client briefing

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HMRC fails the grade on guidance

Taxpayers can avoid a penalty for filing a tax return late if they have a 'reasonable excuse'. But HM Revenue & Customs (HMRC) has come under fire for giving taxpayers guidance on what this means that is at odds with the interpretation given by tribunals. HMRC is also being criticised for delays that allow penalties to mount up.

The term 'reasonable excuse' is not defined in the legislation. In a number of recent cases, tax tribunals have criticised HMRC's guidance, which states that taxpayers would have a 'reasonable excuse' when some unforeseeable and exceptional event beyond their control has prevented them from filing the return on time.

Official interpretation 'too narrow'

The tribunal says that HMRC's official interpretation is too narrow, and in particular the tribunal says that the event need not be 'exceptional'. At some tribunal hearings HMRC has now admitted that its definition is wrong, but so far the guidance on its website has not been changed.

Employers face a different problem. If they file their end-of-year returns late they are charged a penalty of £100 per 50 employees for each month or part month that the return is outstanding. But HMRC does not send out the penalty notice until four months after the filing date of 19 May, which means that employers might accumulate a minimum £500 penalty (four months plus part of the fifth) before realising there is a problem.

How to delay tax payments

For many taxpayers the problem is not so much making the return as paying the tax due. If you know that you will be unable to pay a tax bill (including VAT), HMRC might allow you more time to pay. You must, however, contact HMRC's business payment support service before the tax payment is due. You will need to explain why you cannot pay, what steps you have taken to raise the money, how much you can pay immediately and how long you need to pay the rest. Remember that whatever arrangement you set up to pay a tax bill will only be for that liability. You will have to contact HMRC again if you cannot pay another bill.

Paying on time

If you can pay your tax on time, make sure you actually do so. These days many online payments fall within the banks' faster payments system, which means they take two hours to reach the payee's account, but payments to HMRC still take three working days. Bear in mind also that where the due date is on a weekend or bank holiday, the payment must arrive by the previous working day. If, for example, your monthly PAYE payment is due on Sunday 22 January 2012, you should pay it by Wednesday 18 January to ensure it arrives on Friday 20 January.

For VAT, you should consider using direct debit as it gives you another three days before HMRC takes the payment from your bank account, on top of the seven extra days allowed if you file your VAT returns online.

Post haste?

Although HMRC expects taxpayers to get returns and payments in on time, its attitude to dealing with taxpayers' correspondence is more relaxed. Bulk post issued by HMRC often arrives many days – or even weeks – after it is dated and letters to HMRC go astray all too often.

Such problems only reinforce the need to get your tax right and avoid lengthy enquiry correspondence. If you would like further advice on tax deadlines and paying your tax, please get in touch.

Escaping employee tax status

Some people have tried to avoid being taxed as employees by setting up sham contracts.

The IR35 legislation was introduced to tax income from 'disguised employment' at a rate similar to any other employment income. It has been particularly devastating for freelance contractors who often have little choice but to operate through an intermediary company.

However, contractors have been successfully fighting back by using 'IR35 friendly' contracts so that arrangements with clients are outside the scope of IR35. One of the most important factors in such a contract is the right of substitution. Whereas an employee is obliged to perform work personally, in a contractor/client relationship the contractor will normally be free to provide a substitute if they are ill or on holiday.

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But the problem is that actual working practices must match those stated in the contract – so a substitution clause must be a genuine right. The most recent case to be heard, involving Autoclenz Ltd, reinforces this position as it was heard in the highest court in the land – the Supreme Court.

The case concerned car valets who actually wanted to be treated as employees so that they would be entitled to various employment rights. The valets' contracts stated that they were self-employed and contained an express term allowing them to appoint a substitute. However, the court concluded that the contracts did not reflect the true relationship between the parties, and that the valets were in reality employees.

To rely on a substitution clause the right should ideally be included in the original contract, and you, as the contractor, should be responsible for the substitute's recruitment, their work and their remuneration. Although it is unlikely that a client will permit unfettered use of substitutes, the fewer restrictions placed on their use the better.

Bear in mind that just because the right to use a substitute has never been exercised does not mean that it does not exist. If contractors engaged on similar terms have supplied a substitute then this indicates that the right is genuine.

Although substitution clauses are important in establishing self-employed status, there are many other factors to consider. The goalposts for contractors are constantly moving, so contact us if you need advice.

New proposals aid non-dom investment

A new tax relief for non-domiciled individuals who invest in UK business will have no upper limit and be simple to claim, according to a recent Government consultation document.

In the March 2011 Budget the Chancellor, George Osborne, announced that from April 2012 non-domiciled individuals who are taxed on the remittance basis will not be taxed on overseas income and capital gains brought into the UK for commercial investment. The Government has now published more details, although these might change before becoming law.

Under the proposals, tax-free remittances will be allowed for investment in any company carrying out trading activity, or developing or letting commercial property. The only exclusions will be leasing and residential property letting, although building and developing residential property will be permitted. The investment will have to be in a company, but no decision has yet been made on whether the relief will be confined to investment in companies not listed on a recognised stock exchange. It will be possible to invest in shares or loans.

Investment of overseas income and capital gains held in offshore trusts or other investment vehicles will also attract relief. Another unexpected feature is that the investment can be in a company incorporated and trading outside the UK, as long as it has a permanent establishment in the UK. Furthermore, investors can be connected with the company and draw 'commercial remuneration' for any work they do, for example, as directors.

