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CHARTERED ACCOUNTANTS
REGISTERED AUDITORS

Action stations – A-Day is fast approaching

A-Day – the start of the new pensions tax regime on 6 April 2006 – is a few short months away. There are many planning points that individuals of all ages and employers should review well before it arrives.

If you are due to retire before the new rules take effect next April, it could pay you to postpone taking your benefits until after A-Day, because you may be able to draw more tax-free cash and enjoy more flexible benefits. However, some people will get less tax-free cash under the new rules, although under complex special provisions, they may be able to protect their rights to excess tax-free cash built up before 6 April 2006.

People with total pension funds of more than the lifetime allowance of £1.5 million, face some difficult choices. It might be worth maximising contributions before A-Day because it may not be possible to make further contributions later.

If your pension fund is likely to exceed the new

lifetime allowance, you will want to protect it against any potential penalty. The options are complex and you will need specialist advice well before next April.

The new rules lift many of the restrictions on investment by self-invested pension schemes, in particular that they will be able to buy residential property. However there will be tighter rules on how much these schemes can borrow and the amounts that they will be able to lend to their sponsoring employer. You should consider any borrowing or loans to the employer before A-Day.

Employers will find that the new rules affect employees in differing ways and may have to rethink their remuneration strategy and retirement provision.

These are just a few of the areas you should review with the help of specialist advice covering your own particular circumstances.

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Taxing work in progress



If your business provides services and there is work in progress at the end of your accounting period, you may have to pay more tax this tax year or next as a result of recent guidance from the Accounting Standards Board. However, well-organised businesses can turn the new rules to their advantage.

Solicitors, accountants and other professionals are all affected, as are other businesses that perform services under a contract over a period

of time, regardless of whether billing is by time spent or per a fixed fee.

The guidance, obscurely entitled *UITF Abstract 40*, makes it clear that service businesses must value their work in progress in their accounts at its full billable value. In a partnership's accounts, this means including the billable time of the partners as well as members of staff. In the past, work in progress was essentially based on the cost of staff time, although it might also have included a proportion of overheads.

The guidance has legal force, but its precise application will vary according to the type of business and contract. The new rules will generally result in an uplift in profits in the first year in which it is implemented. In most cases, this will be the year to 31 March 2006 – with the extra tax payable on 31 January 2007. In

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TAXATION

File online or pay the penalty



Medium-sized employers – those with 50 to 249 employees – must file this year's PAYE return (2005/06) online or face a penalty of £600. The return is due by 19 May 2006. Large employers had to file online with effect from the 2004/05 return. Failing to do so attracts a penalty on large employers ranging from £900 to £3,000, depending on the number of employees.

Large employers must also make their monthly payments electronically and on time by the 22nd day of the month. If cleared funds are not received by the 22nd, or previous working day where the 22nd falls on a weekend or bank holiday, HMRC will issue a default notice. The first default notice initiates a 'surcharge period', which does not

end until there has been a complete tax year without a late payment. For example if an employer first defaults in December 2005, the earliest date that the surcharge period can end is April 2007, and then only if all payments in 2006/07 are on time.

The penalty depends on the number of defaults in a surcharge period and ranges from 0.17% to 0.83% of the year's PAYE liability for each default. There is no penalty for the first two defaults in a surcharge period.

For example, an employer may have a continuing surcharge period in which it has received nine default notices in previous tax years. If that employer then pays late four times in the next tax year, each of the first two of these defaults will be charged at 0.58% (the percentage for the 10th and 11th default) and each of the others at 0.83% (the percentage for the 12th and subsequent defaults). This gives a total penalty of 2.82% of the amount shown on the annual PAYE return. This payment and penalty regime is not being extended to medium-sized employers.

New rules for serious tax fraud enquiries

Most taxpayers will never face an HM Revenue and Customs serious tax fraud investigation but for those who do come under suspicion, there is a new procedure from 1 September 2005. It applies to both direct and indirect taxes, and replaces the separate procedures previously used by the Inland Revenue and Customs and Excise.

HMRC's new Serious Civil Investigation office (SCI), which now handles the most serious cases, will encourage taxpayers under enquiry to make a full disclosure, without revealing details of its concerns. If the taxpayer does so, the SCI will then not undertake any active investigation. But HMRC retains the right to institute criminal proceedings where a taxpayer makes a materially false statement.

