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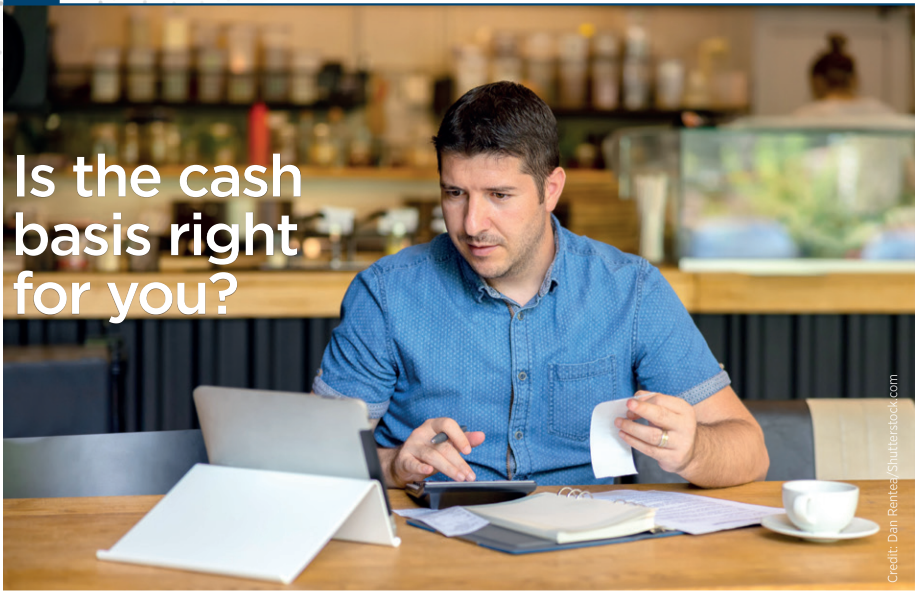
CHARTERED ACCOUNTANTS

TAX

Is the cash basis right for you?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HMRC plans to expand the availability of cash basis accounts preparation, but will it win over businesses from the traditional accruals basis?

The cash basis can currently only be used if a business's annual turnover doesn't exceed £150,000, so one option from HMRC is to increase this turnover limit to £1.35 million. But will this increase uptake?

Why opt for cash basis accounting?

For some businesses, the cash basis is helpful as it stands, because there is no need to take account of debtors, prepayments, creditors and stock. It also allows most equipment purchases to be simply deducted as an expense.

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But there are two significant restrictions:

- Currently, there is a £500 cap on interest costs. When interest rates are higher, this cap is not beneficial. Although HMRC is looking at increasing the limit – possibly to as high as £1,000 – the cap could remain a deterrent for some.
- Losses can only be carried forward – they cannot be relieved against other income or carried back. HMRC is considering relaxing these rules, but relief is unlikely to be as generous as when traditional accruals basis accounting rules are applied.

New businesses, in particular, may have higher borrowings and be more likely to make a loss.

There is also less scope for tax planning. Using the traditional method, a capital allowance claim, for example, can be restricted to maximise use of the personal allowance. Not so with the simplified cash basis.

The accruals basis alternative

Beyond tax, there are several other reasons for preferring accruals basis accounting. Cash accounting is less precise in matching revenues earned with money laid out for expenses, resulting in a less accurate picture of a business's performance. Such simplified accounts might turn out to be inadequate when it comes to applying for a business loan or a personal mortgage, for instance.

EMPLOYMENT

Flexible working – employment update

Employers need to be aware of changes to the flexible working regime expected in summer 2024. But proposals to give employees more flexibility for paternity leave are further away.

Flexible working

The big, expected change – the right to request flexible working from day one – is not included in the Flexible Working Act, which recently received Royal Assent.

However, it seems as if the Government still intends to make this change. The Act includes the following changes:

- Employees will be able to make two flexible working requests in a 12-month period (currently only one such request can be made).
- Employers will have to consult with an employee before rejecting their request. A formal meeting will be required, with no blanket ban on flexible working requests, and a reason will have to be given if a request is rejected.
- Employers will have to respond within two months, rather than the current three.

Flexible working doesn't only mean working from home. An employee might, for example, wish to match working hours with their child's school terms.

