

News update from Hillier Hopkins LLP January 2005

New Years Tax Solutions



Tax is a subject that excites very few people. It is easy to ignore awkward issues involving tax, such as those mentioned in this newsletter. Don't - it could cost you dear. It's a good idea to review your tax affairs at least once a year and the period leading up to the end of the tax

year on 5 April is the best time to do this. We summarise the more important year end tax tips to help you identify areas that should be considered. As always we would be delighted to discuss with you the issues involved and any appropriate action you may need to take.



Income tax saving ideas for all the family



Married couples are taxed separately. They may therefore have opportunities to reduce their total income tax liability.

Consider the split of income between husband and wife. A transfer of assets (which must be outright and unconditional) may serve to redistribute income and reduce or eliminate higher rate tax liabilities. For example it may be possible to save in excess of £8,000 a year by moving £35,000 of savings income from an income-rich spouse to one with no income. This level of tax saving is unlikely to be possible for many but significant savings can be made by much smaller transfers of income. Moving just £1,000 of savings income from a higher rate taxpaying spouse to one with income below the personal allowance (£4,745) will save £400 a year.

Income arising from assets owned jointly is generally split equally between the spouses unless a declaration is made to the Inland Revenue stating that the asset is owned in unequal shares. This election can be made

on a Form 17 but must be made before the income arises. Consider such a declaration when a new jointly owned asset is acquired. The exception to the equal splitting rule is dividend income from jointly owned shares in 'close' companies which is split according to the actual ownership of the shares. Close companies are broadly those owned by the directors or five or fewer people.

Income tax savings may be made if you are self-employed. Your spouse could be taken into partnership or employed by the business. This could be just as relevant for a property investment business producing rental income as for a trade or profession. Extreme caution must be exercised - the Inland Revenue is looking at such situations to ensure they are commercially justified.

A spouse could be employed by the family company. However, the level of remuneration must be justifiable and payment of the wages must actually be made to the spouse. The National Minimum Wage rules may also impact.

Parents must remember that their children are also potentially within the tax system. It may be possible to utilise the children's personal allowances and starting/basic rate tax bands. However, any income arising to a child but deriving from a parent will be taxed on the parent while the child is unmarried and under 18. This rule applies to income from outright gifts by parents as well as to income from trusts set up by parents.

Call Joel Harding on 01923 809414 or email joel.harding@hhllp.co.uk for more information.

National Savings children's bonus bonds (for children under 16) are a means by which parents can provide capital for their children, which earns tax-free interest. For children born from September 2002, the government is introducing a Child Trust Fund planned to be operational from April 2005. Information booklets and vouchers are currently being sent to parents. Please talk to us for further details.

Income to use the child's personal

allowance could be provided by:

- income deriving from capital provided by relatives other than parents (grandparents, uncles, aunts etc)
- distributions from family trusts (set up by relatives other than parents)
- employing teenage children in the family business - remember there is now a National Minimum Wage of £3 per hour for 16 and 17 year olds.

Remember that dividend income is not an effective way to utilise the personal allowance - the tax credits are not repayable. Ensure other sources of income are available to use the allowance.

Taxpayers aged 65 and over are able to claim higher personal allowances. The benefit of these allowances is eroded where income exceeds £18,900. In such circumstances a move to capital growth or tax-free investments may preserve the higher age allowances.

For more information contact Ben Sherwood on 01442 220713 or email ben.sherwood@hhllp.co.uk



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NI Issues



Entitlement to a state pension

Where a spouse is employed by the family business, the earnings are often kept below the national insurance (NI) threshold to avoid payment of contributions.

For 2004/05 it is worth paying earnings of between £79 (the lower earnings limit) and £91 (the earnings threshold) per week. There will be no employees' contributions due on the earnings but entitlement to a state retirement pension and certain other benefits is preserved. No employer contributions are payable unless earnings exceed £91 per week in 2004/05. Note that the lower earnings limit will be £94 per week in 2005/06.

A PAYE scheme would be needed to establish the employee's entitlement to benefits.

Small earnings exemption

For the self-employed there is a requirement to pay a flat rate contribution (Class 2). If your profits are low you can apply for exemption. The limit for 2004/05 is £4,215. If contributions have been paid for 2004/05 and it subsequently turns out that earnings are below £4,215 a claim for repayment of contributions can be made. The deadline for this claim is 31 December 2005. On the other hand it may be advisable to pay the contributions in any event in order to maintain a contributions record. The alternative voluntary Class 3 contributions are £5.10 a week higher.

