2023 AUTUMN NEWS

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All Quiet on the Tax Front

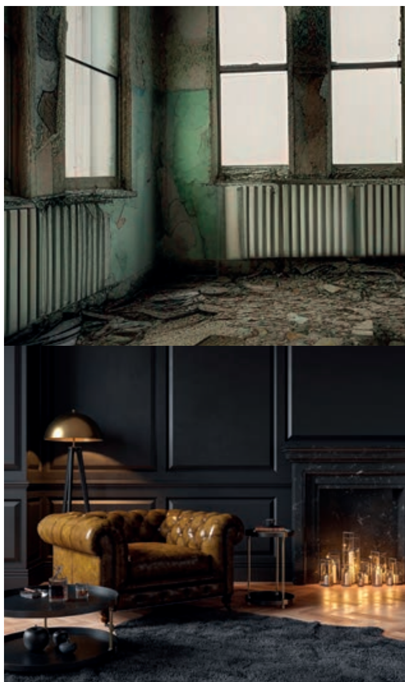
With the government's time taken up in dealing with economic issues such as high inflation and public debt, we are not expecting any significant tax announcements until the Budget, due to be held next March. The General Election is likely to be held later next year, so this Budget may well contain a lot of changes, even if they don't take immediate effect.

This period of relative tax stability gives us the chance to devote a good part of this newsletter to two main topics. We will remind you about many of the tax issues associated with buying business vehicles, particularly electric ones, as this area has been in the news a lot following the recent by-elections. We also explain some of the details of the recent changes to research and development tax reliefs, which remain very generous but less so than in the past. More onerous compliance procedures have also been introduced in this area for those companies wishing to claim relief.

Among the other topics we cover are the expansion of the Seed Enterprise Investment Scheme and stamp taxes when buying run-down properties. We also look at a not uncommon form of tax planning within small companies that HMRC says it will challenge.

If you wish to discuss any of the issues in this newsletter, or anything else concerning tax, we are here to help, so please contact us.

When is a dwelling not a dwelling?



Stamp taxes, whether Stamp Duty Land Tax (SDLT) or its devolved equivalents, are usually higher for residential property than non-residential or mixed-use property. (However, the current nil rate thresholds for SDLT, particularly for first-time buyers, mean that this is not always the case.) 'Second home supplement' may also apply to residential property.

To be residential, the property must be a dwelling. Two recent cases, in which run-down properties have been bought, have looked at how the term 'dwelling' should be interpreted.

In a 2019 case, a dilapidated bungalow was purchased, which cost £200,000. Second home supplement raised the SDLT from £1,500 to £7,500. The property was in a very poor state of repair (e.g. radiators and pipework removed and the presence of significant amounts of asbestos). It was uninhabitable, unmortgageable and was to be demolished and replaced with a new dwelling.

The tribunal held that the bungalow was not suitable for use as a dwelling. It was treated as a non-residential property and, as a result, the SDLT liability was reduced to £1,000.

A very similar case this year has produced a different outcome. Having bought a severely dilapidated property in London for £1.755m, the couple moved into the property with their family in May 2020, by which time the building work was partially completed.

Unlike in the previous case, the property had been used relatively recently as a dwelling and was structurally sound, despite lots of work being required to make it habitable again. While empty, it had not been adapted for another purpose.

With no structural issues, the property was capable of being used as a dwelling once more, once the repairs and renovation work had been carried out. None of this work was sufficiently fundamental to make it a non-residential property at the time of purchase. Thus, the SDLT payable was £177,000, rather than £99,750.

The key distinction from the other case seems to be that this severely dilapidated property was being repaired to become usable as a dwelling again, as opposed to being demolished.

The differences between residential and non-residential stamp tax charges can be huge, so please make sure you know how your property will be categorised before proceeding with a purchase.

Time to go electric?

