

Newsletter

Tel: +44 01 282 432 171 • Fax: +44 01 282 412 510 • accountants@ashworthmoulds.co.uk

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Is your financial risk strategy up to date?



If the pandemic – and now the Ukraine war – have taught small and medium-sized business owners anything, it is the value of staying agile in changing circumstances. Regular assessment of financial risks, and your strategies to meet them, will help to mitigate their short and long term impact.

Ashworth Moulds

11 Nicholas Street
Burnley BB11 2AL

Telephone +44 01 282 432 171
Facsimile +44 01 282 412 510
accountants@ashworthmoulds.co.uk

Partners

D A Pickles
M Holmes
C C Harrison
J Lye

Associates

M R Woodworth
J Nightingale

Registered to carry on audit work in the UK and regulated for a range of investment business activities by the Institute of Chartered Accountants in England and Wales



Financial risk

Financial risk might best be described as any potential future situation that could cause your business to lose money. A business will have more control over some risks than others, but that doesn't mean risks outside a firm's control, such as energy and fuel prices, can simply be ignored.

For example, if part of your business involves visiting customers, fuel costs might be contained by reorganising service areas to reduce travel time for each journey.

“Risks are inevitable, but businesses should do their best to be prepared for the unexpected; and the key to this is agility.”

Cash flow

If you focus primarily on sales and profitability your business' overall financial position could get overlooked. However, cash flow is critical; poor cash flow has led to many business failures.

- Prepare regular cash flow statements so that future liquidity issues can be identified early.
- Where there is a lot of uncertainty, this can be built into cash flow projections.
- If customers regularly pay late, you could consider applying a late payment fee.

Conduct more frequent reviews

Weekly – or even daily – cash flow monitoring could be appropriate given current economic conditions. Risks are inevitable, but a business will be better prepared to deal with them if it has a financial risk strategy in place. Since it is impossible to see the future, businesses should do their best to be prepared for the unexpected; and the key to this is agility.

Think about your business as a series of moving parts, not static fixtures and ask questions such as: What else can this asset be used for? Does this expense scale down if revenue falls? Can we quickly scale up if an opportunity presents itself?

Making the most of business disposal reliefs

If you are a company owner planning to sell your business in the future, you can make sure that the chargeable gain on your shares is taxed at 10% rather than 20% – in other words that the disposal qualifies for business asset disposal relief (BADR).

There are several conditions for the relief and one of them has recently been the subject of a decision in the Upper Tribunal. As a result, HMRC has had to rewrite some of its guidance.

Trading companies qualify

A company must be a trading company for its shares to qualify for BADR. A trading company is one whose activities do not include “to a substantial extent, activities other than trading activities”. Previously HMRC defined ‘substantial’ as “more than 20%” of a company’s income, assets, expenses incurred



and time spent by its officers and employees on trading and non-trading activities.

The Upper Tribunal rejected such a prescriptive test and the application of a strict numerical

threshold. ‘Substantial’ should be “taken to mean of material or real importance in the context of the activities of the company as a whole”. One must look at the nature of the company’s activities and consider how best to measure their extent. The test is both qualitative and quantitative.

The Tribunal decision may create some uncertainty where companies have some non-trading activities. Business owners may prefer to keep any significant non-trading activities separate from their trading company.

If you do not intend to dispose of your business, your heirs will want its value to qualify for business relief for inheritance tax, given at 100% for unlisted company shares or a business or interest in a business. Businesses that consist wholly or mainly of dealing in securities, stocks or shares, land or buildings or making or holding investments are excluded. If there is a mixture of activities, there is no single test for determining whether its activities are ‘wholly or mainly’ excluded. As with BADR, careful advance planning should avoid any unpleasant surprises.

VAT claims on electric cars

New rules apply for claiming VAT on electricity used for charging vehicles.

If an employee charges a vehicle at a public charging point, the supply of electricity is made to the employer, who can then recover the VAT on the cost, just as where the employee charges the car at work. Sole proprietors and partners in a business partnership can also recover VAT when they charge vehicles at home. In all cases, only the VAT relating to business use of the vehicle can be claimed, calculated by reference to mileage records.

However if an employee charges a vehicle at home, the supply of electricity is made to the employee not the employer. The employer therefore cannot recover the VAT. HMRC is reviewing what evidence could be provided to allow employers to claim the VAT where an employee is reimbursed for the cost of charging vehicles at home for business purposes.



