Important note:

We have made best efforts to make sure that the information in this document is accurate, but you should check any points and ensure they apply to your particular situation.

It is advisable to seek the advice of a tax advisor, accountant, or independent financial advisor.

Mayfield
Business Forum

Tax Efficiency Briefing Notes

Prepared by Ray Reeve

For the Mayfield Business Forum Meeting

On 4th November 2014

Ref No.	Tax Considered	Briefing Notes
1	All taxes	Keep all valid receipts to support any claims you make for tax allowable expenses. The general rule for what is allowable is that it must be “wholly and exclusively for business purposes”.
2	VAT	Even if you are below the VAT registration threshold of £81,000, it may be worth voluntarily registering on the “flat rate scheme”. You must be below £150,000 turnover to qualify for the scheme but it can result in significant financial benefit and is very simple to operate. You charge your customers VAT at 20% and only pay HMRC the relevant flat rate % of gross sales, which is calculated to be low enough as to offer a benefit. Under the scheme, you do not need to account for any VAT paid out on purchases (that’s allowed for in the flat rate %) so it’s very simple.
3	Employers National Insurance	On 6th April this year the government introduced a £2,000 Employment Allowance for all employers that opt-in to the scheme. The effect is that the first £2,000 of the employer’s class 1 national insurance contributions does not have to be paid over to HMRC.
4	Corporation Tax and / or Income Tax	On 6th April this year the government increased the Annual Investment Allowance to £500,000 on most types of plant and machinery (including office furniture and equipment but not cars). The effect is that for most capital purchases the full cost is allowed in the first year, against either corporation tax (in the case of companies) or Income tax (in the case of self employed). There is clearly a big advantage to capitalising expenditure and putting it through the books.
5	Corporation Tax and / or Income Tax	When the asset you want to put through the books is a car, Capital Allowances come into play instead of the Annual Investment Allowance. In this case, the cost of the car is allowed over several years, against either corporation tax (in the case of companies) or Income tax (in the case of self employed). Cars with low CO_2 emissions are allowed at 18% of the written down cost value per year whereas, cars with normal or high CO_2 emissions are allowed at 8% per year. As with plant and machinery, there is clearly a big advantage to capitalising expenditure on cars and putting them through the books.

6	Business Rates	You can apply to the council for “small business rates relief” if you only use one property and your rateable value is less than £12,000. You’ll get 100% relief until 31 March 2015 for properties with rateable value of £6,000 or less. The relief gradually reduces from 100% to 0% for properties with rateable values between £6,001 and £12,000.
7	Employees National Insurance	To take advantage of this tax benefit you need to be a limited company rather than self employed. But in many cases the savings are large enough to warrant setting up a company. The primary threshold band for National Insurance Contributions (NICs) is currently between £111 and £153 per week. So, if you pay yourselves between £111 and £153 per week (between £5,772 and £7,956 per year) there is no National Insurance to pay but the government deems the payment to be made; thereby protecting all your state benefits (maternity, sickness, pension, job seekers, etc.). You then top-up your earnings with dividends, which attract no national insurance contributions. Class 1 national insurance is currently levied at 12% of gross earnings above the primary threshold of £7,956 per year - up to the upper earnings limit of £41,865 per year - and then 2% on all earnings above that threshold. So if you pay yourself £50,000 per year (say £7,000 salary and £43,000 dividends) you save £41,865 - £7,956 = £33,909 @12% = £4,069 plus £50,000 - £41,865 = £8,135 @ 2% = £163. A total saving of £4,232 - worth having.

Top tax saving tips for small businesses

1 Get your structure right

The way that a company is set up has significant implications for the amount of tax payable. Whilst many small businesses still trade as sole traders or partnerships, the majority would actually pay less tax and NI if they converted to a limited company. The key is to structure pay and dividends efficiently. As a guideline, any company with profitability in excess of £20k would justify a consideration of incorporation. A director of a limited company can withdraw a total of £38,074 during 2013/2014 without having to pay any additional income tax or national insurance.

A structure involving both a limited company and an unincorporated business can be very tax efficient, especially if anticipating high growth and profitability in the future. This utilises advantageous tax rules relating to Goodwill and involves building up the unincorporated business until it has a decent value. It can then be sold to the limited company for its market value, with significant tax benefits.

