Summer 2017

Kingston Smith

In this issue:

Professional Firms Insight

Editorial

Welcome to the Summer 2017 edition of Professional Firms Insight.

A lot has happened since our last issue: Article 50 has been triggered, we had the last ever Spring Budget and the Finance Bill was published. Uncertainty prevails in politics, with Brexit negotiations set to dominate over the next two years, and the more imminent question of who will lead them to be settled by the General Election.

In this edition we discuss the key points of what was a low-key Budget. Despite the positive fiscal forecasts, with growth expected to exceed targets and borrowing expected to be lower than previously predicted, the Chancellor gave no notable giveaways in either the reduction of taxes or an increase in spending. Partners in professional firms were facing a 1% rate increase in the main rate of Class 4 National Insurance Contributions until the Government backed down a week after the Budget in the face of the political storm it created. Although, it may turn out to be only a temporary reprieve.

We also examine what steps firms will need to take to access funding for apprenticeships through the introduction of the Apprenticeship Levy, and how they should continue to prepare for Making Tax Digital, despite speculation that the timetable will be pushed back due to the General Election.

Finally, we examine the perplexing rules around the tapering of the annual pension allowance and provide tips and strategies to help individuals plan for the future.

There is no doubt that the current economic and political climate is challenging. But amongst the uncertainty, there is also plenty of opportunity. From our decades of experience, we are well-placed to support dynamic firms in taking advantage of these opportunities to help their businesses thrive. Our team are always on hand to help navigate unpredictable times and help firms grow.

I hope you enjoy reading this edition of Professional Firms Insight.

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New regime for apprenticeships

The Apprenticeship Levy was introduced on 6 April 2017. Employers who pay this levy including those within the professional services sector will now able to access funding for apprenticeships through a new online apprenticeship service account.

The Apprenticeship Levy

The Apprenticeship Levy will be charged at 0.5% of an employer's total pay bill, which is defined as the total amount of employees' earnings on which employer's NICs is paid.

There will be a £15,000 annual allowance available to offset against the Levy, meaning that, for most employers the Levy will only in practice become payable where the total pay bill for the year is in excess of £3 million. However, only one annual allowance is available for all of the PAYE schemes of a firm, and of any connected companies or charities. The relevant employer(s) can decide how the allowance is to be allocated between PAYE schemes (it can be split if desired), but the decision must be reported the first time the Apprenticeship Levy is paid and cannot be changed for the rest of the relevant tax year.

From 6 April 2017, employers need to report to HMRC the amount of Apprenticeship Levy due each month, and then pay the amount to HMRC alongside their income tax and NIC liabilities.

Apprenticeship Funding
Government Funding of apprenticeships changed from 1 May 2017. As a result, employers are now able to register online for apprenticeship service accounts with HMRC.

These new online accounts will be linked to one or more PAYE schemes, and firms that pay the Apprenticeship Levy will start to see funds being credited to these accounts – based on the amount of the Apprenticeship Levy paid, plus a top-up – from the end of May.

ONLY ONE ANNUAL ALLOWANCE IS AVAILABLE FOR ALL OF THE PAYE SCHEMES OF A FIRM, AND OF ANY CONNECTED COMPANIES OR CHARITIES

Through the online account, employers will be able to select appropriate apprenticeship frameworks and standards, choose Government-approved training providers and assessment organisations, and post apprenticeship vacancies.

Firms who pay the Apprenticeship Levy will also be able to agree prices with providers, and use the funds that have been credited to their accounts to pay for training and assessment.

Information on how to register a new account with HMRC can be found here: https://www.gov.uk/guidance/manage-apprenticeship-funds

Making Tax Digital

There has been speculation that the timetable for what will undoubtedly be the biggest revolution in the administration of the UK tax system for decades will be pushed back due to the General Election. This is by no means certain and professional firms should continue to prepare.

Although some details are still unclear, the full implications are gradually being revealed. Software developers are currently working hard to create products that can do everything that will be required of them.

A key plan of the proposals is that all businesses including those within the professional firms sector, will be required to maintain their accounting records digitally, and to provide summaries of these to HMRC on a quarterly basis. The records may be maintained within specialist accounting software, or spreadsheets, but the crucial point is that a business must be able to send the required information to HMRC.

Partnerships, self-employed individuals, and unincorporated landlords, are currently due to be within the regime from their first accounting period beginning after 5 April 2018, except in the following cases:

- Businesses and firms with a gross income of less than £10,000 will not be required to join the regime;
- Businesses and firms with gross income of less than the VAT threshold (£85,000 in 2017/18) will have an extra year before they are required to join the regime;
- Partnerships with a turnover above £10 million are not due to join the regime until 2020.

