client briefing

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Incorporating McNaughton & McAra

What price accommodation?

The huge increase in house prices in recent years has led some employers to provide free accommodation for directors and employees. But employers should remember that there is a special tax charge when they provide living accommodation for a director, employee, or a member of their household.

'Living accommodation' is broadly defined and includes everything from houses, flats and apartments to house boats. Some accommodation is exempt from tax, for example where:

- An employer provides board and lodgings or hotel accommodation in conjunction with a qualifying business journey.
- The accommodation is necessary for the proper performance of duties.
- Accommodation is provided as part of customary practice.

The exemptions for necessary performance and for customary practice do not apply to directors unless the director has no material interest in the company (5% or less) and either works full-time for the company, or the company is non-profit making or is set up for charitable purposes only.

Tax on living accommodation

When accommodation costs £75,000 or less, the tax charge is based on the gross rateable value of the property, or the actual rent paid by the employer, less any amounts contributed by the employee.

When accommodation costs more than £75,000, there is an additional tax charge. This is based on the cost of the accommodation and improvements, taking into account any amounts contributed by the employee, less £75,000; this amount is then multiplied by HM Revenue & Customs' official rate of interest.

If the employer has owned the property for more than six years before the employee first occupied it, the market value is substituted for the cost of purchase and any improvements.

For directors and higher paid employees, there is an additional tax charge on the cost of any other services provided.

Redundancy: not just a numbers game

Employers need to take great care when dismissing an employee – especially where age discrimination may be involved, as a recent case has shown.

Employers must act reasonably and follow statutory procedures, or else they could end up facing a potentially expensive claim for unfair dismissal. A dismissal is treated as 'fair' if it is for any of the following reasons:

- Bad conduct or the employee's inability to do the job, or some other duty as imposed by the employment contract.
- Redundancy, which can occur for economic reasons or changes in the business.
- Retirement, where the employee has reached retirement age for that employment, or the default retirement age of, for example, 65.
- Some other substantial reason, for example, where a temporary post has come to an end.

However, employers must show that they followed the correct procedures:

- If dismissal is on disciplinary grounds, employers must use an established procedure, and if dismissal is because of incompetence or lack of capability, it must be shown that an opportunity to improve was offered.
- When redundancy gives rises to dismissal, employers must consult with the employee, or employee representatives, and the redundancy must be on grounds that do not discriminate against workers. The chosen criteria must be consistently applied and be objective and fair.
- Employers must give six months' notice if dismissal is due to retirement, but employers are also obliged to consider an employee's request to work beyond retirement age.

Age discrimination may affect the selection of an older worker for redundancy following the judgement in *Killa v Electronic Motions Systems Ltd* (2008).

59 year-old Mr Killa was selected for redundancy and was immediately dismissed. The Tribunal found that his employer had failed to use objective criteria or a proper selection process to determine which employees were to go, and although there was alternative work available in the company it was not offered to him. In awarding damages for future loss of earnings, the Tribunal increased them to counter the effect of discrimination against older workers when considering Mr Killa's chances of gaining future employment.

VAT on cross-border services

If you supply or receive cross-border services, beware of changes to the VAT rules that will come into effect EU-wide on 1 January 2010. Services that were not liable to UK VAT before that date could now become liable, and vice versa.

A service is liable to UK VAT if it takes place in the UK. Currently, the basic rule (subject to exceptions) is that the service takes place where the supplier 'belongs' (is established). From 1 January 2010, this treatment will still generally be true if the customer is a private consumer (a non-business customer), but if the supply is to another business, the service will generally be treated as taking place where the customers are established. Under the reverse-charge rules customers will then have to account for VAT in their home country on that service. There will, as before, be exceptions to the basic rule, such as for hiring vehicles, transport of goods, services connected with land etc.

Although the new rules will greatly reduce the number of occasions where a business incurs VAT outside its own Member State, there will also be added bureaucracy. Businesses will be expected to report services supplied to and taxed in other Member States, and not just goods (as now), in their EC Sales Lists.

Retaining your title?

When a customer becomes insolvent and you have not been paid for the goods you have supplied a 'Romalpa', or 'retention of title', clause will put you in a much stronger position. A retention of title clause in a sales contract allows a supplier to transfer goods to a customer, yet retain the legal and beneficial title for those goods until they are paid for.

