COMPASS ACCOUNTANTS

TAX ANGLES FOR PROACTIVE PLANNING

Newsletter - August 2019

In this month's edition…

Government childcare scheme – tax-free top-up

Working parents can receive a tax-free top up from the Government to help with their childcare costs. The top up is worth £500 every three months (£2,000 a year). A higher top-up of £4,000 a year (£1,000 every three months) is available for children with disabilities.

To receive the top-up, eligible parents must open an account online. The Government will provide a top-up of £2 for every £8 deposited by the parents, up to the above limits. The money in the account is then used to pay for childcare with a registered provider.

Who is eligible?

To qualify for tax-free childcare, the claimant (and their partner if they have one) should be in work, on sick leave or annual leave or on parental, maternity, paternity or adoption leave. The scheme is open to both the employed and the self-employed. However, earnings conditions apply.

The claimant (and their partner if they have one) must earn a minimum of £131.36 per week on average (which is equivalent to 16 hours at the National Living Wage of £8.21 per hour for 2019/20 for people age 25 and over). This equates to £1,707.68 over three months. This limit does not apply to a self-employed person who started their business within the previous three months.

There is also an earnings cap – tax-free childcare is not available where the claimant or their partner has 'adjusted net income' of more than £100,000. This is broadly taxable income before personal allowances, less items such as gift aid.

The child

Tax-free childcare is available for a child who is 11 or under and who lives with the claimant. Eligibility ceases on 1 September following their 11th birthday. A child with disabilities remains eligible until they are 17.

Using tax-free childcare

Tax-free childcare can be used to pay for childcare that is approved childcare. This includes childminders, nurseries, nannies, after school clubs, playschemes and home care agencies. The childcare provider must sign up to the scheme.

Interaction with tax-credit and Universal Credit

Tax-free childcare is not available at the same time as working tax credit, child tax credit or universal credit. The childcare calculator is available on the Gov.uk website at www.gov.uk/tax-free-childcare.

Employer-supported childcare and childcare vouchers

Similarly, an employee cannot benefit from both the tax-free top-up under the Government scheme and the tax exemption for employer-provided childcare vouchers or employer-supported care. Again, what is the best option will depend on personal circumstances. An employee within an employer scheme must tell their employer they have applied for tax-free childcare within 90 days of making the application.

How to apply

Applications for tax-free childcare can be made online at www.gov.uk/apply-for-tax-free-childcare.

Avoiding common errors when computing business profits

HMRC produce a range of Toolkits for agents, which highlight errors commonly made in returns so that agents can take steps to avoid them. The business profits toolkit provides guidance on errors that are found in relation to business profits for small and medium-sized businesses. They are helpful to anyone computing taxable business profits.

Risk area 1 – Record keeping
Good record-keeping is essential for business profits to be calculated correctly. Poor records may result in sales or allowable expenditure being omitted from the accounts, with the result that the level of profit or loss is incorrect.

Risk area 2 – Business income
The profit or loss will only be correct if all income is included in the accounts. Unless the business is an unincorporated business that has opted to use the cash basis, business income should be included on an accruals basis, matching the income to the period in which it was earned.

Not all sources of business income will be immediately obvious – the income of the business may, for example, include scrap sales, contra sales or barter arrangements. Cash sales may also be overlooked.

Risk area 3 – Expenditure
To ensure that the profit is not overstated, all allowable expenditure should be taken into account. However, a deduction is only permitted for expenses which are wholly and exclusively incurred for the purposes of the business. Attention should also be paid to specific prohibitions, such as for business entertaining.

Purchases and expenses should be reviewed to ensure that they have been included.

Sole traders and partnerships comprising individuals (rather than corporate partners) can use simplified expenses rather than claiming actual expenses.

Risk area 4 – Stock and work in progress
Where the business is one that holds stock, care must be taken to include it at the correct value – this is the lower of cost and net realisable value. Errors will arise if stock is overlooked or valued incorrectly.

Work-in-progress can be a complex area and advice should be taken to ensure that the treatment is correct.

Risk area 5 – Miscellaneous items
Miscellaneous areas should also be considered. These may include a review of post-balance sheet events and consideration as to whether any adjustment to the accounts is required.

Staff costs should also be reviewed and amounts unpaid nine months after the end of the period should be added back. As far as directors are concerned, consideration should be given to the date on which amounts are credited to the director’s loan account.

Inheritance tax and spouses and civil partners

Special rules apply for inheritance tax purposes to married couples and civil partners. To ensure valuable tax reliefs are not lost, it is beneficial to consider the combined position, rather than dealing with each individual separately. Married couples and civil partners benefit from exemptions that are not available to unmarried couples.

Inter-spouse exemption

The main inheritance tax benefit of being married or in a civil partnership is the inter-spouse exemption. Transfers between married couples and civil partners are not subject to inheritance tax. This applies both to lifetime transfers and to those made on death.

The inter-spouse exemption makes it possible for the first spouse or civil partner to die to leave their entire estate to their partner without triggering an IHT liability, regardless of whether it exceeds the nil rate band.

