

expenses as well as amounts spent directly by the intermediary provided the expenses would have been allowable had the worker been employed directly by the client and had met the cost himself. Similarly, relief will be allowed for partners' expenses reimbursed by the partnership.

Deemed salary allowable on cessation

One of the anomalies in the IR35 rules was that following a cessation part way through a tax year, the final deemed salary arose on the following 5 April and technically was not therefore deductible as it fell outside the final trading period. An amendment now treats the deemed salary as paid on the final day of trading and relief can therefore be claimed in the company's final accounts.

(IR Press Release, 15.3.2002)

Unvouched expenses

The Revenue often takes the approach that business expenses cannot be allowed as deductions if they are not supported by documentation. This is not correct. Indeed the Revenue website in the 'Starting up in business' section admits that it is not always possible to obtain evidence for cash expenses, especially small amounts. They advise that a brief note should be made with a suitable explanation of what it was for. This is a reasonable approach and clearly the tax rules allow for some flexibility. There should be no difficulty if a note of expenditure is made at the time rather than simply estimating at the year end.

A practitioner reports two recent cases. In the first case the client had not kept a mileage log. However, there was a business diary in which appointments had been recorded. Using a route planning CD applied to the appointments an accurate business mileage figure was calculated and the Revenue accepted this albeit with some reluctance. Other Inspectors have been persuaded to accept a representative mileage log over say a month or two as satisfying the evidence requirement for the mileage for the year.

In the second case no purchase invoices had been kept but payments had been made by a credit card or cheque drawn on a Coutts account. Dates and names of the suppliers were shown on the

narrative of both the credit card and Coutts statements. The Revenue initially claimed that this was insufficient evidence but eventually conceded. Naturally, in both cases the client was requested to keep better records in the future.

(Practical point in Taxline, March 2002 and contribution by Paul Aplin of A C Mole and Sons, April 2002).

INLAND REVENUE

Collection procedures

We reported the new tough approach of the Revenue to the collection of tax debts on the front page of *The Small Practitioner*, February 2002. In relation to liabilities arising on 31 January 2002 some clients will already have been contacted by the Receivables Management Service.

It would seem that the Revenue's approach has been to stream debts into those above and below £5,000. Those below £5,000 have been handled by Revenue special call centres at Cumbernauld, East Kilbride and Shipley. These centres have state of the art 'intelligent' call making and handling equipment. This automatically dials up the client's telephone number and allocates the call to an officer whose computer screen shows him the name of the client and the tax outstanding.

If the client says he cannot pay, a set procedure is gone through to see if the Revenue can offer to take payment in three monthly instalments. If the client accepts, the call centre issues a confirmation letter but no payslips. Only one call is made.

If the client refuses the offer or disputes the tax due his case is then referred to a local area officer for action. Cases will also be referred for action where the Revenue has no contact number or where the call centre has been unable to speak to the client.

(Robert Lillycrop in Taxline, March 2002)

INHERITANCE TAX

Estate planning tips

With a view to reducing uncertainties in relation to lifetime gifts by elderly clients, consider the contrast between

the two year qualifying period for business and agricultural property relief with the seven year survival period in relation to potentially exempt transfers.

Mrs Z is advancing in years and has surplus assets of £1m. If she were to gift her assets to her son she is faced with having to survive for seven years for her potentially exempt transfer to fall out of account. However, if she instead invested £1m in a farm and entered into a farming partnership with her son, 100 per cent business property relief would be attained after just two years.

The benefit of business property relief can be doubled up for inheritance tax purposes if borrowings are structured in the right way. For example, a client might borrow money secured on his home and use the cash to subscribe for shares in his trading company. For inheritance tax purposes, not only will the charge on the home reduce its value but also the shares will attract 100 per cent business property relief after two years.

(IBC Capital Taxes Conference, points reported by Ralph Ray in Taxation, 28.3.2002)

CAPITAL GAINS TAX

Reluctant farmers

It is important to draft grazing agreements or farm business tenancies carefully if rather than becoming a landlord, Schedule D treatment is to be preserved and the advantages of business asset status for capital gains tax taper relief and rollover are to be obtained.

Historically, land has been handed down through the generations and may have ended up in the possession of persons not interested in farming. Sometimes when farms have been sold some of the land close to villages has been retained for the hope value of potential future developments. As a result, there are many small parcels of agricultural land held in trusts, non farming companies and by individuals and these may only be highlighted when there is a small amount of rental income to be shown on the tax return. This presents a good planning opportunity to ensure that the tax status of reluctant farmers is dealt with correctly so as to preserve both capital gains tax and inheritance tax

reliefs. Business assets status can be obtained if the contract farming agreements or grazing agreements are properly constructed.