There are to be some anti-avoidance rules. They are directed mainly at preventing non-domiciliaries taking out their investment to enjoy in the UK. When they dispose of an investment, the original amount invested will have to be taken out of the UK within two weeks of the disposal, or reinvested in a qualifying business in the same period. The relief will have to be claimed in the investor's tax return.

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Also starting in April 2012 will be the increased £50,000 annual charge for non-domiciled individuals who claim the remittance basis and have been resident in the UK in 12 or more of the 14 previous tax years. This charge will not be affected by the new relief for business investments. Those who decide not to pay the charge will pay tax on all their worldwide income and capital gains in the year they arise.

Surviving the social media whirl

Many businesses are using social media, such as Facebook, LinkedIn and Twitter, to interact with customers and promote their goods and services in an up to date and customer-friendly way.

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Social media can provide a wide range of opportunities for businesses to communicate with customers, suppliers, employees and the public. But the very flexibility and freedom of social media carry risks as well, so it is important for employers to have a robust social media policy and a well thought-out strategy.

First you need to be clear what you want to achieve and how social media are relevant to your business goals and marketing strategy. Are you aiming to improve your brand presence, for example, or to increase traffic to your company website? Do your research by checking out all the potential sites you might use. Try to understand your target audience. You can also join groups and Twitter chats relevant to your business.

Using social media can make staff more productive by helping them to gather instant information and feedback from customers and prospects, but without an effective strategy it can also be a waste of time and effort. Your staff should understand what you are trying to achieve from your social media strategy and a manager needs to monitor its effectiveness. Employees need training on ways to identify the best approaches to take, how to manage any negative coverage you receive, and on what is acceptable to post, both during and outside working hours. It is good practice for employees to have different profiles for their business and social use.

It is vital to let staff know that messages posted to social media sites will be monitored – and you need to have the technology to do this – and that employers can take disciplinary action against employees who post defamatory comments online that bring their company into disrepute, or disclose confidential information. A combination of training and enforcement should help you to make effective use of social media and protect your business from negative publicity.

A clear written social media policy, which you can incorporate into your staff employment contracts, will strengthen your position if you need to dismiss an employee as a result of unacceptable social media use. Please get in touch if you would like any further advice on these issues.

Annuity rates continue to shrink

Falling government bond yields and increasing lifespans are pushing down annuity rates.

Annuity rates are currently at the centre of a perfect storm:

- Yields on long-term government bonds are at historically low levels.
- Life expectancy continues to increase rapidly – witness the Government's efforts to increase the State Pension Age faster than previously planned.
- Forthcoming new EU rules are making it more expensive for insurance companies to underwrite annuities.

The overall result is that today's annuity rates are low and may not increase again soon – at least not by very much. This means that if you are about to draw benefits from a pension plan, you must review all your retirement income options, including:

Open market annuities

You should never accept the annuity rate from your pension plan company without first checking what is on offer elsewhere. Annuity rate setting has become increasingly refined in recent years. For example, some companies now set rates according to your home postcode. If you are a smoker or in less than perfect health, you may be entitled to an enhanced annuity rate.

Phased retirement

Phased retirement involves drawing on your pension plan in stages, with each year's 'income' consisting of a tax free lump sum and annuity payment(s). This route has the advantage of avoiding the one-off annuity purchase, but it does involve more investment risk. Part of your pension plan will remain invested after your retirement income begins and annuity rates could fall further.

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Income drawdown

Income drawdown – drawing your income directly from your pension fund – is normally only a viable option if you have other sources of retirement income. It can offer considerable flexibility, but in most instances your maximum permitted withdrawal will be much the same as an annuity can provide.

Income withdrawal arrangements virtually always carry investment risk and if this concerns you, an annuity could be a better option.

Solving partnership problems

Partnerships can carry on for years without anyone even thinking about the partnership agreement. Then a problem arises and the partners discover that the agreement is inadequate, out-of-date or – worst of all – might not even exist. A well-designed partnership agreement can help solve a number of problems.

The basic problem is that the provisions of the Partnership Act 1890 apply where there is no specific agreement to the contrary. For example, under the Act, it is not possible to expel a partner.

An out-of-date or non-existent partnership agreement could make it difficult to deal with the problem of an under-performing partner. A partnership agreement might give the majority the right to expel an individual partner or at least the power to alter a partner's status, maybe changing them to a salaried partner.

Different problems can arise if a partner leaves of their own accord. It might be desirable to be able to place an outgoing partner on 'gardening leave' to protect the partnership's business interests. Once a partner has actually left, a restrictive covenant can prevent them from soliciting the partnership's clients. But covenants must be carefully constructed or they could turn out to be unenforceable.

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Partnership agreements should be up to date with changes in the law generally – especially discrimination law. Agreements should therefore provide for parental leave, comply with sex discrimination legislation, and take account of the recent changes regarding age discrimination – particularly the recent abolition of the default retirement age of 65.

Firms that have grown in size may be especially vulnerable. An agreement that worked for a small three or four person partnership may no longer be appropriate. Decisions that could once be taken by all the partners may now have to be delegated to an individual or to a small group.

Every partnership should have a proper partnership agreement and then review it regularly.

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