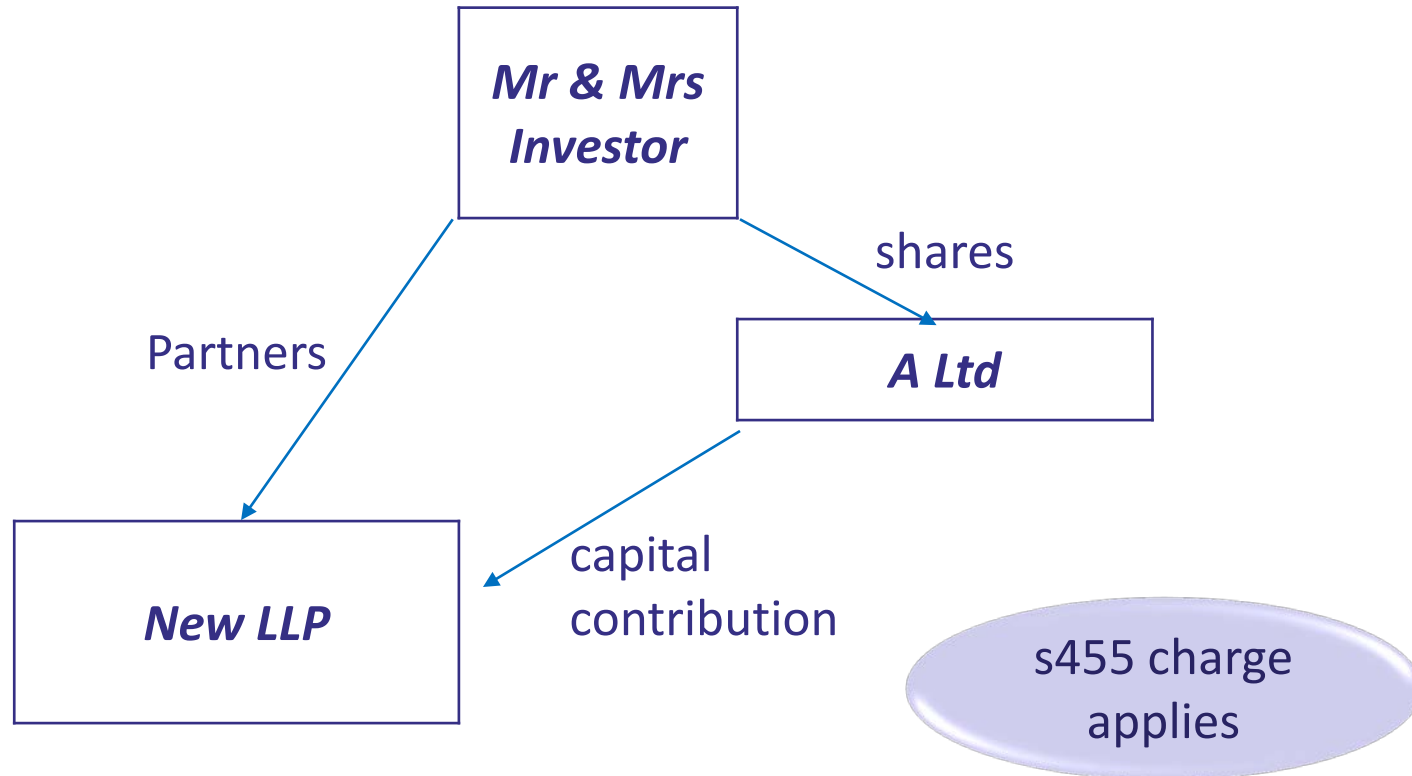
FA 2013 – bed and breakfasting rules

- New provisions (the “30 day rule”) have been introduced into CTA 2010 which deny the relief;
- if within a 30 day period repayments of more than £5,000 are made to the close company and amounts are then redrawn either through a loan or advance of money from the close

FA 2013 - Loans to participants

1. Loan made to someone other than individual participant will create s455 charge if individual is ultimate beneficiary
 - e.g. company makes loan to p'ship of which participant is partner
2. Loans to trusts where trustees own shares brought within s455 and shareholder can benefit

Loans – new rules – situation 1



FA 2013 - Loans to participators

3. 'Arrangement' that is not loan

- participator forms partnership with co and profits allocated to co
 - co does not draw profits and participator draws funds from p'ship
- Difference between this and (1)
- (3) only applies if funds are drawn from p'ship
- (1) charge applies irrespective of whether funds are drawn

Directors' current accounts

- Credited with salary
 - each debit when overdrawn should be subject to PAYE/NIC
 - balance of credit when made then taxable when salary voted
 - further debits not taxable until overdrawn again
- RTI issue?

Directors' current accounts

- Credited with dividend
 - no IT/NIC on debits
 - s455 charge if overdrawn 9m after y/e – so becomes a loan
- Loan w/off taxed in individual as distribution for IT
- NIC?
 - earnings = Class 1
 - dividend – no NIC
- *Stewart Fraser Ltd v HMRC [2011] UKFTT 46 (TC)*

Directors' expenses

- Any not W,E & N incurred debited to current account
- HMRC contend advance of salary
 - ∴ PAYE/Class 1 NIC
- Importance of documentation
 - current account to be cleared by dividend or reimbursement by director
- No automatic aggregation of accounts
 - same director
 - husband and wife

Putting your children through university

- Are there any tricks?
- Employ them in the holidays?
 - must be reasonable salary for work done
 - NMW/ child protection issues
 - and the Slavery Act if <14?
- Give them a new low emissions car
 - taxed as second car for parent
- Possible scholarship – unlikely to succeed unless part of larger scheme

S Kutcha v HMRC

- Company paid scholarships to sons of main director/shareholder
 - took CT deduction
 - no tax for director
- Scheme did not fall within s212 ITEPA 2003
 - therefore treated as earnings of director
 - tax and Class 1 NIC applied

Putting your children through university

- Even make them a shareholder?
 - issues if <18
 - also lose part of value of company as you won't get it back when they have finished
- Also Companies House rules
- What about living accommodation?

University accommodation

- Buy property and let them live their
 - to achieve PPR exemption they must own property so gift it – no gain as only just acquired BUT
 - will you get anything back after 3 years?
- Buy property and gift to trust – minimal gain so no cgt issue
 - or gift cash to trust to buy property
 - will need to be <£325,000 (+£6,000?) for IHT as RPT
 - child lives in property
 - may have other tenants – trust liable to IT on rent less expenses

University accommodation

- Buy property and gift to trust
 - trustees sell at end of 3 years
 - CGT exemption as PPR of beneficiary
- funds returned to parent <first 10 years with no IHT if trust created within nil band

Marcia Willett Ltd

- Benefits provided for directors over a number of years (2002 – 2007)
 - made good through current account in May 2008
- HMRC argued Class 1A due as no equivalent of ‘making good’
- Tribunal – no benefit – no Class 1A
- NB: Need to make good tax on readily convertible assets and restricted shares within 90 days to avoid charge

Cars

- Baseline being reduced for 2013/14 and later
- Electric cars
 - Currently appear attractive with low benefit
 - when 0% abolished in 2015/16 will be taxed at 13% of list price
 - also note list price £5,000 higher than purchase price due to Government subsidy
- List price – exclude cost of special security measures where relate to employment

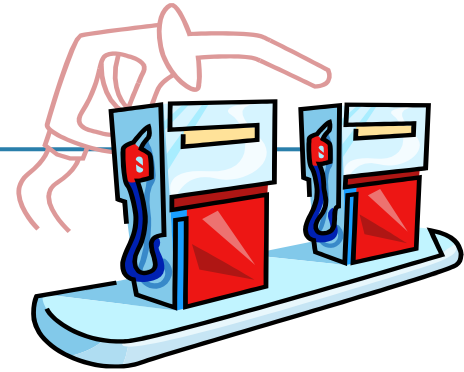
Impact of Changes

CO ₂ emissions Petrol	2012/13 %	2013/14 %	2014/15 %	2015/16 %	2016/17* %
0	0	0	0	13	15
1-75	5	5	5	14	16
76 – 94	10	10	11	15	17
95 – 99	10	11	12	16	18
100 – 104	11	12	13	17	19
Max	35%	35%	35%	37%	37%