In his March Budget, the Chancellor announced the introduction of "full expensing", i.e. allowing most plant and machinery purchases to be allowable fully for tax purposes in the year of acquisition. This was really aimed at encouraging investment by big companies, as most small companies would in any case get immediate full tax relief via the Annual Investment Allowance (AIA), which has now been set permanently at £1million p.a. However, with limited exceptions (such as dual-control driving school vehicles), cars do not qualify for full expensing or the AIA.

Recent controversy over ULEZs (Ultra-Low Emission Zones) has highlighted that there are many reasons, not just tax ones, why businesses may want to switch to electric or low-emission vehicles. However, there are a lot of tax issues to consider when acquiring vehicles. Here are some of the key ones. ***There are also a lot of VAT considerations, but we will cover these in a subsequent newsletter.***

Relief for purchases

Cars with zero emissions qualify for 100% allowance, if purchased NEW (i.e. not second-hand) ***before 1 April 2025.*** Ex-demonstrator vehicles count as new for these purposes.

All other cars qualify for much slower tax relief:

- Cars up to 50g/km CO_2 emissions qualify for 18% p.a. allowances
- Cars above 50g/km qualify for 6% p.a. allowances.

Both these allowances are given on a 'reducing balance' basis, meaning that the tax relief is spread slowly over many years. E.g. for a car costing £30,000 with CO_2 emissions of 70g/km, the allowance in the first year will be 6% of £30,000 = £1,800; in the second year, the allowance will reduce to 6% of (£30,000-1,800) = £1,692.

Note that you have about 18 months remaining to take advantage of the 100% allowance for new electric cars.

Employer-provided cars

Where an employer makes a car available for private use to an employee or director, an annual benefit-in-kind charge applies. This is calculated by multiplying a statutory percentage by the original list price of the car. This benefit charge covers all incidental costs, such as insurance and servicing (but not private fuel).

To incentivise the take-up of electric vehicles, the percentage used for such cars is 2% p.a., through to 5 April 2025. The percentage for other vehicles increases in bands, based on CO_2 emissions (and for lower emission vehicles, how far they can travel in pure electric mode). The maximum percentage is 37%.

Appropriate percentages for electric and ultra-low emission cars (i.e. those emitting less than 75g of CO_2/km) will increase by 1 percentage point in each of 2025/26, 2026/27 and 2027/28, up to a maximum appropriate percentage of 5% for electric cars and 21% for ultra-low emission cars.

Rates for all other vehicle bands will be increased by 1 percentage point for 2025/26 (but still with a maximum percentage of 37%) and will then be fixed in 2026/27 and 2027/28.

Suppose, for example, that this year a new electric car is bought by a company for use by a director. Its list price is £40,000. Currently, there is a benefit charge of 2% of £40,000 = £800, on which the director will be taxed at whatever rate is appropriate to them.

By 2027/28, this benefit charge will have increased by 150% (i.e. to 5% of £40,000 = £2,000). Although this is a big jump, most people would still regard the tax payable on this charge as a price worth paying for having use of such a car, particularly as the director's company has had full tax relief on the purchase price in year 1 and on the service and insurance costs each year. Employers' Class 1A National Insurance will be payable by the company; this will be 13.8% of the benefit charge, but it will also be deductible for corporation tax purposes.

Charging electric vehicles – company cars

Where the employer pays for the cost of charging an employer-provided electric vehicle, there is no taxable fuel benefit for the driver.

Where the driver pays for the electricity to power it, either from their domestic supply or by charging at a roadside station, the employer may reimburse the employee for that cost. The employer can pay the driver 10p per business mile, to reimburse them for the cost of the electricity used for business journeys, with no tax implications. This rate has been raised significantly recently to reflect prevailing electricity prices and is reviewed every three months.

Charging electric vehicles – employees' own cars

Where the company allows employees to charge their own electric vehicles while at work, there is no taxable benefit for the provision of that free electricity. The charging facilities must be provided at or near the workplace (the same requirement that applies to tax-free workplace parking).

This tax exemption does not apply if the employer reimburses the costs of charging the employee's own vehicle away from the workplace (e.g. at a motorway service station).

