

Raising the Bar?

Julie Butler on time recording, duality and the tax advantages of the van

There are proposed changes to barrister time recording put forward by the Legal Services Commission (LSC), the Crown Prosecution Service (CPS) and the Attorney General. The LSC are considering insisting upon records that are readily auditable to demonstrate proper stewardship of public funds. For the Bar these suggestions provide a strong basis for showing good conduct by its practitioners in the billing of publicly funded cases.

It has been argued that the proposals go too far, for example there is a request that the conduct rules be extended so that barristers must maintain case files showing what work has been performed, when that work was performed (time and date) and how long it took. These records should be kept up-to-date by recording information within 48 hours of the work being done.

In addition there is a request that summary information regarding the total number of hours worked per day by barristers across all cases (including private, legal aid, prosecution) be made available to the LSC or CPS. This request is to enable those organisations to be satisfied as to the reasonableness of the hours claimed in legal aid or prosecution cases, in the context of the total hours worked.

The first cynical reaction of the accountant and/or tax advisor would be 'duality of purpose' – that this onerous work would assist with the calculation of barrister work-in-progress (WIP). (Perhaps the second cynical reaction is to thank heavens accountants do not currently have to show *when* their work was performed.)

Work-in-progress and UITF 40

The question is, will this time recording help in the professional judgment and calculation of barrister WIP at their tax year end?

There are many barristers who feel they have taken a severe tax battering of late with the move from cash accounting to include debtors and the introduction of UITF 40. There are concerns that the profession is paying tax now on money that has not been received and possibly (due to the nature of payment terms) will not be received for a long time hence. Help is obtained from the HMRC guidelines on UITF 40.

It is difficult to see therefore how the time recording proposals will help with the calculation. Is the reality that the suggested improvements in time recording would in fact create more arguments for uncertainty and lower work-in-progress, and therefore a lower tax bill?

What are the current rules for time recording? The current Bar Code of Conduct Rule 701(f) only requires barristers to 'ensure that adequate records supporting the fees charged or claimed in a case are kept until at least the last of the following: his fees have been paid; any taxation or determination or assessment of costs in the case has been completed; or the time for lodging an appeal against assessment or the determination of that appeal has expired'.

What are the proposals? That Rule 701(f) be amended to require records to be kept for three years after the last of the stated events has taken place.

Retrospective audit and drawback provisions

The problem of record keeping arises where there is the need occasionally to carry out a retrospective audit of claims submitted on all publicly funded cases to ensure that in their totality claims can be justified.

Does this give greater argument to increase the uncertainty and therefore to justify not recognising revenue until later, and to making greater drawback provisions? In other words, paying less tax! What guidance is given by HMRC?

Legal Aid: 'Returning of the excess'

Legal aid in some cases is not agreed until after the matter has been settled. In lengthy cases agreement can take many years. Often the payments on account will be for a greater amount than the eventually agreed fee and the barrister has to return the excess. It has been agreed with HMRC that the relevant tax point is payment, normally a payment on account, or the agreement of the fee, whichever comes first.

Professional judgment has to be applied in making the decision and the accounting treatment will depend on the degree of uncertainty. In principle, revenue should be recognised according to the work done to date, rather than according to progress payments received, so in this case the new time recording proposals could be useful. If a reasonable estimate can be made of the revenue that has been earned as a result of the work done to date, then that should be recognised in the accounts.

Prudence should be built into that estimate in response to uncertainty. It may be that the level of uncertainty is so high that no reliable estimate can be made until either later in the process or until the case is completed and the fee agreed. A barrister should not recognise all the progress payments received as revenue, even if they do bear a close relationship to the work done to date, if it is likely that some of the amounts received will have to be refunded; hence there should be provision for the excess to be returned.

It would again seem that the new time recording proposals give greater justification for prudence and this could help the barrister's tax position.

'No win, no fee' basis

Where a barrister works on the 'no win, no fee' basis the revenue should not be recognised until a case has been won. Only at that stage does the barrister have the right to consideration.

'Pay at end' basis

When a barrister works on a 'pay at end' basis the fee is not agreed in advance, nor will the rate be fixed. The consideration is negotiated at the conclusion of the case. The difference from 'no win, no fee' is that the fee will always be due.

Where there is some uncertainty about the fee but a reasonable estimate can be made, at least of the minimum that will be earned, then an estimate should be made of the part of the total fee that has been earned as a result of work done to the balance sheet date.

Where there is genuinely so much uncertainty that no reliable estimate can be made of the total fee or of any part of that total that has been earned to date, no revenue should be recognised until such time as the uncertainty has reduced and a reliable estimate can be made.

