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VAT: WHAT TO EXPECT WHEN A BUSINESS DEFAULTS

A VAT registered business is deemed to have defaulted when it fails to submit a VAT return by the due date and/or fails to pay (with cleared funds) the full amount of VAT due to HM Revenue and Customs (HMRC) by that date. HMRC have set up a couple of helpful facilities for such situations and advisers should be aware of them.

In recent years HMRC have set up the Business Payment Support Service (telephone number: 0300 200 3835) in order to assist businesses that are having difficulties in settling the correct amount of VAT by the relevant date.

In the event of a business defaulting, unless the special arrangements for small businesses apply (referred to below), HMRC will issue either of the following:

- Surcharge Liability Notice (SLN) or
- Surcharge Liability Notice Extension

The SLN will specify a surcharge period from the date of the notice to the first twelve month anniversary of the last day of the period for which there has been a default. In the event that the last day occurs during an existing surcharge period, a SLN extension will be issued, extending the existing surcharge period to the first anniversary of the last day of the period of subsequent default.

Special arrangements have recently been put in place if the defaulting business' taxable turnover is £150,000 or less. In these circumstances, for the first default, HMRC will, instead, issue a letter offering help and support rather than a SLN. A further default within the following twelve months will result in the issue of an SLN in the normal way.

There is no surcharge as a result of the issue of the first SLN. These charges only arise for defaults during surcharge periods.

The surcharge is calculated as a percentage of the VAT that is unpaid at the due date. If no return has been submitted, HMRC will estimate the amount of VAT due and calculate the surcharge based on that amount. If no VAT is due, there will be no surcharge however, the default will be recorded and the extension notice will be issued.

For the first late payment during a surcharge period the surcharge will be 2% of the VAT outstanding at the due date. This rate increases progressively to 5%, 10% and 15% for further payment defaults in a surcharge period.

No surcharge is demanded at the 2% and 5% rates if it would be less than £400. In addition, there is a minimum of £30 for surcharges calculated at the 10% or 15% rates.

In the (probably unlikely) event that the VAT has been paid on time but the return has not been submitted, no surcharge will be demanded (as there is no outstanding VAT liability). However, if this arises during a surcharge period, the period will be extended.

Thus, any liability to surcharge expires if all returns and payments for tax periods ending on or before the end of the surcharge liability period have been submitted on time.

Don't forget the possibility of a business having a reasonable excuse for failing to pay or submit on time. Any such situation must be seen to have been remedied as soon as possible following the default if a surcharge is to be avoided. Whether or not a situation might be deemed to have been a reasonable excuse depends on the particular circumstances, and case law tends to be a good guide as to whether an excuse would be accepted. Essentially, a reasonable excuse is something that prevented a tax obligation from being met and reasonable care can be demonstrated to have been taken in order to meet the relevant obligation. The test is stringent though.

In conclusion, HMRC are generally trying to assist businesses to meet their obligations as far as is reasonably possible. It is worth contacting them in advance if a pending deadline may not be met as a cash flow solution can often be found.

LIGHTNING STRIKES THRICE, WILL WE EVER LEARN?

Three very similar tax cases have been reported within the last two years concerning Enterprise Investment Scheme and Seed Enterprise Investment Scheme Investments with unfortunate results for the tax payer.

In X-Wind Power (TC50806) the tax payer sought a compliance certificate from HMRC to enable investors to claim SEIS relief at 50% on their investments.

Unfortunately, the company used form EIS1, which applies to EIS investments where the rate of income tax relief is only 30%, instead of form SEIS1.

HMRC authorised the company to issue EIS3 certificates, allowing the investors relief under EIS.

The company had intended to apply for authorisation to issue SEIS3 certificates and, when it realised its mistake, asked HMRC to accept the application as being an application under SEIS instead of EIS.

HMRC refused and the tax payer appealed.

While the First Tier Tribunal was "entirely satisfied" that the company had indeed intended to apply under SEIS and it had made an error in using the incorrect form, the Judge pointed out that it was clear that EIS relief had in fact been granted and there was no means by which this could be set aside. While the tribunal sympathised, it could do nothing but dismiss the company's appeal.

En garde! Well perhaps not, as the tax payer was once more disadvantaged in the case of GDR Food Technology Ltd v HMRC ((2016) TC05219) after investors were not able to claim SEIS relief following the submission by the company's advisers of an EIS1 compliance statement to HMRC in September 2014.

They wrote to HMRC in January 2015 asking to withdraw the EIS1 on the basis that this had been completed incorrectly and that SEIS relief was being sought rather than EIS relief.

HMRC refused on the basis that an EIS1 claim had already been made in respect of the share issue.

The First Tier Tribunal noted that the company and the investors had intended that SEIS relief should be claimed but, as the accountants had filed the wrong form and had referred to EIS in subsequent correspondence with HMRC, the submission of an EIS1 form meant that SEIS relief could not be given. There was no mechanism to correct the error.

Once again, the tribunal sympathised but dismissed the appeal.

"I don't believe it" is the catch phrase of Victor Meldrew, but surely the First Tier Tribunal in the case of Innovate Commissioning Services Ltd v HMRC (TC06152) must have been thinking this as, once again, an incorrect form was used.

In June 2014, the company sought advance assurance from HMRC that SEIS relief would be available. HMRC agreed that it would.

Despite this however, the company submitted form EIS1 rather than form SEIS1. HMRC actually queried this but then issued form EIS2 authorising the company to issue EIS3 certificates to the investors.

The company then became aware of the mistake and sought to withdraw the EIS1 form and replace it with the SEIS1, which had been intended from the outset. HMRC would not accept this.

On appeal, and despite the fact that the company had advance assurance for SEIS, and that HMRC had queried the submission of an EIS1 form, the tribunal held that an EIS1 form had been submitted and this could not be withdrawn and replaced by an SEIS1.

The EIS and SEIS legislation is some of the most complex on the statute book and, to say the least, it is a great pity that, having met all of the onerous conditions, the investors did not obtain SEIS relief on the basis that an incorrect form had been completed in all three cases. If ever there was a situation where checking, double checking and triple checking is critically important, submitting an EIS or SEIS claim is it!

RARE DISASTERS – TIME TO CHANGE PRACTICE WHEN PAYING DIVIDENDS

Rare disasters
There is a whole economic theory of rare disasters. Events like the Great Depression, a flu epidemic or World War III, may occur, but few people think the disaster will occur during their lifetime. If it does happen the impact could be catastrophic, but it won't happen to me.

Getting it right with company dividends
Nothing on the same scale as the Great Depression, but enough to make one sit up and think, the impact of failing to account for dividends correctly can have very significant impact on individual taxpayers. And these taxpayers could be your clients.

What is the right, and wrong, way to go about it, and what are the risks?

All fiction
Dr Maqbool Baloch worked as a locum GP. He traded via a limited company and his accountant submitted all the returns. A legitimate and potentially tax-saving way to conduct business. Only it didn't actually happen.

