2024 SPRING NEWS

Cheeld Wheeler & Co

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A look into the tax crystal ball

With a General Election due by January 2025 at the latest, we may have three major 'fiscal events' this year: The Budget on 6 March, an early Autumn Statement (possibly in September) and (assuming the Election is in the autumn) a post-Election Budget in November or December. What tax changes might be announced and how might they affect you?

Having cut National Insurance Contributions (NICs) in the 2023 Autumn Statement, the Chancellor and Prime Minister have made it clear that we should expect further tax reductions in the March Budget. The options likely to generate the most political benefit are probably any combination of a cut in the basic rate of tax to 19%, a further reduction in NICs or the unfreezing of the higher rate tax threshold (which has been £50,270 for several years, bringing more and more people into the 40% tax bracket as earnings rise). There has also been talk of changing how the High-Income Child Benefit Charge (HICBC) works, so that fewer people with young children will suffer this additional tax charge.

Given the state of the public finances (which has caused the International Monetary Fund to say that tax cuts are not really affordable at the moment), we may find that there are tax cuts announced but that they are delayed a year in their implementation.

The contents of any post-Election Budget will obviously depend not only on the economic circumstances at the time but also which party is in power. Labour has indicated that it does not intend to raise the main tax rates on income, but may make major reforms to the capital taxes (and in the process increase the tax collected). Either party could follow in the footsteps of George Osborne in 2015, when he raised extra revenue without raising any of the rates of income tax or NICs. This was done by making changes such as restricting top rate tax relief on pension contributions, restricting tax relief on finance costs for residential landlords and increasing the tax rates on dividends. Jeremy Hunt has already effectively done the latter by cutting the dividend allowance from £2,000 to £500 (which is the new figure for 2024/25).

Scotland has different tax rates and bands for non-savings, non-dividend income (e.g. employment income, business profits, rental income and pension income). The Scottish Budget has already taken place. Among the measures announced for 2024/25 were:

- A new 'advanced' tax rate of 45% that will apply to income between £75,000 and £125,140.
- The top rate of tax (that applies above £125,140) will be increased to 48% (from 47%).
- The 19% starter, 20% basic, 21% intermediate and 42% higher rates will be unchanged, along with the higher rate threshold (which is frozen at £43,662, significantly lower than the £50,270 that applies in the rest of the UK).

In this newsletter, we make you aware of recent developments that may affect you or your business, irrespective of the tax uncertainties mentioned above. These include the new National Minimum Wage rates, when it might be worth appealing against penalties for failure to pay the HICBC and (believe it or not) how the VAT rules distinguish between biscuits wholly or partly covered with chocolate and other biscuits! Other topics include a discussion of the VAT rules for cars and how a recent case has clarified the manner in which the Capital Gains Tax (CGT) main residence exemption works when you buy a residence, knock it down and then live in the replacement residence you have built.

It should be an interesting year ahead as far as tax is concerned. We will be here to help you navigate any changes announced, so please contact us if you need further guidance, particularly on topics in this newsletter.

Cars for business: VAT issues

In our Autumn 2023 Newsletter, we covered a number of the tax issues associated with business cars, such as capital allowances and employee benefits. As promised, we now highlight some of the key VAT points of which to be aware.

What is a 'car' for VAT purposes?

The definition of a car, for VAT, is different to the definitions for capital allowances and employee benefit purposes. It is any motor vehicle of a kind normally used on public roads which has three or more wheels and either:

- is constructed or adapted **mainly for carrying passengers;** or
- has, to the rear of the driver's seat, roofed accommodation which is fitted with side windows or which is constructed or adapted for the fitting of side windows

However, there are some exceptions:

- Vehicles capable of accommodating only one person, or suitable for carrying 12 or more people, including the driver;
- Caravans, ambulances and prison vans;
- Vehicles of at least 3 tonnes unladen weight;
- Special purpose vehicles, such as ice cream vans, mobile shops, hearses, bullion vans and breakdown & recovery vehicles;
- Vehicles with a payload of one tonne or more.

Recovery of VAT on car purchases

Normally, a VAT-registered business **cannot** recover the VAT on the purchase of a car. However, you may recover VAT in full on a car which:

- is a **stock-in-trade** of a motor manufacturer or dealer; or
- is intended to be used primarily as a **taxi, driving instruction car, or for self-drive hire;** or
- will be used exclusively for the **purposes of your business** (i.e. there is no intention to make the car available for the private use of anyone); thus, a pool car is eligible for VAT recovery.

Hire purchase v Leasing: VAT comparison example

Suppose a business owner buys a van or car of cash price £20,000 plus VAT (£4,000); ignore finance costs of the agreement for this example.

Hire purchase

Initial invoice will show £20,000 + £4,000 VAT.

