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A list of Directors is available from the Registered Office at Northallerton. Kenneth Easby Limited is a limited company registered in England, No 07107469.
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.

NEWSLETTER

NEW APPOINTMENT

We are pleased to announce the appointment of John Howarth as a Senior Accountant who will be based at our Northallerton office.



After obtaining a degree in Experimental Physics at York University, John qualified as a Chartered Accountant and has developed particular experience on the audit of charities, including a number of educational institutions. John is currently a member of the ICAEW Learning and Professional Development Board.

CHARITY CYCLE RIDE

Director Kevin Bradley and a group of friends are currently in training for a cycle ride in September. The ride is from the Atlantic coast to the Mediterranean, a distance of over 700km and will take in some of the iconic Cols of the Pyrenees.

They are raising funds for the Yorkshire Air Ambulance. If you would like to sponsor Kevin please contact him or visit the group JustGiving site at:- www.justgiving.com/PyreneesC2C

AUTUMN 2015

Self assessment tax returns still need to be submitted on time

You may have seen in the press or on the TV a couple of months ago, news stories that implied that it would be easy to get out of paying an automatic £100 minimum penalty for the late filing of a self assessment tax return.

The background to the initial news stories was the leaking of an internal memo of HMRC to its staff dealing with self assessment penalties. A £100 automatic penalty is charged if a self assessment tax return is not submitted by 31 January. Individuals can successfully appeal against the penalty if they have a 'reasonable excuse'. HMRC provide a list of what they regard as reasonable. Top of the list is 'your partner died shortly before the tax return or payment deadline', which provides an indication of the extreme circumstances listed.

Despite the automatic penalty system, around 900,000 people failed to submit their tax return on time for the 2013/14 tax year, the deadline for which was 31 January 2015. Many of these individuals appealed against the subsequent £100 minimum penalty causing a backlog of cases in HMRC. The internal memo explained a simplified approach to resolving penalties with the effect that HMRC would accept the taxpayer's grounds for appeal in

the majority of cases without questioning the taxpayer and cancel the penalty.

A subsequent press release from HMRC has made it clear that the deadline for appealing fines for the 2013/14 tax year has now passed. It did not state what their approach would be to individuals missing the 2014/15 tax return deadline which is 31 January 2016. The press release does say, in the longer term, HMRC want to move away from sending out penalty notices as a mechanical reaction to a single missed deadline. Instead they want to focus on those who persistently fail to pay or submit their tax returns on time.

It is good news, of course, that HMRC will use their right to send out fixed penalty notices in a fair and proportionate way. But it is far safer to meet the deadlines so please do contact us in plenty of time before the forthcoming 31 January to ensure that your self assessment return does not run the risk of being filed late.



Spreading income around the family

Owner managed companies often seek to minimise the tax position of shareholder-directors by involving members of the same family and using personal reliefs and lower rate tax bands of each person. Income is therefore diverted from the higher rate taxpayer. However, anti-avoidance rules need to be considered as to whether a diversion is effective. This is particularly relevant for spouse scenarios such as husband and wife.

Where it is considered that arrangements have been made by one spouse which contain a gift element, often referred to as 'an element of bounty' then the 'settlements' rules may apply. A key purpose of these rules is to ensure that income alone or a right to income is not diverted from one spouse to the other. Genuine outright gifts of capital or a capital asset from which income then wholly belongs to the other spouse are not caught by the rules because of a specific exemption from the settlement rules.

Family company shares and the dividend income derived therefrom have frequently been the subject of challenge from HMRC on this matter. An example of a structure which will be challenged is the issue of a separate class of shares with very restricted rights to a spouse, with the other spouse owning the voting ordinary shares.

An area of potential risk is the recurrent use of dividend waivers particularly where the level of profits is insufficient to pay a dividend to one spouse without the other waiving dividends. In a recent tax tribunal case dividend waivers executed by two appellant husbands in favour of their spouses constituted a settlement for income tax purposes. The dividends therefore became taxable on the husbands.

The basic facts were that two directors of a company each owned 40% of the shares in the company. Their wives each

owned 10% of the shares. Dividends totalling £130,000 were paid in respect of the shares in the company's accounting period to 31 March 2010. The four individuals received the following:

- Mr D £33,000 (25.38%)
- Mrs D £32,000 (24.62%)
- Mr M £33,000 (25.38%) and
- Mrs M £32,000 (24.62%).

This clearly does not correspond to the legal and beneficial shareholdings and had been achieved through dividend waivers. The same type of mechanism had been used to allocate dividends back to the year ended 31 March 2001.

The arguments

HMRC argued that the taxpayers had waived entitlement to dividends as part of a plan which constituted an arrangement with an intention to avoid tax by seeking equalisation of their dividend income. The appellants' arguments included the contention that the waivers had been executed to maintain the company's reserves and cash balances in order to accumulate sufficient of each to fund the purchase of the company's own freehold property.

