

2024

# AUTUMN NEWS



## Smith-Milne & Co Limited

23 Church Street  
Rickmansworth  
Hertfordshire  
WD3 1DE

t: 01923 83 23 03

f: 01923 71 13 75

e: [office@smithmilne.co.uk](mailto:office@smithmilne.co.uk)

w: [www.smithmilne.co.uk](http://www.smithmilne.co.uk)

ACCA

### Director

Justin Smith-Milne FCCA

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## Tax reform is on the way

The Budget will be held on 30th October and it appears that some taxes will be going up. In this newsletter, we update you on the tax rises we already know about (for example, VAT on private school fees), but where else can Rachel Reeves raise revenue? In the election campaign, she promised not to raise the rates of Income Tax, National Insurance, VAT and Corporation Tax.

There are perhaps three main areas she will look at. Inheritance Tax (IHT) is long overdue major reform. (For example, the allowances for lifetime gifts have not risen since the tax was first introduced almost forty years ago.) Such reform could include a reduction in the many reliefs that are available, particularly the 100% relief for qualifying businesses (which currently includes many quoted on the AIM market on the London Stock Exchange). The extra IHT break for leaving a home to a direct descendent, relieving up to £350,000 of value per married couple, was only introduced in 2017. It is immensely complicated in its detail and could conceivably be abolished, perhaps with an increase in the normal nil rate band (which has been frozen for the best part of twenty years) as partial compensation.

However, IHT is payable on only a small proportion of estates and any changes will probably not raise huge amounts of extra tax.

There may also be significant changes to CGT (in addition to the ending of the tax breaks for furnished holiday lets, which has already been announced). Business asset disposal relief could be completely abolished, having in the recent past had the maximum tax saving reduced from £1 million to £100,000 by the Conservatives. It is possible that the rates of CGT will be raised, perhaps even to align them with income tax rates (something formerly done by Conservative Chancellor Lawson in the 1980s). Again, though, such changes will not bring a vast amount of extra money into the Exchequer purse and the Chancellor would have to consider the effect of higher rates on people's investment decisions.

The third likely area for potential change is pensions tax, where it might be possible to generate a lot more income for the government. George Osborne was part-way through reform of this area when the Brexit referendum intervened. Currently, tax relief is given at the taxpayer's marginal rate of tax, so higher and top rate taxpayers benefit a lot more from this relief than basic rate taxpayers (although some top rate taxpayers have relief restricted). Restricting tax relief to a flat rate of 20% for everyone would bring in many extra billions of tax each year and, in some eyes, also make the system more "fair". Presumably, any such change would not apply retrospectively to pension contributions made before Budget Day.

Changes to the rules on pension withdrawals, perhaps including a reduction in the amount of tax-free lump sum you can take, may also be being considered.

Other tax reliefs may go, particularly where there is no great evidence that they help to produce their intended economic consequences. An example might be the generous 50% income tax relief for investing in start-up companies via the Seed Enterprise Investment Scheme.

Anyway, that is all for the (near) future. In this newsletter, we outline a number of recent tax developments, including updates on claiming tax repayments, Construction Industry Scheme (CIS) compliance and a tax case on pool cars.

***We are here to help, should you have any questions about what you read below. Please get in touch if you want to discuss anything.***



## R&D requires expertise

There are very generous tax breaks to encourage research and development (R&D). However, these tax advantages are only available where the projects undertaken meet a multitude of conditions. A recent tax case showed that a company was some way short of fulfilling all the criteria needed.

An R&D claim was made in respect of several projects, which aimed to make books in the company's digital archive available in the marketplace as curated and searchable resources. HMRC rejected the company's claim for R&D relief on the basis that there was no R&D being undertaken.

The company:

- argued that the government guidelines were open to a degree of interpretation, but the Tax Tribunal said that a narrow approach was required;
- claimed its key staff members were 'competent professionals', but it was clear they lacked detailed and up-to-date knowledge in software, programming and computing;
- acknowledged that the technology utilised by the company may have been used in the same manner by previous users, meaning that it was not a novel solution in the wider context (which is a requirement to get R&D relief);
- provided no evidence for any of the employee costs and other expenditure claimed; and
- did not register any patents resulting from the project.

The R&D claim was denied for the period in question, giving rise to an increase in corporation tax of just over £50,000. The company was unable to neither:

- demonstrate that its projects made any advance in science or technology; nor
- provide evidence as to how the expenditure claimed was directly related to the projects that it did carry out.