2 Paying yourself

Consider your method of drawings from the business. If a limited company, paying a small salary up to the personal allowance and the balance as dividends is normally the most efficient method, however this is not always the case. From 6th April 2013, the optimum salary for a director/shareholder would be £7,690 p/a. The maximum amount of dividends payable without incurring the 40% tax rate would then be £30,384. The salary should be paid as a director's fee rather than as a wage to avoid National Minimum Wage regulations.

You may consider splitting your shareholding with your spouse, as you could benefit from using your other half's tax allowance (especially if they have no other source of income), but only if they play an active part in running the business.

Dividends are not subject to National Insurance Contributions, which represents a significant tax saving compared to the sole trader route, where NICs are payable on all income. Make sure you only declare dividends when there are sufficient accumulated profits in the company to do so. Penalties will apply to any dividends which have been declared illegally.

Consider the timing of your dividend declarations. You may save tax by delaying drawing down profits until a future tax year, if you have already reached the higher rate (or additional rate) threshold in the current year.

3 Claiming expenses

Make the most out of the expenses you can put through your company. As long as you only ever claim for things that have been genuinely incurred on business duties, there are savings to be made. You may be able to claim for the costs of working from home, for example (see (5) below).

Put any mobile phone you have in the business name and all costs of the phone are deductible (you do not have to split business vs non-business calls).

4 Cars

In most cases it is best to run your own vehicle personally and claim mileage using HMRC authorised mileage rates, where you trade via a limited company this will avoid large taxation charges on the use of company cars in most cases.

5 Capital Expenditure

The Annual Investment allowance at 100% has been increased on a temporary basis to £500,000 until 31st December 2015. It is therefore essential to plan purchases carefully to maximise the relief available, particularly where the accounting year end spans the date of the change.

6 Working from home

If you work from home you will be able to claim a deduction to cover part of your home running costs. HMRC allows (a modest) £4/week flat rate without requiring any evidence. If you spend a significant amount of time working from home then it is likely you will be able to claim more using the "appointment method".

7 Married couples/civil partners

Married couples/civil partners who are shareholders in, or work in the business should ensure that their finances are arranged to utilise each personal allowance £9,440 basic for 2013/14 (£10,660 for those born before 05/04/1938 and £10,500 for those born between 06/04/1938 and 05/04/1948) and lower rate tax bands (£34,370 for 2012/2013). It might be sensible to transfer income producing assets to a spouse to take advantage of their lower taxable income.

8 Pensions schemes

Pension contributions tend to be deductible expenses for the company, and suffer no immediate tax charge on the individual. Pension contributions provide tax relief at your marginal tax rate so could save up to 60% in tax, subject to the annual maximum of £50k in 2012-13 and 2013-14. You can also take advantage of any unused allowance from the previous three years.

Where an individual's adjusted net income for 2012/2013 is more than £100,000, their personal allowance will be reduced by £1 for each £2 of excess. Consider making individual pension contributions to preserve personal allowances. Individuals could save £3,776 in 2013/2014 at 40 per cent, or more if relief is available at 50 per cent. This is because adjusted net income is reduced by individual pension contributions. However, the impact of pension anti-forestalling rules and the reduced annual allowance needs to be borne in mind. It may therefore be advantageous to transfer income-producing investments to a spouse.

Consult an Independent Financial Adviser for more information.

9 Employee childcare costs

You can use a salary sacrifice scheme to pay for employees' childcare costs of up to £243 per month tax free. Childcare voucher schemes are tax free for the employee and the business operating the schemes incur no Employer's National Insurance. For higher rate taxpayers joining schemes after 6 April 2011 the level of the tax exemptions may be limited but this will be determined by a "basic earnings assessment" carried out by the employer.

10 Where you work for only one client

Where you work for only one client, or a number of clients on short term engagements, you may have to consider the impact of IR35. IR35 was legislation introduced to ensure that there was no avoidance of tax by the use of limited companies. Broadly where the relationship between the worker and client would have been one of employment had the limited company not have been imposed between the worker and the client then IR35 applies. If you work for just one client then IR35 could apply. This would mean that there would be significant extra national insurance charges etc. imposed on the worker. Factors such as the use of a substitute, holiday pay and mutuality of obligation would be some of the relevant factors used to ascertain whether the worker comes within IR35.

11 'Patent Box'

If you have intellectual property in the form of patents you can reduce your corporation tax bill to 10% for all activities related to the patent.