- Van – trader can recover this VAT in the VAT period of purchase
- Car – the VAT is not recoverable (unless e.g. a pool car)
- No separate VAT is charged on the instalments.

Finance lease

Each instalment will have VAT charged on it, rather than being all on an initial invoice.

- Van – the VAT is recoverable, unless using the Flat Rate Scheme
- Car – **50% of the VAT is recoverable,** irrespective of the CO_2 emissions of the car [NB This is a special rule for leased vehicles]
- Full VAT recovery (subject to the usual partial exemption and business use tests) is available for ongoing maintenance of leased cars.

Motorbikes are not cars, so input VAT is claimable, subject to any adjustments for partial exemption or non-business use.

VAT on electric vehicles

An electric car will still be viewed as a car for VAT purposes so, if there is any private use of the car, VAT is not recoverable on the purchase. The VAT can however be reclaimed if there is no intention to make the car available for private use.

If an electric car is leased, where there is any private use of the car, only 50% of the VAT on the leasing charge can be recovered.

Revenue & Customs Brief 7/21 – Electric vehicles

This gives HMRC's views on the VAT liability of charging of electric vehicles and the circumstances in which the VAT charged can be recovered as input tax.

The reduced rate (5%) that applies to "domestic" supplies of electricity does not apply to charging of vehicles in public places. The standard rate will therefore apply when someone uses a public charging point.

Recovering input tax for charging electric vehicles

You can recover the input tax for charging your electric vehicle if **all** the following apply:

- you are a sole proprietor (i.e. self-employed);
- you charge your electric vehicle at home or a public charging point;
- you charge your electric vehicle for business purposes.

You can recover VAT on only the business use amount, so keep accurate mileage records. The rate for recovery of input tax for charging electric vehicles is the same as the VAT rate charged on the supply of that electricity.

Employees

If employees charge an electric vehicle (which is used for business) at home, they cannot recover the VAT. This is because the supply is made to the employee and not to the business.

If employees charge an employer's electric vehicle (for both business and private use) at the employer's premises, the employee needs to keep a record of their business and private mileage so that the employer can work out the amounts of business use and private use for the vehicle. The employer can recover VAT on only the business element.

Alternatively, the employer can recover the full amount of VAT for the electricity used to charge the electric vehicle (inc. the electricity for private use). However, they will be liable for an output tax charge to reflect the private use. This is because a 'deemed supply' has been made.

If you need any help in understanding the VAT issues of cars for your business, please get in touch.

ULEZ fees

The Ultra Low Emission Zone (ULEZ) was expanded to all London boroughs on 29 August 2023. From this date, drivers of vehicles that do not meet the emissions standards must pay a daily charge of £12.50 when driving within this area.

HMRC has confirmed that self-employed taxpayers are entitled to claim tax relief on LEZ charges, including London's ULEZ fee, as long as they have been incurred 'wholly and exclusively for the purposes of the trade' (i.e. incurred on a journey that was for business purposes).

National Minimum Wage (NMW) rises

The rates of NMW and National Living Wage (NLW) are once again set to rise significantly. The rates that will apply from 1 April 2024 are as follows:

	NMW Rate	Increase(£)	Increase(%)
NLW (21 and older)	£11.44	£1.02	9.8%
18-20 year-old	£8.60	£1.11	14.8%
16-17 year-old	£6.40	£1.12	21.2%
Apprentice Rate	£6.40	£1.12	21.2%

Note that the NLW will apply from the age of 21, rather than from 23 as it currently does. Employers often deduct small sums for uniform, food, childcare vouchers or even for places at the child nurseries where the employee works. All of these sums must be taken into account when calculating the net wage (before tax) which HMRC checks against the relevant NMW rate.

Please talk to us before setting up any form of salary substitution, so that we can check that the NMW rules are not being broken.

More changes for unincorporated businesses

Unincorporated businesses are going through their biggest tax change for a generation, with the switch to a tax year basis of assessment for profits, rather than the 'basis period' system. Further change is on the way.

For the last ten years, smaller businesses have had the option of preparing their tax computations on a cash basis (i.e. looking at when money is received or paid) rather than the normal accruals basis of accounting. The latter matches income and expenditure to the periods to which it relates, irrespective of when amounts are paid or received.

Legislation is being introduced to expand the cash basis for self-employed taxpayers, including those in partnerships, from the tax year 2024/25. The changes will not apply for property businesses, companies or those entities already excluded from the current cash basis regime (such as farming and creative businesses making a profits averaging election).

The changes will make the cash basis the **default method** of calculating profits, with businesses able to opt to use the accruals basis instead. Businesses can currently use the cash basis if their turnover is less than £150,000 p.a. and must leave the cash basis when their turnover exceeds £300,000. These restrictions will be removed completely.

