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MAY 2009 NEWSLETTER

Reasons to incorporate

Is it time to incorporate?

Most businesses start as sole-traders or partnerships, which is a good idea as this structure allows the most flexible use of any losses made in the earlier periods. However, as your business grows and starts to make good profits, there are strong arguments for transferring the business into a company - a process known as incorporation.

A small company currently pays 21% tax on the first £300,000 profits per year, although this rate may increase to 22% from April 2010. As a sole-trader or partner you pay a total of 28% tax and national insurance (NI) on the first £41,275 of profits, then 41% tax and NI on additional profits. A massive 51% rate of tax and NI will apply to profits over £150,000 which are taxed in 2010/11 or later years. If your accounts year end is 30 April, the 51% rate could apply to profits made from May 2009. The NI rates are also due to increase by 0.5% at each level from 6 April 2011.

These figures show you pay more tax on business profits above about £41,000 per year as a sole-trader, than a company does. When you extract the funds from the company for your own personal use there can be further tax charges, but these charges can be minimised with some forward planning.

If you trade through a company you are only personally taxed on the money paid out to you, so you can choose to leave funds within the company to keep your total personal income below the higher tax thresholds. Dividends paid within your basic rate tax band (up to £38,400 gross for 2009/10) do not create any further tax charges for you. Dividends can also be used to pay surplus profits to other family members, although issuing shares to these individuals must be done with care as HMRC will challenge dividends paid to children or where dividend waivers are used.

As an employee of the company you will pay class 1 NI on your wages, once these exceed £110 per week. However, class 1 NI gives you more entitlement to state benefits than the classes 2 & 4 NI you pay as a sole-trader. Employees can also receive tax efficient benefits such as childcare vouchers, training and health-care checks, which are not available to the sole-traders.

If you would like to discuss the tax savings you could make by incorporating your business, please talk to us without delay.

Tax Deadlines

1 May
New VAT scale charges for fuel used for private journeys in company cars. Compulsory VAT registration threshold now £68,000.

3 May
Submit forms P46 (car) for quarter ended 5 April 2009.

19 May
File forms and P60, P35, P14 and pay PAYE & NIC due for month to 5 May.

26 May
Last day HMRC will accept forms P14 & P35 without issuing automatic fine.

22 May
Electronic PAYE payments for month to 5 May must reach HMRC.

31 May
Give forms P60 to all those you employed at 5 April 2009.

19 June
PAYE and NIC due for month to 5 June.

22 June
Electronic payments for PAYE for month to 5 June to reach HMRC

5 July
Last day to reach PAYE settlement agreement for 2008/09.

6 July
Forms P11D & P9D to reach HMRC. Give copies of forms P11D to employees. Forms 42 for reporting shares given to employees in 2008/09 must also reach HMRC.

19 July
PAYE and NIC due for month to 5 July and for 1st quarter. Class 1A NIC due for 2008/09.

31 July
Second payment on account of income tax due for 2008/09. Automatic £100 fine for all 2008/09 tax returns still not submitted. 5% surcharge on unpaid income tax and CGT due for 2008/09.

Health-Care News

For some years employers have been able to pay for annual health checks for their employees, which were tax and NI free if those medical checks were offered on the same terms to all employees. That universal coverage requirement has now been lifted. You can now offer tax-free annual health-checks for employees on different terms, so not all employees have to be included in the health-screening programme. Retired staff can also be offered tax free health-checks.

This is a particularly valuable benefit as a private health-check is a significant cost, although any treatment the employer pays for following the health check is taxable.

Tax Tip

HMRC has changed the bank accounts it uses to receive payments of most taxes including PAYE, and corporation tax. If your bank remembers your frequent bill payments, check the HMRC bank account details before pressing the button to pay the next amount due. If you pay your tax by direct debit you don't have to change anything.