There will also be exemptions for those who are not able to engage digitally. The regime is due to be extended to encompass VAT requirements from April 2019, with companies due to fall within the regime from 2020.

The figures a business submits quarterly will not need to include accounting or tax adjustments, and HMRC will not be able to enquire into these. There will, however, be a penalty regime, and some businesses are going to need a lot of support to get into a position where they can meet the requirements.

These changes are all part of a larger project, and the intention is that submitted business information will feed into individual taxpayers' Digital Tax Accounts, which will also be automatically populated with other information such as salary, benefits, and bank interest.

As and when partnerships come into the regime, a nominated partner will be responsible for submitting the data on behalf of the partnership, with the optional facility for the data to be "pushed" into individual partners' Digital Tax Accounts.

Ultimately, the Government intends that taxpayers will have a much better grip on their tax affairs throughout the year. The "year-end process" will be massively simplified, with many taxpayers no longer being required to submit a tax return but simply being able to approve the information which will already be sitting in their Digital Tax Account.

Ultimately, Making Tax Digital may bring benefits, but the timetable is ambitious and a lot of work is going to be required over the next few years as the new requirements are introduced.

Spring Budget

The final Spring Budget, delivered on 8 March, was a relatively tame affair, perhaps most memorable for the announcement of an increase in Class 4 National Insurance Contributions which was retracted the following week!

Hoped-for concessions on business rates did not materialise, and, while the fiscal forecasts were generally positive, there were no notable giveaways.

But however low-key the Budget, there are always some tax changes and below is a summary of the forthcoming measures – some of which had already been announced – that are going to be of most interest to professional firms.

Clearly,depending on the outcome of the General Election, further changes could be around the corner.

Business Tax

- The Chancellor announced that the introduction of quarterly reporting requirements under the Making Tax Digital regime will be delayed by one year for businesses and firms with turnover below the VAT threshold. This is a welcome move and will give small sole practitioners more time to prepare.
- As previously announced, the rate of corporation tax will fall from 20% to 19% from 1 April 2017.
- Transitional relief worth £435 million will be made available to support businesses facing significant increases in rates bills from April 2017. However the support announced does not address the major concerns raised by occupiers of offices and retailers in London and the South East who are facing huge increases in their rates bills as a result of the rise in property values in the region.
- As previously announced, from 1 April 2017 there will be a new, higher VAT flat rate of 16.5% for "businesses with limited costs". Currently, businesses determine which flat rate percentage to use by reference to their trade sector. From 1 April 2017, however, they must also determine whether they meet the definition of a "business with limited costs", one whose costs of goods is either less than 2% of turnover, or less than £1,000 per year.

FROM APRIL 2018, ALL PAYMENTS IN LIEU OF NOTICE (WHETHER CONTRACTUAL OR NOT) WILL BE SUBJECT TO TAX AND NATIONAL INSURANCE CONTRIBUTIONS

- The Government announced that it would publish various consultation papers related to the tax treatment of employee expenses and benefits in kind. The general rule for valuing benefits in kind for tax purposes (in the absence of special rules that apply, for example, for company cars and accommodation) is to use the cost to the employer of providing the benefit. This rule works very well for employees where benefits with a high market value can be provided at a low cost to the employer, and we may well expect the taxable value of benefits in these circumstances to increase.
- The tax and employer's National Insurance advantages of salary sacrifice schemes will be removed from April 2017, except in respect of arrangements relating to pensions (including advice), childcare, Cycle to Work scheme and cars with CO2 emissions of less than 75g/km. Arrangements in place before April 2017 will be protected until April 2018, and arrangements for cars, accommodation and school fees will be protected until April 2021.
- From April 2018, all payments in lieu of notice (whether contractual or not) will be subject to tax and National Insurance Contributions in the usual way. In addition, foreign service relief, for employees who have spent time working outside the UK, will be removed and termination payments over £30,000 that are subject to income tax will also be subject to employers' NICs. The first £30,000 of a termination payment will remain exempt from both income tax and National Insurance Contributions.

Personal Tax

- In a measure designed to reduce the difference between the tax treatment of employees and self-employed individuals, the Chancellor announced that the main rate of Class 4 National Insurance Contributions was going to increase to 10% from April 2018 and 11% from April 2019. After much resistance, the Chancellor subsequently announced that there would be no increase during the current Parliament. However, the Chancellor will still need to tackle the tax implications of the growth in self-employment, and we can expect alternative measures to be announced in the Autumn Budget. Class 2 National Insurance Contributions will be abolished from April 2018.
- The tax-free dividend allowance available to all UK taxpayers is to reduce from £5,000 to £2,000 with effect from 6 April 2018. Professionals working through limited companies, or with service companies as part of their structures, are going to be affected by this measure, with those paying tax at the top rate due to suffer an increase of up to £1,143 in their tax liabilities each year.