Provision of fuel by the employer

The car benefit charge for employer-provided cars (described above) covers all incidental costs of running a car, except the provision of fuel. If the employer pays for fuel, an additional annual benefit charge applies, calculated (for 2023/24) as £27,800 multiplied by the percentage used in calculating the car benefit. This charge can be avoided if all private fuel costs are reimbursed to the employer, or the employer does not pay for any private fuel.

The rate at which the employer may reimburse fuel for business journeys is set quarterly. See https://www.gov.uk/guidance/advisory-fuel-rates

Business mileage in employee's personally-owned car

Where an employee or director does business travel in their own car, the employer can reimburse at a rate of 45p/mile for the first 10,000 business miles in a tax year, then at a rate 25p/mile. If the employer pays more than these amounts, the excess is a taxable benefit; if they pay less than these limits, the employee can claim the shortfall as an expense against employment income.

Self-employed allowable motor costs

Expenses such as fuel, insurance and servicing, along with capital allowances, are allowable on a proportionate basis, based on business mileage.

Those using the simplified rules for small businesses can instead claim the statutory mileage rates for business journeys (i.e. 45p/mile and 25p/mile, as appropriate).

Note that travel between home and a regular 'place of business' is private travel, even if the home is also a place of business (e.g. because you have a home office). However, itinerant workers whose place of business is their home can normally claim travel costs to and from the locations where they carry out their work.

Time to go electric? (continued)

Vans

Vans are treated as normal plant and machinery, so are eligible for the 100% AIA on purchase. They also have much lower benefit-in-kind charges than most cars where the employee or director has private use, being (for 2023/24):

- Nil for an electric van
- £3,960 for any other van.

If private fuel is paid for by an employer, there is an additional benefit charge of £757.

Note that, unlike for a car, travel from home to your normal place of work counts as business rather than private mileage.

Van or car?

In most cases it will be clear if you have a car or a van, but not always. For benefit purposes, a van is a vehicle of a construction primarily (i.e. first and foremost) suited to the conveyance of goods or burden of any description (but not including people). If a vehicle is not primarily for the conveyance of goods or burden, it will be classified as a car.

Buy or lease?

Whether to buy or lease is obviously a key issue when acquiring business vehicles. The decision will likely be based mainly on the types of deal on offer, but be aware that the tax rules for each option are very different. No capital allowances are available on leased vehicles, but the leasing costs recognised in the profit and loss account under generally accepted accounting practice are deductible for the business, subject to a disallowance of 15% for cars with CO_2 emissions above 50g/km.

We hope this gives you a flavour of the many tax issues associated with cars. Don't rush any decisions in this area and be aware that rules may have changed since your last vehicle purchase. Please contact us if you need any further information but remember, whether you are a director, employee or self-employed, that it is important to keep accurate business mileage records!

Expansion of the Seed EIS scheme

The Seed Enterprise Investment Scheme (Seed EIS) provides very generous tax breaks for investors, including a 50% income tax reduction for the amount invested and exemption from tax on capital gains on disposal of qualifying shares, if they are held for a minimum of three years. In addition, there is a 50% capital gains tax exemption where gains on other assets are invested in Seed EIS shares. These reliefs make it easier for very small companies to raise external finance in their early years.

From 6 April 2023, the annual investment limit for individual investors increased from £100,000 to £200,000, potentially enabling twice as much tax relief as previously. Also from that date, the amount that a company can raise through the Seed EIS has increased by two-thirds, from £150,000 to £250,000.

The base of the scheme has also been broadened, enabling more companies to use it. The gross asset limit has increased from £200,000 to £350,000 and the age limit on a qualifying trade has been extended from two to three years.

Note, however, that there are many types of trade excluded from this scheme. These include property development, providing legal or accountancy services, operating or managing hotels or care homes, farming and market gardening.

If your company is looking to raise SEIS finance, or you are thinking of investing in such a company, please discuss your ideas with us, as the qualifying conditions for a successful issue of such shares are notoriously detailed and complex. We can advise on the tax issues, but you should take suitable financial advice from a qualified advisor before investing, as such small companies are very risky investments.