Where the cash basis is used, there is currently a limit of £500 on the amount of interest which the business can deduct for tax purposes against the profits for the year. This limit will be abolished, allowing tax relief for full interest costs, as long as they are 'wholly and exclusively' for the purposes of the trade.

Lastly, the current restrictions on the utilisation of losses under the cash basis will be removed, so that losses can be set against general income of the same period or carried back to earlier years (as with losses under the accruals basis and subject to the same conditions).

This change will be significant for all unincorporated trading businesses, particularly as regards whether to elect to stay with accruals accounting in 2024/25. We can discuss the pros and cons with you.

Don't look a gift horse...

People come up with all kinds of ways of trying to avoid tax on income. HMRC will usually challenge anything they see as unreasonable tax avoidance or, worse still, tax evasion. A classic example of this has been heard by the Tax Tribunals recently, involving a lawyer working for the Ecclestone family of Formula 1 fame. The main facts were:

- The appellant in the case received payments totalling almost £40 million, from 1999 to 2013.
- Payments of £2.25m were made to induce him to resign as a partner in a law firm so that he could work for the Ecclestone family.
- Three further payments totalling £36m were then made to Mr Mullens by Mrs Ecclestone.
- He did not declare these as income on his tax returns for the relevant years, instead asserting that they were gifts because of his close relationship with the family.

HMRC issued assessments and assessed penalties, some of which were under the provisions allowing them to go back 20 years where there has been fraudulent or deliberate conduct.

The Upper Tax Tribunal upheld the decision of the lower tribunal, finding that all the assessments were properly issued and that the penalties were valid. This was because all the payments in question in the appeal were clearly income derived from his work for the family. The appellant knew that they should have been disclosed on his tax returns for the tax years in question, but he made a conscious and deliberate decision not to disclose them.

If someone suggests to you a simple way of avoiding tax on income completely, it is probably too good to be true. Please get a second opinion from us, to make sure that you don't in fact have a lot of penalties as well as tax to pay.

Blissful biscuits

The rules about whether food is standard rated or zero-rated for VAT purposes are notorious for having some provisions that are open to interpretation, as has been shown in a recent case.

United Biscuits (UK) Ltd manufactures McVitie's 'Blissfuls'. For the benefit of those of you who have not sampled them, they consist of:

- a biscuit cup with a flat bottom base;
- a layer of chocolate hazelnut and a layer of chocolate;
- a McVitie's logo made of biscuit on top, which does not cover the entire top, so leaving some of the underlayer of chocolate exposed .

The company zero-rated this product as food. HMRC argued that the product should be standard rated, as it fell within the exception for 'biscuits wholly or partly covered with chocolate or some product similar in taste and appearance'.

The company claimed that:

- the product's lid served more than a decorative function, as it ensured that the product kept its shape and provided a crunchy texture before the consumer tasted the chocolate filling;
- to be a covering, the chocolate must be the first part of the biscuit to be bitten into;
- as the chocolate was not the first part, it was simply a filling, and the exception did not apply.

The Tax Tribunal agreed with HMRC that the product was standard rated, as the legislation requires the product to be wholly or partly covered with chocolate. The term 'partly' should be interpreted in such a way that it could apply to any part of the biscuit that was covered to some extent with chocolate. The key question was what covered the remaining area of the product that was not covered by the biscuit logo lid. The judge felt that the ordinary person in the street would say that the biscuit was covered by the logo biscuit lid and 'in part' by a layer of chocolate. Being partly covered in chocolate, it fell within the exception to zero-rating and the standard rate of VAT applied.

Losing a VAT case like this can mean having to pay extra VAT, interest and penalties going back many years.

If you are involved in a food or drinks business, don't fall into a similar tax trap. Check with us if you are uncertain of how your products should be treated for VAT.

Child Benefit tax charges

The High-Income Child Benefit Charge (HICBC) was introduced in January 2013. The rules can be quite complex, but it essentially starts to claw back Child Benefit (which remains a tax-free payment) by levying a tax charge on the higher income person of a 'family unit', if that person has relevant income above £50,000. By the time income reaches £60,000, the tax charge is enough to claw back all the child benefit received by either parent. Note that the charge can apply even if the couple are not actually married.

The £50,000 threshold at which the charge begins has not been increased since HICBC was first introduced; indeed, as the threshold at which the 40% tax rate begins to apply is now income above £50,270, you no longer even need to be a higher-rate taxpayer to suffer the charge!