Transferable nil rate band

The proportion of the nil rate band that is unused on the death of the first spouse or civil partner can be used by the surviving partner on his or her death. This makes tax planning easier and there is no panic about each spouse using their own nil rate band. If the entire estate is left to the spouse on the first death, on the death of the surviving spouse or civil partner, there will be two nil rate bands to play with.

If the first spouse or civil partner to die has used some of their nil rate band, for example, to leave part of their estate to their children, the surviving spouse or civil partner can utilise the remaining portion. It should be noticed it is the unused percentage that is transferred, rather than the absolute amount unused at the time of the first death – this provides an automatic uplift for increases in the nil rate band. The nil rate band is currently £325,000.

Residence nil rate band

The residence nil rate band (RNRB) is an additional nil rate band which is available where a main residence is left to a direct descendant. It is set at £150,000 for 2019/20, and will increase to £175,000 for 2020/21. The RNRB is reduced by £1 for every £2 by which the value of the estate exceeds £2 million.

As with the nil rate band, the unused proportion of the RNRB can be transferred to the surviving spouse.

Example

George and Maud have been married for over 50 years. Maud died in 2017 leaving £32,500 to each of her two children. The remainder of her estate, including her share of the family home, was left to her husband George.

George dies in July 2019. At the time of his death, his estate was worth £780,000 and included the family home, valued at £550,000, which was left equally to the couple's children, Paul and Joanna.

At the time of her death Maud had used up £65,000 of her nil rate band. The nil rate band at the time of her death was £325,000. The transfer to George was covered by the inter-spouse exemption and was free from inheritance tax. Maud has used up £65,000 of her nil rate band (20%), leaving 80% unused. She has not used her RNRB band as she left her share of her main residence to George.

On George's death, the executors can claim the unused portion of Maud's nil rate band and RBRB. The nil rate bands available to George are as follows:

Nil rate bands	**£**
George's nil rate band	325,000
George's RNRB	150,000
Unused portion of Maud's nil rate band (80% of £325,000)	260,000
Unused proportion of Maud's RNRB (100% of £150,000)	150,000
Total	£885,000

As George's estate on death is less than the available nil rate bands, no inheritance tax is payable.

Closing a business – when a member's voluntary liquidation is beneficial

Although it is possible to strike off a company and for distributions made prior to dissolution to be treated as capital rather than as a dividend, this is not an option where the amount of the distributions exceeds £25,000.

Where the taxpayer's personal circumstances are such that it is beneficial for the remaining funds to be taxed as capital (and liable to capital gains tax), rather than as a dividend, a member's voluntary liquidation (MVL) can be an attractive option, as depending upon the level of funds to be extracted the costs of the liquidation may be more than covered by the tax savings that can be achieved.

What is an MVL?
An MVL is a process that allows the shareholders to put the company into liquidation. This route is only an option if the company is solvent (i.e. its assets are greater than its liabilities). The directors must sign a declaration of solvency confirming that the company is able to pay its debts in full within the next 12 months and 75% of the members must agree to place the company into liquidation. The shareholders must pass a special resolution to wind up the company. They will also need to pass an ordinary resolution to appoint liquidators. The liquidator must be a licenced insolvency practitioner.

What are the tax implications?
Under an MVL the capital extracted from the company is treated as a capital distribution and is liable to capital gains tax, rather than being taxed as a dividend. Where entrepreneurs' relief is in point, the rate of tax will only be 10%, assuming enough of the entrepreneurs' relief lifetime limit remains available. If significant funds are available for distribution, this can generate considerable tax savings.

Example
Edward and Oliver are directors of a company in which they both own 50% of the shares and 50% of the voting rights. Each is entitled to 50% of the profits available for distribution and 50% of the assets on a winding up.

They wish to wind the company up, but as they have cash and assets of £10 million to distribute, they opt for an MVL, to allow them to take advantage of the capital gains tax treatment. Both are additional rate taxpayers, and both meet the qualifying conditions for entrepreneurs' relief.

Edward and Oliver each receive £5 million on the winding up of the company. They both have the full amount of the entrepreneurs' relief lifetime limit (£10 million) unused, and it is assumed for simplicity that the annual exempt amount has been used elsewhere. The gain is therefore taxed at 10% and each will pay tax of £500,000 on their distribution of £5 million.
Had they not opted for an MVL and the extracted funds taxed as a dividend, they would have each paid £1,905,000 in tax on the £5 million distribution (£5m @ 38.1%).

Anti-avoidance
Anti-avoidance provisions apply which are designed to target 'moneyboxing' (where the company retains more funds than it needs in order to extract them as capital when the company is liquidated) and 'pheonixism' (where the company is liquidated, the value extracted as capital and a new company is set up to carry on what is essentially the same business). Liquidation distributions which are caught by the rules are treated as income rather than capital.

Using a SIPP to save for retirement

A SIPP is a self-invested personal pension which is set up by an insurance company or specialist SIPP provider. It is attractive to those who wish to manage their own investments. Contribution to a SIPP may be made by both the individual and, where appropriate, by the individual's employer.