Dr Maqbool Baloch had been too busy to hold board meetings, and papers after the event were far from convincing. For example 'Dr Baloch's time sheets showed that on 23 December 2012, when he was supposed to be holding a board meeting in North London, he was working in North Somerset'.

As a result of the deficient paperwork, all the income reported as dividends and salary was taxed as income from self-employment (Dr Maqbool Baloch TC06092 [2017] UKFTT 0665 (TC)).

Low salary, high dividends
Back to basics. If we want an effective low salary, high dividend remuneration package, what has to be done?

Salary has to be paid, and reported under RTI if pay over the NIC lower earnings limit (or there are taxable benefits, or the director / employee has other sources of PAYE income).

Directors are normally empowered to declare interim dividends, but must hold a board meeting to do so. At the meeting the directors must consider the financial state of the company and have evidence that the dividend can be paid out of profits. The dividend needs to be correctly minuted and paid / credited to loan accounts contemporaneously.

For income tax purposes, the interim dividend is only treated as income of the director shareholder when it is actually paid – that is put unreservedly at the disposal of the director shareholder.

Final dividends are normally declared in the Annual General Meeting, and may have a specified future payment date. Once declared, final dividends are income of the director shareholder from the date of entitlement – even if they are actually paid later.

Current issue
ICAS has received a number of queries recently from firms about the legality of 'retrospective dividends'. The issue may arise when acquiring a new client, who is 'sorting it all out at the year-end'.

Declaring and paying dividends in close companies is all about contemporaneous recording. HMRC's Making Tax Digital agenda is bringing the issue of contemporaneous recording even more to the fore.

We have outlined what ought to be done. How can we persuade clients to adopt best practice and what are the danger zones?

First hurdle – no dividend at all
The first hurdle is in company law, rather than tax law. If proper procedures aren't followed, then there is no dividend at all. The purported tax advantages of paying dividends go up in smoke, and the director shareholder could even be personally liable to repay the money to the company's creditors.

For a dividend to be valid it must be declared in an appropriate meeting – an AGM for final dividends and a board meeting for interim. Furthermore, there must be a review of the company's financial position. This is essential due to s 830 Companies Act 2006.

S830 says that distributions can only be made 'only out of profits available for the purpose'. Broadly, this means its accumulated realised profits less its accumulated realised losses. While there can be some debate over exactly what falls to be counted, the critical point for most close companies is: has the question actually been asked before a dividend is declared? And is there minuted contemporary evidence?

If there is no minuted evidence, there is no dividend.

Example one
Antrabus Ltd is a close company and the directors are empowered to declare dividends. They decide it would be beneficial to extract money quarterly as dividends and make journal adjustments to directors' loan accounts to reflect quarterly interim dividends.

The snag is that there is no contemporaneous minute showing that the directors actually considered if the company had sufficient distributable profits to cover the dividends, or any minute to prove that a dividend has actually been declared.

In this scenario is the payment a dividend, or is it, for example, employment income?

It's really employment income
Vinod Parmar's accountant found himself in a hard place (Vinod Parmar TC04927 [2016] UKFTT 0142 (TC)). He had advised the client to incorporate and run their small shop as a company, rather than as a husband and wife partnership.

A small salary was taken, and the intention was that all other income would be extracted as dividends. After trading for a while, the business was sold and the company wound up.

HMRC later arrive on the scene and suspect that profits have been under-declared. Re-instating the company would be expensive, so as a second line of attack, HMRC decided to treat undeclared cash income of the company, and some other items, as employment income of the directors.

The directors claimed that they intended that any additional income would be dividends. But where, asked the Tribunal, are the minutes approving the dividends? So whereas the directors had expected to escape tax, on the basis that there would be no additional liability on dividends, instead, they were personally landed with a bill for the PAYE and NIC due on the additional 'employment income' from the company.

So, if you cannot evidence contemporaneous minutes declaring dividends, beware that the income may be reclassified!

(*PA Holdings Ltd v Revenue and Customs Commissioners [2012] STC 582* came to a similar conclusion).

Example two
Extrobus Ltd, is even less careful. The directors realise at the end of the accounting year that it would have been beneficial to have quarterly dividends and make journal entries purporting to be quarterly dividends, but only after the end of the accounting period. These late-declared dividends neatly cover the overdrawn balance on the directors' loan accounts.

Here, there are a number of issues:
i. Have the dividends been 'paid' and if so, when?
ii. Are the dividends utra vires – are they dividends at all?
iii. What are the implications for the directors' loan accounts?

Paid means paid
Per s1168(1) Corporation Tax Act 2010, dividends are treated as paid on the date when they 'become due and payable'. Though this may sound a little circular, there is a reality to it.

A final dividend may be 'paid' when declared, as the shareholder at that date gains a legally enforceable right to the declared dividend from the date it is due, even if the dividend is actually paid later.

HMRC's view is that:
'A dividend is not paid, and there is no distribution, unless and until the shareholder receives money or the distribution is otherwise unreservedly placed at the shareholder's disposal, for instance by being credited to a loan account on which the shareholder has power to draw.' Company Taxation Manual - CTM 15205

Interim hazard
Interim dividends are a particular hazard here. They are only treated as 'paid' when the director shareholder can actually use them.

An interim dividend may be cancelled or varied before payment, so, even if declaration is made that it will be paid on a particular date, this is not binding. It is not considered 'paid' until the shareholder has the money, or is able to utilise the amount credited to a loan account.

A journal entry made in, say, September, cannot validate an interim dividend declared in a board meeting in March. As regards income tax, the dividend will be income of the tax year in which paid, so the tax year that the September falls in – not the previous March.

So for Extrobus Ltd, the dividends will only actually be paid when the journal entries are made. But has there been a dividend at all?

No dividend
Is the dividend ultra vires? We have seen that to declare a valid dividend, the directors must review the financial state of the company.

What evidence is there that the directors looked at the financial position of the company? Did they review a trial balance, or produce quarterly management accounts? If not, how do they know that there are sufficient distributable reserves?

If a distribution is made when the company hasn't sufficient distributable profits, then it is an unlawful distribution. The consequences here depend on the degree of knowledge. A shareholder with only remote connection with the company may be unaware of the financial position of the company, but this is unlikely to be so with close company directors.

The consequences here are set out in s847 Companies Act 2006 (Consequences of unlawful distribution). Essentially, the amount is not a dividend and must be repaid. This can be particularly serious if the company becomes insolvent. HMRC is very aware of this and raise this issue on company insolvency. The directors then become personally liable to repay the supposed dividend to the company.

Uncovered loan accounts
If the company is solvent, the amounts may still need to be repaid, and this can leave an outstanding balance on a director's loan account.

This can trigger a tax charge under Corporation Tax Act 2010 s455.

And the adviser?
From an adviser's point of view, there may be additional ethical and professional considerations: the directors may claim that the dividend journals were made earlier in the year, but in the modern digital world, with sequentially numbered and dated entries; and even more so in the MTD quarterly submission world, it is going to be clear that the entries have not been made contemporaneously.