### 'Competent professional'

Many of the problems with R&D claims arise from the lack of a definition of 'competent professional', which the guidelines say 'goes beyond having an intelligent interest in the field'. Company officers and employees can believe they meet that test when, in fact, they don't, if they are not well advised at the outset of the project.

***If you are planning to undertake R&D, we can advise you as to whether your project qualifies for the relevant tax breaks and also help you to claim them. We can also make sure you don't claim when you shouldn't (as this can lead to extra tax being due and penalties).***

## Non-doms

In our Summer Newsletter, we outlined the last government's proposals for ending the tax advantages that are very beneficial to those who are not domiciled in the UK but have been living here for many years, with effect from 2025/26.

Abolishing such tax breaks was originally a Labour Party idea, so it is no surprise that the new government is going ahead with the proposals. It seems to be intending to follow most of what the last government set out (e.g. abolition of the remittance basis of tax, but with a four-year exemption from tax on foreign income and gains for those becoming resident in the UK after at least ten years of non-residence). However, there are two important differences.

1. Those not eligible for the four-year exemption (because they have been here too long) will be fully taxable

on their foreign income and gains from 2025/26 onwards. Previously, half of their foreign income was due to be exempt from income tax in 2025/26, as a transitional rule.

2. There will be a tightening up of the anti-avoidance rules on offshore trusts.

The government has confirmed that the Inheritance Tax regime will be based on someone's residence status rather than domicile status in the future. They intend this to take effect from 2025/26 also, but we will have to wait until the Budget at the end of October for the final details of all these changes.

***It is important to get expert advice if you are a non-dom, although it may not be possible to know exactly how these changes will affect you until later in the year.***

## Furnished holiday lets

The new government has confirmed that it will proceed with the abolition of the furnished holiday let (FHL) rules from 6 April 2025. The main issues associated with this change were discussed in the Summer Newsletter.

Further information has now been published on the transitional rules, which include that:

- where an existing FHL business has an ongoing capital allowances pool of expenditure, it can continue to claim writing down allowances on that pool; and
- losses on FHL properties can be carried forward and used against

income of the UK or overseas property business in which the properties will now be included.

An anti-forestalling rule will apply from 6 March 2024 to prevent the use of unconditional contracts to obtain capital gains tax relief under the current FHL rules, where completion of the contract would be after 5 April 2025.

***If you own a furnished holiday let, please contact us to see how these changes will affect you and whether, for example, it may be worth disposing of a property this year rather than a bit further into the future.***

## Private school fees



The government has produced draft legislation that charges VAT at 20% on education and boarding services provided by private schools for a fee. However, the changes will not impact pupils with the most acute special educational needs, where those needs can only be met in private schools.

The measure will apply to **fees paid from 29 July 2024** in relation to the **term starting in January 2025 and future terms**. Paying several terms' worth of fees in advance will therefore not get

around the new VAT charge.

The government has also published an overview of its plans to remove the eligibility of private schools in England for business rates charitable relief. It is expected that this measure will apply from April 2025.

***Private schools will need to make sure that they are dealing properly with VAT compliance going forwards. Please get in touch if you have any concerns in this area.***

# Tax misconceptions

Unfortunately, people too often undertake high value transactions without getting proper advice as to the tax consequences. A classic example of this arose recently at the Tax Tribunal.

In 2016, a husband transferred ten commercial properties to a company owned by his wife. The disposal was not reported on his tax return as he believed that:

- the spousal CGT "exemption" applied; and (anyway)
- no gain arose, as the properties were transferred for consideration equal to their CGT base cost (£300,000).

In early 2019 (while an HMRC enquiry was ongoing) the husband and the company agreed to 'rescind' the transfer of the properties, by transferring them back to the husband.

HMRC assessed him to CGT on the capital gain arising on the original transfer, based on the market value of the properties; he was also charged penalties for submitting an inaccurate tax return.

He argued that the transfer of the properties had been rescinded in 2019, such that no taxable disposal had taken place in 2016.

## What did he get wrong?

1. Inter-spousal transfers are not exempt CGT. They take place on a no gain/no loss basis, meaning that the transferee takes over the original owner's CGT cost. Any gain or loss on a subsequent disposal by the transferee will therefore reflect the combined ownership of the couple.