For more information contact Marie Cowen on 01296 480516 or email marie.cowen@hhllp.co.uk



Family Companies - Maximising the potential, minimising the extraction costs

A director/shareholder of a family company can extract profits from the company in a number of ways. The two most common are by way of bonus or dividend. For every £1,500 net paid to the higher rate taxpaying individual, the cost to the company is £2,000 if a dividend is paid and £2,322 if a bonus is paid. This assumes the company is liable to corporation tax on its profits at the small companies rate of 19%. There are many issues to consider in making the decision but paying a dividend can often result in significant tax savings.

If the payment of bonuses to directors or dividends to shareholders is contemplated, careful thought must be given as to whether payment should be made before or after the end of the tax year. This will affect the payment date for any tax and may affect the rate at which it is payable. Remember that any bonuses must be paid within nine months of the company's year end to ensure tax relief for the company in that period.

Call Joel Harding on 01923 809414 or email joel.harding@hhllp.co.uk for more information.

Using tax efficient investments

Some investments benefit from a favourable tax status. We consider the main ones below. Any investment decision should involve consideration of all the relevant factors, including the risk level and the need for income and capital in both the short and long term, as well as the tax advantages.

ISAs

The tax advantages of stockmarket ISAs have been reduced over the years. In most cases basic rate taxpayers save no tax at all by investing in ISAs. The small saving for higher rate taxpayers on dividends and protection from Capital Gains Tax means that higher rate taxpayers should still consider investing via ISAs as long as fees do not outweigh any anticipated benefits.

Since 6 April 2001 it has been possible for 16 and 17 year olds to open a cash ISA. The contribution limit is £3,000 a year. Care must be taken to ensure the funds to open such an ISA did not come from the child's parents. In that case the income would be taxable on the parents if, with any similar income, it exceeded £100 a year.

TESSAs

It has not been possible to open a new TESSA since April 1999. On maturity, the capital (but not interest) could be transferred into the cash component of an existing maxi ISA, or into an existing mini cash ISA or into a TESSA-only ISA within six months of maturity without affecting the annual ISA investment limits.

PEPs

Although new PEPs have not been available since April 1999, it is possible to consolidate single company PEPs with a general PEP or create a general company PEP out of single company PEPs. This has the advantage of allowing more flexibility for sales and purchases of investments.

Other Investments

There is a wide range of National Savings products, eg NSB savings accounts, savings certificates and bonds. These are taxed in a variety of ways. Some, such as National Savings Certificates, are tax-free.

For those whose income may fall in the future, for example due to retirement, investments deferring income to a subsequent period may be attractive. For example single premium life assurance bonds and 'roll-up' funds can achieve this effect.

There are numerous more complicated investment products. Some of these offer, or purport to offer, very significant tax savings. In nearly all cases where significant tax reliefs are available for investment (except pensions) these reliefs exist to encourage investment in areas where the chance of significant gain or loss is substantial. In other words they tend to be higher risk investments. Where risk has been engineered away but substantial reliefs appear to be available the Revenue will take a close interest.

Expert advice is essential before investing in any of these schemes. Examples include:-

Enterprise Investment Schemes (EIS), Venture Capital Trusts (VCT), Film partnerships and Enterprise Zone Trusts (EZTs). We often recommend against investing in these schemes.

For more information contact Ben Sherwood on 01442 220713 or email ben.sherwood@hhllp.co.uk



Pensions - plan ahead - don't take a chance on your future!

There are many opportunities for pension planning but the rules can be complicated. Furthermore the government plans to change the rules on the taxation of pensions very significantly from April 2006. We will of course keep you informed of the detail of the changes but in the meantime if you want to discuss pension planning further please talk to us.

Pensions have received a particularly bad press in recent times for a variety of reasons. However the tax relief on pension contributions, still at 40% for a higher rate taxpayer, is attractive. Pension planning therefore forms an important part of a year end tax planning review.

Employees who are members of an occupational pension scheme attract tax relief on additional voluntary contributions to the extent that, together with the employee's other contributions, they do not exceed 15% of remuneration.