In these cases it would appear improved time recording systems will help with the calculation.

Budget 2008 and 'Plant & Machinery'

Legislation has been included in the *Finance Bill 2008* to introduce a new annual investment allowance (AIA) for the first £50,000 of a business's expenditure on most plant and machinery each year. For tax purposes a barrister is in business and they do use 'plant and machinery'. The tax relief will apply to expenditure incurred on or after 6 April 2008. Will every barrister be able to use their allowance? Barristers can enjoy an immediate 100% tax relief for such expenditure for 2008/09. The interaction with the Chambers 'plant and machinery' will have to be considered. There is no doubt that whether or not the proposed time recording proposals are accepted there will be more emphasis on electronic recording and improved IT systems and hardware.

What constitutes a barrister's plant and machinery? For example:

- Home computers and IT links
- Furniture for the home office or study

Motor cars do not qualify as 'plant and machinery' for the purposes of the annual AIA but vans do qualify, so obviously anticipate to see a change of vehicle parked outside Chambers in a 'hunger' to use the £50,000 allowance! The main caution to be observed is that for a van to remain a van and not a car, it must be 'of a type not commonly used as a private vehicle and unsuitable for such use' (section 81, *Capital Allowances Act 2001*). Years ago there were interesting arguments about mini-vans, and it is something of an 'own goal' if the vehicle is in fact used for private motoring. Could you imagine a barrister driving around in a white van anyway? There are however some very expensive and attractive double cab 4x4s which just may tempt some barristers. After all, have you seen how many boxes of documents they have to carry?

Those barristers claiming the AIA might have worries about the concept of duality of purpose for tax – this can be explained by the case *Mallalieu v Drummond [HMIT]* (1983) 57 TC 330, where the black clothing required for a barrister's appearance in Court was held to be needed for the more conventional use of clothing the body as well. The legislation defines the allowability of expenses in section 34, *Income Tax (Trading and Other Income) Act (ITTOIA) 2005*. Under this section if an expense is incurred for more than one purpose, say for business and for pleasure, then no deduction for the business proportion is allowed.

Clearly with the claim for 'plant and machinery' utilised in the office at home, care must be taken to protect claims for tax relief from restriction under the duality rules. What is the purpose of the expenditure?

Chambers: Shared premises

What is the tax planning interaction of Chambers' new plant and machinery purchases – for example, of furniture, fittings and IT systems – and the individual barrister and his AIA?

What is the tax position of Chambers? Where an individual or individuals control(s) an unincorporated business or more than one unincorporated business, but he/she/they do not control a related unincorporated business, each separate and distinct business will be entitled to its own AIA. However, if they are deemed to be 'related' then the AIA will be shared between the businesses. The conditions that determine whether two businesses are related are 'the shared premises' condition and 'the similar activities' condition.

The 'shared premises' condition is met if at the end of the accounting period the two businesses are carried on from the same premises. The 'similar activities' condition is met if two businesses under common control carry out the same qualifying activity in a tax year.

Barristers are quite clearly trading in their own capacity and, although they share their Chambers, they are not under common control. However, this position has yet to sink in with the Barristers' Clerk!

There is great scope for tax planning to maximize the use of the allowance amongst the profession of barristers but how can the £50,000 annual allowance be fully used?

To clarify, a barrister in his/her sole trader capacity is therefore a business and entitled to his/her own AIA. It is assumed that Chambers will be classified as a Trade Protection Association and again entitled to an AIA if chargeable to corporation tax – for this not to be allowed there would need to be a very aggressive stance by HMRC.

Chambers: J D Wetherspoon case and budgets

The *Wetherspoon* case (SpC 657) has highlighted how building improvements such as toilets and drainage can qualify as 'plant and machinery'. The key point here is that all barristers should be linking with Chambers to review the 'plant and machinery' budgets, including green expenditure, 'features not fixtures' and the impact of the AIA.

So who said the Budget 2008 was dull?

Chambers: Green warmth

It is well known that the traditional buildings used by barristers' Chambers are 'slightly' old-fashioned and in winter might be described as 'a tad chilly'. Do not worry, the taxman is going to create a tax incentive for green warmth.

Improvements to the Enhanced Capital Allowances scheme will extend 100% first-year allowances to a wider range of energy efficient equipment and heating systems, including those fuelled by solid refuse waste. New lists of qualifying technologies will be published later in 2008 and will be available on the internet at www.eca.gov.uk.

Summary

It would appear that (possibly) in 2008 it will be 'goodbye Aston Martin' and 'hello White Van Brief' – tax efficient, cash flow efficient and helps reduce higher tax bills created by UITF 40 and the onerous inclusion of WIP.

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