A taxpayer who refuses to co-operate will face a full investigation and significantly higher penalties than if they had co-operated. Direct tax and VAT settlements will be negotiated separately for the time being.

As the procedure will be wholly civil, there will be no PACE (Police and Criminal Evidence Act) safeguards, such as the formal caution and tape recording of interviews, which HMRC uses in investigations that may give rise to prosecution.

Plant and machinery leases reform

Plant and machinery leases are often essentially financing transactions – and from 1 April 2006 the tax system will treat them as such. Under the new rules, only the finance charge element of the rentals under the lease will be taxed as income of the lessor and be deductible by the lessee. The lessee, rather than the lessor, will now be entitled to capital allowances on the leased asset. The current tax rules generally treat a plant and machinery lease as the hire of an asset.

The reform will apply to finance leases and some operating leases, though most leases of less than five years will not be affected. Leases in existence before 1 April 2006 will remain under the old rules and transitional rules effective from 21 July 2005 will allow some leases finalised after 31 March 2006 also to remain within the old regime. An HMRC technical note contains details of the proposed changes, which will be included in the Finance Act 2006.



VAT avoidance

Arrangements designed solely to confer a VAT advantage are an abuse of law, but only if they frustrate the purpose of the VAT legislation, according to the Advocate General of the European Court of Justice. His opinion in favour of HMRC in the cases of Halifax plc, BUPA and Huddersfield University, which had entered into separate complex VAT planning schemes, opens the way for HMRC to challenge certain VAT avoidance arrangements. However it stops short of the general anti-avoidance doctrine that HMRC wanted, and upholds the right of businesses to enter into VAT mitigation arrangements provided there is a valid business reason for the transactions in addition to tax planning.

The opinion emphasises that the VAT treatment of transactions must be decided objectively and that the taxpayer's intention is irrelevant. The decision has implications for all types of VAT planning and should reduce uncertainty for businesses.

Discrimination law comes of age

Age discrimination in employment will be unlawful from 1 October 2006. With some exceptions, employers will no longer be able to use age-related criteria in recruitment, selection and promotion, and they will have to be more flexible as regards the age when employees retire. Employers should start reviewing their employment practices and procedures to check whether they need to make any changes.

The retirement rules are likely to make the greatest difference. Businesses will no longer be allowed to set a compulsory retirement age below 65 unless they can objectively justify it, a test that is likely to be difficult to satisfy. Where a business sets a compulsory retirement age of 65 or above, employees will have the right to ask to continue working beyond that age and the employer must consider the request seriously.

Employers will have to follow a set procedure should they want an employee to retire. Failure to do so may result in the employee having a claim for unfair dismissal, since this will no longer have an upper age limit of 65.

Businesses will still be able to have pension

schemes with a commencement age below 65. At present employees cannot start drawing their pension and continue working for the same employer, but this will be allowed from 6 April 2006 under the new pensions regime. Most age-related rules and practices in occupational pension schemes will be exempt from the age discrimination rules.

There will be some scope for different treatment on the grounds of age provided employers can justify it objectively. For example employers may be able to fix a maximum age for recruitment or promotion based on the training requirements of the post or the need for a reasonable period of employment before retirement. And 'positive action' will be permitted, such as encouraging people of a particular age to undergo training if this compensates for disadvantages suffered by such people.

Age discrimination is not only about older workers. For example requiring a certain period of experience when recruiting may



constitute indirect discrimination against very young people. Employers will only be allowed to impose such a requirement if there is a real need for it in order to carry out the work. Graduate recruitment schemes must not exclude older students.

The regulations, which will also cover access to vocational training, will apply to all workers, including contract workers, and job applicants. They will also cover self-employed people contracted to do work personally. In addition, there will be special rules to protect partners in professional firms and barristers from age discrimination.

Equal benefits for civil partnerships

Employers will have to treat members of registered same-sex partnerships in the same way as married couples when the Civil Partnership Act comes into force on 5 December 2005.

For example if employee benefits such as health care are extended to husbands and wives of employees, they must also be made available to civil partners. If an employer gives time off for a wedding, the same should be given for a civil partnership registration ceremony. Employers should examine their policies and procedures to check that married couples and civil partnerships are treated alike, and that employees are aware of the benefits that can be claimed.