So, even if there are purported minutes of a directors' meeting which considered if there were sufficient distributable profits, the actual book-keeping entries may give the lie to it.

For a final dividend, there would normally need to be an AGM and a statement of the amount and due date of the dividend, and a review of the company reserves and trading position.

Code of ethics and Professional Conduct in Relation to Tax guideline (PCRT)
All members of ICAS and the other main professional bodies are covered by PCRT. These guidelines inform all tax-related advice.

The guidance at 2.29 is perhaps particularly relevant here as payment of a dividend, rather than salary, could be seen as part of tax planning.

The principles here are that professional advice should be:

- Client Specific
- Lawful
- Disclosed and transparent - fairly represent all relevant facts
- Tax planning arrangements should not be contrary to the clear intention of Parliament, and
- Professional judgement should be exercised and appropriately documented

The most recent version of PCRT can be downloaded from the ICAS website (https://www.icas.com/__data/assets/pdf_file/0007/266056/20161101-Professional-Conduct-in-Relation-to-Taxation-FINAL.pdf).

ICAS members are also covered by the code of ethics (https://www.icas.com/ethics/icas-code-of-ethics).

Unraveling world
When things go wrong, they can go seriously wrong. If HMRC investigates your client and considers that the client has deliberately falsified documents, you could be next in line. HMRC can charge Dishonest Agent penalties where they think a tax agent has been dishonest. This would include doing anything dishonest with a view to bringing about a loss of tax revenue.

Conclusion
It is time to get things right with dividends. Best practice needs to be mainstream and clients need to be advised on how to get it right.

Challenges from HMRC are likely to increase and the consequences could be significant.

AUDIT TENDER GUIDANCE FOR PRIVATE COMPANIES

The ICAS Business Policy Panel has published a new guide on tendering the external audit which has been tailored to private companies.

The guide explains why it is a good idea for a private company to put its audit out to tender; the risks of not rotating auditors; and details good practice to help companies get the quality audit needed. It offers a more proportionate approach to tendering for private companies, and contains tips from experienced members in both the private and listed sectors.

Good practice for a listed company can be too unwieldy for smaller private companies – and the Business Policy Panel has distilled what it believes to be the key drivers and tailored this for the private company to make it more accessible.

The guide reminds people that a quality audit can benefit the business and a good auditor brings professional scepticism and independent, professional judgement. The process of tendering the audit can help directors make sure that the company is getting what it should from its auditors.

Key themes explained include:

- Why and when to tender;
- The benefits of a quality audit;
- What makes a good company-auditor working relationship;
- Auditor independence – what it means and how to get this right;
- The drivers for a quality audit, what to look for and key assessment criteria to help directors evaluate tenders; and
- What to expect at each stage of the tender process with practical tips.

The guide also explains how auditors are regulated; provides useful links to relevant legislation and regulation; and also contains a checklist summarising key questions for directors throughout the tender process.

Other publications in this series include:

- Selecting your auditor - a guide to tendering the external auditor appointment for public interest companies; and
- Selecting your auditor - a guide to tendering the external auditor appointment for publicly funded, third sector and not-for-profit bodies interest entities https://www.icas.com/technical-resources/public-sector-selecting-an-auditor

CYBER SECURITY ADVICE – WINDOWS 7

Windows 7 is nearly 9 years old, which is a long time in computer security terms. Malicious software has significantly increased in sophistication and volume since 2009, and the threats are very different today.

It is nearly 3½ years since Microsoft ended mainstream support for Windows 7, and security updates will cease in Jan 2020. Newer operating systems, like Windows 10, have many more modern security features that make it far more difficult for attackers to compromise. This doesn't mean Windows 7 isn't safe however, and whilst security updates are still being released and applied, it should be resilient to common attacks.

Microsoft also offers EMET (the Enhanced Mitigation Experience Toolkit), which can protect Windows 7 further with some of the advanced security features found in Windows 10. If you are still running Windows 7 and have an IT team able to configure EMET, it is certainly worth considering. It is also worth planning your upgrade from Windows 7 before Jan 2020, when Microsoft will stop fixing security holes, leaving remaining Windows 7 users at significant risk.

The National Cyber Security Centre offers a range of guidance on staying secure online, which can be found at: https://www.ncsc.gov.uk/guidance.

HMRC'S NEW PRIORITIES REVEALED

HMRC have re-prioritised

On 30 April Jon Thompson and Jim Harra of HMRC gave oral evidence to the House of Commons Public Accounts Committee, as part of the Committee's review of HMRC's performance across a range of issues (http://data.parliament.uk/writtene vidence/committeeevidence.svc/evidencedocument/public-accounts-committee/hmrcs-performance-progress-review/oral/82230.html) .

This evidence session was an opportunity to discuss HMRC's re-prioritisation, in which they have decided to pause some work and stop other projects completely to make room for their additional work relating to Britain's forthcoming exit from the EU. Afterwards, HMRC sent a short briefing note to ICAS and other organisations, providing some further details of their revised plans.

Brexit
The Customs Declaration Service (CDS) is currently HMRC's "top project". By completion it will have cost £270 million.

One of its most crucial aspects is the migration to CDS of current users of Customs Handling of Import and Export Freight (CHIEF), the existing system for processing trader declarations. Results of system testing of CDS will "probably" be known by July 2018, and then it goes "live" when the first traders start to migrate to CDS a month later in August. Even though the project has met all recent timetable targets, that sounds dauntingly ambitious.

Further testing will follow to ensure that CDS can handle volumes of up to 300 million transactions a year and performance of up to 100 transactions a second. Even if both these benchmarks are achieved, don't forget that the shape of customs post-Brexit is as yet unknown, and therefore the precise day-to-day working requirements of CDS are still uncertain.

HMRC have differing contingency plans in mind (but not yet in progress) to scale up CHIEF in the event that CDS is still unavailable after Brexit. A "low effort" option might increase its capacity from 80 million to 230 million transactions a year. A "high effort" solution might be feasible, offering up to 600 million. To set either of these in motion, time seems alarmingly short.

Questioned about traders' awareness of CDS, Harra stressed that HMRC see intermediaries (i.e. software providers and customs agents) as the key players. HMRC are communicating with such intermediaries and with trade associations. Haven't we heard this before, with HMRC consulting on implementation of Making Tax Digital (MTD) almost exclusively with software houses rather than end users? In both instances, HMRC may be ignoring their key audience.

The unpredictability of Brexit affects not only the number of traders and transactions with which CDS will have to cope. It is the crux of the fundamental uncertainties about customs. To take one example, the EU concept of 'authorised economic operator' (AEO) status has varying advantages in different members states; HMRC are currently seeing an increase in applications for AEO status, apparently because it might have greater relevance under a new-style customs agreement – but on the other hand it might not.

Thompson and Harra were grilled about the need for infrastructure at transit points such as ports and airports, and unsurprisingly the politically sensitive border between Northern Ireland and the Republic of Ireland was raised. They explained that HMRC are considering three different models for that border, aiming to support the seemingly irreconcilable objectives of free flow of goods and revenue collection.