Extension of NICs top-up period

You need at least

- 35 complete NICs years to receive the maximum state retirement pension, and
- 10 complete NICs years to receive any of the state retirement pension.

Where there is a gap in your NICs record, you can normally pay voluntary Class 3 contributions for periods in the last six tax years.

Currently there is a dispensation that allows women born after 5 April 1953 and men born after 5 April 1951 to complete gaps in their NICs records right back to 6 April 2006. You can pay the voluntary NICs at the 2022/23 rate of £15.85 per week instead of the current rate of £17.45 per week.

This opportunity to make up these old years with voluntary NICs payments now closes on 5 April 2025, rather than 31 July 2023.

Note that in some circumstances, for example if you have been claiming child benefit for young children while earning below contribution thresholds, you should have been credited with having paid NICs.

Avoid the spotlight!

'Spotlights' published by HMRC highlight schemes that HMRC has not yet had the opportunity to formally challenge, but where they are indicating, in advance, that they will enquire into any taxpayer who has utilised the planning. If someone uses a scheme which has been highlighted by a Spotlight, it is likely HMRC will argue that a deliberate offence has been committed, so penalties will be higher if the planning is shown not to work.

The recent Spotlight 62 highlights something that is commonly done. The arrangements seek to avoid tax by allowing the directors, who are also the main shareholders of a company, to divert dividend income from themselves to their minor children.

The arrangements work as follows:

- a company issues a new class of shares, which usually entitles the owner of the shares to certain dividend and voting rights;
- Person A, usually a grandparent or sibling of the company owner, purchases the new shares for an amount significantly below market value;
- Person A usually gifts the shares to a trust for the benefit of the company owner's children;
- The company owners vote for substantial dividend payments in respect of the new class of share;
- this dividend payment is paid to the trustees of the trust; as the beneficiaries of the trust, the company owner's children are entitled to the dividend.

The company owner's children pay tax on the dividend received, but much less tax than if the company owners received the dividend, due to their children's:

- £12,570 personal allowance;
- £1,000 dividend allowance;
- eligibility for the dividend basic tax rate.

HMRC's view is that this is caught by wide-ranging anti-avoidance legislation and that arrangements which operate in a similar way may also be caught.

If you have entered into any form of tax planning similar to this, we should discuss whether it may be subject to challenge by HMRC

Major changes to R&D reliefs

There have been major tax incentives for research and development expenditure for many years. Until recently, HMRC has adopted a 'light touch' approach to compliance in this area. However, those days are now over, as Finance Act 2023 introduces a number of changes, including more onerous compliance rules. The main changes are outlined below.

The legislation will apply generally to accounting periods starting on or after 1 April 2023, except for the requirement to provide additional information, which will apply to all claims made on or after 1 August 2023.

New categories of qualifying expenditure

There are three new categories of qualifying expenditure for R&D tax relief, namely:

- Data licences and cloud computing services; a data licence is defined as one to access and use a collection of data services.
- Cloud computing services, which include providing access to, and maintenance of, remote data storage, operating systems, software platforms and hardware facilities.
- Pure mathematics (previously a specifically excluded category); the types of companies that will benefit from this are wide-ranging, from software companies, especially those working in the areas of cybersecurity and crypto currencies, through to insurance companies and engineering firms.

Notification of intention to claim

Companies are mandated to inform HMRC of their intention to make a claim for R&D tax relief using a new digital form, **within 6 months of the end of the AP in which the expenditure is incurred.**

This measure is intended to allow HMRC to perform more upfront compliance checks on new claimants, so companies that have claimed R&D tax relief in any of the previous three years will be exempted from this requirement.