Paternity leave

The paternity leave regime currently means an employee can take two weeks of leave in the first 56 days after birth or adoption. Should the changes come into force, employees will be able to take two separate one-week blocks at any point during the first year.

Forrester Boyd
Chartered Accountants

Offices in:
Grimsby 01472 350601
Louth 01507 606111
Scunthorpe 01724 863105
Skegness 01754 761777
Beverley 01482 889400
Hull 01482 889400
Lincoln 01522 701843

info@forrester-boyd.co.uk
forrester-boyd.co.uk

TAX

Making the dividend or bonus decision

The end of the tax year is drawing near and many owner-directors of companies will turn their minds to deciding which is more tax-efficient: a bonus or a dividend.

Tax laws and rates that will affect your decision have changed since 2022:

- The dividend allowance has been halved, from £2,000 to £1,000 (with a similar cut to the capital gains tax annual exempt amount).
- The additional rate (top rate in Scotland) tax threshold has fallen from £150,000 to £125,140.
- Corporation tax rates have increased for companies with profits of more than £50,000 a year.
- National insurance contribution rates have been reduced for directors and employers.
- The pensions annual allowance has increased to £60,000 and the abolition of the pensions lifetime allowance is being phased in.

All these changes, which interact with each other, mean that the most tax-efficient way to draw profits from a company is likely to differ in 2023 from 2022.

Pension contributions?

An employer pension contribution could be a more attractive option for dealing with profits in 2023 than in 2022. For some, a pension contribution may not have made sense in 2022, because the lifetime allowance rules were still in force. These essentially limited the amount you could hold in your pension scheme. If those rules prevented you and/or your company from making pension contributions in recent years, this financial year end could be the ideal time to catch up.

There is no lifetime allowance charge in 2023/24 and the lifetime allowance is abolished entirely from 6 April 2024, meaning that you, or your company, can add as much as you like to your pension scheme. While they have to be justified, employer pension contributions can be significant, and would benefit from full corporation tax relief at the new, higher rates.

In practice, the complexities of pensions alongside other tax changes mean it is vital to seek advice before taking any action.

TAX

Inheritance tax penalties soar

The value of inheritance tax (IHT) penalties to government receipts has increased by more than half over the past two years, with higher property values and the frozen IHT nil rate band pushing more estates into the IHT net.

Last year, 4% of estates had to pay IHT, with an average tax bill of over £210,000. The most common reasons for HMRC charging a penalty are because:

- Forms are not filed on time or IHT is paid late. (The deadline is six months after the month of the death).
- Assets are undervalued or even omitted entirely. Valuing property of an unusual nature can be difficult, so it's wise to obtain a formal valuation from a qualified surveyor.
- Lifetime gifts, made by the deceased in the seven years before death, are overlooked. It can be difficult enough trying to establish cash gifts from bank statements, and there may be no record at all where gifts of assets, such as jewellery or antiques, have been made.

The seven-year look back requirement can be particularly confusing. More confusing still is where the deceased 'gifted' an asset, such as their main residence, to children, but then continued to live in it. Regardless of when the 'gift' was made, the property is still part of the deceased's estate.

Penalties for underpayment

The amount of penalty will depend on the circumstances leading to the IHT underpayment:

- Reasonable care has been taken – up to 30% penalty (but be warned that this let-out will not apply if a professional valuation hasn't been obtained for a property or other valuable assets).
- Assets have been deliberately omitted from an IHT return – up to 70% penalty.
- Hiding a deliberate error – up to 100%.

TAX

Accounts filing

Private companies and limited liability partnerships (LLPs) have nine months from the end of their accounting period to submit accounts to Companies House. The deadline is therefore fast approaching for those with 31 March year ends.

A late filing penalty can be as much as £1,500, even if a company is inactive:

Lateness	Penalty
Up to 1 month	£150
1 to 3 months	£375
3 to 6 months	£750
Over 6 months	£1,500

The penalty is doubled if accounts are submitted late two years in a row.

Given the holiday closures in December, don't leave accounts submission to the last moment. This is particularly the case for LLPs who cannot file online. Also, you should allow more time if filing online for the first time.

In extreme circumstances – such as company records being destroyed in a fire – you can apply for a filing extension. This avoids a penalty but must be applied for before the original deadline.