Making Tax Digital
For businesses, HMRC launched their voluntary MTD for income tax on 15 March. Their timetable for mandatory MTD for VAT remains on track, with implementation beginning from April 2019, but they will not impose any further MTD changes on businesses before 2020 at the earliest. Plans to create a single Business Tax Account for each business taxpayer have been slowed down.

Some progress has been made in the seemingly piecemeal development of functions which HMRC categorise under the broad heading of 'MTD for individuals'. These include simple assessment and real time tax code changes, but progress on these has been halted – to be revived when future resources allow.

HMRC will continue to encourage more individual taxpayers to use their Personal Tax Accounts and will focus on improving the existing service, but will add new services only where they reduce phone and post contact or deliver significant savings.

IT projects have been paused where they would affect relatively few taxpayers, such as inheritance tax, tax-advantaged venture capital schemes, and PAYE settlement agreements. Resources will be re-deployed from tax credits (where new claims will cease in January 2019) to the tax-free childcare system.

Business as usual
HMRC are committed to delivering all additional work arising from "Budgets and Autumn Statements" for which they were given funding. No mention here of the latest Spring Statement, and perhaps a coded warning to the Chancellor that HMRC must be adequately funded to avoid overload.
Their current work covers a variety of projects including the soft drinks industry levy, the trust registration service, and work to tackle avoidance schemes that seek to exploit tax and NIC advantages through disguised

remuneration and salary sacrifice arrangements.

In spite of the strong political pressures on the Government to tackle tax avoidance, planned improvements to the tools and processes used by HMRC's compliance teams to identify, work and resolve compliance risks will now be delivered over five years instead of three.

The Committee spent a considerable time discussing new measures which are improving collection of VAT from overseas suppliers selling goods to UK customers. In January 2018 alone, some 27,550 overseas online retailers registered for VAT, raising an extra £100 million a year. Online marketplaces are being asked to commit to educating their sellers about their VAT obligations.

HMRC have also issued 1,300 'joint and several liability' notices to online marketplaces, hoping to gather in an additional £110 million of VAT; perhaps such a statistic should be viewed with caution, given recent revelations that HMRC had to withdraw 1.28 million late filing penalty notices in the three years from 2014 to 2016 and 6,000 accelerated payment notices (APNs) over a similar period.

Also on VAT, HMRC are currently consulting (https://www.gov.uk/government/consultations/alternative-method-of-vat-collection-split-payment) on a new split payment scheme. The Committee expressed support for this but noted that the concept is not strongly supported by the EU. Subject to consultation feedback, Thompson hopes that the UK will take a global lead on it.

HMRC Regional Centres

HMRC regard their move to thirteen regional centres as an essential feature of their transformation to maintain business as usual. Nonetheless, they have slowed down their plans for Longbenton and Nottingham to ensure that progress is manageable and costs are spread over a longer period.

Conclusions

Thompson explained how HMRC's re-prioritisation exercise had sought to free resources for Brexit-related projects. In doing so they had stopped or slowed down 39 pre-existing projects and consolidated 70 others.

Committee member Lee Rowley, a former project manager, observed that the number of projects had reduced by between a third and a half, while project benefits in terms of running costs and efficiency savings would only be 5% less than previously expected. Noting that HMRC had managed to retain almost all of their benefits, reduce their projects quite significantly, and still deliver the Brexit 'must haves', he thought this a very ambitious place to be.

CHANGES TO FORMS 64-8 AND SA1 FORMS

If you deal with clients who have been seconded to work in the UK, there are some procedural changes that have taken place within HMRC that you should be aware of.

The principle changes are where the individual has a full National Insurance number. In such cases, if you wish to submit a 64-8 or SA1, these should be submitted direct to the CAAT team at:

HMRC
CAAT
Benton Park View
Longbenton
Newcastle Upon Tyne
NE98 1ZZ

using either the online forms or bespoke versions – both of which must be printed and sent direct to the CAAT team at the above address. You can also go through the agents portal when you have the customer's UTR available, instead of using a form 64-8.

Any forms that have already been submitted to the Expat team for Secondees will be dealt with. However any future receipts of the form 64-8 or SA1 **that has a full National Insurance number** (irrespective of being received via Shared Workspace or normal post) will be returned with a request for you to submit directly to CAAT.

The web addresses below should be passed to anyone involved in this work.

https://www.gov.uk/government/publications/tax-agents-and-advisers-authorising-your-agent-64-8

https://www.gov.uk/government/publications/self-assessment-register-for-self-assessment-and-get-a-tax-return-sa1

LETTING OF RESIDENTIAL PROPERTY

The tax system contains provisions taxing three types of residential property letting businesses. The rental of property in the UK forms a UK property business whereby the profits and losses can generally be calculated for the whole business rather than the individual properties.

Buy to Lets
This is perhaps the most common form of letting of residential property where the owners let individual properties, usually furnished, and usually for periods of at least six months at a time. The profits from such a business are calculated by deducting allowable expenditure from the rental income.

There have been changes recently in respect of the tax deductibility of certain types of expense:

- Finance Costs.
  Up until 5 April 2017, income tax payers were able to deduct the full cost of interest on loans for the purchase or improvement of their properties. From 6 April 2017 the ability to deduct the interest is progressively being reduced and, by 6 April 2020, relief for individual landlords will be restricted to the basic rate of income tax. The interest restriction does not apply to individual commercial landlords nor in respect of furnished holiday lettings.
- The 10% wear and tear allowance was withdrawn from 6 April 2016 where a property was let furnished. Capital allowances have never been available on furniture, etc provided in a furnished letting. From 6 April 2016, a deduction is available in respect of the replacement of domestic items where the old item is no longer available for use and the new item is solely used by the tenant. The allowance extends to furniture, furnishings, household appliances and kitchen wear which are not fixtures. Where the new item is similar to the old one then a deduction is available for the cost of the new item. Where the new item is not the same, the deduction is restricted to the cost of an item similar to the old one.

Furnished Holiday Lettings
Furnished holiday lettings are treated more generously than the letting of an ordinary buy to let property.

Furnished holiday accommodation is defined by Section 323 ITTOIA 2005 and the conditions for a property to qualify are covered in the subsequent sections of the act. It is not proposed to go into the detail of this here.

The advantages of a furnished holiday letting over a normal buy to let are:

- The losses of a furnished holiday let are treated as a trade loss. Finance Act 2011 restricted the use of such a loss and these can now only be set off against income from furnished holiday letting business. Previously, it was possible to offset such a loss against general income or under the term of loss relief provisions for income tax purposes.
- Rollover relief and entrepreneurs relief is available for capital gains tax purposes, if a furnished holiday letting property is sold.
- Capital allowances are available on plant and machinery, which will include furnishings and fittings in the property.
- The profits from a furnished holiday letting owned jointly by spouses can be allocated between the spouses as they agree.