Claim must include specified information

A new provision is introduced which specifies that any claim must include specified information. The claim must be completed by a representative of the company or an agent acting on behalf of the company and will include:

- Company details, including unique tax reference (UTR), PAYE reference number, VAT registration number and business type;
- Contact details of main senior internal R&D contact who is responsible for the claim and the agent involved in the claim;
- Accounting period for which relief is claimed;
- Full details of qualifying expenditure;
- Amount of qualifying expenditure, for each project, of qualifying indirect activities;
- Project details including
  - What is the main field of science and technology?
  - What was the baseline level of science or technology that the company planned to advance?
  - What advance did the company aim to achieve?
  - The scientific or technological uncertainty that the company faced.
  - How the project sought to overcome the uncertainty.
- Which tax relief is being claimed and the amount

Restriction to UK expenditure

The previously announced restriction on some overseas expenditure will now come into effect from 1 April 2024 instead of 1 April 2023. Relief for subcontracted work and externally provided workers will be limited to focus on UK activity. Expenditure must either be:

- 'UK expenditure' on R&D in the UK; or
- 'qualifying overseas expenditure' undertaken outside the UK because the necessary conditions are not present in the UK due to:
  - geographical, environmental or social factors, e.g. deep ocean research; or
  - legal or regulatory requirements, e.g. clinical trials.

Reduction in tax relief

Most small and medium-sized companies incurring qualifying R&D expenditure get tax relief via the 'enhanced deduction' scheme, under which expenditure is deemed to be increased for tax purposes, thus giving a greater deduction than the actual amount spent. Where this deduction creates a tax loss, the loss can be surrendered to HMRC in exchange for a 'payable tax credit'.

Previous legislation had already reduced this tax relief for expenditure incurred on or after 1 April 2023, as follows:

- The additional deduction decreased from 130% to 86%; and
- the payable credit rate decreased from 14.5% to 10%.

For a loss-making company with, say, £20,000 of qualifying R&D expenditure, the payable tax credit will reduce from £6,670 to £3,720. So, as you can see, these changes may be very significant for some R&D businesses.

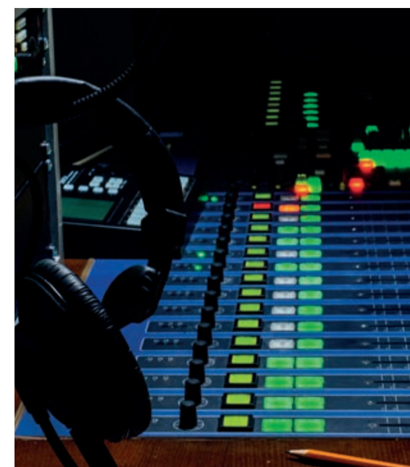
At the Budget in March, the Chancellor announced that a new credit rate will be available to 'R&D intensive companies', i.e. loss-making companies where R&D expenditure constitutes at least 40% of total expenditure. Qualifying companies will be able to claim a payable credit rate of 14.5% for qualifying R&D expenditure, instead of the new 10% credit rate under the existing SME scheme.

Further changes ahead

Large companies have a completely different scheme to encourage R&D expenditure, called the RDEC (Research and Development Expenditure Credit). A minority of small and medium companies also have to use this relief, for example if their R&D is grant-aided.

The government has announced that it intends to move all companies to an RDEC-type system of R&D relief in the future, although whether this will be formalised before the upcoming General Election is not yet clear.

If your company incurs qualifying R&D, please make sure you understand the implications of all these changes and speak to us if you need help in navigating this new, more onerous compliance regime. We don't want you to miss out on valuable tax relief.



Audio-visual tax reliefs

The film, TV and video games tax reliefs will be reformed, becoming expenditure credits (similar to RDEC) instead of enhanced deductions, from 1 April 2024.

The new Audio-Visual Expenditure Credit (AVEC) will replace the current film, high-end TV, animation and children's TV tax reliefs. The expenditure threshold for high-end TV will remain at £1 million per hour.

There will also be a new Video Games Expenditure Credit (VGEC). Qualifying expenditure for the VGEC will be expenditure on goods and services that are used or consumed in the UK. Games that have not concluded development on 1 April 2025 may continue to claim EEA expenditure under the current video games tax relief, until this relief ends in April 2027.

Full details of these changes are still to be confirmed, but please contact us if you are concerned as to how they might affect your company.

This newsletter is written for the benefit of our clients. Further advice should be obtained before any action is taken.