*Diesel = + 3% - abolished from 2016/17

Fuel for private mileage

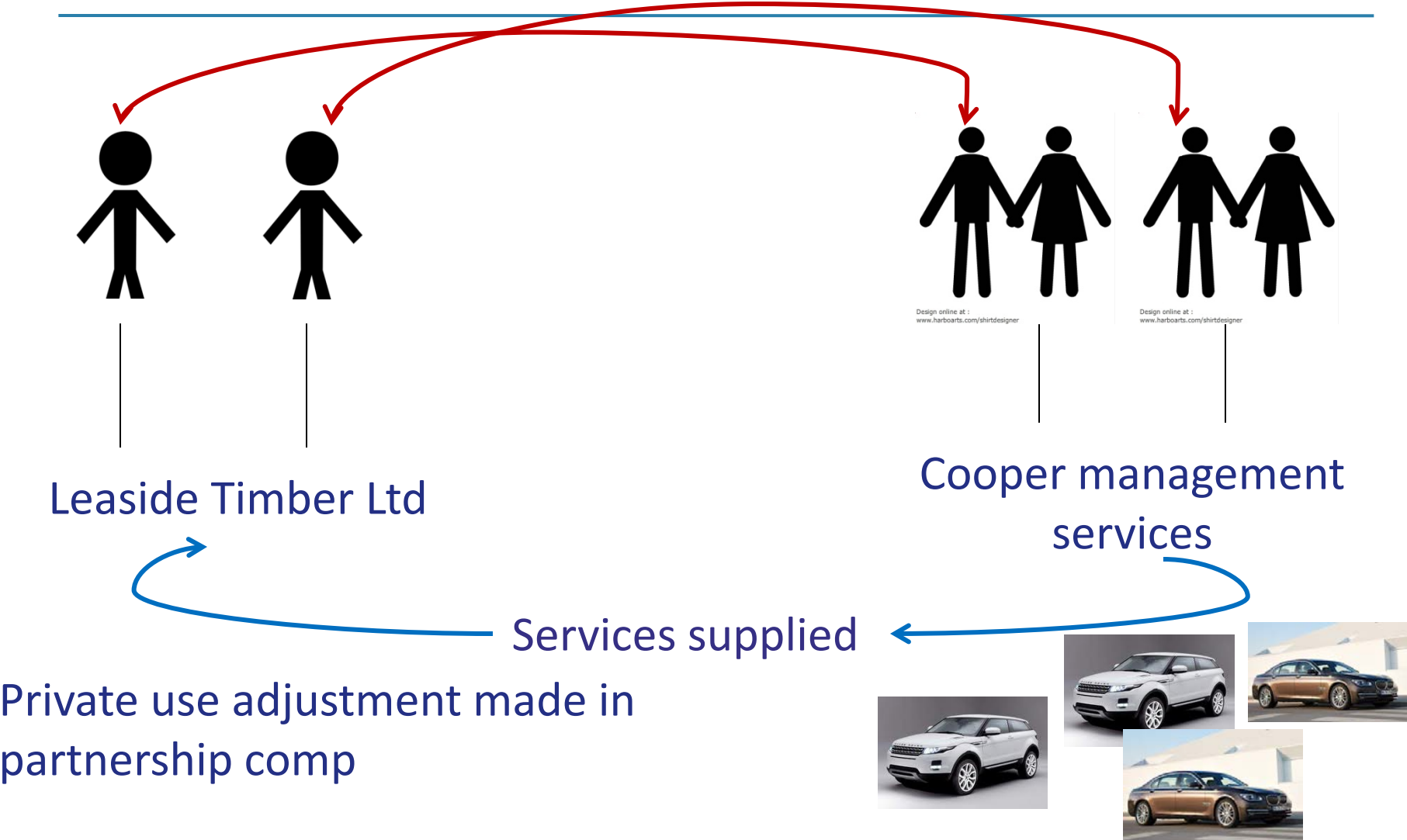
- Taxed on $\% \times £20,200$ 2012/13
 - increased to £21,100 for 2013/14
 - future increases 2% above RPI in subsequent years
 - van rate for current year £564
- Electric cars – no benefit where employer provides power for employer provided car
 - if provided for employee's car benefit = cost of provision



General considerations

- Tax v non-tax issues
 - Status of having a company car
 - Administration issues for employer
 - Company leasing may be less expensive
- Tax burden v convenience and cash flow
 - cost of extracting funds to buy own car
- Better to start (and continue?) with the AMAP

Coopers & Ors (2012)



Cooper - 2

- HMRC imposed BIK charge through company
 - on directors by reason of their employment
 - plus second benefit for cars for family members
- Accepted – cars made available for private use by p'ship but
 - was it as a result of their directorship of the company?
- Taxpayers argued
 - no contractual obligation between p'ship and co
 - private use adjustment made in tax comps
 - benefit would create double charge

Cooper - 3

- HMRC
 - provided because of directorship
 - p'ship has no commercial function other than to provide services to company
 - costs of cars borne by company via management charge from p'ship
 - no other cars provided by p'ship
- Tribunal – p'ship had no commercial reason for existing other than to provide cars for company
 - no cars if weren't directors
 - benefit applied

Cooper - 4

- Now effectively taxed twice – p’ship add-back and BiK
- “if there is an element of double taxation, it arises not by reason of any discretionary powers conferred upon the Commissioners, or by reason of any ambiguity in the terms of the relevant provisions, but because the parties concerned have voluntarily chosen, upon advice, to arrange their affairs in a particular way. They have to live with the consequence of that.”

> £200K

ONLY ETT

GR Solutions Ltd (2012)

Company car

- Mr H bought a car
 - then sold 90% of it to company of which he was director/shareholder
 - he paid 10% of running costs
- argued that as it was jointly owned it cannot have been provided by reason of employment

Tribunal disagreed and benefit taxed

**Exempt benefits – fine tuning or more
fundamental?**

Exempt benefits include.....

- Pension contributions
- Liability insurance – relating to employment
- Travel home after working late
- Bicycles and safety equipment
 - no breakfasts any more
- Parking facilities at or near work
- Canteen meals – available to all employees
- Third party entertainment – not arranged by employer

More exempt benefits

- Security assets – threat caused by employment
- Sports and recreational activities – not open to public
- Redundancy and outplacement counselling
- Redundancy payments
- Phones (one per employee)
- Health care check-ups
- Some working from home payments

I phones and blackberries

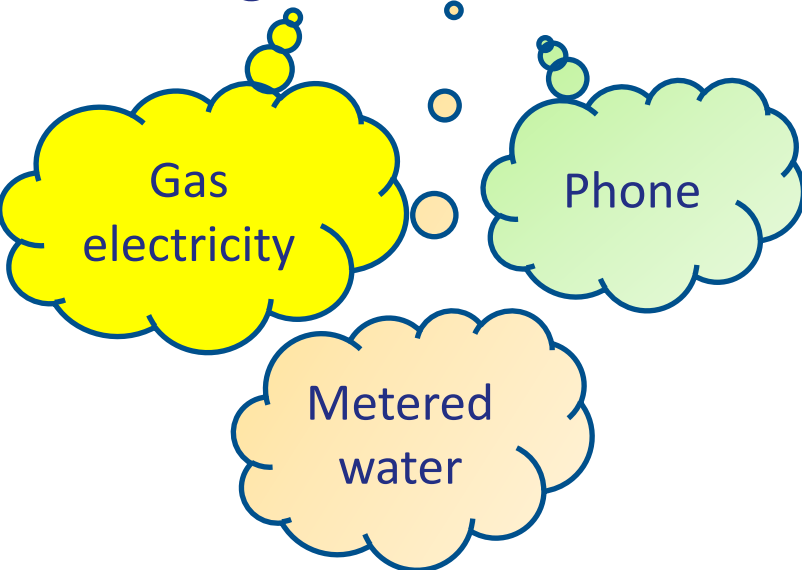
- Phones or computers?
 - HMRC original view – computers (PDA)
 - Could still exempt under s.316
 - Private use insignificant
- R&C Brief 02/12 – mobile phones
 - Ignore in 2011/12 P11D if only one
 - Possible Class 1A refund 07/08 – 10/11
- N/a to laptops / tablets



Working from home

No choice

- Substantive duties
- No employer premises reasonably available
- Marginal costs allowable



Choice

- s316A still available
- Reasonable employer contribution tax free
- £4pw from April 2012

Medical check-ups

- 2009/10 and later -allow one health check per employee per tax year
- No benefit on eye tests required by H&S legislation
 - nor glasses/contacts required as result of VDU work
 - if for general use allow element for VDU and tax remainder
 - if no special prescription for VDU use whole cost is taxable benefit
- No benefit on medical treatment arising from work related injury/disease



Business travel issues for OMBs

Business travel

- Employers can pay employees for business travel
- If not business travel should be included in payroll
- Qualifying travel
 - journey employee has to make for employment
 - not travel to and from permanent workplace = ordinary commuting nor
 - private travel

Permanent workplace

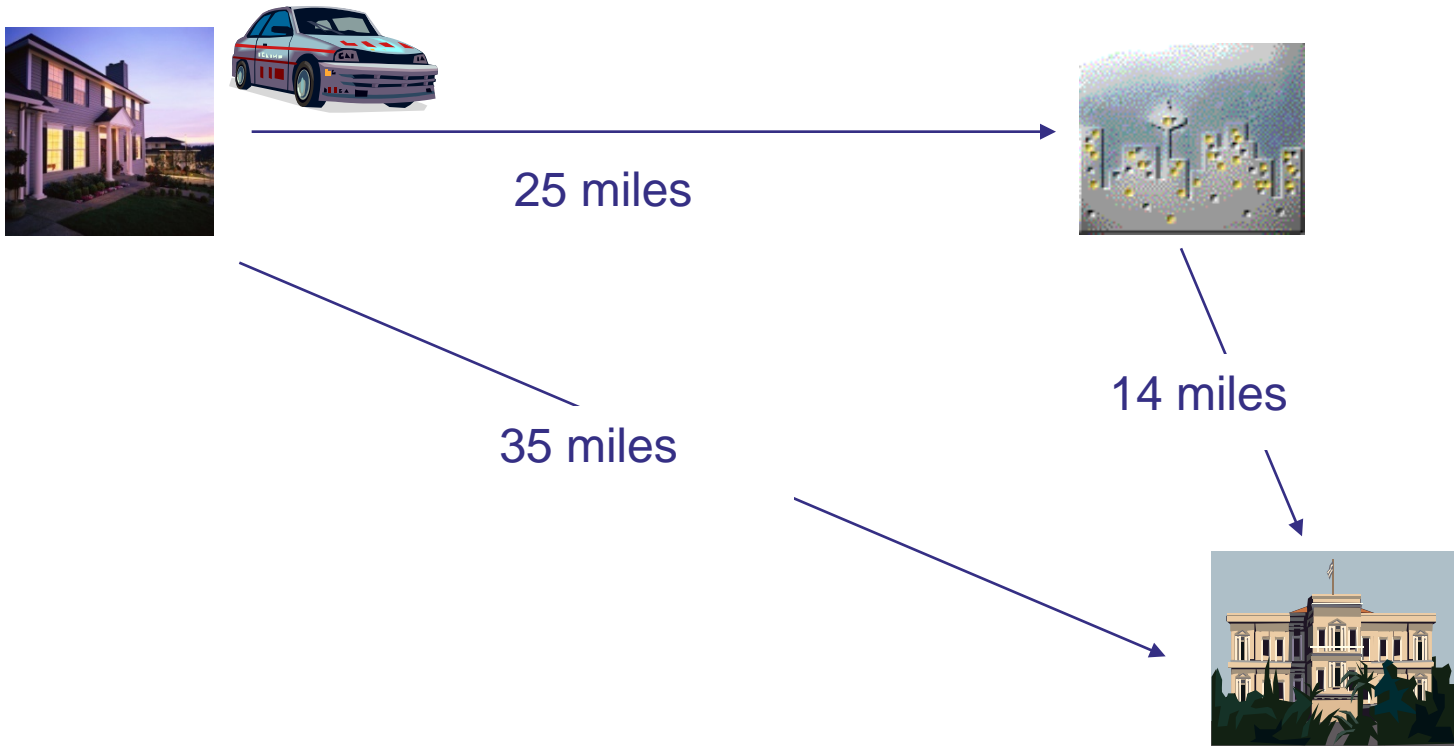
- Workplace employee regularly attends in performance of duties
 - and is not temporary
- Does not have to be all week
 - can have more than one PW
 - pattern of work
 - client and employer expectation
 - facilities available