Rent A Room Relief
Whereas a buy to let property or furnished holiday let is normally occupied by lessees to the exclusion of the owner, rent a room relief is available where an individual lets furnished accommodation in his only or main residence.

Rent a room relief was originally introduced as a simplification in that, if the rent received fell below a specified figure, currently £7,500 per annum, there would be no income tax payable. No relief would be available for the expenses incurred by the property owner.

It is possible to elect to dis-apply the relief for a particular year of assessment where, for example, a loss is incurred.

Where the rent received exceeds £7,500, the landlord is taxable on the excess. As noted above, however, it is possible for the landlord to elect to be taxed in the normal way with the actual expenses incurred being offset against the amount of the rent. This will be advantageous where the deductible expenses exceed £7,500.

On 1 December 2017, the Treasury published a call for evidence concerning rent a room relief. The stated objectives are:

- To find out more about the use of the relief including who uses it, what kinds of activity they are carrying out, why they may choose to let spare accommodation in their main residence and the effect of the relief on the housing market.
- To establish whether the relief is working as the Government intends. The original purpose was to increase supply and variety of low cost residential housing. However, the relief applies to furnished

accommodation of any length and could include very short term holiday accommodation. The Government would like views on whether the relief should be restricted to support residential accommodation provided on a longer term basis or for certain purposes.

- To help inform any potential reform of the relief. The Government has apparently not yet formed a view on whether the relief should be reformed.

The document can be found at https://www.gov.uk/government/consultations/rent-a-room-relief/call-for-evidence-rent-a-room-relief.

ACCOUNTING AND AUDITING QUERY

Query: Our client, a limited company, is a legal firm that holds considerable sums in their client accounts. These appear in their balance sheet and cause them to exceed the asset threshold for audit exemption this year. They also breach the employee numbers threshold.

They have asked us if they can exclude the client accounts when considering audit thresholds as this is not their money. Please can you advise.

Answer: Eligibility for audit exemption is based on an entity meeting the qualifying criteria for a small company. This means that, although the thresholds may have been breached in a particular year, just as for reporting purposes, the company only ceases to be considered a small entity, and therefore ineligible for audit exemption, if the thresholds have been breached for two successive years.

Therefore, if this is the first year that the qualifying criteria have been breached, then audit exemption could still be taken, assuming the company is not an ineligible one. If the thresholds are breached again next year, then next year would be the second successive year of breach and therefore no audit exemption would be permitted in that year.

This position is explained in more detailed in the article: Audit exemption the rules one year on.

Otherwise, if no exemption is possible using the two-year rule, you would have to consider whether it would be appropriate to exclude the client account balances from the calculation. As the total assets calculation is based on the balance sheet figures, assuming that this amount appears as an asset on the balance sheet, then it would not be appropriate to exclude this number from the calculation. Effectively what you would be doing would be offsetting the corresponding creditor against this asset.

FRS 102 has very clear rules on offsetting in section 11.38A as follows:

11.38A A financial asset and a financial liability shall be off-set and the net amount presented in the statement of financial position when, and only when, an entity:

(a) currently has a legally enforceable right to set off the recognised amounts; and

(b) intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

It is unlikely that such a right would exist in this case and therefore it would not be possible to off-set and you should advise the client accordingly.

In conclusion therefore, the first option above, i.e. no breach of thresholds unless they have been breached for two years, would be the least contentious option if it is possible and appropriate in these circumstances.

REVISED ICAS CODE OF ETHICS (APPLICABLE FROM 1 NOVEMBER 2017)

The ICAS Code of Ethics is largely based on the International Ethics Standards Board for Accountants (IESBA) Code. ICAS issued a revised Code of Ethics (https://www.icas.com/ethics/icas-code-of-ethics) with an applicable date of 1 November 2017. The changes are as follows:

1. Non-compliance with laws and regulations (NOCLAR)

The introduction of the IESBA content on what a professional accountant should do if they encounter actual or suspected "Non-Compliance with laws and Regulations (NOCLAR)" at their client or employer (new Sections 225 and 360 of the Code respectively).

Laws and Regulations
The laws and regulations which are relevant to the professional accountant for the purposes of the NOCLAR guidance are those which have a direct impact on material items in the financial statements, or are fundamental to the organisation's operations.

The NOCLAR provisions in the Code do not take precedence over local laws and regulations regarding the reporting of actual or suspected non-compliance with laws and regulations. If there is a conflict between local legislation and the provisions of the Code, the professional accountant must adhere to local legislation. Therefore, CAs must always be aware of the disclosures that could amount to "tipping-off" under the UK Anti-Money Laundering laws and regulations.

NOCLAR framework
The underlying principle of NOCLAR is the same for all professional accountants i.e. they should respond to an issue and not turn a blind eye. However, NOCLAR has different requirements depending on the particular role and level of seniority of the professional accountant. Four categories of professional accountant are distinguished and specific steps are identified for each. The classifications are:

- Auditors.
- Other Professional Accountants in Public Practice (PAPP).
- Senior-level Professional Accountants In Business (PAIB).
- Other Professional Accountants In Business.

Greater responsibility is placed on auditors and senior-level professional accountants in business.

Further guidance on implementing NOCLAR is available via the IESBA website. (http://www.ethicsboard.org/responding-non-compliance-laws-and-regulations)

2. Moral courage
An amendment to Section 100.5 of the ICAS Code to establish that "Moral Courage" is an enabler – an underpinning qualitative characteristic - which helps CAs to comply with the fundamental principles:

"***Moral courage***
In order to ensure compliance with the fundamental principles, an underpinning qualitative characteristic required of the professional accountant is the 'courage' to act morally. 'Courage' for the professional accountant is the need to act in accordance with the fundamental principles, especially in situations where there is a risk of suffering adverse personal consequences. "There is a need for the professional accountant to confront ethical dilemmas with courage. When facing an ethical dilemma, the professional accountant needs to have the courage to acknowledge the dilemma, to make a reasoned judgement as to the ethical action required to resolve the dilemma, and then to act accordingly."

The global reach of the ICAS promotion of "moral courage" has been recognised by the International Ethics Standards Board for Accountants (IESBA) with reference to the ICAS publication "Moral courage" (https://www.icas.com/ethics/moral-courage) being made in IESBA's May 2018 consultation paper on 'professional scepticism' (http://www.ifac.org/news-events/2018-05/global-ethics-board-consults-professional-skepticism)

3. Other conforming amendments
There are also certain other conforming amendments which are not seen as substantial.

Future Revisions to the ICAS Code of Ethics
The next envisaged revision of the ICAS Code of Ethics will have an applicable date of either June 2019 or January 2020 - the ICAS Ethics Board will make a decision on this in the near future. This revision will take account of the recent changes that have been made by IESBA to its Code of Ethics. This latest version of the IESBA Code has been completely restructured to improve the readability, understandability, and navigability of the IESBA Code. There are also some changes of substance.
The new restructured Code will be the subject of future articles.