More and more people are coming within the scope of the HICBC as earnings rise. Consequently, there have been a lot of tax cases over the last three years where appellants have argued that they have a 'reasonable excuse' for not having declared and paid the charge. Most of these cases are won by HMRC. To be successful at appeal, the appellant would normally need to show that they:

- were not under an obligation to complete a tax return for the tax years prior to that in which the HICBC applied because, primarily, they were paid through PAYE and had no other income to justify a return being made;
- were in receipt of child benefit payments prior to the introduction of HICBC, with the consequence that the application for Child Benefit made no reference to HICBC; [NB the Child Benefit claim form, since the introduction of HICBC, clearly sets out when the charge applies.]
- had not received notification from HMRC directly at any point prior to the contact which led to the issues of the tax assessment; but
- acted promptly in ceasing to claim Child Benefit and engaged actively with resolving the historic tax liabilities as soon as HMRC did make contact.

If you feel you may have unwittingly failed to pay the HICBC, please get in touch to discuss the best way of disclosing this to HMRC, as this will lead to greatly reduced penalties compared to HMRC coming after you for the tax!

PPR relief: Demolished and rebuilt dwellings

Principal private residence (PPR) relief (broadly) applies to gains accruing to individuals on the disposal of (or of an interest in) all or part of a dwelling house that has (or has at any time during their period of ownership) been their only or main residence.

No part of a gain to which PPR relief applies is a chargeable gain if the dwelling house has been the individual's only or main residence:

- throughout their period of ownership, or
- throughout their period of ownership, except for all or any part of the last nine months.

Period of ownership

Suppose someone buys a dwelling house, has it demolished and builds a new dwelling house on the same land as the old one. For PPR relief purposes, does the 'period of ownership' relate to

- the land on which both houses were built, or
- the period during which the new house existed.

If the period of ownership relates to the land, there will be a period between the old house being demolished and the new house being built when there was no residence as such (and therefore no occupation as a residence), resulting in a potential restriction on the amount of PPR relief available on a future disposal.

If the period of ownership relates to the newly built dwelling, then if it was occupied as the individual's only or main residence until its eventual disposal, PPR relief shouldn't be restricted at all.

A recent case at the Upper Tax Tribunal has confirmed that it is occupation of the newly built dwelling that is relevant and that there should be no apportionment of relief to restrict it for the period when no dwelling existed on the land. This is the case, even if the land was increasing in value while the new property was being built!

The decision ties in with a similar case at the Court of Appeal in 2019, where someone bought a property 'off-plan' and occupied it when it was finally completed over three years later. After living in it for two years, the property was then sold for a considerable profit. The gain he made on sale was held to be fully exempt under PPR relief, even though he could have sold the property before the dwelling was completed and, if he had done so, no PPR relief would have applied to any gain.

PPR relief can be a lot more complicated than people think. For example:

- You need to show that you have occupied the property with the intention of living there as a 'home' with a degree of permanence; and
- There are special 'deemed occupation' rules that mean you can be treated as having been living in a property even when you weren't!

Please contact us if you wish to discuss any aspects of PPR relief, but note that it will never be available on a property that you have never occupied as a home.

Environmental and technical studies

Windfarms have been much in the news recently and there are certainly lots of start-up companies looking to make money from the switch to green energy. Many of them will be incurring significant costs before, hopefully, starting to make profits.

Unfortunately, the tax rules do not always work in a way that encourages such businesses, as was shown in a recent Upper Tax Tribunal case. The companies were involved in the trade of generating and selling electricity from UK offshore wind farms.

Numerous pre-installation studies were carried out (costing £48m) to assess the best positioning for the wind turbines, for example in relation to wind, ocean and seabed conditions. The appellants included this expenditure, along with expenditure on the actual wind turbines, as part of their qualifying expenditure for capital allowances.

Section 11 of the Capital Allowances Act 2001 sets out that expenditure can be considered qualifying when incurred 'on the provision of' plant and machinery. HMRC accepted that the building and installation of the wind turbines and associated cabling (the generation assets) qualified, but rejected the claim regarding the studies.

As earlier case law had held, the key principle here was that expenditure on the construction, transport and installation of plant could be qualifying, provided that the effect of the expenditure was the provision of plant. Expenditure (such as the studies in this case) could be necessary, but not have the effect of providing the plant. Thus, the £48m was not eligible for capital allowances.

An alternative argument, that the expenditure should be regarded as an allowable revenue expense on the basis that it was wholly and exclusively for the purposes of the company's trade, was also rejected. It was clearly capital expenditure, as it was linked to the installation of capital assets (the turbines), despite not being on the 'provision of' them.

As you can see, in our complex tax code, the treatment of expenditure is not always obvious! Failing to attract tax relief increases the effective cost to the business of the expenditure.

Please check the tax treatment with us before your business incurs significant expenditure, as the tax relief available may impact the decision as to whether to proceed or not.