

Newsletter February 2008

This month we have included details of the Chancellor's proposed changes to the Capital Gains Tax legislation which will now take place on 6 April 2008. The expected concessions to ease the impact of CGT on certain business sales are included. We have also included a check list outlining personal tax planning opportunities pre 6 April 2008, a discussion of the associated company dilemma, and finally an article about code numbers!

Our next newsletter is due to be published on Wednesday 5th March 2008.

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Employment Law Myths

Employment Law is continually changing and it's easy to get your wires crossed! Here are some Employment Law myths that you may think are true!

No employment contract exists if there is nothing in writing

Even verbal agreements are binding. Obviously, where terms are agreed orally, the situation is ripe for dispute at a later date, and it therefore makes sense for employers to ensure that the terms agreed are put in writing.

An employee does not begin to accrue service for the purpose of statutory rights until completion of any probationary period

Probationary periods have no meaning in law, so the existence of a probationary period will not affect a new employee's length of service or statutory employment rights. Statutory rights – including the right not to be unfairly dismissed – that are dependent on a minimum period of service will be based on length of service from the employee's original start date, not from the date that marks the end of the probationary period. You can, however, specify that different procedures apply during the probationary period, although this must be clearly stated in the Contract of Employment.

A worker can be accompanied by a union official at a discipline or grievance hearing only if the employer recognises the relevant union

Under the Employment Relations Act 1999, workers have the right to be accompanied at a disciplinary or grievance hearing by a companion of their choice who is a full-time trade union official, a lay trade union official or another of the employer's workers. There is, however, no requirement for the trade union to be recognised by the Company. If the worker is a member of a non-recognised trade union, he or she may be accompanied by an official from that trade union. Indeed, there is no necessity for the worker to be a member of any trade union to be accompanied by a trade union official, although, in practice, trade unions rarely support workers who are not their members.

New Factsheets

We now have over 60 client information factsheets on our website. These factsheets cover starting up in business, general business, corporate and business tax, VAT, employment issues, employment and related matters, personal tax, capital taxes, pensions, ICT and specialist areas. We hope you will find them useful.

Capital Gains Tax Update

As expected the Chancellor has bowed to the small business lobby and offered a reduced CGT charge for gains realised on the disposal of certain businesses after 5 April 2008 - details are highlighted below. All the other declared changes to CGT are to go ahead. They will affect the tax charge on all disposals after 5 April 2008. There will be winners and losers in the process!

In a nutshell indexation and taper relief will no longer be available from 6 April 2008. All gains, with the exception of the gains on disposal of certain business assets, will be taxable at a flat rate of 18%. If you own assets which have appreciated in value since purchase you should certainly take a look at the possible opportunities to utilise the existing indexation and taper relief before 6 April 2008. The clock is now ticking!

Entrepreneur Relief - The Revenue have called the reduced rate which will be applied to gains on disposal of certain businesses, as Entrepreneur Relief. The basic details are:

- The first £1m of qualifying gains will be subject to tax at a flat rate of 10%. Gains in excess of £1m will be taxed at 18%.
- The £1m is a lifetime limit. So it will be possible for an individual to make a series of qualifying gains at the 10% rate as long as the cumulative total does not exceed £1m, and the other conditions are met.
- The new relief is based on the broad principles of the now extinct Retirement Relief. Unlike Retirement Relief the new rules will be simpler - there will be no minimum age limit, and taxpayers will qualify if the relevant conditions are met for just one year. (The qualifying period for Retirement Relief was 10 years.)

Personal Tax Planning reminders 2007-2008

Readers may like to scan the list of possible tax planning options that could be considered prior to 6 April 2008. The list is not complete. Tax payers with complex affairs should consider a formal review before the end of the present tax year.

Savings:

1. Maximising ISA's for younger savers.
2. Maximising ISA's for other savers.
3. Appropriate redistribution of savings among family members with differing tax rates, to reduce overall tax spend.
4. Utilisation of Child Trust Funds.

Pensions:

1. Consider maximising contributions for the year.
2. Non-tax payers can also contribute up to £3,600 per annum with no earnings.

Inheritance Tax:

1. Utilising available allowances and reliefs to protect assets from excessive IHT risks.
2. Time to review Wills to ensure they are compatible wealth protection strategies.

Capital Gains Tax:

1. If appropriate make sure you utilise your Annual Exemption, £9,200, for 2007-2008.
2. Consider inter-spouse transfer of assets with "pregnant" gains if the other partner has capital losses which will not otherwise be utilised.
3. Review portfolios to consider holdings that may have negligible value for tax purposes. This offers opportunities to reduce other taxable gains in the current tax year.

Charitable Giving:

1. Consider Gift Aid donations. The same gifts made after 5 April 2008 will result in slightly less cash benefit to charities as the tax they will reclaim on your donations will decrease from 22% to 20%.

Associated companies and corporation tax

Most smaller companies pay corporation tax on their profits at the "Small companies rate" - presently 20%. However if profits exceed £300,000 the average rate of corporation tax payable gradually increases, until at profits of £1,500,000 and above all profits are taxable at the main rate of corporation tax, 30%.

Enterprising entrepreneurs might be tempted to make the most of the small companies rate, and transfer certain parts of their businesses to separate companies. If each separate company made profits of £300,000 or under, the possible tax saving could be significant - a reduction in tax payable from 30% of "grouped" profits, to 20%.

Not surprisingly the Revenue saw that strategy coming, hence the Associated Company rules.

