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Bleaker Outlook for Husband and Wife Companies

On 27 April 2005, the High Court in England handed down its judgement in *Jones –v- Garnett* (the Arctic Systems case). By way of background, Mr & Mrs Jones each held one share in a company which provided Mr Jones' services to clients. He drew a low salary and profits were distributed to Mr and Mrs Jones by way of dividend.

The Inland Revenue said that this was an arrangement which under trust and tax law made Mr Jones a "settlor". Tax legislation in these circumstances requires that Mr Jones' wife's dividend income be treated as his income for tax purposes (and not his wife's income). When the case was originally heard by two Special Commissioners, the presiding Commissioner agreed with the Revenue while the other Commissioner agreed with Jones. The presiding Commissioner exercised her casting vote in favour of the Revenue and Jones lost.

On appeal, the High Court held that the "arrangement" included not only the things that happened when it was made but also the reasons why it was made. In particular the possibility of it being a means of channelling bounty to Mrs Jones in the future.

After the Special Commissioners decision, many believed that the High Court would reverse this in favour of the taxpayers. It is not known, at this stage, whether the case will be appealed further.

In the meantime, many husband and wife companies will be affected, particularly those where one spouse does most of the work, draws low remuneration with the other spouse receiving a substantial dividend. Other cases where both spouses work or are adequately remunerated should not be caught.

You should contact us if you would like to discuss your own particular circumstances.

“... It usually purports to be from a relative of a deceased Nigerian dictator who needs your help ...”

VAT Relief for the Disabled

If you are a supplier of goods and related services provided to adapt property for use by the disabled you should be aware that such supplies/services may be zero-rated, if the customer who is benefitting provides you with a written declaration.

Services and supplies included are :

1. Supplies to a disabled person for constructing ramps or widening doorways or passages to facilitate his movement within his residence.
2. Supplies to a charity to facilitate a disabled person's movement within any building.
3. Supplies to a disabled person for providing, extending or adapting a bathroom or lavatory to suits his needs.
4. Supplies to a charity for providing, extending or adapting a bathroom for use by disabled persons in either a residential home or a day care centre.

5. Supplies to a charity for providing, extending or adapting a bathroom for use by disabled persons in a building used by the charity for charitable purposes.

6. Supplies to a disabled person necessary for the installation of a lift in his own home.

7. Supplies to a charity of services for the provision of a lift in a temporary or permanent residence or day care centre for use by the disabled.

8. Supplies to a disabled person or to a charity that are necessary for the installation of certain equipment.

Preparatory, restoration and repair work in respect of any of the above items may also be zero-rated.

If you require advice on this or any aspect of zero rating supplies to or services for the disabled, please contact us.

Do You Use Construction Industry Sub-Contractors?

If the answer to this question is "yes" then you should make sure that any who are not limited companies can be shown to be genuinely self-employed rather than employees.

The Inland Revenue has made many enquiries about the employed/self-employed status of sub-contractors in recent years. Using technology they identified 13,000 contractors and 44,000 sub-contractors where the pattern of payments indicated that the sub-contractors wrongly believe they are self-employed. The consequence of getting this wrong for the contractor can be very serious as the Revenue will want PAYE and NIC from the contractor as well as interest and a possible penalty.

You should contact us if you have any concerns in this area.

Protect Yourself From E-Mail Scams

The chances are that if you have an active e-mail account, at some point you'll have received at least one of the fraudulent e-mails detailed below.

● '419'

The most well-known of all the e-mail scams. It usually purports to be from a relative of a deceased Nigerian dictator who needs your help in smuggling the family's millions out of the country. Just put down an initial sum, or hand over your account details, and millions will be yours.

● 'Phishing'

An e-mail claiming to be from your

bank asks you to confirm your bank and password details as part of a security update. You innocently key in your personal details and the fraudsters have access to your funds.

● Lottery Scam

The e-mail informs you that you have won a foreign Lottery via the random selection of your e-mail address. In order to claim your prize you'll have to pay some money up front to cover supposed handling charges.

● Hot Penny Shares

Company XYZ- a small but real company – is about to announce a major breakthrough and apparently the

share price will soar. Buy now and you'll make a fortune. The Motley Fool claims that "these e-mails will be from someone who already has shares in the company and is hoping that enough gullible people will rush to buy some themselves pushing the share price up. They'll cash in before you realise the company's a dud."

● Cheap Software

A fake online store is selling expensive software at bargain prices. But the store doesn't exist and the website is just a means of getting hold of your personal bank or credit card details.

“... Major changes are coming which will simplify the pensions regime ...”

Business Start Up Grant for Young People

From 1 October 2004 a new Business Start Up Grant of £1,000 has been available. The grant is targeted at those in the 18 – 30 age group who are starting their own business. This funding is on offer from Business Gateway. Contact us or Business Gateway direct for further details

Civil Partnerships and Taxation

The 2005 Finance Act provided that same sex individuals who form a civil partnership under the Civil Partnership Act are to be treated, for tax purposes, in the same way as a married couple.

