

# Tax Matters

## Tax Efficient Strategies in the Current Economic Climate

In the current economic climate businesses are focusing on reducing costs wherever they can. As with other business costs, business and personal taxes are inevitably set to increase as the government faces the consequences of huge budget deficits. Managing tax costs should therefore be a vital part of your business's overall cost and cash flow management strategy.

This newsletter aims to highlight some of the available tax reliefs, exemptions and planning ideas that may assist in managing your business costs and cash flows.

## Management of Current Tax Liabilities

### Deferring Tax Payments

If you are currently facing cash flow problems and you are unable to pay your tax on time then we could assist you by negotiating a deferral of your tax liabilities with HMRC. HMRC have stated their commitment to assist taxpayers (both individuals and businesses) having genuine difficulties in meeting their tax liabilities. They are doing this by facilitating formal "Time to Pay" arrangements which are designed to bring businesses' and individuals' tax affairs back on track within reasonable timescales which are appropriate to the taxpayer's particular situation.

This "Time to Pay" initiative covers most taxes and duties including Income Tax, Corporation Tax, VAT, PAYE and NIC. In our experience HMRC's dedicated Business Support Service have been receptive in accommodating proposals put forward on behalf of businesses suffering from short term cash flow problems as a result of the credit crisis and who have therefore found themselves unable to settle their business (or personal) tax liabilities on the normal tax due dates.



## Making Best Use of Tax Losses

The 2008 Pre-Budget Report extended the loss carry back rules from 12 months to 3 years for business losses generated in the period from 24th November 2008 to 23rd November 2010. There is a cap of £50,000 on losses that may be carried back further than 12 months but for many small businesses a potential tax refund of £10,000 [20% of £50,000] can provide a much needed boost to their cash flow.

We can assist you by undertaking a full review of any losses to ensure their optimal utilization and with a view to potentially generating accelerated tax refunds by way of extended loss carry back claims which could provide your business with a vital cash flow boost.

## Maximising Capital Allowances

All businesses are entitled to 100% relief on the first £50,000 of expenditure on plant and machinery (excluding cars). This allowance is given for each tax year or accounting period but note that if it is not used in any period it cannot be carried forward for offset in a later period.

For expenditure over and above this £50,000 threshold, broadly speaking capital allowances would be available at a flat rate of either 10% or 20% depending on the type of expenditure incurred. Therefore, all expenditure above £50,000 needs to be carefully analysed in order to determine the applicable rate for capital allowances.

An exception to this general rule would apply to capital expenditure incurred on certain qualifying research and development projects where capital allowances at the rate of 100% of the expenditure would be available.

If you have company cars due for renewal, consider selecting a model with lower CO<sub>2</sub> emissions as this will save Class 1A NIC for you as employer and your employee will also save income tax. If the CO<sub>2</sub> rating of the car is less than 110g/km or is electrically propelled then first year allowances are available at the rate of 100% of the underlying expenditure.

If the CO<sub>2</sub> rating is between 110 g/km and 160 g/km, capital allowances of 20% of the underlying expenditure would be available. Note that this change compares favourably to the previous flat rate restriction of £3,000 per annum for cars costing over £12,000 under the old rules.

If the CO<sub>2</sub> rating exceeds 160 g/km the available capital allowances will be restricted to 10% but for the more expensive cars (i.e. those over £30,000) this may nevertheless be greater than under the old rules.

In addition there are 100% first year allowances available for the purchase of qualifying assets which are classified as “energy and water efficient technologies” and a tax repayment for losses arising from capital expenditure on such ‘green technologies’.

# Property Tax – Relief and Allowances

## Construction & Refurbishment

Capital allowances are a very complex area of the tax law and many property owners and investors lose out on thousands of pounds each year as a direct result of either lost or under-claimed capital allowances.

Whether you are engaged in a new build project of a commercial building or if you are simply refurbishing or extending an existing commercial building, you would be entitled to claim capital allowances on any capital expenditure incurred. This is regardless of the type of interest (long/short lease, freehold etc) you hold in the property. Every type of commercial construction contract will, bar a few exceptions, include expenditure which would qualify for capital allowances. If these allowances are not correctly identified and claimed, your business will be paying more tax than it needs to.

In some cases, it may even be possible to claim capital allowances in respect of historical expenditure incurred in prior tax periods and to obtain a tax repayment.

On a typical refurbishment project it is not uncommon to find that more than 75% of the total costs would constitute qualifying expenditure either as capital expenditure eligible for capital allowances or as revenue expenditure which would be wholly tax deductible in arriving at the taxable profits of the business.

If you have undertaken a construction or refurbishment project it is vital that a detailed review of the costs is carried out to identify those costs which would qualify for the normal 10% or 20% capital allowances, as well as those which may qualify as “energy or water efficient technology” as designated by HMRC, which would qualify for an immediate 100% relief against your business profits. If your business is loss making then these costs may be formally surrendered for a tax credit payment.

## Buying a Property

When buying a property it is essential that you consider the availability of capital allowances at the earliest possible opportunity and to ensure that your entitlement to claim these as the property purchaser is adequately protected prior to exchange of the purchase contract.

We have had significant experience in making claims for capital allowances in this context and we have helped many of our clients to substantially improve on the net yield generated by their properties by maximising capital allowance claims.

## Selling a Property

The consequences of inadequate planning prior to selling a property may result in a full repayment of capital allowances previously claimed. It may be possible to structure the disposal of your property in such a way as would allow you to retain the benefit of capital allowances already claimed and thereby retain the significant tax benefits already secured. This is only possible with adequate advance planning during the course of your negotiations with the purchaser and by incorporating the necessary provisions into the property sale and purchase contract.