Temporary workplace

- Place an employee attends to perform duties
 - which is not a permanent workplace
- Limited duration – 24 month rule
 - employee assigned to new workplace
 - <24m – all travel allowed
 - >24m – none allowed
 - Change of circumstances effective from date of change and not backdated
- A contract for < 24m does not make workplace temporary if travelling to same place for period of contract = permanent

Business travel

Use own car for business travel



Work at client 4 weeks

Tax position

Say employer reimburses excess over normal commuting:

$4 \times 5 \times 2 \times 10 = 400$ miles @ say 15p = £60

Allowed by HMRC:

$4 \times 5 \times 2 \times 35 = 1,400$ miles @ 45p = £630

Difference £570

If HR taxpayer, refund = £570 @ 40% = £200

More on travel

- Self-contained visits
 - task is self-contained
 - each journey will usually be treated as temporary
- Depots and bases
 - base from which work or
 - place where work allocated
 - probably permanent workplace

Geographical areas

- Geographical area treated as permanent workplace if
 - duties are defined by area
 - but not necessarily restricted to that area
 - employee attends different places in area
 - none of which are permanent workplaces
- Employee lives outside area
 - costs of getting to area are ordinary commuting and so not allowed
 - costs of travel outside area should be allowable if business travel

Travel

- Home as permanent workplace
 - must be objective requirement of duties to work from home
 - not a choice by the employee
- Site-based workers
 - Sites may be regarded as temporary workplaces
 - change in site must have substantial affect on employee's journey
 - IT consultant working for client in Square Mile?
 - or substantial affect on cost of travel

Case study - Jay

- Jay is an IT consultant with his own limited company
- He lives in Manchester
- He has a contract in London for 6 months
- He looks into the figures and deduces that it is cheaper to stay in a flat than in a hotel.
- Will he get the tax deduction for the flat expenses?

New Image Training Ltd (2012)

- Company set-up for training
 - registered office and business from home
 - operated from clients premises
 - car only used for business purposes
 - then acquired new business premises
- HMRC – taxable benefit
- Tribunal – individual had two permanent workplaces and driving between 2 not private use.
 - no taxable benefit



Case study - Paul and Mel

- Paul and Mel live in town 1. They have two shops – one in town 2 (run by Mel) and one in town 3 (run by Paul) – both of them are in a single company which is owned by them.
- They have a company Land Rover (seats in the front only) which is used to buy stock for the shops and pull trailers to various trade shows which they attend to show their wares
- Each morning they leave the house and drive to town 1 where Paul drops Mel off. He then drives to town 2 for the day. In the evening they reverse the process.
- Tax implications?

PMS International Group plc

- Fuel cards provided for all fuel
 - employees required to reimburse private fuel
- HMRC compliance check revealed errors in reimbursement
 - employees did not understand difference between private and business travel
 - no guidance provided to employees
 - policy required daily totals but only provided monthly
 - internal checking failed to pick up obvious anomalies
- Class 1A payable on benefit of private fuel

Vans – BIK rule

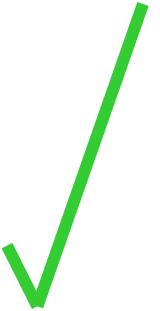
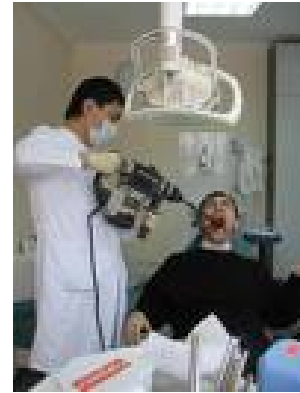
Electric vans exempt

- Van used for private purposes - £3,000
- Exempt if insignificant private use
- Reduced if not available
- £550 private fuel charge for 2012/13
 - £564 for 2013/14



Insignificant Private Use

- No benefit for normal commuting, plus
 - Infrequent trips to tip
 - Detours to newsagent
 - Calls at dentist
- Significant
 - Weekly trips to supermarket
 - Holiday
 - Social purposes out of hours



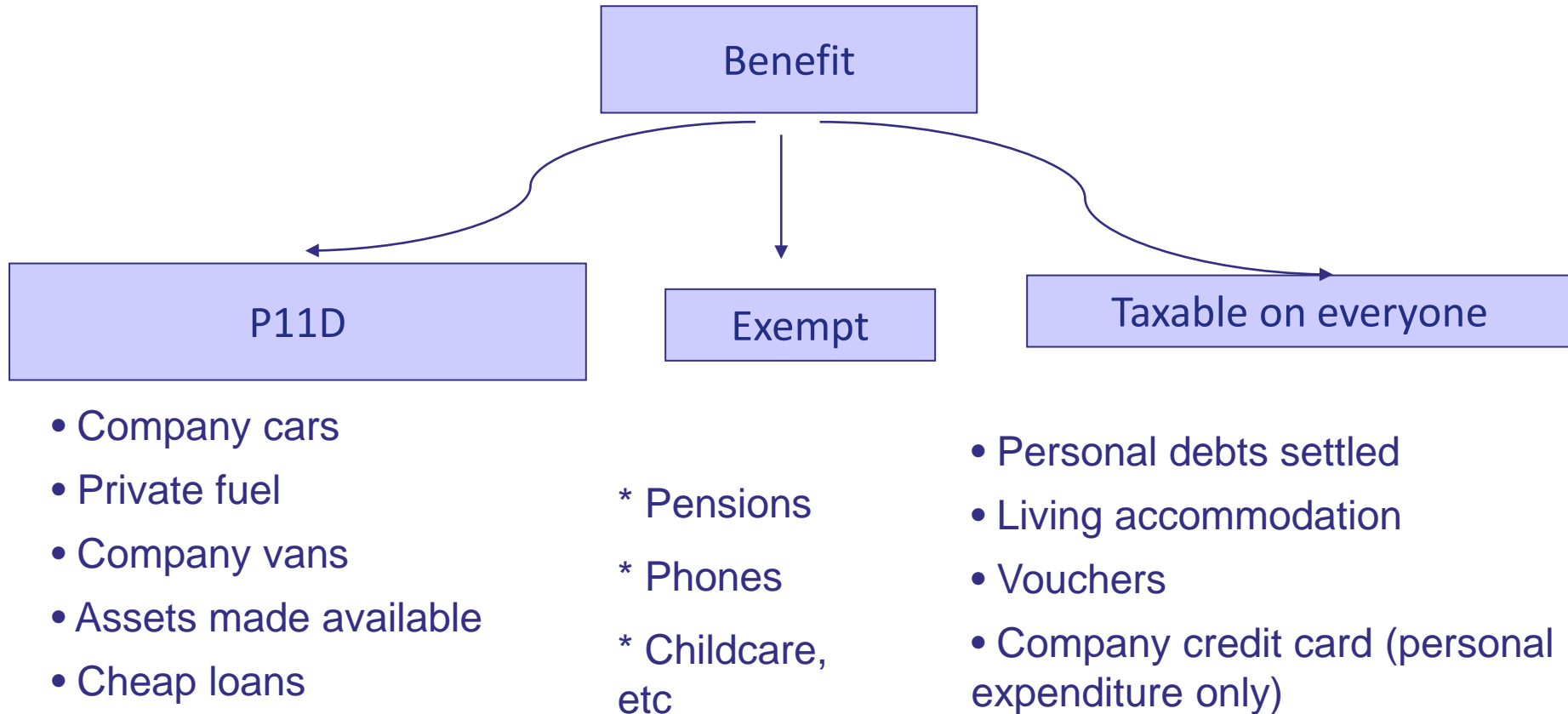
Business entertaining

- Not deductible
 - no impact on employee where employer makes tax disallowance for cost
 - section N P11D
 - expense must be reimbursed or paid from entertaining allowance
- No deduction for entertaining colleagues of different companies as not employees – treated as business entertaining
- No deduction for employees of non-resident co's as no matching disallowance for CT
 - therefore cost added to employee's income and taxable

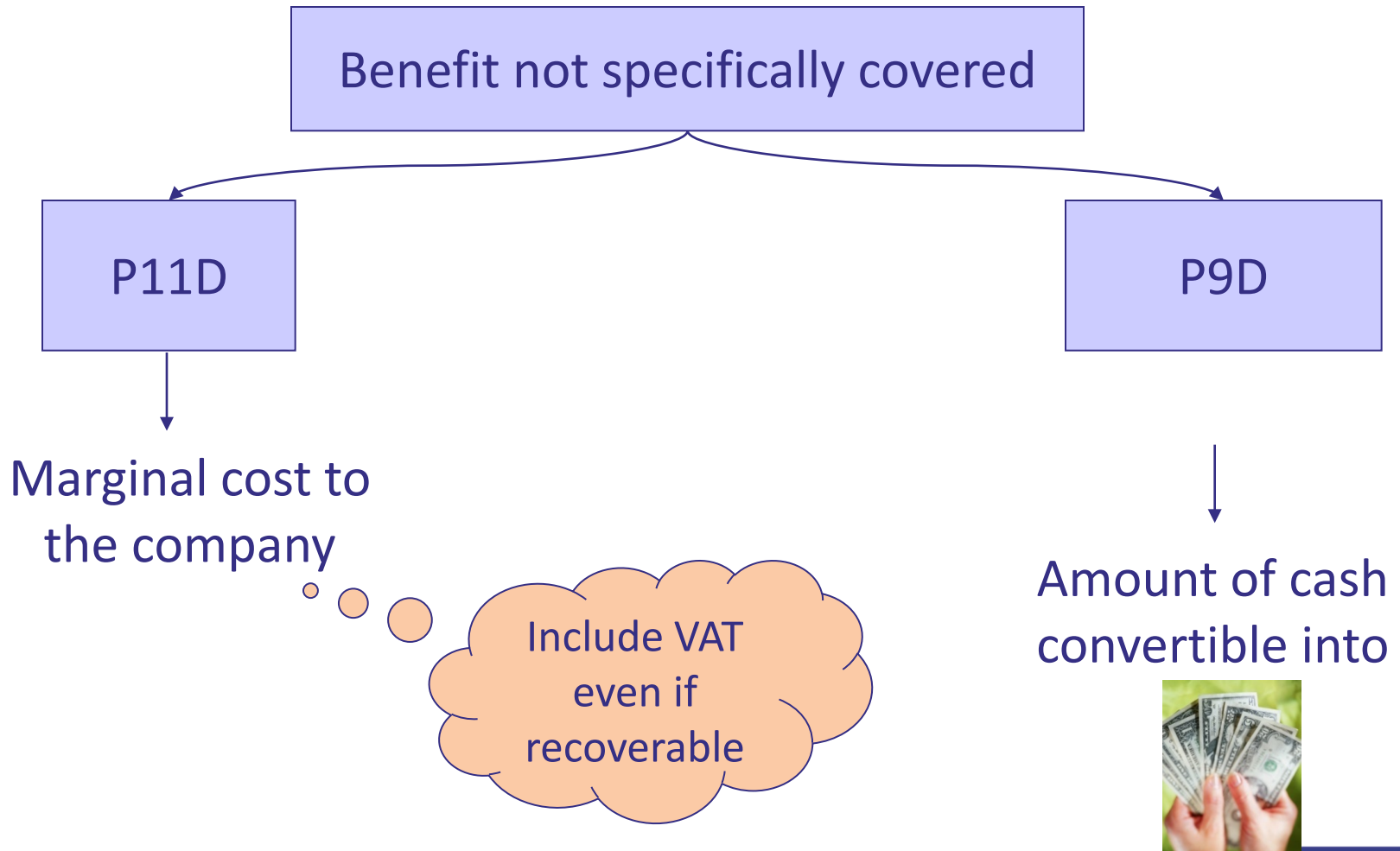
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A little something for employees?