Investments
The range of potential investment is greater for a SIPP than for a personal pension or group personal pension scheme.

The SIPP can invest in a wide range of assets, including:

- quoted and unquoted shares;
- unlisted shares;
- collective investment schemes (OEICs and unit trusts);
- investment trusts;
- property and land (but excluding residential property); and
- insurance funds.

A SIPP can also borrow money to purchase investments. For example, a SIPP could take out a mortgage to fund the purchase a commercial property, which could be rented out. The rental income would be paid into the SIPP and this could be used to pay the mortgage and other costs associated with the property.

Making contributions
Tax-relieved contributions can be made to the SIPP up to the normal limits set by the annual allowance.

This is set at £40,000 for 2019/20. The annual allowance is reduced by £1 for every £2 which adjusted net income exceeds £150,000 where threshold income exceeds £110,000, until the minimum level of £10,000 is reached.

Anyone with adjusted net income of £210,000 and above and threshold income of at least £110,000 will only receive the minimum annual allowance of £10,000.

Where the annual allowance is unused, it can be carried forward for three years. Any contributions made by the employer also count towards the annual allowance.

SIPPs operate on a relief at source basis, meaning that the individual makes contributions from net pay. The SIPP provider claims back basic rate relief, with any higher or additional rate relief being claimed through the self-assessment return.

Drawing a pension
A SIPP is a money purchase scheme and the value of benefits available to provide a pension depend on contributions that have been made to the scheme, investment growth (or reduction) and charges.

It is possible to draw retirement benefits at age 55. A tax-free lump sum can be taken to the value of 25% of the accumulated funds. Withdrawals in excess of this are taxed at the individual's marginal rate of tax.

To prevent recycling contributions, where pension benefits have been flexibly accessed a reduced money purchase annual allowance, set at £4,000 for 2019/20, applies.

Introducing …. Matrix IT

Compass Accountants would like to introduce you to Gareth McQuaid- the Business Development Director at Matrix IT- 'The South Coast's Favourite IT Company'

Matrix IT are providers of fully managed IT solutions working closely with their clients to provide cost-effective IT support to meet their business needs. They pride themselves on their ability to provide solutions that fit within clients' budgets. As a result of the company's excellent service, Compass Accountants has been a Matrix IT client for a number of years.

Their services include IT Support, IT Strategy Planning, Business Phone Systems, Connectivity (Broadband/Leased lines/WiFi), Cloud Services (365/SharePoint etc), Cloud Migrations, Cyber Security Solutions, Cyber Essentials Preparation & Certification.

As a business that is over 15 years old, Matrix has evolved and continuously improved over the years.
"I have worked in the IT sector for over 20 years now," says Gareth McQuaid, Business Development Director at Matrix. "Collectively, the other Directors and I have over 100 years of experience that we can draw on to best understand how to approach any issue, which is ideal for problem solving. Many other service providers simply charge a small fee per month just to oversee the IT function, but they are not doing their due diligence, and rarely have an overall strategy or a client's business needs in mind."

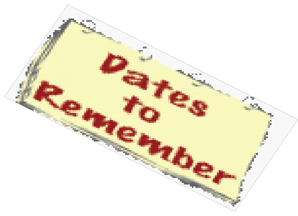
"At Matrix, we become your internal IT Department. Our job is also about finding solutions - which is very satisfying for me as problem solving is my passion. It is very rewarding when a client has a problem and you can solve it whilst also enabling their business to flourish."

Matrix's clients are located in across the South Coast - however proximity is not necessarily relevant to its clientele as Gareth explains- "Many clients are under the impression that a managed service provider needs to be close by - however, 95% of all issues can be resolved remotely, so we have clients in Bournemouth, Basingstoke and Brighton and even further. However, for the clients that prefer site visits we are also able to provide these too."

A wealth of experience…
Matrix consists of a team of 16 members of staff and tends to work with small to medium businesses. "Our clientele ranges from companies with 15 staff right up to 100 user businesses, and we can cater for small teams as well. Outsourcing your IT is most obvious and, in most instances, makes the most sense. We work with over 100 clients from a variety of industries, allowing us to have a strong knowledge base of best practice and how to successfully approach specific issues."

If you would like to find out more about how Matrix IT can help you call-
01329 888444 or email- moreinfo@mtxit.com or go to www.mtxit.com for further details.

Tax Diary
August/September 2019



1 August 2018 - Due date for Corporation Tax due for the year ended 31 October 2017**.**

19 August 2018 - PAYE and NIC deductions due for month ended 5 August 2018. (If you pay your tax electronically the due date is 22 August 2018)

19 August 2018 - Filing deadline for the CIS300 monthly return for the month ended 5 August 2018.

19 August 2018 - CIS tax deducted for the month ended 5 August 2018 is payable by today.

1 September 2018 - Due date for Corporation Tax due for the year ended 30 November 2017.

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Contact us

For further information on any of the stories in this month's newsletter, or for any other matter that Compass Accountants can assist you with, please contact us on 01329 844145.

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