If the customer defaults on payment, the supplier can enter the customer's premises to inspect or remove its goods. The customer will also accept an obligation to insure the goods and store them separately so that they can be identified.

Contract clauses need to be modified for different types of goods and according to what the supplier wants. It depends on what the customer intends to do with them after taking delivery.

For example, the most basic retention of title clause will not be effective if the goods are immediately re-sold, or are incorporated into a building or manufacturing process because they can no longer be separately identified.

Where a supplier is selling a high volume of goods on credit to the same customer, it may not be practical to separately identify each item and match it to a particular payment made.

Contract clauses can be modified to include:

A **retention of title clause**, allowing the supplier to remove its own goods. It will generally contain a clause to claim the proceeds if its own goods have already been sold on.

An **aggregated title clause**, allowing the supplier to retain title of the output, or a portion of it, that has been produced after its goods have been incorporated into a building or manufacturing process.

An **all sums clause, or all monies clause**, which is suitable where there is a high volume of goods and matching each item to an amount paid is complicated. Title to goods will not pass until all sums for all debts owed by the customer are paid.

A **proceeds of sale clause**, which is useful where the goods are to be modified for use in a manufacturing process or building. This will allow the supplier to sell off or acquire the title in the goods or building that is created.

While these clauses all provide a protection for the supplier if a customer defaults on payment or goes bankrupt, it is difficult to ensure that goods are not damaged. Conflicts may also arise with other suppliers if they have also included aggregated title and proceeds of sale clauses into their contracts. Of course, a contract will combine several clauses so legal advice is required.

All companies will have to file their tax returns online from 1 April 2011 for accounting periods ending after 31 March 2010. They will also have to pay corporation tax electronically. The requirements also apply to clubs, associations and other unincorporated bodies that make corporation tax returns. Paper returns will no longer be accepted by HM Revenue & Customs.

Many companies already file online, but at present you simply attach your accounts as a pdf document. From 1 April 2011, accounts and tax computations will have to be in Inline XBRL (eXtensible Business Reporting Language). Companies House will use the same system and joint filing should be possible.

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There is no longer a £100 fixed penalty for people who are more than three months late in telling HM Revenue & Customs (HMRC) that they are self-employed – but delay could still be very expensive. Anyone who starts a business after 5 April 2009 should still tell HMRC immediately so they can start paying the right amount of national insurance contributions (NICs). However, they will only be penalised if they have not notified HMRC by 31 January following the end of the tax year in which they became self-employed. The downside is that the penalty can then be up to 100% of the unpaid NICs, depending on the circumstances, although it will usually be 30%. There will be further penalties if income tax is paid late as a result of late notification.

The road ahead for car benefits

A dramatic rise in the tax charge on company cars at the luxury end of the market is in store for some high-earning directors and employees from 6 April 2011.

The main change is the removal of the £80,000 price cap. The car benefit is calculated by applying a percentage to the car's list price. This percentage depends on the car's CO_2 emissions figure, and ranges from 15% to 35%. However, the maximum list price for this at present is £80,000. This means that the highest annual car benefit an employee or director could face in a year is currently £80,000 x 35% = £28,000. At a top rate of tax of 40%, this results in extra income tax of £11,200.

From the 2011/12 tax year, the price cap will be removed and the actual list price will be used to calculate the benefit. When you consider that the top rate of income tax will then be 50% for individuals with taxable income of more than £150,000, the resulting effect will in some cases be quite startling. For example, a director earning well in excess of £150,000 and driving a car costing £140,000 will be paying tax of £11,200 this year (2009/10), £14,000 next year (2010/11) but £24,500 in 2011/12.

Other changes include lowering the emissions bands to which each 'appropriate percentage' applies by 5g/km next year and another 5g/km in 2011/12. The effect for most drivers will be to increase the percentage used by 1% in both years. For the majority of directors and employees, who have cars below £80,000 in value and earn less than £150,000, the change will mean an extra £80 of tax for 2010/11 and another £80 the following year.

Whereas this is relatively insignificant, the cumulative effect of the changes is to further increase the tax burden on company cars, both for employees and employers through increased national insurance contributions. Nor is any government likely to lighten it in the foreseeable future.

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