The self-employed or those in non-pensionable employment obtain tax relief for payments under personal pension contracts (PPCs). Individuals can contribute £3,600 (gross) per year with no link to earnings. This makes it possible for non-earning spouses and children to make substantial contributions to pension schemes. Further contributions can be made depending on age and earnings levels, generally referred to as net relevant earnings (NRE).

Furthermore the NRE of a particularly good year can be used as the basis of contributions for that year and the next five. If NRE increases in future years, a new base year can be notified to the pension provider.

If an individual stops work, goes abroad or retires, they have no NRE. This has previously meant that no further PPCs could be made. However, where an individual ceases to have NRE, they can look at the year of cessation or any of the previous five years and select the best NRE figure. This can then be used as the NRE figure for the five years after cessation.

Different rules apply to those paying old style 'retirement annuity premiums' under policies that started before 1 August 1988.

Family company directors should consider making additional employer's contributions to existing company pension schemes. If a spouse is employed by the company, consider including them in the company pension scheme or setting up such a scheme for the purpose. Even where salary levels are modest, such a scheme can provide significant benefits.

Remember that pension funds can no longer reclaim dividend tax credits. There may be a case for making extra contributions to compensate for the potential loss of income.

For more information contact Ben Sherwood on 01442 220713 or email ben.sherwood@hhllp.co.uk



Deadlines looming for employers

Ignore them at your peril! Remember that in most instances interest will be charged on tax paid late and penalties can be levied if forms are late or incorrect.

19 April 2005 - Interest will run on any 2004/05 PAYE and NIC deductions not paid over by this date.

19 May 2005 - Employers' year end returns (P35/P14/P38) due for submission.

31 May 2005 - Employees must be provided with their P60 (certificate of pay and tax deducted).

6 July 2005 - Submission of P11Ds and P9Ds returning details of expenses paid and benefits provided to employees and directors. A copy of the P9D/P11D must also be given to each employee.

A dispensation, allowing certain items to be omitted from the forms, can be granted by the Inland Revenue.

19 July 2005 - Class 1A NIC for 2004/05 on most benefits in kind provided to employees must be paid. Interest runs from this date on late payments.

19 Oct 2005 - PAYE settlement agreement liabilities for 2004/05 due, together with Class 1B NIC. Interest runs from this date on late payments.

Electronic filing and payment

Large employers (those with 250 employees or more) have been required to pay their PAYE to the Inland Revenue electronically since May 2004. They will also have to file their 2004/05 end of year returns

electronically. Medium employers (those with between 50 and 249 employees) will be required to file their 2005/06 end of year returns electronically.

Employers' action points

Contact us if:

- you have any concerns over the accuracy or completeness of your PAYE records
- you need assistance with the completion of P11Ds or application for a dispensation.

Have you thought about

- a PAYE settlement agreement as a useful way to account for tax on minor benefits provided to employees
- obtaining a dispensation.

Benefits for employees

Much of the planning for employment income (including directors' remuneration) focuses on the provision of tax efficient benefits. However, most taxable benefits in kind give rise to employers' (but not employees') national insurance. To discuss remuneration packages and the provision of benefits further, please contact Joel Harding on 01923 809414 or email joel.harding@hhllp.co.uk for more information.



Most people aim at nothing.....and hit it with amazing accuracy



When did you last do any strategic planning for your business or personal life? If the answer is more than three years ago – you're in danger of not realising your dreams.

Adrian Baker, Managing Director of Doric Signs Ltd., appreciated this and wanted to address two areas in particular, succession planning and sustaining long term growth.

Doric, a key player in the signage industry and founded in 1957, made its name by manufacturing signs for the British Rail network and the National Health Service and now develops solutions across a wide range of applications.

Colin Howe, Hillier Hopkins LLP's Managing Partner, took them through a process of Strategic Planning unlocking a

number of key issues that were affecting Doric's growth. Colin was able to better prepare Doric by focussing their business efforts, planning for future growth and tying this in with an achievable strategy.

Call Colin Howe on 01442 220738 or email colin.howe@hhllp.co.uk for more information on our Strategic Planning service.



Capital gains tax



Could you benefit from planning ahead?

If you have assets that could give rise to capital gains tax (CGT) when sold then here are some points to consider.