Tapering of the Annual Allowance

Since 6 April 2016, anyone with an 'adjusted income' of over £150,000 is impacted by the tapering of the annual allowance (AA) to a minimum of £10,000. However, anyone with total earnings above £110,000 may also be affected by the taper rules.

Individuals such as partners in professional firms who have a 'threshold income' in excess of £110,000 in any tax year will have their adjusted income tested to see if this is in excess of £150,000 in that tax year.

The standard £40,000 AA is reduced by £1 for every £2 of adjusted income over £150,000 in a tax year. Thus restricting the level of tax-efficient pension funding that high earners and their employers can make into pension schemes.

The maximum AA reduction is £30,000, so those individuals who have an income of £210,000 or more will have an AA of £10,000.

There are a number of key contributors to an individual's taxable income and these factors can be variable or totally unknown at the commencement of the tax year, such as large bonuses or fluctuations in rental income and partners in professional firms are likely to be among those who's taxable income could be affected in this way.

The rules of tapering can be perplexing and it is important to understand the definitions of threshold and adjusted income to recognise if an individual is affected by the tapered allowance or not.

The two tapering tests are:

Threshold Income includes all taxable income plus salary sacrificed for pension contributions (unless the arrangement pre-dates 8 July 2015), but excludes employer pension contributions.
If an individual's threshold income is less than £110,000 then there are no further tests required and the full AA of £40,000 is available for the 2017/2018 tax year.

The threshold income assessment provides some protection for lower earners who may have significant one-off bonuses or a sizeable ad hoc employer pension contribution.

Adjusted Income is the individuals' taxable income from all sources plus personal pension contributions via net pay arrangements and employer contributions.

For individuals who have defined benefit schemes, AA is calculated by the notional employer contribution to fund the additional benefit accrued and excludes any element of personal contribution into the scheme. Contributions into any other scheme or an AVC are included.

The table below illustrates the impact to the AA:

Individual's 'adjusted income'	Annual allowance
£150,000	£40,000
£170,000	£30,000
£190,000	£20,000
£210,000	£10,000
£230,000	£10,000

Annual Allowance Charge

The AA charge is calculated by the excess contributions being added to the individual's income for the relevant tax year and taxed at their highest rate. This negates the tax benefit of contributing to a pension and for some will result in higher rates of tax being paid.

Carry forward

The carry forward of unused AA from previous tax years still provides higher earners the opportunity to maximise tax-relieved contributions into pensions. AA tapering will be calculated and applied each tax year. Therefore, an individual may have varied AA in different tax years as the AA is dependent upon their income each year.

An individual may have a fully tapered AA for 2017/18 but may have a carry forward allowance for any unused relief from the previous three tax years if they were a member of a registered pension scheme.

Planning Strategies

- The first step for individuals caught by tapering is to consider reducing contributions paid by them and/or their employer which may result in an AA charge. However, reducing employer contributions can have a bearing on future income in retirement years.
- Higher earners can use their carry forward allowance from previous tax years to maximise contributions into their pensions.
- All UK residents can have a pension. It is worth considering making contributions to a spouse's pension, or those of other family members, including children. A net contribution of up to £2,880 (£3,600 gross) can be made regardless of earnings.
- For business owners who can control their remuneration, employer pension contributions are an efficient way of extracting profits and may be viewed as a tax-efficient means of paying a deferred income.
- All UK residents over the age of 16 have an ISA allowance of £20,000 for the 2017/2018 tax year. For a married couple this amounts to £40,000 per household per tax year. Growth and income retained in or distributed from an ISA is tax-free and does not count toward the threshold income test.
- Offshore investment bonds can be useful for providing tax deferred income or growth for individuals who will be moving down through the tax bands in future years, e.g. gearing up for retirement, planning to or currently living abroad.
- Enterprise investment schemes (EIS)[1] and venture capital trusts (VCT)[2] are higher risk than pensions or ISAs, but have significant tax efficiencies such as 30% income tax relief and profits free from capital gains tax. They offer the potential to roll over maturing investments for further tax relief. Because of the enhanced risks, professional financial advice is far more important.

[1]Enterprise Investment Schemes (EISs) are very high-risk investments. An EIS investment is usually concentrated in one single unquoted trading company. Often there is no market for the shares and it may therefore be very difficult to make a disposal. There is a possibility of the chosen company failing.