Managing employment costs



The National Minimum Wage and Living Wage increased from April, alongside the rise in national insurance contributions (NICs). Employers need to plan for the changes.

National Living Wage

The hourly rate of National Living Wage that must be paid to workers aged 23 and over has gone up to £9.50; a 6.6% increase, equating to extra annual salary of at least £1,000.

The minimum rate going up nearly in line with the expected rate of inflation puts pressure on employers to match this when it comes to settlements higher up the salary scale. Small and medium-sized businesses in particular could find the higher rates of minimum pay a strain on their finances.

National insurance contributions

Higher paid employees will see a big drop in their take-home pay from April following the 1.25% increase to the rate of NICs, even though the starting threshold is going up. For example, someone earning £100,000 annually will have take-home pay of nearly £91 less in April compared with March, but an increase of nearly £32 in July compared with June. July is when the starting threshold will see another,

more substantial, raise to match the personal allowance at £12,570.

- Employers will also see a broadly similar increase in what they have to pay (with no reduction from July). It will be expensive if there is a team of highly paid personnel unless costs can be passed on to clients.
- Make sure additional costs are reflected in financial projections.

Salary sacrifice

The higher rates of NICs make salary sacrifice arrangements more attractive than ever, especially regarding employer pension contributions. A company car salary sacrifice arrangement also works well for full electric and certain hybrids.

Salary sacrifice will not, however, suit everyone. Employees need to be aware that a lower base salary will normally mean a lower level of potential mortgage borrowing — a real problem given current property prices.



Understanding directors' loan accounts

The tax charge on loans between a director and their company goes up from April. Such loans are common practice, but problems can arise if these transactions are not properly accounted for.

There are various reasons why a director can end up having an overdrawn loan account with their company, but the tax charge is the same regardless. A higher charge is payable from 6 April.

The tax charge, which has gone up by 1.25 percentage points to 33.75%, is payable when a director, who is also a participator, has an outstanding loan with a close company and the loan is not repaid within nine months and a day of the end of the company's accounting period.

Broadly, a participator is a shareholder in a company, and a close company is one controlled by five or fewer participators.

Approval

A loan to a director should be approved by a written ordinary resolution from the shareholders, although this can be done retrospectively. Approval is not required for loans up to £10,000, or for indirect loans such as where the company has paid for a director's personal expenses.

How the tax charge works

When a director's current account is overdrawn, this can be cleared by the company voting the director a dividend or bonus. There might be situations, however, where this does not happen. For example, on 1 July 2022, a director withdraws £100,000 from their personal company to help fund a private property purchase. The company has an accounting date of 30 June.

- The loan falls in the company's year ending 30 June 2023, so there will be no tax charge if it is repaid by 1 April 2024. So, by careful timing, the director will have had use of company funds for 21 months, with the only tax being what is charged for having a beneficial loan.
- If not repaid by 1 April 2024, the company will have to pay a tax charge of £33,750 (£100,000 at 33.75%) along with its corporation tax liability.
- The tax charge will be refunded by HMRC if – after 1 April 2024 – the loan is repaid or written off. A write off will of course have tax implications for the director.

Repayment

It might well be the case that it is cheaper, in tax terms, to simply leave a director's loan outstanding. This could be the situation if the only way to repay it is by taking a bonus that, apart from being taxed, will also mean both employee and employer NICs are payable. The repayment could take several forms:

- A dividend will often be the favoured option, but this could be impractical if there are other shareholders involved who have different dividend requirements.
- Although clearing a loan before the tax charge is due is generally preferable, there is no reason why dividends cannot be used to clear a loan over several years.
- The director could introduce funds into the company, for example from a property disposal.
- Another, often overlooked option, is the director transferring assets to the company, with the value transferred then credited to their director's loan account. Other tax considerations come into play when it comes to a car or property, but, for example, a personal loan owed to the director can be assigned to the company.

If you need help managing a loan, please get in touch.



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PROPERTY



Eviction law set to change

Reform of the private rented sector in England has been on the agenda for some time, but it looks like the end of section 21 evictions might come later this year. Landlords will no longer be able to evict tenants without giving a specific reason.

Most residential tenancies in England are assured shorthold tenancies lasting for a minimum six months. After this initial fixed term period, a landlord can – subject to sufficient notice – currently end the tenancy without giving any reason. Many section 21 evictions are, of course, because of rent arrears. The proposed reform mirrors the system already in place in Scotland.