The Tribunal preferred the submissions of HMRC that had this been the case the aim could have been achieved by other means, such as voting a lower dividend per share. The Tribunal determined that the waivers would not have been made if the other shareholders were a third party and therefore there was 'an element of bounty' sufficient to create a settlement.

Basic tax planning is still an activity that many will seek to use to mitigate tax liabilities but care has to be taken in the current anti avoidance environment to avoid the traps. If we can be of assistance in reviewing your position please do not hesitate to contact us.

Should I continue trading through a limited company?

In the Summer 2015 Budget, George Osborne announced fundamental changes to the way in which dividends are taxed. The changes take place for dividends received from 6 April 2016. Some individuals who extract profits from their company as dividends may need to consider whether to increase dividend payments before this date.

When a dividend is paid to an individual, it is subject to different tax rates compared to other income due to a 10% notional tax credit being added to the dividend. So for an individual who has dividend income which falls into the basic rate band the effective tax rate is nil as the 10% tax credit covers the 10% tax liability. For a higher rate (40%) taxpayer, the effective tax rate on a dividend receipt is 25%.

From 6 April 2016:

- The 10% dividend tax credit is abolished with the result that the cash dividend received will be the gross amount potentially subject to tax.
- New rates of tax on dividend income will be 7.5% for basic rate taxpayers, 32.5% for higher rate taxpayers and 38.1% for additional rate taxpayers.
- A new Dividend Tax Allowance will remove the first £5,000 of dividends received in a tax year from taxation.

Many owner-managers running their business through a limited company will pay more tax next year if most of the profits are paid out as dividends rather than as a salary. This prospect raises a number of issues which we address below.

- There is still a benefit in tax terms for most individuals to continue to trade as a limited company. The tax saved by incorporation compared to being unincorporated will be reduced next year but there is still an annual tax saving.
- There is still a benefit for a director-shareholder to take a dividend rather than a salary. The amount of the tax saved will be less than under the current regime.
- If you do not currently extract all the company profits as a dividend you may wish to consider increasing dividends before 6 April 2016. However, other tax issues may come into play, for example the loss of the personal tax allowance if your total 'adjusted net income' exceeds £100,000. There will also be non-tax issues such as the availability of funds or profits in the company to pay the dividend.

Please contact us before you make any decisions about changing the amount of dividends taken. Please note our conclusions above are based on only limited information that has been supplied by the government on the new regime. We expect draft legislation for the regime to be published by the end of the year.





Looking forward to the new flat-rate State Pension?

To ask any question about the new flat-rate State Pension scheme seems to suggest a straightforward answer. Everyone will get the same amount won't they?

The answer to the latter question is no. The amount you will get will depend upon a number of factors including:

- how many qualifying years you have on your National Insurance (NI) record
- how many years you have built up an entitlement to the additional State Pension under the current system
- how many years you may have been paying lower NI contributions because you have been in a salary-related workplace pension scheme or you received NI rebates which went into a personal pension plan. Either of these scenarios had the effect of 'contracting out' a person from full entitlements under the State Pension scheme.

The new State Pension scheme applies to everyone who reaches State Pension age on or after 6 April 2016. The full State Pension will be at least £151.25 but the actual amount will be set this Autumn. People who have no contribution record under the current system will have to obtain 35 qualifying years of NI credits on their record to give them the flat-rate amount.

However, for individuals who have already built up a NI record (which is nearly everyone reading this article) there are transitional provisions which take into account the NI record accrued up to 5 April 2016. This is a very reasonable complication to have in moving to the new system. Otherwise, people who have accrued a substantial entitlement under the current system of basic and additional State Pension would be treated very differently depending on whether they reach State Pension Age on the 5 April 2016 (and thus receive a pension under the current system) or on the 6 April 2016 (and therefore receive a pension under the new system).

Under the transitional provisions, your NI record before 6 April 2016 is used to calculate your 'starting amount' for the new system at 6 April 2016. Your starting amount will be the higher of either:

- the amount you would get under the current State Pension rules (which includes basic State Pension and additional State Pension)
- the amount you would get if the new State Pension had been in place at the start of your working life.

For many of those reaching State Pension age in the near future, the transitional provisions offer the best of the current and new systems. Employees who have built up a significant entitlement to the additional State Pension will retain their entitlement. People who have been self-employed for most of their working lives may have little or no entitlement to the additional State Pension and thus will benefit from the new State Pension rules.

Example – self employed

Joe will reach his State Pension age in October 2020 (the State Pension will have risen from 65 to 66 by then). He has been self-employed except for the early part of his working life and he has no entitlement to additional State Pension. He has 32 qualifying years on his NI record.

His starting amount on 6 April 2016 (based on current figures) will be:

- under the existing rules - 30 years NI record would give a full entitlement to the basic State Pension of £115.95 a week
- using the new rules - Joe would get £138.29 a week ($£151.25 \times 32/35$).

