

# KENNETH EASBY LIMITED

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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 Sharon Adams as Senior Tax Consultant. After obtaining a Mathematics degree at Durham University, Sharon trained with Grant Thornton in Newcastle and qualified as a Chartered Accountant in 1992. She moved to a local firm, where she qualified as a Chartered Tax Adviser in 1994, with distinction. She was made Tax Partner at that firm in 1997, where she remained until 2014, when she joined Kenneth Easby Limited.



Sharon has accumulated considerable expertise and experience in providing tax advice and proactive tax planning services to owner managed businesses, professional practices and high net worth individuals. Her role at Kenneth Easbys is to expand the range of tax work of the practice across all three offices and to ensure we provide the highest quality of tax advice to all our clients in a prompt and effective way.

## Exam Success

Congratulations go to Tom Burt of our Bedale office who has recently passed his final exams and is now a fully qualified Chartered Accountant.



## SPRING 2015

### Residential reductions

One of the welcome announcements in the Autumn Statement included the immediate reform of Stamp Duty Land Tax (SDLT) on the purchase of residential property.

Until this announcement SDLT was charged at a single percentage of the price paid for the property, depending on the rate band within which the purchase price falls. This created a distortion as the tax due jumped at set thresholds and deterred potential purchasers. For example a house with a value of £255,000 attracted a charge of £7,650 as it was subject to the 3% rate yet if sold for £250,000 (or less) only a 1% charge applied reducing the cost to £2,500.

For contracts which complete on or after 4 December 2014 SDLT will be payable at each rate on the portion of the purchase price which falls within each band, rather than at a single rate on the whole transaction value as follows:

Price of residential property	Rate
£0 - £125,000	0%
£125,001 - £250,000	2%
£250,001 - £925,000	5%
£925,001 - £1,500,000	10%
£1,500,001 and above	12%

The effect of the changes means that all purchasers of residential property valued at less than £937,500 will pay less tax than they would have paid under the old rules.

For example using the property above valued at £255,000. The SDLT will now be £2,750. This is calculated as 0% on £125,000, then 2% on the next £125,000 and 5% on the final £5,000. This is a saving of £4,900!

The measures will only apply in Scotland until 1 April 2015 when the new land and buildings transaction tax (LBTT) takes effect. This will also operate on a progressive basis with LBTT payable at each rate on the portion of the purchase price which falls within each band. The price at which SDLT and LBTT produce the same liability on a residential purchase is set to be £333,000. Prices below this will produce a saving under LBTT.

If you require any assistance or further information about the operation of SDLT or LBTT please do not hesitate to contact us.



# No relief for incorporations

Owner managers have increasingly chosen to operate their businesses through the company medium in recent years as some regulation has reduced for the smaller company and because it is more conducive to minimising personal tax and National Insurance liabilities. Various reliefs exist for those who start as an unincorporated business who wish to transfer into a company arrangement so that tax costs can be minimised. However, it is considered that some of these reliefs are too generous with some obtaining a potentially unfair tax advantage so two key changes took place with effect from 3 December 2014.

## Corporation tax relief for goodwill

Corporation tax relief is given to companies when goodwill and intangible assets are recognised in the financial accounts. Relief is normally given on the cost of the asset as the expenditure is written off in accordance with Generally Accepted Accounting Practice or at a fixed 4% rate, following an election. This is subject to the general proviso that it is a transaction on or after 1 April 2002.

The rules allow relief to be claimed even when there is continuing economic ownership, referred to as a related party transaction. For example, on incorporation of a sole trader or partnership business where the individual(s) transfers their business to a company provided that the business itself commenced on or after 1 April 2002. For valuation purposes the rules require that the goodwill in such circumstances is recognised by the related party when the asset is transferred at market value.

However, an anti-avoidance measure has been announced to restrict corporation tax relief where a company acquires internally-generated goodwill and certain other intangible assets from related individuals on the incorporation of a business.

The measure means that corporation tax relief can no longer be obtained on such assets on acquisition. Relief is still available if a loss arises on a subsequent realisation of the asset.

## No Entrepreneurs' Relief

In addition, individuals will be prevented from claiming Entrepreneurs' Relief on disposals of goodwill when they transfer the business to a related company. Capital gains tax will be payable on the gain at the normal rates of 18% or 28% rather than 10%.

This means that to relieve capital gains arising on goodwill and any other affected intangibles transferred to the company, only the deferral reliefs will be available. Deferral of gains can be achieved through business asset holdover (gift) relief, Enterprise Investment Scheme holdover or what is known as 'incorporation' relief. These alternative reliefs have different criteria and conditions of usage and will result in either the individual or the related company incurring the deferred gain on a subsequent event. Please contact us for further information about these alternatives if you are considering incorporating your business.

These measures will apply to all transfers on or after 3 December 2014 unless made pursuant to an unconditional obligation entered into before that date.