This mistake of itself would not have triggered a CGT liability for the husband, but the no gain/no loss rule only applies to direct transfers between spouses, not (as in this case) transfers from one spouse to a company owned by the other spouse.

2. A taxpayer is 'connected' (for CGT purposes) to a company controlled by a spouse, so the transfer is

deemed to take place at market value for CGT purposes. The husband only receiving consideration equal to the base cost of the asset therefore did not mean that no gain arose.

3. Although a transaction may be void if entered on the basis of a mistaken legal assumption, this only applies where the mistake is sufficiently fundamental and affects either the subject matter or the performance of the transaction. That was clearly not the case here, as the CGT liability had no effect on:
  - the terms or subject matter of the transaction (i.e. the transfer of the properties in return for consideration left outstanding as a debt in the company); nor
  - how the transaction was performed (i.e. the transfer of legal title from the husband to the company, using the appropriate land registry forms).

## When can a transaction be rescinded?

Rescission is possible, but only where the transaction has not been fully executed. This means that one or both parties must still have outstanding obligations to perform. (This was clearly not relevant in this case, as the contract had been fully executed.) However, any rescission in such circumstances would not mean that the transfer of the properties could be ignored; it would simply put an end to any further obligations yet to be performed.

In summary, the fact that the transfer was reversed by his wife's company transferring the properties back to him did not mean that the original transfer could be treated as if it had never taken place. There was a disposal of the properties for CGT purposes by the husband in 2016, at their market value.

***Don't end up with the sort of problems that this taxpayer had. Even if what you are planning to do appears to have no tax consequences, please contact us to check.***

## New process for tax repayments

At the end of each tax year, HMRC send taxpayers an 'End of Year Tax Calculation - P800' if they have underpaid or overpaid their taxes. This personalised letter indicates:

- whether the recipient needs to pay more tax or is eligible for a refund;
- the amount involved; and
- how the payment or refund will be made.

It also provides a more detailed breakdown of the tax calculations, to help the taxpayer understand how HMRC has arrived at the figures. Taxpayers are asked to contact HMRC if they think there is an error.

Following a change of policy, employees must now usually take action to claim P800 PAYE repayments; the option to wait 21 days for a cheque to be issued automatically has been removed. However, these changes do not yet apply to all P800 repayments. Some taxpayers will continue to receive P800s with a message to say that a cheque will be issued if the repayment is not claimed within 21 days. This includes repayments where multiple tax years or claims by agents are involved.

However, most taxpayers will receive a P800 with instructions that the new process must be followed, with the **repayment claimed online**. You can request a cheque to be sent by post or arrange a transfer into your bank account.

Note that there is:

- no requirement to set up government gateway credentials for this service; and
- no opportunity to nominate the repayment to a third party.

All that is needed is the P800 reference number and your National Insurance number.

A cheque will only be sent to the taxpayer's address on HMRC's records. If that address is not correct, the taxpayer will need to change the address by

- phoning HMRC; or
- using the online change of address service (which is behind sign in credentials).

If the bank transfer option is chosen, you will need to have your banking app installed on the device you are using, as you will be transferred to sign in to your bank account as part of the process.

***If you are confused by these new rules, or have any other concerns, we can help you claim any tax repayment due to you.***



## CIS update

HMRC is writing to contractors and asking them to regularly verify the construction industry scheme (CIS) status of their subcontractors.

HMRC's records show that some contractors have made incorrect CIS tax deductions, so HMRC is reminding contractors that they must:

- verify all new subcontractors before they pay them;
- verify subcontractors they've used before if they haven't included them on a CIS return in the current tax year (or the previous two tax years); and
- make sure they apply the correct CIS deductions.

The contractor can verify subcontractors using HMRC's online service or using commercial software, but must use the latter if they want to verify more than 50 subcontractors. ***We can help you make sure you are compliant in this regard.***

HMRC may open a compliance check if the contractor does not take any action. If HMRC starts a compliance check and finds errors in a CIS return, it will treat a disclosure made by the contractor as 'prompted', which will likely increase the amount of any penalties the contractor may incur.



# A dip into pool cars!

The conditions for a car to be a pool car include that:

- the car was made available to, and actually used by, more than one employee;
- the car was not ordinarily used by one of those employees to the exclusion of the others;
- in the case of each of those employees, any private use of the car made by the employee was merely incidental to the employee's other use of the car in that year; and
- the car was not normally kept overnight on, or in the vicinity of, any residential premises where any of the employees was residing, except while being kept overnight on premises occupied by the person making the car available to them.

