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Welcome...

To July's Tax Tips & News, our newsletter designed to bring you tax tips and news to keep you one step ahead of the taxman.

If you need further assistance just let us know or you can send us a question for our Question and Answer Section.

We are committed to ensuring none of our clients pay a penny more in tax than is necessary and they receive useful tax and business advice and support throughout the year.

Please contact us for advice on your own specific circumstances. **We're here to help!**

July 2017

Working from home

top

Over recent years, it has become increasingly popular for employers to allow their employees to work from home, and in doing so, pay an amount to cover any additional household costs incurred. What are the tax implications of such expenses for the employee?

Broadly, **no tax liability will arise where an employer make a payment to an employee for reasonable additional household expenses**, which the employee incurs in carrying out duties of the employment at home under 'homeworking arrangements'.

'Homeworking arrangements' are arrangements between the employee and the employer under which the employee regularly performs some or all of the duties of the employment at home. There is no requirement for any part of the employee's home to be used exclusively for the purposes of the employment - in fact, if any part of the home is used exclusively for work, problems could arise on the future sale of the house as part of the capital gains tax exemption on private residences may be lost.

HMRC have stated that they will accept that homeworking arrangements exist where:

- there are arrangements between the employer and the employee; and
- the employee works at home regularly under those arrangements.

The HMRC guidance also advises that:

'the arrangements need not be in writing but usually will be. They do not need to apply to all employees. The exemption does not apply where an employee works at home informally and not by arrangement with the employer. For example, it will not apply where an employee simply takes work home in the evenings. It applies where an employee works at home by arrangement with the employer instead of working on the employer's premises.'

HMRC accept that the 'regularly' condition is met if working at home is frequent or follows a pattern. The fact that the days spent at home vary from week to week is not a bar to claiming the exemption.

'Household expenses' are defined as expenses connected with the day-to-day running of the employee's home. The exemption applies to additional household expenses, and HMRC have given the following guidance:

'Typically this will include the additional costs of heating and lighting the work area or the metered cost of increased water use. There might also be increased charges for Internet access, home contents insurance or business telephone calls. Where working at home leads to a liability for business rates the additional cost incurred can also be included.

The additional household costs must be reasonable and must be incurred in carrying out the duties. This excludes costs that would be the same whether or not the employee works at home, for example mortgage interest, rent, council tax or water rates. It also excludes expenses that put the employee into a position to work at home, for example building alterations or the cost of furniture or office equipment.'

Amount of exemption

To minimise the need for record-keeping, employers can pay up to £4 per week (£208 per year) without supporting evidence of the costs the employee has incurred. If an employer pays more than that amount, the exemption will still be available but the employer must provide supporting evidence that the payment is wholly in respect of additional household expenses incurred by the employee in carrying out his duties at home.

If an employer wishes to pay more than the guideline rate per week tax-free, then it is recommended that the employer should agree in advance with HMRC a scale rate. Failing that, records will need to be kept of the actual additional costs incurred by each employee.

VAT: zero-rating of adapted motor vehicles

top

Finance Act 2017 introduced legislation designed to end perceived abuse of the VAT relief on substantially and permanently adapted motor vehicles for disabled wheelchair users.

The amended rules, which took effect from 1 April 2017, now specify a **limit on the number of vehicles within a specified period of time that an individual can purchase** under this relief.

An eligible individual will be able to purchase one vehicle every three years. There are some instances when this limit can be exceeded, so if an individual's car is written off or stolen or if the vehicle has ceased to be suitable for the disabled person's use because of changes in the person's condition.

In addition to the new limitations above, there is now a mandatory requirement for eligibility declaration forms to be submitted to HMRC. This form clarifies exactly what information an individual needs to provide to support their claim to a zero rated supply.

Motor dealers are also required to send information regarding these zero-rated sales to HMRC.

Individuals in breach of these new requirements may be denied the benefit of the zero rate, or may be subject to a penalty (under VATA 1994, s 62) if the declaration they make is incorrect.

Rent a room scheme

top

Although Budget 2017 announced that the Government intends to review the rent-a-room scheme, it currently remains **a tax-efficient way of letting out a spare room.** Broadly, HMRC's rent-a-room scheme is an optional exemption scheme, which allows individuals to receive up to £7,500 of tax-free gross income (income before expenses) from renting out spare rooms in their only or main home. The exemption is halved where the income is shared with a partner or someone else. Broadly, as long as income is below the annual threshold, it does not need to be reported to HMRC. If income exceeds the threshold, it needs to be reported to HMRC via the self-assessment system.