Types of benefit



General rules



Rewarding employees – some ideas

- 1 Pension contributions
- 2 Childcare
- 3 Christmas gifts
- 4 Entertaining and the £150 rule – more than one party?
- 5 Share incentives
- 6 Using salary sacrifice

1 Pension contributions for employees

- The effect of auto-enrolment
 - watch owner/managers who have made claim for protections on earlier pension changes
- OMBs from 2016 (depends on number of employees)
- Company scheme, NEST or contribute to personal schemes?
- Good tax relief and exempt benefits
- Can the company afford it?

2 Employer supported child care

- Workplace nurseries – exempt
- Employer contracts with provider or vouchers provided
- Scheme must be open to all employees in same location
 - but can prioritise if over subscribed
- HMRC allow exclusions if NMW issue



Employer supported child care

- Employer contracts with provider or vouchers provided
 - 2010/11 – allowed £55 per week exempt benefit
 - 2011/12 and later - relief restricted to basic rate only
 - BR = £55 per week
 - HR = £28 per week
 - AR = £22 per week
 - 2013/14 - AR now 45%, so AR is £25 per week



Points on eligible employees

- Applied and accepted by 5 April 2011
 - even if no vouchers issued
- Employed by company on 6 April 2011
- Annual renewal not treated as new start
- Increasing amount available not new start
- Employees on 'gap periods' not treated as new starters
- Will be new starter even if 'old' employer provided vouchers if move employers
 - unless TUPE transfer

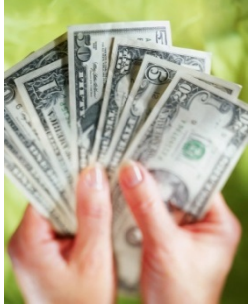
Childcare

- Earnings assessment acceptable providing best estimate at time valid for year
 - even if incorrect
- Provide $>$ max
 - direct contract with provider – P11D and Class 1A NIC
 - vouchers – P11D and Class 1 NIC
- Provide $<$ max – no claim for employee

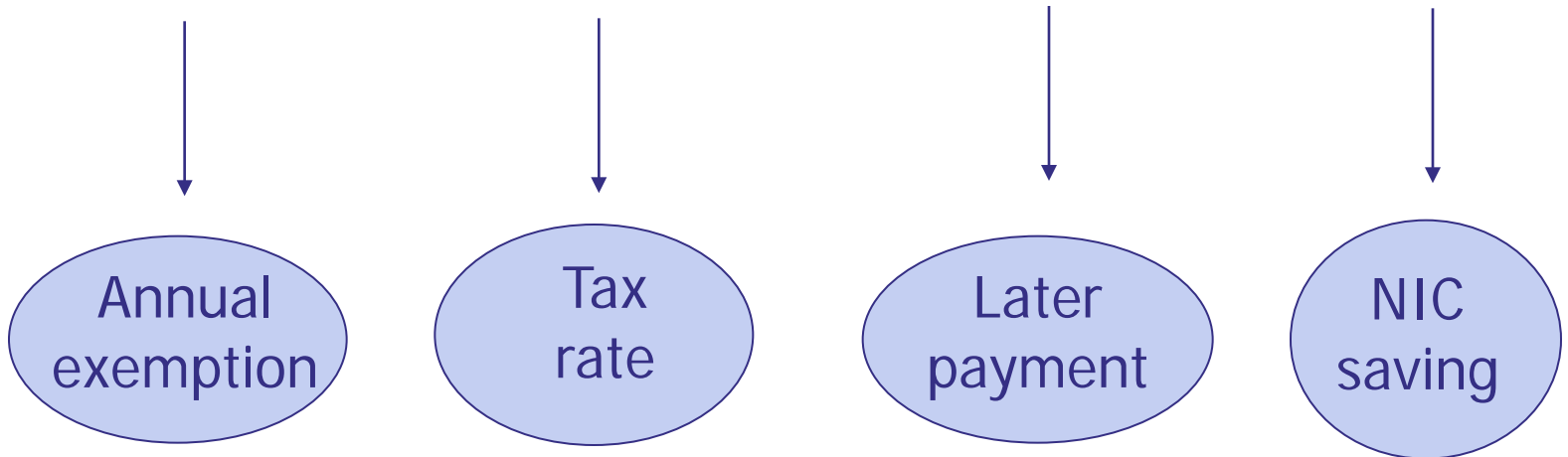
Case study - Trevor

- Trevor has his own company with 10 employees
- As it's coming up to Christmas, he wants to give them all a "Christmas box"
- He wants to take them all out for an Xmas party and they can bring their partners/spouses
- He also wants to give them a turkey, an M&S voucher for £50 and a case of wine
- He has asked you if that's OK for tax.

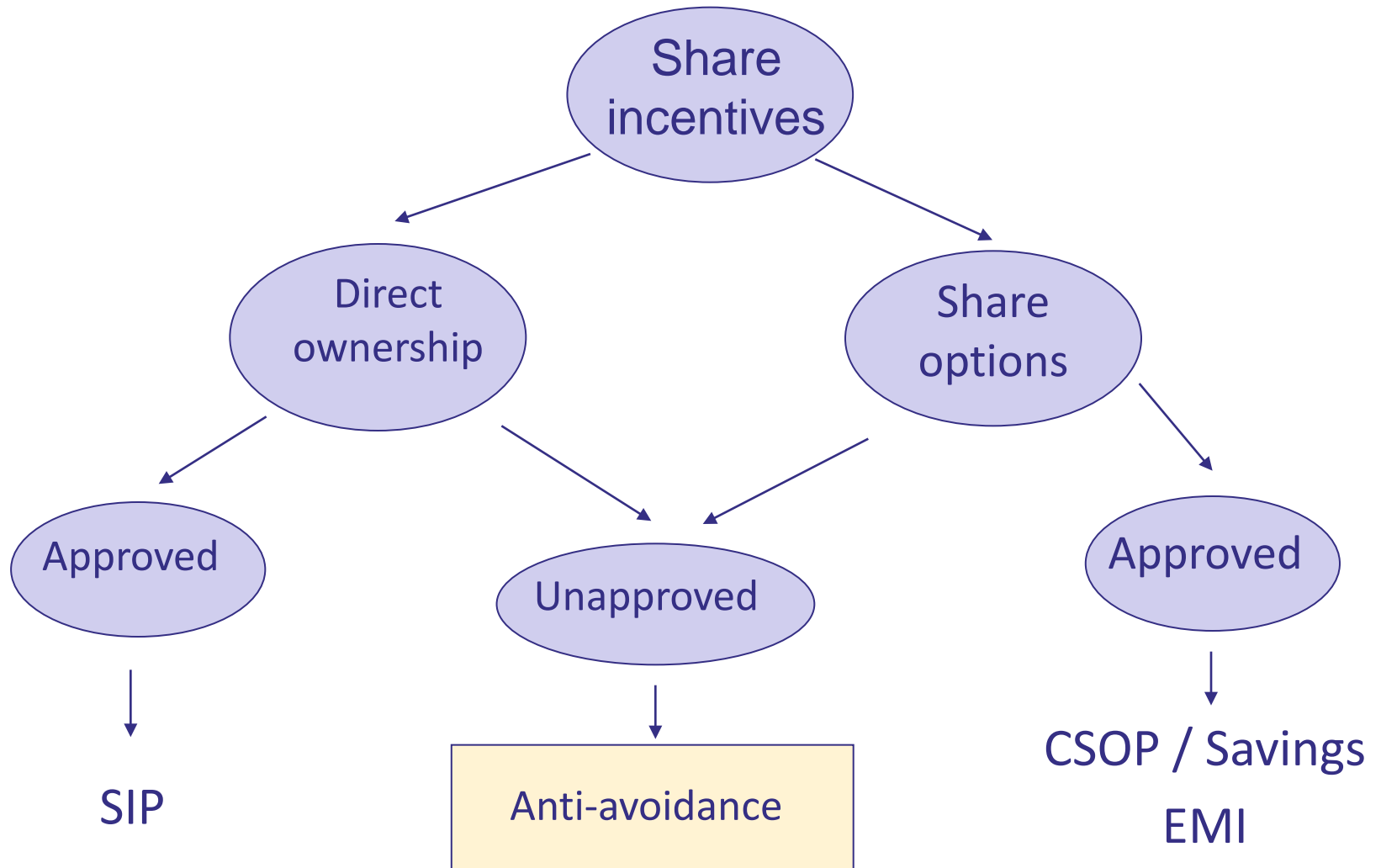
5 Share schemes



- Companies paying staff with shares
- Seeking to convert employment income into gains



Overview



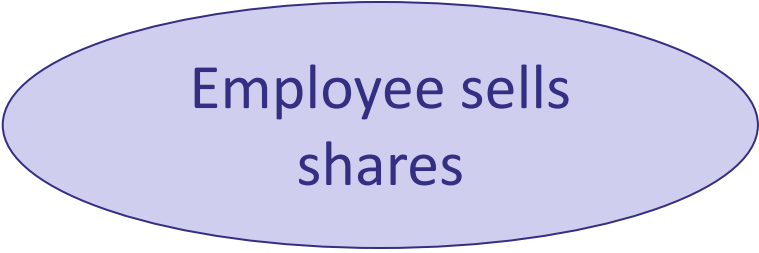
Share Option Scheme

GRANT OF OPTION

Employee given (or buys) right to buy shares at some time in the future at a price fixed now

EXERCISE OF OPTION

Employee pays company and company issues shares



Employee sells shares

Who to if unlisted company?
How are they valued?