If all conditions are met, no taxable benefit arises on those who have had use of the car.

## 'Merely incidental'

If the private use is in some way a result of the business use, it can be considered merely incidental. Private use being small in comparison to the business use is not, on its own, sufficient to meet the test.

For example, if an employee takes a car home to make an early start on a business journey the following morning (where that business journey could not reasonably be undertaken the next day starting from the normal place of work) then the journey from work to home, although private, is merely incidental to the business use. This would also be the

case if an employee who is staying away from home overnight on a business trip uses the car to go to a nearby restaurant in the evening.

## A recent case

The issue of pool cars has recently come up before the Tax Tribunal.

At a 1993 meeting, the HMRC inspector made a representation to a company director as to what was required for a car to be a qualifying pool car. Among the conditions mentioned was apparently that "... each employee who had use of the car owned another car which was available for private use."



This representation was relied upon by the taxpayer, but (many years later) HMRC sought to collect Class 1A National Insurance from the company on the benefits provided, having concluded that certain cars leased by the company were not pool cars.

The Tribunal agreed with HMRC, concluding that the director and his family members clearly used the cars for private purposes that were not merely incidental to business travel.

The appellant advanced further arguments about what they saw as the unfairness of the situation, but the Tribunal found that:

- HMRC could not be stopped from enforcing a statutory provision; and
- the Inspector had had no authority to enter into a forward agreement relating to the company's tax position.

**Don't rely on things that HMRC may or may not have told you. Please speak to us to check on the correct tax treatment of what you are undertaking.**

## Note

As there is no private use, VAT is (in principle) recoverable on a pool car, unlike a normal business car with private use. However, for capital allowances purposes, pool cars are governed by the normal rules for cars, meaning that they do not qualify for annual investment allowance (AIA) or 'full expensing'. You therefore cannot (with the current exception of zero-emission vehicles) write the cost off immediately for tax purposes.

## Same gains, more tax and reporting!

For 2024/25, the CGT annual exempt amount has fallen to £3,000, having been £12,300 two years ago. Where gains are above the new threshold, this will mean higher CGT to pay than in the past.

Those disposing of residential property have the added complications of 60-day reporting of gains and payment of any CGT liabilities within the same time frame. If you get it wrong, hefty penalties may apply and late payment interest (currently 7.5% pa) will be incurred.

### 60-day reporting

In broad terms, you must report the gain on a special return, having previously set up a UK property account, and pay the tax due within 60 days of completion of the sale or disposal. Given the tight timescale, being prepared in advance is key. **Please let us know immediately if you are considering the disposal of any property to which this could apply, so that we can make sure you have all the paperwork needed to calculate any gain promptly.**

It has been possible to print a paper return from HMRC's website since April

2023, but this can only be used by the 'digitally excluded' and certain other persons who will be unable to submit returns online. In any event, there are often delays in processing paper forms and, when used, it is not possible to make a payment before the payment reference is issued.

Note that payments of any tax due under the 60-day regime are dealt with separately from any other HMRC liabilities, including those due under self-assessment.

### Payment reference

This should be a 14-digit number starting with X and is found in the taxpayer's online UK property account (or in a letter sent to them by HMRC after they've submitted a paper return). Do not make the payment into your HMRC self-assessment (SA) account using your unique tax reference (UTR), as the payment may be allocated against other liabilities, after which it may not be possible to re-allocate it to the property gain.

If you are within SA, you will need to report the disposal on your SA

return after the end of the tax year. Unfortunately, this is in addition to, not instead of, the 60-day return. This could show that there has been an overpayment of CGT (e.g. if you have made a capital loss later in the tax year). Overpayments should now automatically be set against other tax liabilities for the year (e.g. income tax), but if there is an excess, HMRC will have to be contacted directly to arrange a repayment.

A penalty of £100 is charged if a return is filed after the deadline. A further penalty of either £300 or 5% of the tax due – whichever is higher – is charged if the deadline is missed by six months, and then that penalty is repeated if the failure continues after 12 months.

Although it is not currently HMRC's practice to do so, they can also charge a £10 daily penalty if the return is more than three months late, up to a maximum of £900.

**If you have any concerns about the onerous reporting rules for UK residential property gains, please get in touch and let us help.**