In order to qualify under the rent-a-room scheme, the accommodation must be furnished and a lodger can occupy a single room or an entire floor of the house. However, the scheme doesn't apply if the house is converted into separate flats that are rented out. The scheme cannot be used if the accommodation is in a UK home which is let whilst the landlord lives abroad.

The rent-a-room tax break does not apply where part of a home is let as an office or other business premises. The relief only covers the circumstance where payments are made for the use of living accommodation.

Sometimes additional services are provided, for example, cleaning and laundry. The payments for such services must be added to the rent to work out the total receipts. If income exceeds £7,500 a year in total, a liability to tax will arise, even if the rent itself is less than that.

Accounting for tax

Where the annual threshold is exceeded, there are two options available:

- the first £7,500 is counted as the tax-free allowance and income tax is paid on the remaining income; or
- the landlord opts to treat the renting of the room as a normal rental business, working out a profit and loss account using the normal income and expenditure rules.

In most cases, the first option will be more advantageous. The principal point to bear in mind is that those using the rent-a-room scheme cannot claim any expenses relating to the letting (e.g. insurance, repairs, heating).

To work out whether it is preferable to join the scheme, the following mehods of calculation should be compared:

- Method A: paying tax on the profit from letting worked out in the normal way for a rental business (i.e. rents received less expenses).
- Method B: paying tax on the gross amount of receipts (including receipts for any related services they provide) less the £7,500 exemption limit.

Method A applies automatically unless the taxpayer tells their tax office within the time limit that they want method B.

Once a taxpayer has elected for method B, it continues to apply in the future until they tell HMRC they want method A. The taxpayer may want to switch methods where the taxable profit is less under method A, or where expenses are more than the rents (so there is a loss).

Example

During 2016/17, Flo lets out a room in her home. She receives total income of £11,000 (£10,800 rent plus £200 towards bills). She incurs expenses of £3,000. If she uses method A to calculate her tax liability she will pay tax on £8,000 (£11,000 less £3,000). If she uses method B, she will pay tax on £3,500 (£11,000 less £7,500). Flo is better off using method B.

Even though the tax rules for the rent-a-room scheme are different to the general property income tax rules, a resident landlord will still have certain responsibilities towards tenants, particularly in relation to safety. For further information, see the GOV.UK website at https://www.gov.uk/rent-room-in-your-home.

New state pension and contracted-out NICs

top

Most people will be aware that the state retirement pension system has changed for people who reach state pension age on or after 6 April 2016 - that is men born after 5 April 1951 and women born after 5 April 1953. The full new state pension is currently £159.55 per week, but the amount that employees who have previously paid National Insurance contributions (NIC) at the contracted-out rate may be affected under the new system. The introduction of the new state pension from 6 April 2016 brought an end to the contracting-out rules.

In very broad terms, to qualify for the **minimum amount of state pension an individual needs 10 years of NIC contributions.** 35 years or contributions or credits will be needed to qualify for the full amount.

For those people who were already in the workforce at April 2016, transitional arrangements were put in place which means that everyone will be assessed for a 'starting amount' under the new system. Using the number of qualifying years on the individual's National Insurance record as at 5 April 2016, their 'starting amount' will be the higher of either:

- the amount they would get under the old state pension, or
- the amount they would get if the new state pension had been in place at the start of their working life.

Both amounts will reflect any periods when they have been contracted out of the additional state pension.

The rules governing contracting out and new state pension are complex, but broadly, if an individual has a 'starting amount' of less than the full amount of new state pension, then for each 'qualifying year', a certain amount is added to their National Insurance record after 5 April 2016. This equates to around £4.56 a week, (£159.55/35). This amount will be added to the person's 'starting amount', until they reach the full amount of the new state pension, or they reach state pension age, whichever happens first.

For some people it is possible to have a starting amount higher than the full new state pension if they have some 'additional' state pension. The difference between the full new state pension and their 'starting amount' is called a 'protected payment'. Those who have a 'starting amount' which is equal to the full new state pension will get the full new state pension when they reach state pension age. Before the new state pension was introduces, state retirement pension was made of two parts, namely:

- basic state pension, and
- additional state pension, often referred to as state second pension or SERPS (State Earnings-Related Pension Scheme).

If an individual was in what is known as a defined benefit company pension scheme - where what they are paid in retirement is related to salary - they are likely to have been 'contracted out' of the additional state pension. This means that they would have paid a lower rate of NICs and will have earned replacement pension benefits in an employer scheme or a personal pension.