- Each individual has an annual exemption of £8,200 for CGT purposes. Review your chargeable assets and consider selling before 6 April 2005 to utilise the exemption. Note that husband and wife both have their own annual exemption. A transfer of assets between them may enable them both fully to use this. Bed and breakfasting (sale and purchase) of shares is no longer effective. However sale by one spouse and repurchase by the other, or sale outside an ISA and repurchase inside, can achieve the same effect. This can be done either to utilise the annual exemption or to establish a capital loss to set against gains.
- Children also have their own annual exemption and this may be utilised by investing for capital growth.
- Traded or 'second hand' endorsement policies (SHEPs) can also produce gains to utilise the annual exemption. An unwanted policy is acquired and paid to maturity. On maturity, the proceeds payable less the acquisition cost and premiums paid creates a capital gain. Careful planning could lead to £8,200 of gain per family member being realised every year tax-free.
- If a planned disposal is likely to give rise to a gain in excess of the annual exemption and therefore a CGT liability, then it may be better to defer it until after 5 April 2005 as this will delay the payment of CGT. The due date will be deferred from 31 January 2006 (for 2004/05) to 31 January 2007 (for 2005/06).
- Deferral of a gain to a later date may also give a higher rate of taper relief. This can make a very significant difference to the ultimate chargeable gain. Capital gains can be deferred by investing via the EIS scheme.
- If you have two homes then consider making an election so that future gains on your 'main residence' are exempt from CGT. Talk to us if this is relevant for you.
- Remember that capital losses can be established by making a claim where assets no longer have any value - a 'negligible value' claim.

For more information contact Debbie Wilson on 01442 220710 or email debbie.wilson@hhllp.co.uk

Charity watch - please give generously!



No doubt many of you have donated to the recent Asian Tsunami appeal, a disaster that has touched all our hearts, but could we give more generously?

The government continues to make favourable changes to the rules on tax efficient charitable giving. There are a number of ways of securing tax relief on charitable donations.

Example 1 - Alex makes a one-off donation under Gift Aid. The scheme potentially applies to any charitable donation large or small, whether regular or one-off. The charity is able to claim basic rate tax (at 22%) back from the Inland Revenue. As a higher rate taxpayer Alex will also qualify for 40% tax relief on the gift. Tax relief against 2004/05 income is possible for charitable donations made between 6 April 2005 and 31 January 2006 providing the payment is made before filing the 2004/05 tax return.

Example 2 - Ben agrees to a regular deduction from his salary under the Payroll Giving scheme. There is no upper limit on the amount that can be donated in this way. His tax bill is reduced as his PAYE liability is calculated after deducting the charitable donation.

Example 3 - Camilla decides to leave a substantial bequest to charity in her Will. This saves inheritance tax.

Example 4 - David gives some quoted shares to a charity, on which there is a substantial unrealised capital gain. However, no CGT arises on a gift to a charity. The charity can then sell the shares free of CGT providing it applies the proceeds for charitable purposes. Furthermore, income tax relief is available on the value of the shares gifted. The same rules apply to gifts of land and buildings.

For more information contact Marie Cowen on 01296 480516 or email marie.cowen@hhllp.co.uk



Audit...just a legal requirement or is IT a hidden opportunity?



Although a legal requirement, a good quality audit can be extremely valuable in establishing the financial performance of a company, highlighting potential risks and opportunities for the future. However, by only analysing your company's financial performance we cannot see the whole picture, as surely this is affected by every aspect of the business?

Hillier Hopkins LLP is developing a more holistic approach to auditing, assessing your areas of need across all functions of your business, such as:

- financial analysis of your company
- accounting issues that are facing your industry and business
- IT and Marketing audit conducted by a specialist member of staff

- benchmarking reports of your nearest competitors
- an evaluation of existing business conditions and how best to prepare for the future.

Focus on IT

IT is often a key contributor to the growth and profitability of a business. For many companies their IT strategy gives them a clear advantage over the competition. We are now able to offer clients a free IT audit carried out by Chartered IT Solutions, our specialist business solutions company. This gives you a snapshot of how well your systems perform for the business and how they could work harder for you.

To find out how your company can benefit from a free IT audit contact Alan Meaning on 01442 220723 or email alanm@charteredit.co.uk www.charteredit.co.uk



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