Tax on share option scheme

	APPROVED SCHEME	UNAPPROVED SCHEME
Grant of option	No income tax	Usually no IT
Exercise of option	No income tax	IT on difference between current mv and price paid*
Sale of shares	CGT Annual exemption £10,900 Balance at 18% or 28%	CGT on further growth in shares since exercise *Profit on exercise liable to class 1 NIC

Example - Tax on share option scheme

Fred was granted the right to buy 10,000 shares at £10 each, in May 2008, when their market value was £10 per share.

He exercised the option in May 2013 when they were worth £15 per share.

He sold them in September 2013 for £17 per share.

Example - Tax on share option scheme

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	APPROVED SCHEME	UNAPPROVED SCHEME
Grant of option	No tax	No tax

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	APPROVED SCHEME	UNAPPROVED SCHEME
Grant of option	No tax	No tax
Exercise of option	No income tax	IT on $(10,000 \times (15 - 10))$ $\text{£}50,000 \times 40\%$ $=\text{£}20,000$

Example - Tax on share option scheme

Fred was granted the right to buy 10,000 shares at £10 each, in May 2008, when their market value was £10 per share. He exercised the option in May 2013 when they were worth £15 per share. He sold them in Sept. 2013 for £17 per share.

	APPROVED SCHEME	UNAPPROVED SCHEME
Grant of option	No tax	No tax
Exercise of option	No income tax	IT on $(10,000 \times (15 - 10))$ $£50,000 \times 40\%$ $=£20,000$
Sale of shares	Gain $10,000 \times (17 - 10)$ $£70,000$ $(70,000 - 10,900) \times 28\% = £16,548$	

Example - Tax on share option scheme

	APPROVED SCHEME	UNAPPROVED SCHEME
Grant of option	No tax	No tax
Exercise of option	No income tax	IT on £50,000 10,000 x £5 (15 – 10) per share & Class 1 or 1A NIC
Sale of shares	Gain 10,000 x (17 – 10) £70,000 (70,000 – 10,900) x 28% £16,548	Gain 10,000 x (17 – 15) £20,000 (20,000 – 10,900) x 28% £2,548

Approved Share Option Schemes

- CSOP
 - max £30,000 options
 - To employees and / or full time directors
 - Probably not suitable for OMB as want to reward 'key' employees
- EMI
 - max £250,000 per employee
 - £3m for company
 - can be selective
 - much more restrictive on which companies can have EMI schemes
 - lots of excluded businesses

EMI and CGT

- ‘Profit’ charged to CGT – will Entrepreneurs’ Relief apply?
- Normal rules
 - for 12m before disposal
 - since April 2012 shares treated as owned when option granted (previously from exercise)
 - individual must work for company as officer or employee
 - company must be trading company
 - individual must own 5% of shares
 - options since April 2012 5% limit removed for EMI shares only
- Conclusion – newer options likely to attract ER

6 Salary sacrifice

- Employee gives up 'cash' salary in exchange for benefit
 - Must be done before benefit received
 - Contract must be amended – again before benefit provided
 - Employee does not have the right to give up benefits for salary
 - unless due to 'lifestyle change'
 - not recognised for pension restrictions and workplace canteens
- VAT adjustment may be required by employer

Salary sacrifice

- Need to consider impact on tax credits
 - especially if for child care vouchers
 - credits restricted based on income
 - element of tax credit given for childcare costs
- Also consider impact on High Income Child Benefit Charge
 - earning >£50,000 (individual or spouse/partner)
 - lose 1% for every £100 earnings over limit
 - earnings = income less gift aid and pension contributions (both gross)

VAT and salary sacrifice

- ECJ ruling in AstraZeneca
- Salary sacrifice is consideration for what is received
 - therefore should account for output tax on value
- HMRC – extends to where cost met by deduction from payroll instead of sacrifice
- New rules effective from 1 Jan 2012 include
 - cycle to work
 - face value vouchers
 - some food/catering
- Not child care vouchers/cars

Holding commercial property personally or in SIPP

Entrepreneurs' relief

Fred's
commercial
property

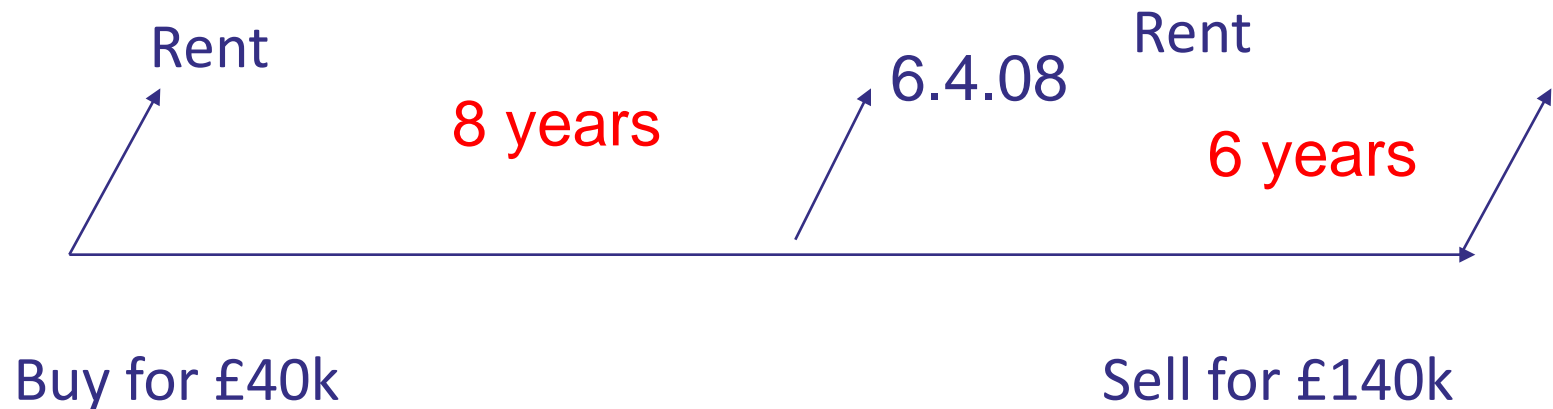
Rent?



Fred Ltd



Entrepreneurs' relief (ER)



Gain needs to be apportioned!

8/14 qualifies for ER – 6/14 does NOT qualify!

If stopped charging rent 6
April 2008 whole gain will
qualify for ER

Case study - Bert

- Bert currently operates as a sole trader but has been persuaded to incorporate the business.
- The business owns a freehold property used as the main office/warehouse which is expected to increase in value over the next few years
- Should the property be transferred to the company or retained by Bert?
 - if he retains it should rent be charged?

Buying property through SIPP

- SIPP can be used to be commercial freehold or leasehold
 - not residential property
- Property outside company ownership if liquidated
- Either transfer existing property to fund
 - or make cash contributions to allow SIPP to buy
 - if buying from 'connected' person must be at mv
 - if property owned by company contribution will be CT deductible

Buying property through SIPP - 2

- Element of borrowing by SIPP allowed (up to 50% of value)
 - but will need qualified advice
- Company pays rent to SIPP
 - no tax in SIPP and CT deductible for company
- Possible problems
 - more than one PF member
 - annual allowance charge
 - lifetime allowance charge
 - no access to funds until trigger 'retirement' options

Getting tax efficiencies out of property investment



What's the best way of holding property?

- Better in a company?
- CT rate 20% - IT 20/40/45% - may depend on number of properties
- But double tax effect
- No CGT AE if held through company
- LLPs?
- Implications?

Income tax issues

- Core principles:
- Income from a UK property business
- Income from an overseas property business
- ITTOIA 2005.



Income tax issues

- Both of these “property boxes” are separate
- All profits and losses within the boxes must be aggregated
- Losses from one cannot be put against the other
- They can only be carried forward against future losses from the same “box”.

A person's UK property business

- Arising basis (ie accruals) – not cash (officially)!
- Deductions:
 - Wholly and exclusively and
 - Not capital
- Non-resident landlords scheme

Strategies for property

1 Gifting property

2 Making the most of the PPR

3 Buy-to-let properties

4 Furnished holiday lets

5 Borrowing against equity

6 SDLT considerations.



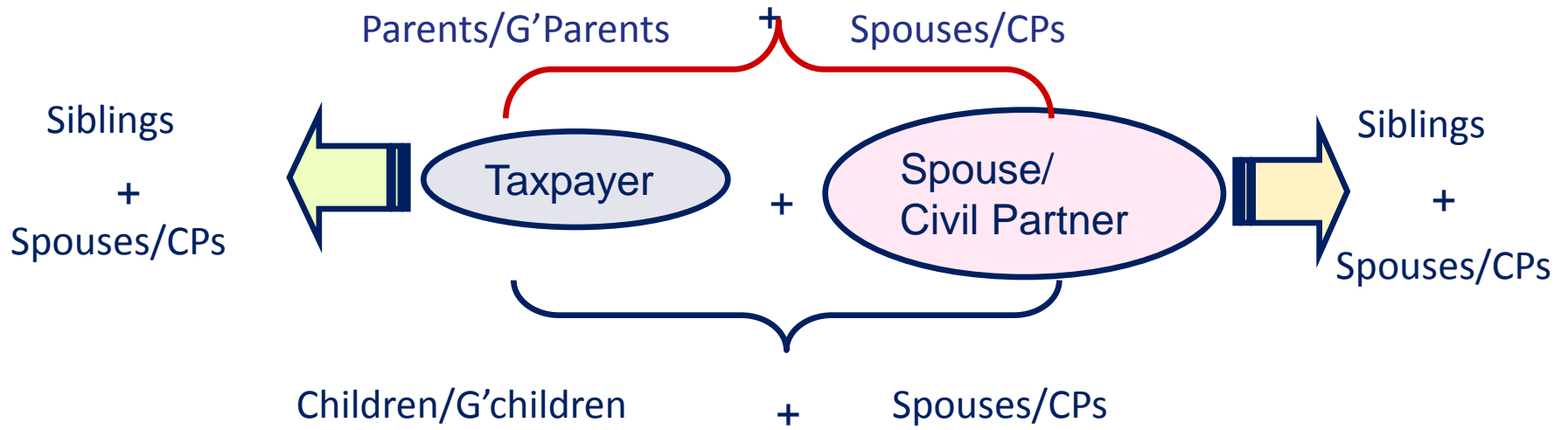
1 Making gifts in a tax efficient way - CGT