Basically if two, on the face of it, separate companies are owned or controlled by persons who the tax man considers to be "Associated" then the amount of profits that each company can earn at the small companies rate (20%) is reduced pro rata. For example if two companies are judged to be associated in this way each company can earn up to £150,000 at the 20% rate. (£300,000 divided by the number of associated companies, in our example 2.)

It is easy to see that companies may be associated if they are both owned and controlled by the same person(s). Unfortunately the Revenue will also associate companies owned by the following groups as well.

1. Husband, wife, or civil partners, including separated but not divorced couples.
2. Parents, grandparents and more remote forebears.
3. Children or grandchildren or remoter issue.
4. Brothers or sisters, including half siblings but not step.
5. Business partners.
6. Certain trustees or personal representatives.
7. Certain beneficiaries of a settlement, or estate.

It is beyond the scope of this article to describe in detail the interesting possibilities that these associated groups can produce. For example spouses of business partners can be taken into account. To add to the mix the Revenue have also granted a concessionary treatment in the case of certain related persons, whose separate business interests have no "substantial commercial trading interdependence". (This concession does not extend to husbands, wives and minor children.)

So beware. If a husband and wife each own totally independent businesses, they will be associated under these rules. Consequently each company can only earn up to £150,000 at the 20% corporation tax rate. Substitute any of the other 7 categories listed above and potentially large numbers of companies may be associated. If 6 companies are associated each can only earn up to £50,000 at the 20% rate.

If you are concerned that you may be caught by these rules, please call to discuss. This is a complex area of taxation, with its own unique "grey" areas.

Adjustments to your tax code

Employees and employers receive periodic updates to tax code numbers. This number is used by your employer/pension provider to calculate the amount of tax you are stopped on your salary and/or pension.

If your affairs are straight forward (and you are not able to claim certain age related allowances) you are entitled to earn the first £5,225 of your income in 2007-2008, tax free. If this were the case your code number would be 522L.

If your code number drops, to say 200L, you will pay more tax each pay period. If the tax code increases, you will pay less tax. (But see note on K codes below.)

We have listed below a number of generalised factors that may affect your code number. The list is not comprehensive so do contact us if you receive a code number adjustment that is difficult to understand.

1. **Reduction for unpaid tax in earlier years.** If you had underpaid tax in the tax year to 5 April 2006 by say £500 the Revenue will allow you, in certain circumstances, to pay the tax back in a following tax year. To facilitate this, the Revenue will deduct an amount from your tax code. For instance if you are a standard rate tax payer, currently 22%, your tax allowances would need to be reduced by £2,272 to effectively recover the £500 you owe. (For those of you who like to see the maths this is calculated by dividing £500 by 22 and multiplying the result by 100 = £2,272). On your notice of coding you would see a reduction in your code number from say 522L to 295L. (522-227).
2. **Reduction for benefits provided by employer.** If your employer provides you with a company car, or private medical insurance, or indeed any other form of benefit, without an adjustment to your tax code you would always owe the Revenue the tax on the benefit at the end of each tax year. So that this does not happen your code number will be reduced accordingly. The reduction works by deducting the value of the benefit from your code; thus a benefit of £500 will result in a reduction in your code number of £500, i.e. 50 points.
3. **Reduction for higher rate tax payers.** If your earnings are part subject to tax at 40%, and they include significant interest received or dividend income, you will owe the higher rate tax on your investment income at the end of the tax year. To counter this the estimated higher rate tax on your non-salaried/pensionable income will be recovered by reducing your tax code. As your interest and dividends received are taxed at the basic rate, only the marginal increase above the tax already deducted will be taken into account.

What happens if the reduction in your code number is more than your present code?

K Codes - If your tax free allowance of £5,225 is reduced by £2,272, as in example 1 above, you will still have a positive tax code of 295L. If however the deduction from your tax allowance is £10,000 you will have changed a positive tax free deduction of £5,225 into a negative position of -£4,775. This "negative deduction" is actually taxable income. Instead of receiving a tax free allowance of £5,225 you are being taxed on additional income of £4,775.

Your tax code could be changed from 522L to -477L. In their wisdom the Revenue have chosen to display -477L as K477. When you see a tax code prefixed by the letter "K" add on a zero and this is the equivalent income being added to your tax assessment for the year. The larger the K code, the more tax you will pay - although the revenue cannot take more than 50% of your salary in tax in this way!

Tax Diary February/March 2008

1 February 2008 - Due date for corporation tax due for the year ended 30 April 2007.

19 February 2008 - PAYE and NIC deductions due for month ended 5 February 2008. (If you pay your tax electronically the due date is 22 February 2008)

19 February 2008 - Filing deadline for the CIS300 monthly return for the month ended 5 February 2008.

19 February 2008 - CIS tax deducted for the month ended 5 February 2008 is payable by today.

28 February 2008 - Last day to pay your balance of self assessed tax for the year ending 5 April 2007 in order to avoid interest and surcharges. Payment made after this date will be subject to a 5% surcharge on tax outstanding, plus interest.

1 March 2008 - Due date for corporation tax due for the year ended 31 May 2007.

19 March 2008 - PAYE and NIC deductions due for month ended 5 March 2008. (If you pay your tax electronically the due date is 22 March 2008)

19 March 2008 - Filing deadline for the CIS300 monthly return for the month ended 5 March 2008.

19 March 2008 - CIS tax deducted for the month ended 5 March 2008 is payable by today.

DISCLAIMER - PLEASE NOTE: The ideas shared with you in this email are intended to inform rather than advise. Taxpayers circumstances do vary and if you feel that tax strategies we have outlined may be beneficial it is important that you contact us before implementation. If you do or do not take action as a result of reading this newsletter, before receiving our written endorsement, we will accept no responsibility for any financial loss incurred.

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