# Capital or Revenue expenditure? That is the question.....

Should a client face an enquiry from HMRC into their tax return and accounts, a common area that is reviewed is any deduction that may have been claimed in the accounts for repairs and renewals. This arises because whilst a repair to an asset is an allowable item of expenditure for tax purposes, if the asset is altered, improved or replaced the expenditure is capital expenditure and is not allowable. Capital allowances may or may not be allowable on this capital expenditure.

Recently, HMRC have published revised guidance in their internal manuals about what they accept is a repair for tax purposes.

One point that the guidance focuses on is the concept of the entirety. Over many years there have been a number of court decisions on this area following disagreements between taxpayers and HMRC. In general terms if the entire asset has been replaced this will be treated as capital expenditure, whereas if less than the entire asset has been replaced this will be treated as revenue expenditure and is therefore tax deductible.

The guidance stipulates that what actually forms the asset or the entirety is a question of fact and that the question to decide is whether the asset is a separate distinct asset or if it is part of a bigger asset. For example:

- Does it look like a separate asset?
- Is it something that stands apart from other assets?
- Is it freestanding or is it something that is removable?

Another important test to consider, especially where there has been a lot of work undertaken, is to consider if the character of the asset has changed as a result of the work. In simple terms, is it the same object both before and after the work is undertaken? If it is like for like in that the asset simply does the same job as before then this is an indication that the work is a repair, but if the function or capacity of the asset is altered or improved then it is capital.

The following examples which are based on HMRC updated guidance illustrate these points.

### Example 1

Pat is a dairy farmer and the driveway leading to her farm is in a very poor state of repair having been initially created some 30 years ago.

The Dairy Company advise Pat that the driveway is causing damage to their milk tanker vehicles and refuse to call at the farm until it is repaired.

Pat has the driveway repaired at a cost of some £25,000. The tarmac is removed and the sub-surface repaired.

It is then re-surfaced with new kerbing added to bring the driveway up to modern standards.

Even if the driveway is an asset in its own right the entirety has not been replaced. It has been re-surfaced and the expenditure is allowable for tax purposes as a repair.

The drive was not widened nor was its load bearing capacity increased, so no improvement was involved.

**Example 2**

Pedro runs a farm near Clacton-on-Sea and has diversified so that he has a number of chalets that are used as a furnished holiday lettings business. One of the chalets is damaged beyond repair and Pedro replaces it with a new chalet of the same model. As most of the cost is covered by insurance, Pedro only has to spend £3,500.

For tax purposes the chalet is an identifiable asset in its own right. Pedro has replaced the asset in its entirety and the expenditure is therefore capital expenditure and is not tax deductible as a repair.

This is an area where the incorrect tax treatment can cause potential difficulties with HMRC and key to a successful outcome is planning in advance and documentary evidence so please do contact us if you are considering carrying out this type of substantial expenditure.

# Improving the Construction Industry Scheme (CIS)

In Budget 2014 the Government announced that it would consult on options to improve the operation of the CIS and on the introduction of mandatory online CIS filing for contractors. The consultation has now taken place and the legislative process will commence in April 2015.

## Turnover test for gross payment status

Currently the turnover test for gross payment status requires businesses to have a construction turnover, excluding VAT and the cost of materials, of at least £30,000 each year for a sole trader, or £30,000 for each partner or director, with a minimum turnover level of £200,000 for the whole partnership or company. This limit has been in place since 1999 and it is estimated that 90% of sole trader subcontractors have turnover below the £30,000 limit.

There is no intention to change the £30,000 turnover test for sole traders but the proposals to take effect from April 2016 are to lower the threshold for the entity turnover test to help more established businesses with multiple partners or directors qualify for gross

payment status. The current threshold of £200,000 is to reduce to £100,000.

## Compliance test for gross payment status

The other test that has to be satisfied to obtain and retain gross payment status is the compliance test and there have been complaints that the detailed obligations make it difficult to pass and minor infringements result in the loss of status.

To ensure that smaller businesses are not disadvantaged compared to larger ones the test will be simplified but will still include an obligation to:

- submit monthly CIS returns on time
- submit income tax and corporation tax self-assessment returns on time

- pay all CIS, PAYE and National Insurance contributions on time.

## CIS online

At present, contractors can submit monthly CIS returns by paper or online. The Government is proposing mandatory online filing of monthly CIS returns from April 2016. Improvements will be made to the IT systems to provide a better CIS online service. There will continue to be an alternative method of filing for customers unable to file online by reason of age, disability or remote location.

## NIL returns

At present, contractors are obliged to submit a monthly CIS return whether or not any payments have been made to subcontractors. Failure to do so can result in a penalty being charged.

The intention is to remove the obligation to report a nil return from April 2015 and thus remove the potential for a penalty to arise in these circumstances. However, when a return is not received by the filing date, HMRC systems will not know whether the reason is because the contractor is simply late filing the return or there is no return due. Therefore, HMRC intends to operate a simple nil voluntary notification to enable contractors to notify them if they did not pay subcontractors and this will stop a penalty notice being sent out. Otherwise the online appeals service can be used to make an appeal on the basis that no payments were made to subcontractors.