- Consider a gift to a family member:
 - Spousal gifts covered by both a CGT and an IHT exemption
- Gifts to family members not covered by such exemptions – so chargeable to CGT under the basic rules
- Holdover relief may be available if
 - business asset (s165 TCGA 1992) – FHL
 - asset transferred to trust (s260 TCGA 1992) any property

Spousal/CP gifts

- Remember, you can't split the income and the capital
- If say a property in one name is transferred from 100:0 to say 50:50, then both the income entitlement and the capital entitlement passes
- (Form 17 procedure)

Connected persons



ALSO:

- Business partners + spouses
- Company = connected to persons controlling it

- Proceeds = MV
- 'Ring fence' losses

What about the IHT angles?

- An outright gift from an individual to another individual is a PET
- So no immediate IHT charge and none ever, if the donor survives 7 years from the gift
- If donor dies within 7 years, then tax liability falls on the donee of the gift
- Taper relief may be available (donor must have survived at least 3 years).

Case study - Ghazanfar

- Ghazanfar has a buy to let property which he bought some years ago for £50,000
- It has appreciated significantly in value over this period
- It is now worth £250,000 – there is no mortgage
- He would like to give it to his son who cannot afford to get a foot on the property ladder on his own
- What tax implications should Ghazanfar be aware of?



2 Making sure we've maximised the tax benefit of the PPR



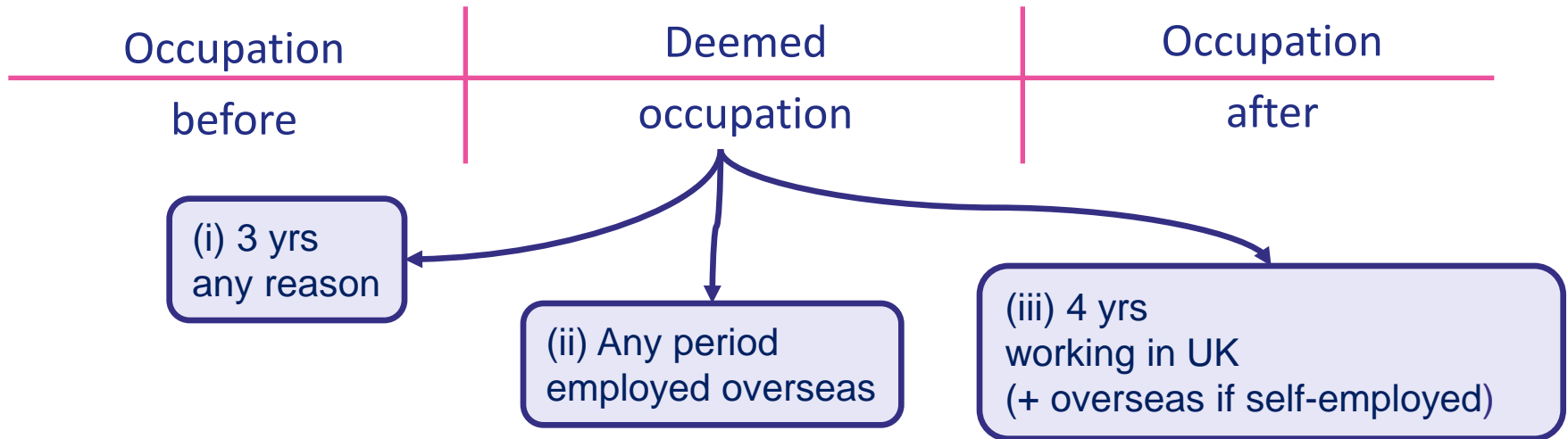
The PPR – quick review

- Exempts principal or only residences from the CGT charge on sale
- Issues include:
 - Other buildings within the curtilage
 - Absences
 - Lettings relief
 - More than one residence
 - Buy to let properties
 - Selling off the garden for building
 - Leaving a PPR to children – IHT angles

Don't forget the “deemed occupation” rules

- If I live in a PPR for any (reasonable?) period then I can have the last 3 years free of CGT
- It doesn't matter when the actual occupation is on the timeline of ownership
- Decision qualitative rather than quantitative occupation
- But there is also a second set of “deemed occupation” rules – see next slide

The deemed occupation rules - 2



No need for 'occupation after' for (ii) & (iii)
if required by terms of employment to work away from home

Don't forget Letting relief – a subsidiary relief – can be valuable!

Letting exemption

s.223(4) TCGA 1992

Lowest of:

PPR relief

Gain in let period

£40,000 (max)



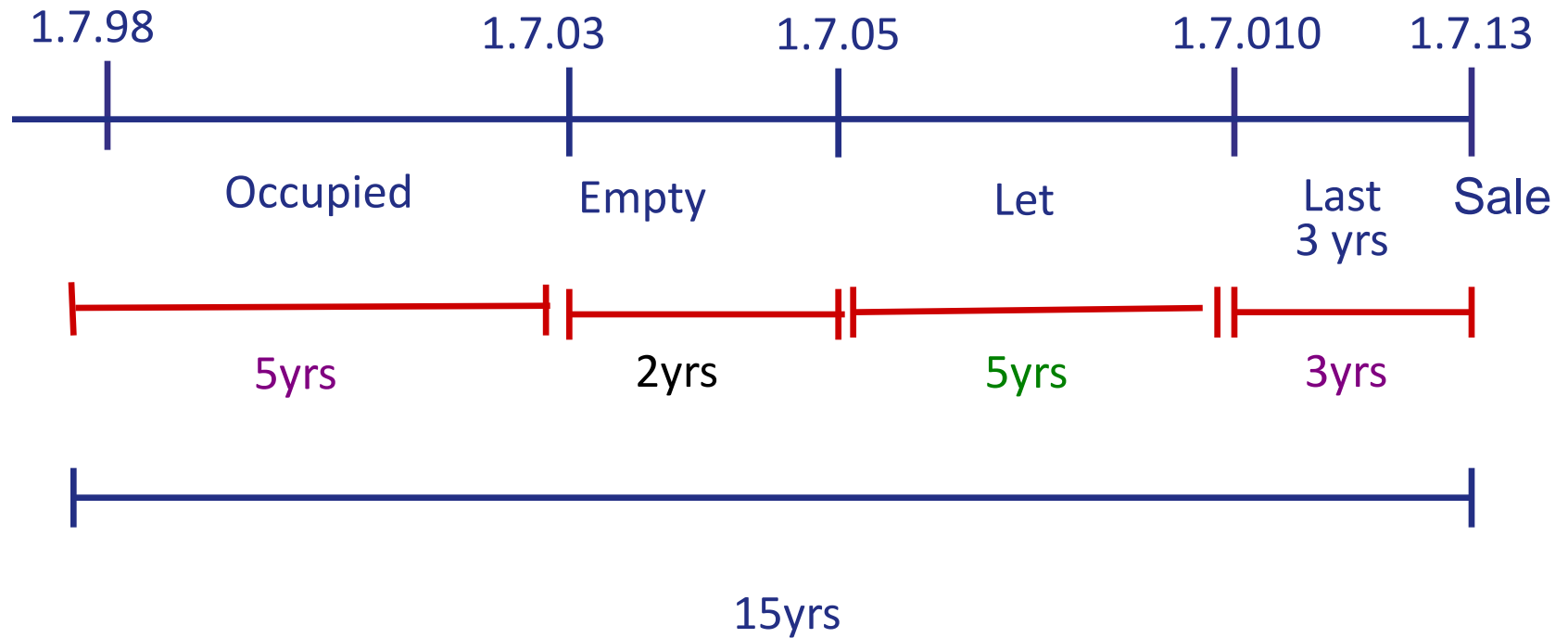
Example – Kevin

Kevin sold his house on 1 July 2013, realising a gain of £100,000. He acquired the house on 1 July 1998 and lived there until 1 July 2003 at which point he moved in with his girlfriend, living in her house.

Kevin let the property to a residential tenant from 1 July 2005 until the date of sale.

Calculate Kevin's gain after all available reliefs.

Solution – Kevin



Solution – Kevin

	£	£
Gain		100,000
Less: PPR		
8/15 x £100,000		(53,333)
Less: Letting exemption		
Lowest of: PPR claimed	<u>53,333</u>	
Gain relating to let period		
5/15 x £100,000	<u>33,333</u>	
Max	<u>40,000</u>	
		<u>(33,333)</u>
Chargeable gain		<u>13,334</u>

More than one residence



House 1



House 2

Last 36 months exempt
for **any** property that has been
PPR at any time

Consider a bounce election

Dr Amin Aghbal-Omidi (TC02841),(2013).

- Taxpayer (an experienced buy-to-let investor) purchased a property
- Got PP for a development and then sold it
- Said he'd lived in it for a short period
- Claimed PPR
- Denied by the court.

Dr Amin Aghbal-Omidi (TC02841),(2013).

- Factors taken into account by the FTT:
 - The loan on the property was taken out on the basis of the future development value
 - Information provided did not provide actual evidence that Dr Omidi lived in the property -any evidence that was available pointed to the occupation being no more than temporary
 - The property must have been marketed immediately after completion
- Dr Omidi was an experienced buy to let investor, who was well aware of the significance of a successful claim to private residence relief

Dr Amin Aghbal-Omidi (TC02841),(2013).