LEGAL CHANGE MAKES IT EASIER TO PROTECT RESIDENTIAL ADDRESSES ON THE COMPANY REGISTER

The Government has introduced the Companies (Disclosure of Address) (Amendment) Regulations 2018 to make it easier for company directors and others such as secretaries, Persons with Significant Control (PSC) and Limited Liability Partnership (LLP) members to protect their residential addresses on the company register, to help safeguard them from identity fraud and personal harm. The change came into force on 26 April 2018.

As concern grows about the public availability of residential addresses in a digital world, the Government believes there is a balance to be struck between ensuring that the information on the companies' register is of real practical use in achieving corporate transparency and ensuring that the information does not become a tool for abuse. The Government believes that concerns about having residential addresses available on the register are justified and has therefore amended the law to allow directors and other individuals to remove their residential address from being publicly available, other than where it has been used as a registered office address.

Applications to remove a home address incur a charge of £55 for each document that a person wants to be suppressed. An alternative correspondence address must be provided if the person is still appointed to a live company, such as a current director. This will replace the person's home address on the public register. If a person is no longer appointed to a company, then they do not need to provide an alternative address. Instead, only the first half of their postcode will be available to the public.

Companies House has produced the following guidance:

Restricting the disclosure of your information (of Relevance to Directors, Advisers to companies and PSCs)

https://www.gov.uk/government/publications/restricting-the-disclosure-of-your-psc-information/restricting-the-disclosure-of-your-information

Restricting the disclosure of your information: Limited Liability Partnerships

https://www.gov.uk/government/publications/restricting-the-disclosure-of-your-psc-information-limited-liability-partnerships

Restricting the disclosure of your information: Scottish Limited Partnerships and Scottish Qualifying Partnerships

https://www.gov.uk/government/publications/restricting-the-disclosure-of-your-information-scottish-limited-partnerships-and-scottish-qualifying-partnerships/restricting-the-disclosure-of-your-information-scottish-limited-partnerships-and-scottish-qualifying-partnerships

Restricting the disclosure of your information: Overseas Companies

https://www.gov.uk/government/publications/restricting-disclosure-of-your-address

TAX RETURNS FOR DIRECTORS

And here is your starter for ten: Company directors are obliged to submit a self assessment tax return (SATR). True or false?

At present, it rather looks as though the answer depends on whether you rely on gov.uk or not. https://www.gov.uk/self-assessment-tax-returns/who-must-send-a-tax-return and https://www.gov.uk/running-a-limited-company. It is clear here that HMRC thinks SATRs are due from directors. However this is not an accurate representation of the law.

Statute

If you look at the Taxes Management Act 1970 (TMA 1970), a different picture arises, and also a degree of confusion.

In s7 we find a duty to notify. The duty is for all taxpayers to notify HMRC within six months of the end of a tax year where there is untaxed income or gains on which there is a liability -unless tax due (all tax due) has been paid at source. For failure to notify, penalties may arise.

In s8 we have a duty to file a tax return. The obligation is to file a return where taxpayers have received notice to file from HMRC. For failure to submit a return on time when there has been a notice to file, penalties may arise.

It is possible to go round in something of a do-loop with these two sections. If HMRC withdraws a notice to file, the s8 requirement, it's possible for the s7 requirement to kick back in.

So HMRC withdraws the notice to file, but there is untaxed income – then the taxpayer duty to notify untaxed income again comes into play. Thus should HMRC withdraw the notice to file in error, the onus is back on the taxpayer to contact HMRC. And the timelimit for notifying is normally within 30 days.

Obligation to notify

The obligation to notify comes into play in other circumstances. For example where the recipient of a Simple Assessment (a dwindling species, per the latest announcement on MTD for Individuals) finds that the Assessment does not include all their income: or where someone is liable to High Income Child Benefit Charge.

The obligation to notify does not exist where a taxpayer has untaxed income wholly within the personal allowance, trading or property allowance. Nor with a new source of PAYE income which is correctly taxed at source. Nor with a gain on the sale of a main private residence – where the property has been owner-occupied throughout.

Interaction of the two obligations
A taxpayer has an obligation to notify HMRC of untaxed income on which a tax liability arises. The obligation to file a return arises only when HMRC asks for a return to be made.

To return to our initial question – is there some special category into which directors fall? The answer is no. Directors are treated the same as the rest of the taxpayer population. If their income is taxed under PAYE, if their income is dividend income on which no further liability arises, directors have no duty to notify, and no duty to file a tax return. But that's not quite the end of the matter, and it brings us to the second question. When, then, may a director have to file a return? We could continue the preceding sentence like this: "In such circumstances, directors have no duty to notify, and no duty to file a tax return – unless – "

Unless
Unless HMRC issues a notice to file.

This is the point at which confusion and practical problems can arise. HMRC can be somewhat gung-ho about issuing notice to file, and on occasions, company director clients may receive a clutch of such invitations. Such a situation can arise in a number of ways: the reduction in Dividend Allowance from 6 April 2018, bringing more directors a tax liability on dividends, for example, may well trigger the issue of more notices to file by HMRC. What then, is the politic response?

Don't !
There are in fact two don'ts.

First, don't file the return if the client has no liability. File a return and it can't be withdrawn. The winning tactic is to ask HMRC to withdraw the notice to file (frequently wrongly referred to as asking HMRC to withdraw the return) under s8B TMA 1970.

Withdrawing notice to file means penalties for late filing no longer apply. Penalties are for failure to comply with a notice to file a return: where there is no requirement to file, penalties should be cancelled.
Note though, that HMRC is not obliged to withdraw a notice to file. It may however do so if it is satisfied that there is not an additional tax liability for the year, the taxpayer has not filed a return, and HMRC has not issued an estimated tax assessment (determination).

Evidence that there is no tax liability should be submitted with the request to withdraw notice to file. HMRC can withdraw a return within two years from the end of the year of assessment, although 'in exceptional circumstances' this period can be extended at HMRC's discretion.

Second, don't file and then appeal. Filing a return when there is no tax liability means incurring the possibility of late filing penalties, with all the concomitant problems of proving reasonable excuse.

Weapon in the armoury
There have been a number of tax tribunal cases recently which provide weapons in the armoury.

Firstly, Karen Symes (TC0632 [2018] UKFTT 0042) is ammunition on the position of company directors. HMRC argument that directors must submit SATRs is not acceptable.

'No one has a statutory obligation to do anything in relation to income tax simply because they are a director of a company which is not a not-for-profit company. The statutory obligation on every person is to notify liability if they are chargeable to tax and their income and gains do not fall within at least one of the exceptions in subsections (4) to (7) of s7 TMA.'

http://financeandtax.decisions.tribunals.gov.uk/judgmentfiles/j10287/TC06320.pdf)

We also have Mohammed Salem Kadhem, where http://financeandtax.decisions.tribunals.gov.uk/judgmentfiles/j9898/TC05929.pdf the director's only income was a salary subject to PAYE, and as a result he was unaware that a SATR could be required. HMRC maintained that it had sent him notice to file a 2014/15 tax return in April 2015, but no return was filed until September 2016.