A number of tax advantages accrue to couples who form a civil partnership:

1. Inheritance tax

The spouse exemption will apply, which means that gifts during life and on death between the partners will be exempt, except where the recipient is not UK domiciled when the exemption is restricted to £55,000.

In this way the partner who dies first can provide for the survivor.

2. Capital gains tax

The spouse exemption will apply. One partner can transfer assets such as property and shares to the other without a capital gains tax charge arising. For example, this will allow partners to put an asset into joint-names and, on sale, each will have a gain and be able to offset their own annual exemption.

3. Income tax

Married couples are treated independently for income tax purposes. One advantage, however, is the age allowance for married couples which

will be available to qualifying partners.

While there are substantial inheritance tax and capital gains tax advantages, there will be disadvantages in other areas, particularly in relation to a number of anti-avoidance provisions. For example,

- One partner may own all of the shares in A Limited while the other owns all of the shares in B Limited. If the two individuals form a civil partnership, A Limited and B Limited will become "associated" for corporation tax purposes. As associates, each company will only have a £5,000 starting rate band and a £150,000 small company's rate band instead of £10,000 and £300,000, which apply where a company has no associated company.
- The Settlements Legislation which applies to husband and wife companies could also apply to situations where civil partners receive dividends from a company which they own but one partner does most of the work for modest remuneration.
- Each partner's shareholding in an unquoted company will be valued as if it were part of a combined holding for inheritance tax purposes. This will have relevance in situations where shares are gifted to a person other than the civil partner.

Pensions A-Day

Major changes are coming which will simplify the pensions regime. The changes come into effect on 6th April 2006. Some important features are:

- Most people will be able to contribute more than at present. It will be possible for an individual to contribute the lower of the amount of his earnings and £215,000 per annum. Company contributions can be made of up to £215,000 per employee per annum regardless of an employee's salary level.
- There will be a lifetime limit to the amount of your pension fund of, initially, £1.5 million. If your fund is already at or above this level, you should take advice if you have not already done so.
- Flexibility at retirement is greatly increased. For example, you will be able to take up to 25% of the fund as a tax free lump sum and draw an income from the balance. The income level can be set at zero.
- The assets into which pension schemes can invest are being widened to include residential property. Commercial property has been a possible investment for many years and will still be available.
- Members of a pension scheme will be able to sell assets to pension funds. You may have a commercial or residential property or quoted shares which you could sell to your pension fund. Presently, it is not possible for a pension fund to buy an asset which has been owned by a member within the previous three years.

“ ... In many professional practices, partners' time is excluded from work in progress ... ”

Professional Services - Firms facing a tax increase

A recent change in the way in which revenue is to be recognised for contracts for professional and other services may have a major impact on the tax bills of some professional firms.

The question of whether revenue should be recognised as a contract progresses or on its completion has long been a matter of debate. However, the latest pronouncement from the accounting authorities has confirmed that where the seller's contractual obligations are performed gradually over time, revenue should be recognised as the contract progresses to reflect the seller's partial performance

of its contractual obligations. As a result it is rarely correct to defer recognition of revenue until contract completion.

Therefore, in the vast majority of cases no work in progress will be reported in the financial statements and the work carried out not invoiced will be shown on the balance sheet within debtors as "amount recoverable on contracts".

The result will be to recognise revenue sooner. Although on an ongoing basis, there may be little effect on tax liabilities, in the first year of change, accounting periods ending on or after 22 June 2005, an increase in the tax charge is likely.

It is important to remember that the

amount of revenue recognised will be the appropriate percentage of the final fee less any provision. In many professional practices, partners' time is excluded from work in progress, being considered to be pure profit, and consequently is not taxable until the client is invoiced. The percentage of the final fee approach will change the position since the fee will include partners' profit and this too will impact on tax liabilities.

ICAS and other UK Accountancy Bodies are discussing with the Inland Revenue what can be done to reduce the effect on cash flow of these developments. In the meantime if you have any concerns about this, please contact us.

Payroll Giving Grant Schemes

The Home Office has launched its new Payroll Giving grants programme, which offers employers with less than 500 staff a grant of up to £500 for setting up a Payroll Giving Scheme.

The grants will be administered as follows:

- Employers with 1-199 employees will be entitled to £300
- Employers with 200-249 employees will receive £400; and
- Employers with 250-499 staff will receive the full amount of £500

Under the Payroll Giving system, employees can make regular gifts to the charities of their choice.

The donations are made before tax is deducted from the donor's salary, so that a gift of £10 costs a basic rate taxpayer £7.80, or a higher rate payer, just £6.

The government will also be matching the first £10 donated by each employee every month, for a period of six months.

Further information may be obtained from www.payrollgivinggrants.org.uk

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