- HMRC referred to *Goodwin v Curtis (1998 STC 475) (CA)* which confirmed that residence denotes some degree of permanence, some degree of continuity or some expectation of continuity
- Temporary occupation at an address does not amount to residence.

Dr Amin Aghbal-Omidi (TC02841),(2013).

- Note the keyword “intention” of the taxpayer when purchasing the property
- Also, the FTT decision in *David Morgan v HMRC (2013 TC 02596)*, where the intention of the Appellant was the deciding factor rather than the quality of the occupation.

David Morgan v HMRC (2013 TC 02596),

- *David Morgan v HMRC [2013] TC 02596* a taxpayer was successful in a claim for PPR
- He lived at his property for a matter of weeks before deciding to let it out because his girlfriend had left him
- Finely balanced tribunal decision, but it shows that intention and the quality of occupation are both important.



3 Buy-to-let properties



Capital allowances for property

- Property deduction rules generally follow the trading deduction rules
 - But no CAs for domestic properties (unless FHL – see below)
- OK in respect of p&m eg ladders, mowers, vans etc.
- Options are “renewals” or “wear and tear” – changes from April 2013 – ESC B47 now gone
 - renewals basis no longer available
 - NB no W&T allowance unless fully furnished property

Can I get a deduction for.....

- Pre-letting expenses?
 - Generally not – this includes redecoration, new bathrooms, kitchens etc
- Follows the *Law Shipping* case
- BUT HMRC seem to be relaxed about properties that could have been let before work.

Landlords Energy Savings Allowance

- LESA is a tax allowance that allows you to claim up to £1,500 per property against tax
- UK and overseas properties
- Individual or corporate landlords



LESA

- You can claim LESA for what you have spent on:
 - Cavity wall and loft insulation
 - Solid wall insulation
 - Draught proofing and hot water system insulation
 - Floor insulation

Rent a room relief

- Valuable in certain circumstances
- Pensioners living alone in big houses?
- Up to £4,250 per annum, from room(s) rented in own PPR
- Does not cover buy-to-lets
- Option to be taxed on actual receipts and expenses – could be more tax-efficient
 - or excess of rent >£4,250

Spouse/life partner as a property manager

- One way of getting some money to a spouse/life partner without giving them equity is to make them a property manager;
- They do some management in return for payment;
- Allowable for tax.



4 Furnished Holiday lettings



Furnished holiday lets

- Lots of changes over the last few years
- Principally the loss of sideways relief
- Losses can only now be carried forward
- UK and EEA properties only eligible – not outside
- Useful HMRC Helpsheet 253.

Advantages of furnished holiday lets

- Plant and machinery allowances in the property
- Capital gains tax reliefs
 - Rollover relief
 - Gift relief
 - Entrepreneurs' relief
- But no IHT BPR relief unless can show it is a 'business'
- Counts as earnings for pension purposes



Furnished holiday lets (FHLs)

- Changes from April 2012:

- changing (upwards) letting days

Availability	140	→	210
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Actually let	70	→	105
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5 Borrowing against equity

- Sue and John own a house that they live in
- As part of their pension planning, they are keen to get a buy to let and wonder if they can borrow against the equity that's grown in the house over the years
- Will it be tax deductible?
- Yes, because the source of the borrowing is irrelevant it's the application that's vital.

Borrowing against equity in buy-to-lets (BTL)

- Again the source doesn't matter
- If BTL1 has grown in value, then it is possible to get tax relief to buy BTL2
- But only up to the value of BTL1 when it first entered the letting market
- It is possible to take equity out of a BTL for any purpose



6 Stamp Duty Land Tax (SDLT) considerations



New residential rates from 21 March 2012

Relevant consideration	Percentage
Not more than £125,000	0%
>£125,000, but not > £250,000	1%
>£250,000, but not more than £500,000	3%
> £500,000, but not more than £1m	4%
>£1m but not >£2m	5% (from 2011)
More than £2million	7% (new for 2012)

Note the special charge of 15% for
“enveloped properties” from 21 March 2012

Non-residential or mixed property

Relevant consideration	Percentage
Not more than £150,000	0%
>£150,000, but not > £250,000	1%
>£250,000, but not > £500,000	3%
> £500,000	4%

These rates have not changed for
some years

True love and SDLT.....

- Don't forget that love can come with a tax cost!
- Debt (transfer or assumption) is taxable
- Dave meets Sasha – they both have flats with mortgages
- They decide to move into Sasha's flat and rent Dave's flat
- Sasha's flat is worth £500,000 and she has a mortgage of £300,000.
- What are the SDLT implications of this?

True love and SDLT.....

- The SDLT implications at the time he moves in are zero
- If however, they decide in time to put Dave's name on the deeds, he in effect, is taking half of the mortgage, so there is SDLT on the assumption of half the debt
- £150,000 at 1% = £1,500
- This is the price of love.....

Property case studies

Case study - Sue

- Sue is 18 and is going to university after her gap year
- The costs of renting in Derby (where she will be studying) are around £400 per month.
- Mum and Dad have some spare cash.
- Are there any ways that they can help?

Bank of Mum and Dad

- Son Sam wants to buy a flat
- He can afford a flat for £100,000
- But a good flat costs £150,000
- He has a girlfriend that he's likely to marry, but Mum and Dad are sceptical about whether the relationship will last
- What's the best way for Mum and Dad to help with the purchase?

Case study - George

- George wants to buy an investment property in his town.
- He has seen a one-bedroom flat for £100,000. The flat is let to a good long-term tenant (through a series of ASTs) and the rent (after service charges, insurance and ground rent) is £6,000 per annum.
- George has £100,000 of cash left by his mother. He asked whether putting the money into his pension would be a better investment. He is a 40% tax-payer and is married with two children.
- Advise on the tax implications – could he do both?

General will and IHT planning – strategies for success

Why make a will?

- The alternative is intestacy - Especially important if couple not married/CP
 - Will gives certainty of disposition
 - But post death challenge may make lifetime gifting preferable if controversial distribution
 - Easier to administer estate?
 - What's the best will planning?
 - mix of lifetime gifts and legacies?
 - but difficult to know lifetime 'needs'
 - will assets be received in future allowing more to be gifted now
- Do we need to consider use of trusts?

It's not just will planning

- It's also about lifetime giving
- Get the balance right
- The earlier the lifetime gift, the more likely they will escape IHT
 - but lifetime gift may trigger CGT
- Clients sometimes don't like talking about IHT and death – it makes them feel uncomfortable

IHT - Fundamental planning

- Do not allow planning to over-ride financial security of donor or their family
- ‘Schemes’ can be expensive and are frequently blocked by HMRC
 - quite often retrospectively so cost of buying into scheme plus cost of getting out of it
- Do not overlook CGT aspects of plan
- Valid will – regularly reviewed?

Need to review will?

Death of
relatives

Position of
beneficiary

Death of
beneficiary

Change in
tax law

Birth of
g'child

Beneficiary
becomes
bankrupt

Marriage/
divorce



Illness reduces
life expectancy

Lifetime gift

- Exempt
- Potentially exempt (PET)
- Chargeable lifetime transfer (CLT)
- Gift with reservation of benefit of use (GWROB)

Exempt Transfers

- Lifetime and death
 - Between spouses/civil partners
 - From 6 April 2013 £325,000 limit to non domiciled spouse (previously £55,000)
 - can elect to be UK domiciled for IHT from 6 April 2013
 - Charities and political parties
 - For national purposes or public benefit

Lifetime exemptions

- Regular expenditure out of income
 - Pattern of giving
 - Out of income
 - Normally in cash
 - Does not damage standard of living
 - eg life assurance, covenants
- Marriage gifts

Lifetime exemptions

- Small gifts
 - <£250 per person pa
- Annual exemption:
 - £3,000 per annum
 - Unused, carry forward 1 year
 - Applied FIFO against gifts
- strictly chronological even if PET before CLT.

PETs

- Gift by individual/trustees of an IIP Trust to
 - an individual or
 - trust for the disabled
- Gifts in lifetime to trusts no longer PETs – since 22 March 2006

PETs (2)

- No immediate tax liability
- Liability if death within 7 years of gift
 - Nil rate band effective at death
 - Cumulative clock in 7 yrs to PET
 - Tax tapered if more than 3 years
 - Liability falls on donee
- Value frozen at date of PET
 - relief given for non-wasting assets if value falls by death.

Chargeable Lifetime Transfers

- Before 22 March 2006
 - Gift to trustees of Discretionary Trust
- From 22 March 2006
 - Transfers in lifetime to any trust
- NB The term Relevant Property Trust = all trusts created in lifetime plus Discretionary Trust created on death.

CLT's - 2

- Tax at lifetime rates when made
 - Nil rate band effective at time of gift
 - Cumulative clock in 7 years to gift
- Donor's liability at grossed-up rates
 - If donee pays tax on gross gift
- Recalculate liability if death within 7 years
 - Taper relief if more than 3 years
 - Credit for lifetime tax paid
 - No refund of lifetime tax

Death Estate

- Assets and income accrued to death
 - Less:
- Liabilities and reasonable funeral costs
 - Plus:
- Overseas estate
 - Plus:
- Settled property subject to life interest

Nil band and spouses

- Deaths after 8 October 2007
 - unused nil band c/f to increase nil band for surviving spouse
 - unused amount expressed as % of nil band at first death
- no limit to date of earlier death
 - problems with ED
 - problems with documentation/proof
 - HMRC suggested docs list

Example

Bob died on 1 August 2008 when the nil band was £312,000.

He leaves £10,000 to each of his 6 Grandchildren and the remainder to his wife Norma.