HMRC contended that as a director, he should have registered for self assessment and filed a return, and done so 'without prompt or reminder from HMRC.'

'As a company director one of the appellant's responsibilities is to register for self-assessment and send a personal self-assessment tax return each year.'

Tribunal pointed out that HMRC was relying on the gov.uk advice here. It said 'This guidance does not have the force of law and the appellant was under no obligation to follow it, even if he was aware of the guidance – which the Tribunal considers was doubtful. In the Tribunal's opinion this Government guidance notice does not accurately reflect what the law says.

In the event, the case was won on the basis that there was not sufficient evidence to show that HMRC had sent notice to file, deemed delivery under s7 Interpretations Act 1978 applying only where post is correctly addressed.

So a winning line can be to ask HMRC to prove that a s8 notice was correctly delivered.

Finally

Mr Kadhem's case also instances the problem of clients running to hoist themselves with their own petard. Per Mr Kadhem,'Had I received a letter I would have filed a return immediately; as I had no liability that tax year, it would have been very easy and straight forward for me to do so.'

Actually the wrong question. No duty to notify, but HMRC had issued a s8 notice….
See Don't number one. Better by far not to let them do it.

NEW REQUIREMENT FOR FARMERS IN ENGLAND TO OBTAIN AN ACCOUNTANTS' CERTIFICATE

Firms in England may receive requests from farming clients regarding a recent letter issued by the Rural Payments Agency (RPA) of the Department for Environment, Food & Rural Affairs (DEFRA) to farmers in England regarding rural payments.

The letter advises farmers that they need to get an active farmer certificate signed by an accountant to confirm 'active farmer status' and that they have to respond within 10 days or they won't get their payments on time. The stated deadline for accountants to have submitted their reports was 27 October 2017.

The Active Farmer readmission guidance (dated 13 October 2017): Accountants Certificate Guidance and Procedures 2017 refers to Annex C(1) ICAEW framework document for accountants.

Please be aware that the deadline of 27 October 2017 is not a legal/regulatory deadline. It is not enforceable and there is no penalty if farmers do not meet this deadline. Discussions are now taking place between the accountancy profession and the RPA to arrive at a sensible way forward.

In the meantime, firms and members are reminded that when carrying out work on grant schemes or other similar assurance work, they are required to follow the Financial Reporting Council's Ethical Standard (where appropriate), and the ICAS Code of Ethics. They should therefore, not feel pressured to sign off on reports for which they do not have an adequate framework or guidance from third parties that are requesting these reports.

FRC ISSUES REVISED PRACTICE NOTE 11: THE AUDIT OF CHARITIES IN THE UK

The Financial Reporting Council (FRC) published a revised Practice Note 11: The audit of charities in the United Kingdom in November 2017. The Practice Note was revised to reflect:

- Revisions to International Standards on Auditing (UK) (ISAs (UK)), for the audit of financial statements for periods commencing on or after 17 June 2016.
- Changes to UK accounting standards, specifically Financial Reporting Standard (FRS) 102, and the revision of the Charities SORP.
- Continuing developments in regulation and guidance issued by the UK Charity Regulators.
- Changes in relevant legislation, including charity law.

Practice Note 11 has also been updated to omit material that merely repeats wording from ISAs (UK); and guidance that an auditor would be able to find elsewhere.

Main revisions
The main revisions from the previous Practice Note 11 are:

- An update of the 'Legislative and regulatory framework' section to reflect changes across the different charity law jurisdictions in the United Kingdom (England & Wales; Northern Ireland; and Scotland). Additional detail about the legislative and regulatory framework is included in Appendix 2 'Charity accounting and audit requirements in the United Kingdom' with enhanced coverage of charity law developments in Northern Ireland since the previous edition of the Practice Note.
- The inclusion of a new section on 'Reporting matters of material significance to UK charity regulators'. Guidance on reporting to UK charity regulators had previously been linked to ISA (UK) 250 - Section B. Included within the scope of this section is new guidance issued jointly by the UK charity regulators, in 2017, on the duty of the auditor to report matters of material significance.
- The incorporation of updated material into the sections on ISAs (UK) 250 - Section A, 315, 330 and 600 which reflect the special features of charities.
- Updates to the sections on ISAs (UK) 315 and 330 to reflect changes in the financial reporting framework for charities.
- A new Appendix 1 'Conditions and events that may indicate risks of material misstatement', which sets out conditions and events which may give rise to a risk of material misstatement specific to charities.
- An expanded and updated section on ISA (UK) 570 to provide more guidance to auditors on going concern. The responsibility of trustees for assessing whether a charity remains a going concern is highlighted along with the auditor's role in evaluating the trustees' assessment. Examples of charity specific indicators of potential going concern issues are provided.
- Updates to the section on ISA (UK) 720 to provide guidance on how this standard applies to other information in the annual report, including the trustees' annual report. The other information accompanying the financial statements is considered 'statutory other information'. This means that auditors will be required to report on the consistency of other information with the financial statements as well as considering whether it has been properly prepared.

ISAs (UK) in full
The full titles of each ISA (UK) referred to above are:

- 250 - Section A: Consideration of laws and regulations in an audit of financial statements.
- 250 - Section B: The auditor's statutory right and duty to report to regulators of public interest entities and regulators of other entities in the financial sector.
- 315 - Identifying and assessing the risks of material misstatement through an understanding of the entity and its environment.
- 330 - The auditor's responses to assessed risks.
- 570 - Going concern.
- 600 - Special considerations: Audits of group financial statements (including the work of component auditors).
- 720 - The auditor's responsibilities relating to other information.

Status of the Practice Note
Practice Note 11 is intended to assist auditors in applying the requirements of ISAs (UK) and sets out the specific considerations relating to the audit of charities. It is persuasive rather than prescriptive; however, it is indicative of good practice.

The Practice Note has a revision date of November 2017, with the revised guidance taking immediate effect.

Other developments
ISA (UK) 250 – Section A, has been subsequently updated for audits of financial statements for periods commencing on or after 15 December 2017. A new appendix is included, providing revised guidance on the auditor's responsibilities in respect of money laundering, terrorist financing and proceeds of crime in the UK. The appendix supersedes the guidance included in Practice Note 12: Money laundering – guidance for auditors.
There are consequential amendments to several other ISAs (UK) which are also effective for the audits of financial statements commencing on or after 15 December 2017.

FRS 101 REDUCED DISCLOSURE FRAMEWORK

After considering the 2017/18 annual review of Financial Reporting Standard (FRS) 101, the Financial Reporting Council (FRC) has decided to make no amendments to the standard. The Basis for Conclusions has been amended to reflect this decision.

The latest, March 2018 version of FRS 101 is available at:
https://www.frc.org.uk/getattachment/a7d5c00c-93a4-4796-b23a-7cc50af34a94/FRS-101-Reduced-Disclosure-Framework-(March-2018).pdf
As a reminder:

(i) FRS 101 sets out an optional reduced disclosure framework which addresses the financial reporting requirements and disclosure exemptions for the individual financial statements of subsidiaries and ultimate parents that otherwise apply the recognition, measurement and disclosure requirements of EU-adopted International Financial Reporting Standards (IFRS).