12 Late payment of tax

Whatever you do, make sure you meet your accounting and statutory deadlines, especially for submission of the Annual Return (AR01) and your company accounts. The penalties for late submission can be great and automatic penalties are now imposed if you do not file your Self Assessment Tax Return on time. There is an automatic £100 fine if you do not file your return by 31 January following the end of the tax year (by 31 October if you are filing paper returns).

You may find it useful to open a separate savings account for the business and keep some money back each month for the eventual tax bills. As a company, you should think of depositing approximately 25% of your profits each month (before any dividends) for your future corporation tax bill. As a sole trader a sensible figure would be 30% of your profits to allow for your self-assessment tax plus class 4 National Insurance. As a sole trader you could open a mini cash ISA to store these savings and let the money grow tax free.

13 Utilise family tax allowances

If spouses, children or other relatives aren't using their Personal Allowance (currently £8,105), there may be legitimate ways of ensuring this is maximised. For example, children can legally work from the age of 13, which means that children and other relatives are eligible to carry out basic tasks for your business. However, these activities must be relevant and justifiable. There are also ways of splitting assets to reduce the tax rate on the income.

If you have children over 18 with skills that are useful to the business, they can either be paid as an employee or can form their own company and invoice you. For example, they may be able to help with design work, IT, website administration or creating business apps. This can also be a good way of funding university costs, rather than from your own income, taxed at up to 40%.

14 Make use of tax efficient investments and payments

ISAs provide tax free income. The annual contribution limit is £11,280, of which £5640 can be in cash. It's also worth considering the new Junior ISA for under 18s where £3600 can be invested.
Other tax efficient investments include Enterprise Investment Schemes (EIS), Venture Capital Trusts (VCT) and Seed EIS (which may be suitable for small business investments where your shareholding is less than 30%).
You can invest up to £200,000 in a VCT which gives you 30% tax relief on the initial investment (if you hold it for 5 years); the VCT is also free of Capital Gains Tax (CGT). After 5 years you may be able to reinvest your initial investment and obtain a further 30% tax relief.
With EIS investments you can invest up to £1m and get 30% tax relief if you hold them for 3 years. There is an added benefit for an investor who has a CGT liability – this can be deferred by investing in EIS and after three years will become exempt.

15 Plan to save Inheritance Tax

HMRC saves the largest tax until you're not around to protest. However, there are many things you can do to avoid IHT. With careful planning you could increase your inheritance by 67%.

If you have concerns about your children frittering away the assets, rather than leaving assets to them directly, they could be left in a trust. This way your children still have the same access to the assets, but if they get divorced or go bankrupt, for example, these assets won't be lost but will still be in trust for your children's benefit. As an added benefit, this kind of planning could also protect assets from care fees.

16 On sale of your business

Subject to eligibility (e.g. you must have held shares in the company and been a director or employee for a year or more), you may qualify for Entrepreneurs' Relief on the sale of your limited company. The current ER rate is a mere 10%, compared to standard CGT rates of 18% or 28% (higher rate).

17 VAT

You must register for VAT if your turnover reaches £81,000 over the past 12 months (2014/15 tax year). HMRC has recently been clamping down on businesses who have failed to do so, and you could be fined. You have three options:

a) joining the Flat Rate VAT Scheme. Not only does this make your VAT accounting simpler, but you may pay less tax overall depending on the amount of VAT you charge, and reclaim. During the first year, you receive an additional 1% discount on the flat rate you have to pay to HMRC.

b) the VAT cash accounting scheme offers more of a cash flow benefit than ‘tax saving’ per se – it allows you to only account for VAT once an invoice has been paid as opposed to being issued.

c) the standard scheme for businesses, where VAT is due once an invoice has been issued, as opposed to when the invoice is paid.

Important note:

a) For all of the above the advice of a tax advisor, accountant, or independent financial advisor should be sought before proceeding.
b) Useful information can be obtained from the HMRC website.