	£
Nil band August 2008	312,000
Utilised in estate	<u>60,000</u>
	<u>252,000</u>
$\frac{252,000}{312,000} = 80.77\%$	

Norma dies on 1 August 2012 when the nil band is £325,000. Her nil band becomes:

	£
Normal amount	325,000
Addition $80.77\% \times £325,000$	<u>262,503</u>
	<u>587,503</u>

Unused nil band

- More than one spouse
 - max b/f = 100% of current nil band
- Used against tax arising on death –
 - failed PET's
 - additional tax on CLT's
 - estate at death
- HMRC allow b/f to be used before own nil band

Valuation – unlisted shares

- Must take account of same shares owned by spouse/CP
- David owns 4,000 shares in Brand Ltd, and his wife owns 3,000 shares. The total shareholding is 10,000.
- Valuations have been agreed as follows:
 - Up to 25% £10 per share
 - 26% to 50% £12 per share
 - 51% - 75% £18 per share
 - 76% - 100% £25 per share
- Value of David's holding:
 - 4,000 x £18 per share £72,000
- Value of wife's holding
 - 3,000 x £18 per share £54,000

Charitable giving for IHT

- Individual leave 10% or more of estate to charity
 - rate applicable to eligible component becomes 36%
 - based on net estate after reliefs, exemptions and available nil band
 - must be recognised charity
- Suggested wording available for ‘flexible will’

Example

Robert died on 17 June 2012 leaving an estate valued at £750,000 after the deduction of liabilities. He leaves £50,000 to the National Trust in his will.

	£
Estate at death	750,000
Less: exempt legacy	<u>(50,000)</u>
	700,000
Available nil band	<u>(325,000)</u>
	<u>375,000</u>
 10% x (375,000 + 50,000) = £42,500	
Legacy to charity >10%	
∴ £375,000 x 36%	<u>135,000</u>

Maximising use of BPR and APR

Key planning points

- Both APR and BPR good in both life and death
- So which is best?
- It depends....choice!
- BUT, you also need to consider the CGT aspects if lifetime gifting used

Case study - Andrew

- Andrew owns a farm in Dorset. He paid £140,000 for it 25 years ago and it's now worth around £800,000. He has a small mortgage (£80,000) secured against the property.
- He has a son and would like him to have the farm in due course
- Andrew farms it himself and it makes a small profit each year
- Is it best to gift the farm in life or on death?
- What tax (and other non-tax issues does he need to consider?

Business property relief

Relevant business property	% <i>relief</i>
A business or interest in a business	100
Shares in an unquoted company (or holding company of a group)	100
Controlling shareholding in a quoted company	50
Land, buildings, plant and machinery used in the business of a company controlled by the transferor or by a partnership where the donor is a partner	50
Settled property being land, buildings, machinery or plant in which the donor has a qualifying IIP and is used mainly in his/her business	50

Business asset

- Investment activity can jeopardise relief
- If company has non-trading activity no BPR if >50%
 - watch cash in excess of working capital requirements
- Property development companies will normally qualify
 - property investment companies will not
- HMRC currently accepting some letting of property while can't be sold will not jeopardise trading status of development companies
 - watch wording of directors report and balance sheet

Business property relief

- AIM shares treated as unlisted
- Include spouse's holding for control
- Company must be trading but not
 - dealing in shares, stocks or securities unless market makers or discount houses
 - dealing in land and buildings
 - making/holding investments

BPR and lifetime gifts

- PET or CLT and then death < 7 years
- Relief only available on death where
 - donor qualified at time of gift and
 - donee qualifies at date of death
- problems
 - sale without replacement
 - donee has gifted asset
 - unlisted company becomes listed

Trusts – why use them?

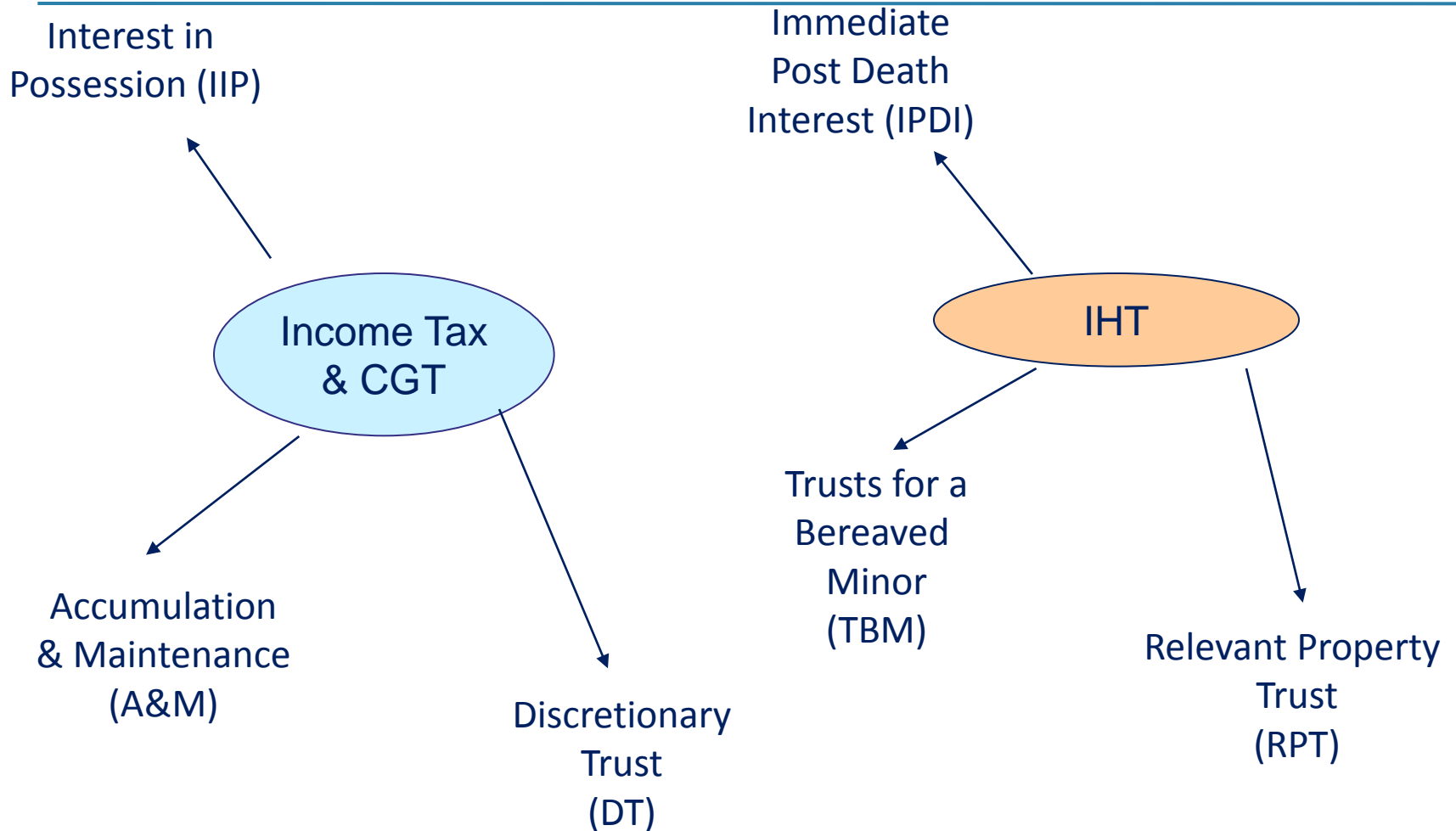
Trusts – why use them?

- Protect underlying capital
- Manage assets and income where beneficiaries minor children
- Legatees not financially ‘savvy’
 - or profligate
- Married to someone you don’t like
 - and split possible
- Tax planning is then which one to use
- Schemes – already discussed

Trusts - 2

- Set up 'by operation of law' intestacy distributions
- Trust deed in lifetime of settlor
- By will on death of settlor
- Managed by trustees
- Major changes implemented in March 2006.

Trusts Terminology



Case study - Robert



- Robert is 65.
- He is considering a Legal & General life insurance policy that pays out £3,743 for a £15 per month premium and has asked you about it.
- What advice would you give about the tax aspects of this proposal?

Will and IHT planning on a second marriage

Case study - John

- John is divorced
- He has children from his first marriage
- He is marrying again
- His wife is younger and has also children from a previous marriage
- He wants a roof over her head if he dies first but the main part of the estate should go to his children

General will planning and will trusts

Why use a will trust?

- Will Trust allows spouses/CPs to carry out IHT planning without losing access to their capital or the income arising on it during their lifetimes
- It is particularly useful where:
 - joint wealth exceeds two nil rate bands
 - where there may be nursing care requirements in the future or
 - where there are children from previous relationships.

Why use a will trust? - 2

- It provides IHT planning for couples/partners who cannot afford to give away their capital and the income it generates
- Potentially safeguards the capital of the trust from the impact of nursing home fees and long-term care costs of the surviving spouse/partner

Using will trusts

- The nil rate band of the first spouse is used on first death, the IHT saving does not occur until the second spouse dies.
- Each spouse/partner can take regular withdrawals from the bond during their lifetime, if required
- Allows the surviving spouse/partner access to the capital of the Will Trust
- Reduces the potential IHT liability on the death of the surviving spouse.

Death planning

- Assets left to DT on death
 - if fully distributed within 2 years of death IHT calculated on basis of distribution from trust
 - gives time to reflect on who needs what
 - must not distribute any assets within 3 months of the death
 - not effective for CGT

Deed of variation

- Made within 2 years of death
 - delivered to HMRC <6m of having been made
- Read instead of will for IHT and CGT (if specified)
 - not effective for CGT on assets held within p'ship
 - for IT only effective from date of deed
 - watch rule of 'parents disposition'
- Must be signed by executors (if additional tax payable) and anyone whose share is reduced
- Can be used for will or intestacy

Deed of Variation

- No consideration can be given for the variation
 - legal costs etc must be borne by original beneficiary
- Can be issues if estate includes assets overseas
 - what are the rules in the local environment?
- No SDLT or SD on DoV

Use of DoV

- Creating IPDI/nil band legacy post death
- Leaving part of property to 'next generation' where tenants in common
- Skipping a generation
- Creating 'double dip' for BPR

Double dipping for BPR

- Shares in family company left to spouse
 - estate exempt as spouse transfer
- DoV moves legacy of shares to children
 - nil value – BPR 100%
- Spouse buys shares (at full value) from children
 - swapping shares for cash in their hands
- Providing she survives 2 years shares will attract 100% BPR in her estate at death

Using a DOV

- Dan dies leaving his holiday cottage to wife Doris
 - they have 2 adult children
 - if Doris retains holiday cottage it will be included in her estate so she gifts it to the children to try to achieve 7 year survivorship
 - she still wants to use it as a holiday home GWROB rules apply
- Use DoV to leave holiday home to children – if within nil band no IHT on Dan's death
 - Doris can now use holiday home without GWROB as children treated as acquired from Dan