Despite having what they thought were 35 years of qualifying years, they will not necessarily get the full amount of new state pension - although entitlement can be improved by paying contributions after 5 April 2016. The Government has advised that while someone in this situation will get less than the full amount, retirees will still be paid at least what they would have got under the old state pension.

July questions and answers

top

Q. Can I give my house to my children and continue to live in it and avoid inheritance tax?

A. It may be possible if you pay a full market rent for your home, but if you do this, then your children will have to pay income tax on the rent they receive. Capital gains tax may also be payable at some time in the future if they sell the house. The new inheritance tax residence nil rate band (RNRB), which is being phased in from April 2017 over a 4-year period, is designed to help people in your position to pass on the family home to children or grand- children, tax-free after their death. HMRC's guidance Inheritance tax: additional threshold (RNRB) provides further information. Always seek professional advice before entering into any arrangement where the main purpose, or one of the main purposes, is to obtain a tax advantage.

Q. I am thinking of selling a property that I have owned and rented out for the last ten years, and once it is sold, I will reinvest the proceeds in another property. Will I have to pay capital gains tax on the proceeds from the sale even if all the money is reinvested in another property that is also let?

A. Yes, you will be liable to capital gains tax on the gain arising on the sale, even though you will be reinvesting the money in another property that is also let. Rollover relief is available for residential investment property only in relation to qualifying furnished holiday lettings, and for compulsory purchases.

Q. I lent my brother some money, which I borrowed from my company, for him to use in his business. He is paying it back in monthly instalments over three years. What are the tax implications of this loan?

A. I presume that you are a director and a substantial shareholder of the limited company. I also presume that the company lent the money on an interest-free basis.

The tax implications for the company are that the loan is deemed to have been made to an associate of a participator in the company, and as such, it will be caught by what are commonly referred to as the 'section 455 rules'. Broadly, these rules mean that the company will have to pay tax at 32.5% on the amount of the loan outstanding nine months after the accounting year end of the company. When the loan has subsequently been repaid to the company, HMRC will refund the tax paid.

There is an exception to this, namely where a loan does not exceed £15,000, but only when the shareholder does not own more than 5% of the shares.

If an employee of a relative of an employee receives an interest-free loan from an employer, this will be a benefit-in-kind for the employee. Interest at the 'official rate' (currently 3%) is calculated, and this deemed interest is subject to tax. However, there are exceptions to this tax charge where:

- the loan is a 'qualifying loan';
- a qualifying or non-qualifying loan is less than £10,000; and
- the employee can show that they received no benefit from the loan to the relative.

As your brother used the loan for business purposes, it should be a qualifying loan because 'the interest would be deductible in computing the borrower's profit from a trade' (HMRC Employment Income Manual, paragraph EIM26136). With regard to the 'no benefit received from a loan to a relative', HMRC are generally reluctant to apply this when the employee is a director who controls the company.

July key tax dates

top

5 - Deadline for PAYE settlement agreement for 2016/17

6 - Deadline for 2016/17 forms P11D and P11D(b) to be submitted and copies of P11D to be issued to relevant employees

Deadline for employers to report share incentives for 2016/17 - form 42

14 - Return and Payment of CT61 tax due for quarter to 30 June 2017

19/22 - PAYE/NIC, student loan and CIS deductions due for month to 5/7/2017 or quarter 1 of 2017/18 for small employers
Class 1A NIC due in respect of the tax year 2016/17

31 - Second self assessment payment on account due for 2016/17
Second 5% penalty surcharge on any 2015/16 outstanding tax due on 31 January 2017 still unpaid
Deadline for Tax Credits to finalise claims for 2016/17 and renew claims for 2017/18
Half yearly Class 2 NIC payment due
Penalty of 5% of tax due or £300, whichever is greater for 2015/16 personal tax returns still not filed

Need Help?

top

Please contact us if we can help you with these or any other tax or accounts matters.

In addition, if there's anyone else who you think would benefit from the newsletter, please forward the email to them or ask them to contact us to be added to the newsletter list.

New Clients Welcome

top

If you are not already a client and are interested in becoming one, we would love to come to meet with you to discuss how we can help and provide you with a competitive quote for our services.

All new client consultations are provided free of charge and without obligation.

About Us

top

Smith Craven Accountants are based in Doncaster, Sheffield, Worksop and Chesterfield, offering local business owners and individuals a wide range of services.

Visit our website http://www.smithcraven.co.uk for more information.

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