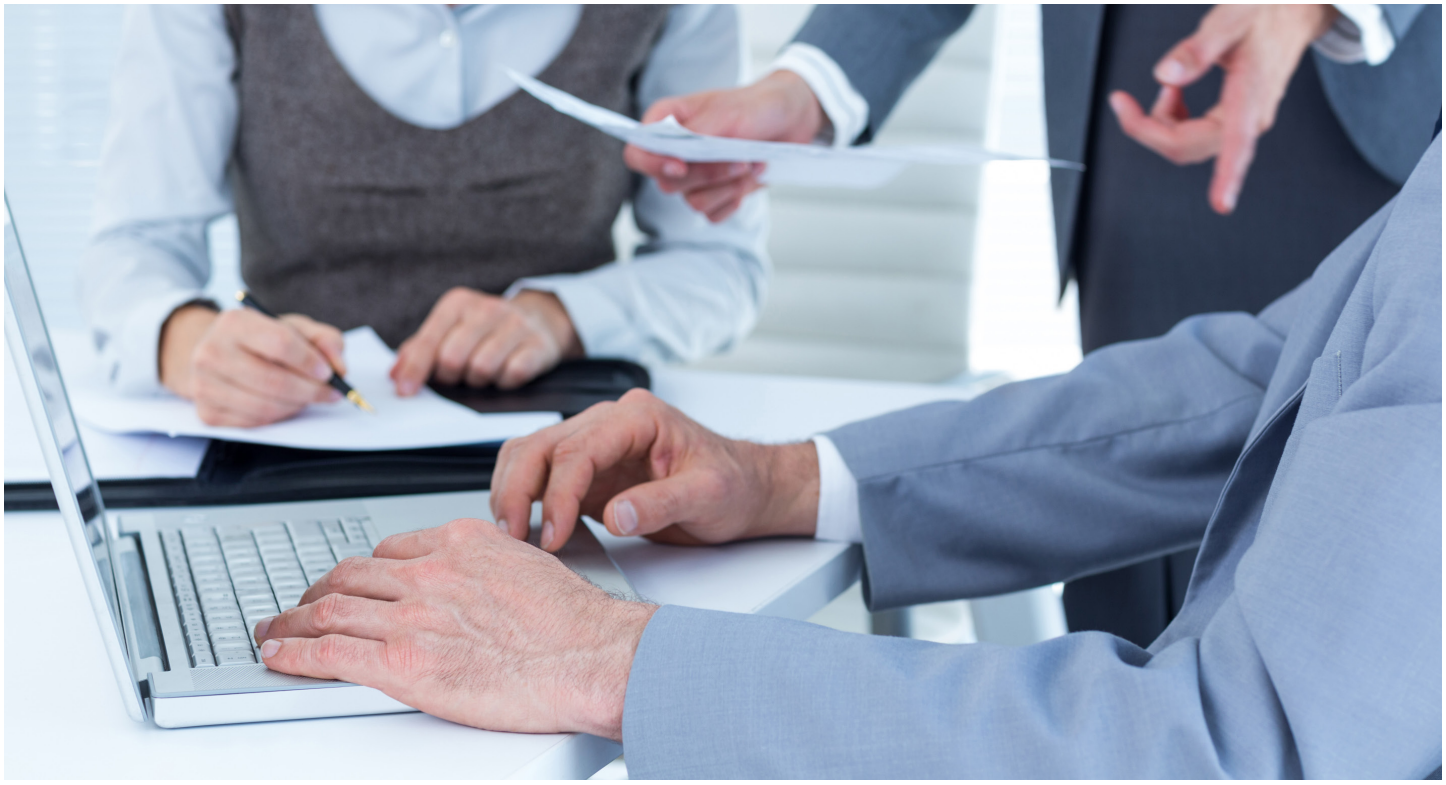
[2]VCTs are high risk investments and there may be no market for the shares should you wish to dispose of them. There is a possibility of the chosen company failing.

Summary

Pensions are a very tax efficient way for UK individuals to save for their retirement, however the tapering rules are complex and impact many partners and directors in our professional firm clients. We have the expertise and sector knowledge to pick through the complexity and advise on appropriate planning strategies.

Professional advice should always be sought and any changes to your financial plan and strategy requires consideration to ensure that it assesses and addresses all of the risks. The details of any advantages or disadvantages are beyond of the scope of this article.

Tax and legal advice should be taken to ensure that any benefit changes or alterations to earnings do not potentially fall foul of any anti avoidance rules.



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Kingston Smith has been helping clients build their businesses for more than 90 years.

As chartered accountants and business advisers, we work with clients to understand their potential and ambitions, and provide all the information and support they need to achieve them.

Most of our commercial client businesses are managed by the people who own them. We have over 60 partners and more than 500 professional staff focused in and around the London/South East region, where our commitment to the more entrepreneurial types of business has created long-lasting successes. Our sector focus provides us with the insight our clients need to deliver strategic and practical advice.

Our founder membership of international accountancy association, Morison KSi, offers our clients the strength and experience of offices in 88 countries to support their international reach. That combination of geographic knowledge, commercial expertise and client empathy has given us a great track record in helping clients grow their business.

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