(Julie M. Butler of Butler and Co. in Taxline, April 2002)

Advice: Farming has become a complex and specialist area with matters such as herd basis, profits averaging and the interaction of capital gains tax and inheritance tax reliefs amongst other complications. If you find that you have reluctant farmers amongst your clients you should consider taking specialist advice.

EMPLOYMENT TAX

86.5 per cent tax on PAYE settlement agreements

PAYE settlement agreements have a number of points to commend them. They can reduce payroll work and avoid difficulties in accurately apportioning benefits between employees. Furthermore, payment is deferred until October after the end of the tax year. However, employers may not necessarily realise that they are paying the employees' tax on a grossed up basis and NIC on top of that. Take the following example which produces an effective overall tax rate of 86.5 per cent.

Benefits of £10,000 (2001-02)	£
Notional higher rate tax	<u>4,000</u>
Grossed up tax $4,000 \times 100/60 =$	6,666.67
Class 1B NIC	
$(10,000 + 6,666.67) @ 11.9\% =$	<u>1,983.33</u>
Total tax/NIC	<u>8,650.00</u>

Effective rate 86.5%

If the £10,000 benefits were VAT inclusive and the employer could recover the VAT in full, the net cost of the benefit to the employer after claiming input tax is £8,510 and in this case the total tax/NIC payable of £8,650 in the example produces an effective rate of tax of over 100 per cent.

(Tolleys Practical NIC, March 2002)

PERSONAL TAX

Pensions – immediate vesting

The stakeholder pension regime has created an investment opportunity for the over fifties which beats present very low market interest rates. Stakeholder pensions are available to anyone except those with a job related pension scheme and earnings of over £30,000.

If the investor is over fifty he can elect to take pension benefits immediately, in particular, a cash sum of 25 per cent of the fund. With a basic stakeholder contribution of £3,600 the net amount paid in will be £2,808 reducing to £2,160 after higher rate relief. The tax free cash available will be £900 leaving a residual fund of £2,700 to be used to buy an annuity. Current rates for a fifty year old man are around 6 per cent with a ten

year guarantee. This produces annual gross income of £162. On an investment of £1,260 (£2,160 less £900 tax free cash) this represents a return of 12.8 per cent. The equivalent return for a basic rate taxpayer is 8.5 per cent. There seems to be no reason why this exercise cannot be repeated on a regular annual basis.

(Roger H Jones, in Tolleys Practical Tax, 5.3 2002)

Advice: In practice insurance companies take a 1 per cent charge on stakeholder schemes so the fund will be slightly less. Nevertheless this is a very good 'ruse'. The insurance companies may get wise to this if the exercise is repeated regularly and may not be too happy due to the high cost of administration. However a different pension company could be used each year. Do not forget that the annuity is a very long term investment.

USEFUL FIGURES

Retail Prices Index

	1999	2000	2001	2002
Jan	163.4	166.6	171.1	173.3
Feb	163.7	167.5	172.0	173.8
Mar	164.1	168.4	172.2	174.5
Apr	165.2	170.1	173.1	
May	165.6	170.7	174.2	
Jun	165.6	171.1	174.4	
Jul	165.1	170.5	173.3	
Aug	165.5	170.5	174.0	
Sep	166.2	171.7	174.6	
Oct	166.5	171.6	174.3	
Nov	166.7	172.1	173.6	
Dec	167.3	172.2	173.4	

Annual Inflation Rate

	1999	2000	2001	2002
Jan	2.4%	2.0%	2.7%	1.3%
Feb	2.1%	2.3%	2.7%	1.0%
Mar	2.5%	2.6%	2.3%	1.3%
Apr	1.6%	3.0%	1.8%	
May	1.3%	3.1%	2.1%	
Jun	1.3%	3.3%	1.9%	
Jul	1.3%	3.3%	1.6%	
Aug	1.1%	3.0%	2.1%	
Sep	1.1%	3.3%	1.7%	
Oct	1.2%	3.1%	1.6%	
Nov	1.4%	3.2%	0.9%	
Dec	1.8%	2.9%	0.7%	

Indexed rise March 1982 to January 2002 = 1.197

Clearing Bank Base Rates (as at 25.03.02)

06/06/97	6.50%	10/09/97	6.75%	07/08/97	7.00%	06/11/97	7.25%	04/06/98	7.50%
08/10/98	7.25%	05/11/98	6.75%	10/12/98	6.25%	07/01/99	6.00%	04/02/99	5.50%
08/04/99	5.25%	10/06/99	5.00%	08/09/99	5.25%	04/11/99	5.50%	13/01/00	5.75%
10/02/00	6.00%	08/02/01	5.75%	05/04/01	5.50%	10/05/01	5.25%	02/08/01	5.00%
18/09/01	4.75%	04/10/01	4.50%	08/11/01	4.00%				