## Online verification of subcontractors

At present, contractors have to verify if subcontractors can be paid gross or whether a withholding tax has to be made from the payments. This verification can be undertaken by telephone or online. The proposal is to remove the telephone option, other than for non-routine cases from April 2017. In the meantime, improvements are to be made to the online verification process.

Please contact us if you require any further advice on this area.



# State Pension top up – is it for me?

Pensioners will, from later this year, be able to purchase up to a maximum of £25 per week extra State Pension. This has been introduced by the Government so that those pensioners who have done less favourably under the existing State Pension rules get an opportunity to top up their State Pension, before the new flat rate State Pension system is introduced.

Existing pensioners and those who reach State Pension age before 6 April 2016 can gain this additional State Pension by paying Class 3A Voluntary National Insurance contributions. In essence it will provide an opportunity for pensioners to improve their retirement income by obtaining inflation-proofed extra State Pension.

In order to qualify there are two entitlement conditions:

- You must have reached State Pension age before 6 April 2016, and
- You must have an entitlement to a UK State Pension (either basic State Pension or additional State Pension).

The rules on additional State Pension will apply to entitlements resulting from Class 3A contributions including inheritance. This means that a surviving spouse or civil partner will be entitled to at least 50% of the additional State Pension.

## But isn't there already an existing top up system?

Yes, at present workers approaching retirement can make Class 3 Voluntary National Insurance contributions which allow people to fill gaps in their contributions record. For example, if someone has accrued less than the 30 years of contributions to qualify for the full basic State Pension.

The new scheme is not replacing these arrangements and the Government is advising pensioners to ensure that they have full entitlement to the basic payment before purchasing the new top up.

## Who will benefit?

The Government have identified a number of existing pensioners and people who could benefit:

- people who may have lost out because of the structure of the legacy State Second Pension system
- hard pressed pensioners, especially those who rely on their capital to supplement their income
- people with small amounts of pension savings
- women who paid the married woman's reduced contribution rate, who are not eligible to pay Class 3 contributions for the years in which the married woman's stamp was in force.

## How much will it cost me?

This is a key question. The top up has been set at an actuarially fair rate ensuring a fair deal for both contributors and the taxpayer. Prices will be lower for older pensioners simply because on average they will have a shorter life in retirement at the point they take up Class 3A. The rates are the same for males and females.

As an illustration for a person aged 65, the contribution required to receive an extra £1 pension per week is £890. To receive an extra £5 per week the contribution would be £4,450.

Further illustrations of cost can be found at [www.gov.uk/state-pension-topup](http://www.gov.uk/state-pension-topup) and accessing the personal calculator.

## I am interested when will this be available?

There will be a short 18 month window to apply commencing 12 October 2015 and ending 1 April 2017.

If you are interested in obtaining further information you can register your interest at the above web address to receive updates in advance of the commencement date. Additionally a dedicated telephone line facility is available on 0845 600 4270 (0345 600 4270 from mobile phones).

# Restricting relief on residential lettings

Capital allowances are generally not available for common items of plant and equipment such as white goods used in a residential lettings business.

Instead for many years, owners of partly furnished residential lettings used the non statutory renewals basis which was a concessionary treatment allowed by HMRC. On the original acquisition of an asset, such as a fridge, no tax deduction could be made against the letting income. However, when the fridge was replaced a full deduction could then be made.

Owners of fully furnished residential lettings were allowed to either use a 10% 'wear and tear' allowance which is based on rents received less some standard expenses or the non statutory renewals basis.

The non-statutory renewals basis ceased to have effect for expenditure on replacements of plant and machinery when incurred on or after 6 April 2013 (1 April 2013 if a company). This means that no tax relief is available for such replacements.

Following correspondence with HMRC, they have stated that the owners of partly furnished residential lettings cannot use a different relief known as the statutory renewals allowance as an alternative except in limited situations. This allowance would typically be used to obtain a tax deduction for the replacement of small low cost implements or utensils, for example glasses in a public house or cutlery in a café.

However, they have confirmed that they will accept in respect of a residential lettings business, low value items such as crockery, rugs and low cost soft furnishings which are replaced on a regular basis to qualify under this basis. However, this would not extend to items such as carpets as they are of a potentially higher value and are not expected to be replaced on a regular basis.

Specifically, HMRC have advised that anything freestanding, such as a fridge freezer are not covered as they are capital items and entireties in their own right. However, where they are an integral part of a fixture, such as an integrated oven in a fitted kitchen, these are part of the entirety (the house) and therefore would be deductible as a repair when replaced.

As you can see this is an area where the incorrect tax treatment can cause potential difficulties with HMRC. Please contact us for further advice.

