UK200Group tax
talking tax

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Child Benefit Income Tax charges…

At time of writing, the Finance Bill 2012 is passing through the House of Commons. Comprised within that Bill is legislation imposing a new income tax charge on a taxpayer who has adjusted net income over £50,000 in a tax year, where either they, or their partner, is in receipt of Child Benefit for the year.

Put very simply if an individual or their partner receive Child Benefit and either of them have net taxable income of more than £50,000 per year, they will have to pay more tax. The charge will be one per cent of the amount of child benefit for every £100 of income that exceeds £50,000. Once the annual income hits £60,000 the full amount of Child Benefit will be cancelled out by an equal amount of extra tax.

Child benefit itself is not becoming taxable income and the amount that can be claimed is unaffected by the new charge. Individuals can however elect not to receive their child benefit if they or their partner do not wish to pay the new charge. That election may subsequently be withdrawn if they or their partner are no longer liable to pay the charge.

Those entitled to Child Benefit can qualify for National Insurance credits which can help to protect future entitlement to State Pension. Therefore those on high incomes, or whose partners are on high incomes and are facing the tax charge, may wish to give up receiving their Child Benefit but need to keep their claim in place to preserve their rights.

There is a useful overview of the proposals in a Q &A document found on HMRC's website at:
http://www.hmrc.gov.uk/budget2012/cb-income-tax.htm

There are a couple of important definitions not detailed in the Q & As :-

1. What comprises a "partnership" for these purposes?

It is defined as:

- a married couple living together;
- civil partners living together;
- a man and a woman who are not married to each other but who are living together; or
- a man living with a man or a woman living with a woman who are living together as if they were civil partners.

2. What is "adjusted net income"?

In order to calculate this, the starting point is "net income" which is the total of the individual's taxable income. This includes income from employment, self – employment profits, pensions, property income, savings and dividends – less specified deductions. The most important of the specified deductions are trading losses and gross pension scheme contributions.

This net income is then reduced by the grossed-up amount of the individual's gift aid contributions and the grossed-up amount of the individual's pension contributions. The final step is to add back any relief for payments to trade unions or police organisations deducted in arriving at the net income.

It is proposed that the regulations will have effect from 7 January 2013 and will affect approximately 1.2 million families. Approximately 70 per cent of these households will lose all of their Child Benefit, and 30 per cent will lose a portion. In addition it is estimated that these regulations will mean an additional 0.5 million individuals will need to complete a SA tax return!

HMRC will receive a list from the Child Benefits Office of all those receiving benefit and in the Autumn of this year will be writing to all those potentially affected.

Without wishing to be cynical, it will be interesting to see how this will work in practice. For instance, how will HMRC obtain reliable and up-to-date information about an individual's living arrangements?

It is not unreasonable to assume that in a lot of cases the latest records of income and financial information that HMRC will have will be for the year ended 5th April 2011. This in itself will cause a myriad of logistical issues where for instance:

- Since then, the personal income of the individual or their partner has risen or fallen above the £50,000 limit;
- The individuals have separated or one individual starts living with someone in receipt of Child Benefit.
- An individual receives Child Benefit and starts living with someone who has income of more than £50,000 – would they necessarily know their new "Partner's" income?

Closer to home, as Tax Agents, we need to address both tax-planning to reduce net income below the £50,000 threshold and the new information we may now need to ask of clients.

For example if we do not already know, we will have to enquire into household living arrangements, number and ages of children, and co-habitee's earnings.

About the author …

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Page 2 *- for Q&A's this month from Tax Panel member Duncan Montgomery of Whittingham Riddell LLP*

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UK200Group Talking Tax Q & As – May 2012

Members of our Tax Panel each month look at issues they have come across and share these with members and readers of UK200Group's Talking Tax.

This month's Q & As are supplied by Duncan Montgomery of Whittingham Riddell LLP

Q I have a large Director's Loan Account with my company which arose on incorporation; how can I mitigate the potential IHT on his balance?

A To the extent that your Director's Loan Account with the company remains positive (that is, with money owed by the company to you personally) this balance would normally be viewed as a cash-equivalent asset in your estate for IHT purposes and would not attract BPR on death. This could therefore give rise to a 40% IHT liability were you to die prior to the loan being repaid. Once the loan is repaid by the company, to the extent that those funds are not reinvested in qualifying assets and/or gifted out of your estate, the cash would also form part of your chargeable estate for IHT purposes.

With qualifying trading companies it may be possible to structure such loan agreements so as to confer certain voting rights and thus ensure that they too would attract BPR in the same way as a shareholding in that company. The drafting of the loan agreement is key to securing the entitlement to BPR on death and it is important that this document is reviewed and updated by your legal and tax advisors so as to ensure that BPR would be available on the loan, were you to die prior to it being repaid by the company.

Q I plan to dispose of my 5% shareholding in a company of which I am an employee but the company does not have sufficient cash to purchase my entire holding outright – how can I preserve Entrepreneurs' Relief on a future disposal? The shares have been held for a minimum of five years and with no ready market for the shares a company buy-back of shares was the preferred route.

A It is still possible to dispose of your shareholding in its entirety, so as to effectively lock-in your entitlement to claim Entrepreneurs' Relief on disposal, by selling your entire holding to a newly-formed company under your control, with a subsequent on-sale of a proportion of the shares to the company when it has sufficient cash to buy-back the remaining shares.

Under either of these routes the full gain on the entire shareholding would be brought into charge at the time of the disposal, notwithstanding the fact that a proportion (or indeed all) of the consideration would not be cash-paid at the point at which the Capital Gains Tax was due.

The sale of shares to the newly-formed company would create a liability from that company to the individual, by way of a Director's Loan Account; to the extent that subsequent disposals of shares in the company are made from the newly-formed company the cash consideration could be paid out to you tax free, so as to reduce the outstanding loan account.

Any increase in value of the company's shares in the intervening period would be chargeable to Corporation Tax, (around 20%), however the shares would benefit from uplift in base cost to market value at the time of the original disposal.

Q Are parking fines always disallowable in computing trading profits of a business?

A Fines (including parking fines) are generally not deductible expenses, which historically has been based upon the fact that they have represented a penalty for breaking the law.

In our experience there may be scope to claim a deduction for parking fines if this expense is regarded as "compensatory" rather than "punitive". The fact that these 'fines' are in many cases levied by an agent of the landlord (as opposed to the police or other statutory body) may support grounds for a claim. Depending on the nature and frequency of these charges there may be merit in revisiting the underlying paperwork to see whether the 'fines' are in fact described as such, rather than, say, additional parking surcharges. In some instances there may be scope to claim a deduction for these amounts, though of course care should be given to how these are described in the computations to mitigate risk of enquiry from HMRC.

For further information on any of the above …
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UK200Group tax

UK200Group Tax Panel members are renowned for their depth of knowledge and can advise on all areas of taxation with special expertise and experience of multinationals, UK companies, privately-owned organisations, sole traders, family businesses, trusts, partnerships and private individuals. Straight forward general enquiries will be dealt with quickly and free of charge. More complex specific client enquiries may require a fee charge which will be discussed and agreed by both parties prior to any work being undertaken.

Tax enquiries can be posted to www.uk200group.co.uk members' home page under member's queries. The Centre is alerted to all enquiries posted on the UK200Group web site.

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