Tax efficient charitable giving

The most tax efficient way for you as an individual to make charitable gifts is under the gift aid scheme. All you have to do is declare to the charity that you pay enough UK tax to cover the 20% tax that is deemed to be deducted from the gift. If you pay tax at 40% you can claim extra tax relief through your tax return.

A company can't make gift-aided donations, but it can receive tax relief for the gross value of the charitable gift it makes. The donation is deducted from the company's total profits before corporation tax is calculated, so the company receives tax relief at its highest marginal tax rate. This gift is treated as a non-trading charge against profits, which cannot increase a trading loss, or be carried over to another accounting period. The company must be making profits in the year it makes the donation to get tax relief for the gift. There are restrictions on the tax relief if the company, or a connected person, receives benefit back from the charity, with special rules for companies that are controlled by charities.

Whether it is more tax efficient to give to charity from your own personal funds or through your own company depends on your relative marginal tax rates (see page 1). Higher rate tax relief for charitable donations has not been restricted for those who will pay tax at 50% from 2001/11, as has been proposed for pension contributions. Although there are restrictions on tax relief where gifts from one person exceed £25,000 a year, and the doner has other transactions with the charity.

Reduce your expenses hassle

It's time to start work on those tiresome forms P11D to report expenses and benefits paid to employees and directors in the year to 5 April 2009. The deadline for submitting the forms to HMRC, and giving copies to employees, is 6 July 2009.

If you have a dispensation for business expenses in place with HMRC your life is made easier, as expenses falling in the categories specified in the dispensation are not to be reported on the form P11D. However, taxable benefits such as a car or accommodation must be reported and the taxable benefit calculated.

Some benefits are tax free, so don't have to be reported within the tax-free limit. For example childcare vouchers worth up to £55 per week are tax free, but additional amounts must be reported and taxed.

Most reportable business expenses consist of travel and subsistence costs. In the past HMRC have been happy to include the cost of tickets in a dispensation, but they have been less likely to agree to an allowance to cover meals. HMRC required employers to prove the meal allowance was representative of the actual costs incurred.

Now HMRC have agreed a scale rate for meals taken while travelling in the UK. These are: one meal £5, two meals £10, and late evening meal £15. The employee must be away from his home or normal place of work for at least 5 hours to claim one meal, 10 hours for 2 meals, and work to after 8pm for the evening meal. The rates only apply from 6 April 2009, where the employer has agreed to stick to the scale rates within his dispensation agreement with HMRC. This is another good reason for getting a dispensation in place, or updating the one you have.

New penalties for tax mistakes

There is a new set of rules in place that govern the level of penalties HMRC officers can impose when they find a tax form which contains an error or mistake. These rules apply to most tax forms and other documents you send to HMRC, including P11d forms, corporation tax, VAT and income tax forms.

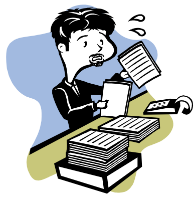
The level of penalties applied depends on how you behaved when completing the document. If you:

- made a mistake in spite of taking reasonable care: no penalty is imposed.
- failed to take reasonable care: up to 30% penalty.
- made a deliberate inaccuracy: 20% to 70% penalty.
- made a deliberate inaccuracy and tired to conceal it: 30% to 100% penalty.

The penalty is a percentage of the tax lost to HMRC, or in some cases the tax deferred to be paid in a later period. You have a good chance of escaping a penalty if you can show you did take reasonable care with your tax affairs, but your mistake was due to another factor, perhaps the guidance on the form was so badly written it was impossible to understand.

HMRC say 'reasonable care' involves a lot more than paying attention to their guidance notes, as it will include:

- keeping accurate records to make sure your tax returns are correct.
- checking what the correct position is when you don't understand something.
- telling HMRC promptly about any error you discover in a tax return or document after you've submitted it.



More haste, less speed

These new penalties mean you have to be confident at all times that you are treating each transaction correctly for tax or VAT purposes and you have recorded it accurately. If you have any doubts over the tax treatment of an unusual transaction please ask us for advice. A timely check could save you a huge penalty later.