The alternative

As an alternative, a landlord can evict using section 8 of the Housing Act. Such evictions can happen at any time during a tenancy – including the initial fixed term – but only if a tenant has broken the terms of the tenancy agreement such as rent arrears, unsociable conduct or property damage. This process carries no certainty of regaining possession and can be more expensive.

The reform should include strengthened repossession grounds when a landlord has valid cause.

If the reform is introduced, the average landlord with just two or three properties will need to be more careful than ever about who they take on as tenants. They might consider asking for several months' rent paid upfront or for a guarantor to be provided.

Simplified probate reporting requirements

Changes introduced from the start of this year have simplified the process for obtaining a grant of probate (certificate of confirmation in Scotland) and limited the circumstances when a full inheritance tax (IHT) account needs to be delivered to HMRC.

Anyone acting as an executor for someone who has died on or after 1 January 2022 with an excepted estate is no longer required to submit a separate form IHT205 (C5 in Scotland). You can now report all relevant information on the probate/confirmation application.

Excepted estates

An excepted estate is one that does not require a full IHT account. There are two main circumstances when an estate will be considered excepted.

Low value: This is an estate with a gross value of less than the IHT nil rate band of £325,000, or up to twice this threshold if the unused nil rate band of a predeceased spouse or civil partner is available. There are three value limits which also need to be met for an estate to qualify as low value, and two of these have been increased from 1 January:

- The value of trust property included in the estate must not exceed £250,000 (increased from £150,000).
- The value of foreign assets must not exceed £100,000 (no change).
- The value of chargeable transfers made in the seven years before death (this is something of a simplification of the actual rules) must not exceed £250,000 (increased from £150,000).

Exempt: This is an estate with a net value – after deducting liabilities, exemptions and reliefs – that does not exceed the available nil rate band(s). The limit for the gross value (before the deductions) has been increased from £1 million to £3 million. The three low value estate limits also apply.

With the removal of the IHT205/C5 obligation, more people may consider managing the estate administration process themselves.

News round up

HMRC late payment interest rate rise

HMRC's late payment interest rate has increased to 3.25% from 5 April 2022. It applies to the main taxes and duties administered by HMRC. If you are at risk of making a late payment, you will need to factor in both late payment interest and possible penalties.

Advisory fuel rate change

Despite current fuel price volatility, HMRC's advisory fuel rates effective 1 March 2022 have increased by just 1p, and then only for LPG. Employers who want to pay more than advisory rates can do so without tax consequences if the higher rates can be justified.

MTD for VAT comes in

From 1 April 2022, all VAT-registered businesses must use MTD for their first VAT return that starts on or after that date. Payments for VAT will not have to be made through MTD until July 2022. Make sure you have signed up in time.

Register of overseas entities

The government will introduce reforms to improve transparency over ownership of companies and property in the UK by foreign entities. The reforms include the long-delayed register identifying ultimate beneficial ownership of property, with restrictions over selling for those who do not comply.

Closing tax loophole on second homes

Owners of second homes in England who claim exemption from council tax by reporting them as holiday lets will in future have to provide evidence of actual letting.

The current rules allow owners to pay business rates instead of council tax if they simply declare an intention to let the property. They can also apply for small business rates relief, and, if they meet the conditions, pay nothing on properties with a rateable value of £12,000 or less.

From April 2023 only genuine holiday lets will be eligible for small business rates relief. Owners will have to provide evidence such as the website or brochure used to advertise the property, letting details and receipts in order to be assessed for business rates rather than council tax. This evidence will have to prove that:

- The property will be available for letting commercially as self-catering accommodation for short periods totalling at least 140 days in the coming year and was also available for 140 days in the previous year.
- During the previous year it was actually

let commercially as self-catering accommodation for short periods totalling at least 70 days.

Around 65,000 holiday lets in England are liable for business rates of which around 97% have rateable values of up to £12,000. Small business rates relief will usually only be available where the owner has only one holiday letting property, although the relief is retained for 12 months when the owner buys a second property. Relief may also continue on the main property if none of the additional properties have a rateable value above £2,899.

In Scotland if a let self-catering premises is available for 140 days or more a year it may be liable for business rates. Similar changes to those in England come in a year earlier over the border, so from 6 April holiday lets must be booked for a minimum of 70 days in a financial year. The rules in Wales are currently under consultation for similar amendments.