Ross Management Accountancy

Tax Efficiency and Opportunity Briefing Notes for Mayfield Business Forum
Prepared by Gavin Ross 4 November 2014

Enterprise Zones

- There are twenty four Enterprise Zones throughout the UK where the government offers a range of incentives to new businesses.
- The closest of these to us is probably the London Royal Docks which includes London City Airport.
- You may not have considered this as an opportunity but I have recently helped a company obtain £600k of investment funding which although it meant moving the future production to another area of the country it gave them the funds they were struggling to find.
- http://enterprisezones.communities.gov.uk/

Seed Enterprise Investment Scheme (SEIS)

- This is a scheme implemented by the government in 2012 and it complements the Enterprise Investment Scheme (EIS). They are both all about tax efficient ways of investing giving real encouragement to high net worth individuals to invest in your business.
- Both schemes are complicated and have many pitfalls to avoid and manage so it is important to have careful expert advice and assistance.
- SEIS is geared towards smaller investments and fledgling companies allowing the investor to invest up to £100,000 with income tax relief of 50% of the sum invested. There is also capital gains reinvestment relief and relief from capital gain on shares held for more three years.
- http://www.seiswindow.org.uk/
- http://www.hmrc.gov.uk/seedeis/

Enterprise Investment Scheme (EIS)

- As with SEIS the rules are very detailed and need to be followed carefully.
- Under EIS the investor can invest up to £1 million but has lower income tax relief set at 30%. If in the event the investment fails then the remaining 70% is allowable against income tax in the year of the loss.

Ross Management Accountancy
Upper Floor, 39a High Street, Heathfield, East Sussex TN21 8HU
Tel: 01435 865606 Email: gavin@rossma.co.uk

- Like SEIS if the shares are held for at least three years any capital gain is exempt from capital gains tax.
- It is worth noting that shares issued under both SEIS and EIS schemes are exempt from inheritance tax once they have been held for a two year qualifying period.
- http://www.hmrc.gov.uk/eis/part2/2-5.htm

Research & development tax credits

- This scheme allows small and medium sized companies to apply for tax relief of 225% of the R&D cost i.e. for each £100 of qualifying costs, your company or organisation could have the income on which corporation tax is paid reduced by an additional £125 on top of the £100 spent. It also includes a payable credit in some circumstances.

- Which costs qualify for R&D Relief?

  i) To qualify as R&D, any activity must meet the definitions set out by the Department of Trade and Industry (DTI). (This organisation is now known as the Department for Business, Innovation and Skills).These guidelines state that the activity must contribute directly to seeking the advance in science or technology or must be a qualifying indirect activity. (Follow this link for more information http://www.hmrc.gov.uk/manuals/cirdmanual/cird81300.htm

  ii) If your company and the project both meet the necessary conditions, then you can claim tax relief on revenue expenditure (generally, this means costs incurred in the day-to-day running of the business - not capital expenditure on assets) in the areas outlined below, if all necessary conditions are met.

  iii) If you've spent money on something such as staff costs where the employee was only partly engaged on R&D activities, you can only claim for an appropriate proportion of the cost.

- http://www.hmrc.gov.uk/ct/forms-rates/claims/randd.htm#2

Ross Management Accountancy
Upper Floor, 39a High Street, Heathfield, East Sussex TN21 8HU
Tel: 01435 865606 Email: gavin@rossma.co.uk

Patent Box

- Enables companies to apply a lower rate of Corporation Tax to profits earned after 1 April 2013 from its patented inventions and certain other innovations. The rate is 10% phased in over five years with 100% applicable from 1 April 2017
- http://www.hmrc.gov.uk/ct/forms-rates/claims/patent-box.htm

Office at home

- If you use part of your home for your business then you can claim the proportion of costs for this part of your home including business telephone calls, extra gas and electricity.
- Do be aware the proportion you make this claim for may be calculated as a capital gain when your home is sold.
- https://www.gov.uk/tax-relief-for-employees/working-at-**home**

Use of car in business

- You are allowed to claim the business proportion of the running costs for your vehicle. This can either be calculated by totalling all the running costs of your vehicle for the accounting period and allowing the business proportion of the period mileage as a cost or by taking the business mileage and applying HMRC's rates.
- These are 45p per mile for the first 10,000 miles and then 25p per mile.
- Unless the running costs of your vehicle are extremely high you will find the pence per mile allowance is far more beneficial.
- https://www.gov.uk/government/publications/rates-and-allowances-travel-mileage-and-fuel-allowances/rates-and-allowances-travel-mileage-and-fuel-allowances

Introducing assets to your business

- If you introduce personal assets into your business not only can you reimburse yourself for the value of the asset but this value is then applicable for capital allowances within the business. This includes for example, cars, computers, tools, desks etc.
- The value of the asset should be based on its value at the time it is added to the business not the purchase cost.
- http://www.hmrc.gov.uk/manuals/bimmanual/bim45690.htm

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Tel: 01435 865606 Email: gavin@rossma.co.uk