Civil partnership will also make available all the tax benefits and obligations of married couples. For example partners will be able to transfer assets to one another free of capital gains tax and inheritance tax. But they will also be treated as connected persons for the purposes of various anti-avoidance rules. For



example if each partner controls their own company, the two companies will become associated to each other if the partnership is registered. This may increase the companies' corporation tax liabilities.

Same-sex partners who claim working and child tax credits will have to make joint claims from 5 December 2005 even if their partnership is not registered. This mirrors the rules that apply to unmarried heterosexual couples. If you are claiming as a

single person but living with a same-sex partner, you must report this fact to HM Revenue and Customs from 5 December 2005. If notification is not made, you could become liable for a penalty on top of having to pay back any overpayment. Claiming jointly may reduce entitlement to tax credits because the claim will be based on joint income. However, in some cases a joint claim will actually increase the amount payable since there might now be entitlement to an allowance for a second adult.

Partners who receive income-related social security benefits, such as income support, pension credit and housing benefit, must similarly inform the Department for Work and Pensions or local authority of their circumstances.

These are just some of the consequences of the civil partnership rules. We will be happy to review their implications in individual cases.

LAW

Intestacy limits set to rise

The amount you can inherit if your spouse dies without making a will could go up. A government consultation paper proposes that a husband or wife in England and Wales should inherit the first £350,000 of an estate where the deceased leaves children, and the first £650,000 where there are no children but where there are surviving parents or siblings.

The current limits of £125,000 and £200,000 were set in 1993, when more than 90% of estates were worth less than £125,000. House price inflation has ensured that in up to 9,000 cases a year a surviving spouse will not receive all of their partner's estate. In some cases the family home must be sold to enable children or other relatives to inherit under the intestacy rules.

The intestacy rules are different in Scotland. There the limits increased in June 2005 and a surviving spouse now has a prior right to the first £300,000 of the deceased's home, or

share of the home, plus specified amounts from other assets.

From 5 December 2005 members of registered same-sex partnerships will have the same rights as a spouse if their partner dies without making a will.

Dying without a will rarely results in distribution of the estate in the way the deceased would have wished. Many people believe that their husband or wife will inherit everything automatically but this is far from the truth. Dying intestate can leave your spouse or partner in financial difficulties, and it is often not tax efficient.

Research carried out in March by Standard



Life suggested that 57% of adults in the UK had not drawn up a will, including 40% of people with homes worth more than £150,000. If you have no will, or have one but have not reviewed it recently, or want to ensure that inheritance tax on your estate is minimised, please ask us for advice.

REGULATION

Money laundering update

Changes to the money laundering reporting requirements have gone a small way towards reducing the burden on accountants, lawyers and others as regards reporting suspicions to the National Criminal Intelligence Service, NCIS.

Reporting parties no longer have to file a suspicious activity report where they know neither the name of the perpetrator nor the location of the laundered property – a requirement that gave rise to huge numbers of reports that NCIS could not act upon. A report now need only be filed where at least one of these details is known or the reporting party has information that would assist in this regard.

Another new rule exempts banks, but not others, from filing a report where the value of the property concerned is less than £250. However there is no start date yet for a further provision that will exclude from the



money laundering rules conduct overseas which is lawful in the jurisdiction concerned but would be a criminal offence if it took place in the UK.

It is estimated that 250,000 suspicious activity reports were made to NCIS in 2004, the first year in which accountants, lawyers, estate agents and sellers of high value goods for cash were included. Failing to report an offence remains punishable by an unlimited fine and/or up to 14 years in prison.

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many other cases it will be the year to 30 April 2006 – with the tax payable on 31 January 2008. There are no provisions for spreading the additional tax over several years, as there was when the cash basis of accounting was abolished.

The additional tax may be substantial and businesses need to gear up for the change now. One obvious question is whether your accounting systems can cope, but more importantly the new rules are an opportunity to maximise financial efficiency. The aim should be to receive payment from clients before the related tax bill becomes due. Work in progress needs to be turned into bills sent to clients throughout the year – not just at the year end. You may need to change engagement letters to allow regular billing on account, and the use of standing orders would improve cash flow. These are best practices that will benefit your business generally, as well as raise the money to pay the tax.

We are keen to discuss all the implications with you and help your business use this change positively. Please contact us for more information.