Therefore his starting amount is £138.29. As his starting amount is less than the full rate of the State Pension, if he continues working for three years after 6 April 2016 he will accrue sufficient additional pension rights under the new system to bring him up to the full rate of £151.25.

Example – employed

Maureen will reach her State Pension age in October 2020. On 6 April 2016, Maureen has 35 qualifying years on her NI contribution record. During her working life, Maureen has had short periods when she was contracted out of the additional State Pension.

Her starting amount on 6 April 2016 will be:

- under the existing rules - her 35 years NI record would give her a basic State Pension of £115.95 a week plus £86 additional State Pension but a deduction for her contracted out period of £32. (This will be computed by the Department of Work and Pensions.) This totals £169.95.
- using the new rules Maureen would get £151.25 less a deduction of £32. This totals £119.25.

Maureen's starting amount will be the higher of these two amounts, which is £169.95 a week. As her starting amount is more than the full rate of the State Pension, she cannot accrue additional pension rights under the new system.

How do you get a state pension forecast?

You can get a forecast in some cases online – in other cases you need to ask for a forecast by post. Go to www.gov.uk/state-pension-statement to find out.



Annual Investment Allowance set at £200,000

The Annual Investment Allowance (AIA) provides an immediate deduction to many businesses for the cost of most plant and machinery (not cars) purchased by a business up to an annual limit.

The maximum annual amount of the AIA was increased to £500,000 from 1 April 2014 for companies or 6 April 2014 for unincorporated businesses until 31 December 2015. George Osborne has now told us in the Summer Budget what the 'permanent' amount will be from 1 January 2016. It is £200,000.

What have also been confirmed are the transitional provisions to calculate the amount of AIA in an accounting period which straddles the date of change. Two calculations need to be made:

1. A calculation which sets the maximum AIA available to a business in an accounting period which straddles 1 January 2016.
2. A further calculation which limits the maximum AIA relief that will be available for expenditure incurred from 1 January 2016 to the end of that accounting period.

It is the second figure that can catch a business out. For a company with a 31 March year end, under calculation 1 the company will be entitled to up to £425,000 of AIA ($9/12 \times £500,000 + 3/12 \times £200,000$). However for expenditure incurred on or after 1 January to 31 March 2016 the maximum amount of relief will only be £50,000 ($3/12 \times £200,000$).

So check with us what will be the tax efficient capital expenditure limits between 1 January 2016 and the end of the accounting period for your business.

Maximising tax relief for two homes

The UK tax regime provides an important relief from the capital gains tax charge (CGT) on the gains made by owner-occupiers on the sale of their private homes. This is known as Principal Private Residence relief (PPR).

The general principle is that only one home can count as a PPR at any one time. However prior to 6 April 2014, where a private home qualified for PPR at any stage during the period of ownership, the last three years of ownership qualified for PPR, even if the property was not lived in during that three year period. That period was reduced for most individuals to 18 months for disposals made on or after 6 April 2014.

Although the period has been reduced there is still useful tax planning that can be achieved for someone who has recently acquired an additional property which will also be a home, for example a property 'in the country' which will be lived in at various periods in the year. The example shows the potential advantages of making a 'PPR election'.

Example

Mr and Mrs White have lived in a property in Leeds for a number of years. They are now semi-retired and acquire a second property in Wales in which they intend to also reside. They start to occupy the Welsh property on 1 June 2015.

As the Leeds property already qualifies for PPR up to 1 June 2015 the gains accruing on a time apportioned basis to the last 18 months of ownership will be relieved even if they nominate the other property to be their PPR.

They therefore elect for the Welsh property to be their PPR on 1 December 2016. This means this property will also benefit from PPR for the last 18 months of ownership.

They may vary that nomination back to the Leeds property at any time. If the variation is made within a short period of time then any resulting gain on the Leeds property will likely be covered by their annual exemptions.

If they want to change their minds again about the nomination, they can do so. However none of this flexibility is available if the first election has not been made to HMRC within two years of the time when the second property became available to live in.

Last year the government issued proposals to remove the ability for everyone to make an election but it has changed its mind. Instead the government has implemented changes which affect non-resident individuals with property in the UK and UK residents with property abroad.

Prior to 6 April 2015, an individual who was not resident in the UK was not subject to UK CGT on residential property so could sell the property free from UK CGT irrespective of the availability of PPR relief. From 6 April 2015 UK residential property classed as 'dwellings' is brought into UK CGT for non-UK resident persons.

Further changes restrict the availability of nominating a property for PPR. Examples of the individuals affected by these changes are:

- UK residents who go to work abroad and acquire an overseas second home in the country in which they work
- individuals who retire overseas but keep their homes in the UK.

They may be entitled to PPR for the period prior to 6 April 2015 but will have difficulty in getting the PPR to apply to the UK property after that date. However the last 18 months of ownership may continue to qualify for PPR.

Please contact us if you consider these changes affect you or you wish to consider making an election for PPR where you have two homes in the UK.