Where capital allowances have not yet been claimed on a property which is to be sold, you

can justifiably use the inherent tax relief (by virtue of future capital allowances claims) as a valuable negotiating tool in pursuing higher and more competitive bids for the acquisition of your property.



## Business Premises Renovation Allowance (BPPRA) and Landlords Energy Saving Allowance

BPPRA can result in valuable cash flow savings by providing 100% initial capital allowances on the renovation or conversion of business properties that have been vacant for a year or longer in specified designated disadvantaged areas within the UK. If you have renovated or converted a previously vacant business property in one of the designated areas since April 2007 then this could represent a real cash flow saving opportunity. A formal claim for BPPRA must be made to HMRC so it is vital that all qualifying expenditure is properly identified.

Landlords (individuals, partnerships or corporates) who incur capital expenditure in installing loft insulation, floor insulation, hot water system insulation, draught proofing or solid wall insulation in residential properties may claim a tax deduction for the relevant expenditure up to a maximum of £1,500 per property in computing their taxable rental income.

## Business Rates on Empty Properties

It is now also possible to claim a temporary exemption for business rates if you own property with an annual rental value of £15,000 or lower. This was a change introduced in the November 2008 Pre Budget Report and will be applicable for a 12 month period starting from April 2009.

# Research & Development (R&D) Tax Relief



We have found that many companies are not aware that R&D tax reliefs could apply to their businesses and as a result they may be inadvertently losing out on substantial reductions in their corporation tax liabilities. Each company should critically evaluate all of its activities and operations and consider whether any part of these may be classified as constituting “development activities” under the provisions of the R&D legislation.

R&D tax relief is based on the ‘qualifying expenditure’ of a company (small or medium sized) being enhanced by 175% and for this enhanced expenditure to then be deducted from the company’s taxable profits for the relevant accounting period.

The main element of any R&D project’s qualifying expenditure will be the wages of the relevant staff engaged in the R&D project. If any part of the work is subcontracted to third parties then only 65% of the overall staff costs will qualify for the tax relief. Full relief will be available against the cost of any consumable items used in the R&D project.

In order to be eligible for R&D tax relief the company undertaking the qualifying expenditure must either own or have an interest in the intellectual property arising from the R&D activity. Where the relevant expenditure has been subsidised by non qualifying government grants, the relief will be reduced to only 130% of the expenditure.

Examples of qualifying R&D activities may include:

- The development of a new process or strategy that advances an area of your business or leads to the solving of technological uncertainty regarding a product, process or service
- Production technology that increases quality, reliability and performance or that reduces waste
- The creation of specialised tools or prototype tooling and machines
- Experimental trials and prototypes
- The transition from new product production to the production line
- The development of new production processes that are more environmentally friendly to meet the new and more onerous environmental legislation
- The creation of new software programming languages and interaction with other systems.

To summarise, any process or innovation that expands the level of technical knowledge in a particular field may potentially qualify for R&D tax relief. If a claim can be successfully agreed with HMRC this will generate a direct economic benefit in terms of reducing your company’s taxable profits or, where your company is currently loss making, in securing a tax credit payment from HMRC. Claims can be backdated to two years and (subject to this time limit) it is not too late to lodge a claim in respect of a

project which may have already been completed and to potentially secure a repayment of a historic corporation tax payment.

## Planning for Employment Related Costs

### Salary Sacrifice/Flexible Benefits Schemes

A significant component of typical business overheads would comprise employment related costs. A key consideration for any business in mapping out general cost cutting strategies whilst trying to maintain existing staff must include measures which would produce employment cost savings.

In an environment of pay freezes or even where pay cuts may be considered inevitable, salary sacrifice initiatives may be worth exploring whereby the employer and the employee mutually agree to a reduction in the cash salary payable in return for the provision of a non-cash benefit of equivalent value. Staff may be receptive to alternative non-cash incentives in lieu of salary like:

- flexible working arrangements
- the opportunity to buy additional annual leave, sacrificing their salary on a pro rata basis,
- salary sacrifice in lieu of pension contributions or the provision of childcare vouchers, both of which would provide both employee and employer with tax and NIC savings

We would also recommend that you review the costs of any existing benefits that you are already providing to your employees. You may be able to reduce the cost of certain benefits (for example medical insurance, life insurance) by shopping around for cheaper alternatives in what is currently a very competitive market.

*\* It should be noted that a salary sacrifice scheme may only be implemented with the prior approval of HMRC.*





## Share Incentive Schemes

A historically popular non-cash incentive scheme particularly for senior key employees within a business is the provision of share options as part of their overall remuneration package. The use of HMRC approved share option schemes is a very tax efficient method of rewarding key employees and it helps to encourage a sense of job security and loyalty to the employer company.

Broadly, an employee will be liable to income tax on the market value of any shares given to him (either directly or by way of an option to acquire them at a later date) by virtue of his employment. The benefit of providing shares by way of an HMRC approved share option scheme is that this income tax liability will be based on the market value of the underlying shares as at the date of the option grant and not on the date when the option is exercised and the underlying shares acquired.

Given the current economic climate when business values are generally depressed and are quite possibly at an all time low, it may be an opportune time to award shares or share options to key employees to lock them in for the long term in a tax efficient way and which can save the employer company immediate employment costs where such an incentive is structured to be partially in lieu of cash remuneration.

There are no immediate tax costs of establishing an employee share option scheme on either the employee or the business, thus providing you with a tax efficient method of rewarding employees.

## How we can help

If you would like to obtain additional information on any of these points, or you would like to discuss how we can help your business, please contact Kelly Garside on 01204 414263 or email [kelly.garside@cowgills.co.uk](mailto:kelly.garside@cowgills.co.uk)

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The information in this fact sheet should not be relied upon as giving sufficient advice in any specific case

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