(ii) Disclosure exemptions are available to a qualifying entity, as defined in the glossary to FRS 101 (see below), in its individual financial statements (but not in consolidated financial statements which it is required or voluntarily chooses to prepare). However, a qualifying entity which is a financial institution is not exempt from the disclosure requirements of IFRS 7 'Financial Instruments: Disclosures', IFRS 13 'Fair Value Measurement' to the extent that they apply to financial instruments, and paragraphs 134 to 136 of International Accounting Standard (IAS) 1 Presentation of Financial Statements.

(iii) A qualifying entity may apply the reduced disclosure framework regardless of the financial reporting framework applied in the consolidated financial statements of the group.

(iv) Financial statements prepared by a qualifying entity in accordance with this FRS are not accounts prepared in accordance with EU-adopted IFRS. A qualifying entity must ensure it complies with any relevant legal requirements applicable to it. For example, individual financial statements prepared by companies in accordance with FRS 101 are Companies Act accounts and not IAS accounts as set out in section 395(1) of the Act, and therefore such accounts must comply with the requirements of the Act and any relevant regulations such as the Large and Medium-Sized Companies and Groups (Accounts and Reports) Regulations 2008 (SI 2008/410).

In the Glossary to FRS 101, a qualifying entity is defined as:

A member of a group where the parent of that group prepares publicly available consolidated financial statements which are intended to give a true and fair view (of the assets, liabilities, financial position and profit or loss) and that member is included in the consolidation. A charity may not be a qualifying entity.

GUIDANCE FOR CHARITY INDEPENDENT EXAMINERS ON GOING CONCERN

The ICAS Charities Panel has issued a Guide on going concern for ICAS members acting as charity independent examiners. This has been prepared in recognition of increasing stakeholder focus on the going concern status of charities. The Guide applies to reporting periods commencing on or after 1 January 2016.

The Guide:

- Applies UK-wide to the independent examination of accounts prepared to give a 'true and fair' view. It is intended to be practical and contains decision-making tools and a case study to support the independent examiner's own professional judgement.
- Is designed to support the independent examiner's work relevant to the accounting concept of going concern and to meet any related reporting requirements. It is not designed to increase the independent examiner's workload or broaden the scope of the examination.
- Reflects the requirements of UK charity regulators' guidance on Matters of material significance, to the extent that this is pertinent to the examiner's work on going concern, and the recently revised mandatory Directions for independent examiners published by the Charity Commission for England and Wales.

The Guide is intended to set out how an independent examiner can address the accounting concept of going concern, as far as possible, within the routine work undertaken as part of the engagement. Of course, additional investigations may need to be undertaken around the going concern concept as the examiner's preliminary findings dictate. In order to provide structured, accessible guidance, the Guide has three core chapters:

(i) identifying going concern issues;
(ii) gathering and assessing evidence; and
(iii) reporting on going concern issues.

Identifying going concern issues
An independent examiner's routine planned work should normally provide insights into a charity's going concern status and should be designed to do so.

Gathering and assessing evidence
Should a going concern issue be identified during an independent examiner's routine work, the examiner should obtain additional evidence or make additional inquiries sufficient to determine the implications for their independent examiner's report.

Reporting on going concern issues
In addition to evaluating whether and how to report on a going concern issue in the independent examiner's report, the independent examiner has other reporting considerations. For example, if the independent examiner refers to a going concern matter in their independent examiner's report, the report is considered by the UK charity regulators to give rise to a statutory duty to report to them. The independent examiner may also wish to issue a written report to the trustees setting out their findings and recommendations, although there is no requirement for the examiner to do so.

Independent examination and 'true and fair' accounts*:* *legal Context*
All UK charities by law are subject to independent external scrutiny, except for charities registered with the Charity Commission for England and Wales with a gross income of under £25,000. Therefore, in the main, charities not receiving an audit will be independently examined.

Non-company charities exceeding the gross income threshold for their charity law jurisdiction, and all charitable companies, must prepare accounts which give a 'true and fair' view. Charities below the threshold have the option of preparing receipts and payments accounts.

The accounting concept of going concern relates solely to 'true and fair' accounts and, for UK charities, this means accounts prepared in accordance with FRS 102 and the Charities SORP (FRS 102).

ICAS members acting as independent examiners
Many ICAS members support the charity sector by acting as independent examiners either in public practice or in a voluntary capacity.

Any ICAS member acting as an independent examiner must have the necessary skills and knowledge to
deliver a high standard of service. This is achieved through compliance with the ICAS requirements for continuing professional development (CPD). ICAS members must also comply with other relevant regulatory and professional requirements, including those contained within:

- The ICAS Charter, Rules and Regulations.
- The ICAS Code of Ethics.
- ICAS guidance on Practising Certificates, specifically the guidance on whether a practising certificate (PC) is needed to provide accountancy services to charities.

NEW GUIDANCE FOR CHARITY AUDITORS AND INDEPENDENT EXAMINERS ON REPORTING MATTERS OF MATERIAL SIGNIFICANCE

The Office for the Scottish Charity Regulator (OSCR), the Charity Commission for England and Wales and the Charity Commission for Northern Ireland have issued joint guidance for charity auditors and independent examiners on reporting matters of material significance.

All auditors and independent examiners have a statutory duty to report matters of material significance to the appropriate charity regulator. The duty is underpinned by different legislation in each of the three charity law jurisdictions of the United Kingdom and is accompanied by a statutory right to report.

Charity law, therefore, gives auditors and independent examiners legal protection against claims for breach of confidentiality.

The guidance sets out nine matters, including two new matters, which the regulators consider to be of material significance. The two new matters are described in the guidance as follows:

- If an auditor or independent examiner has concerns regarding a charity's accounts and issues a modified audit report or qualified independent examiner's report (matter 8).
- Where an auditor or independent examiner has concerns that conflicts of

interest or related party transactions have not been properly managed or declared (matter 9).

The risk of over reporting

ICAS is concerned that matter 8 will lead to over reporting which could obfuscate genuinely significant issues. However, in their consultation report, the charity regulators state

"We agreed that it is for [us] to determine whether there is a burden placed upon [us] in receiving these reports".

ICAS responded to the charity regulators' consultation in September 2016 which focused specifically on the matters to be reported and was therefore narrower in scope than the published guidance.

The guidance applies to matters to be reported after 1 May 2017 regardless of the accounting period under audit or examination.

Other reporting duties

Auditors fall within the UK's anti-money laundering and counter terrorism financing (AMLCTF) reporting regime as do ICAS members who provide other accountancy-related services, including independent examinations, by way of business.

Reporting to a UK charity regulator does not discharge an auditor or independent examiner from any statutory obligations under the AMLCTF regime.

Subsequent to the issue of this guidance, the Financial Reporting Council (FRC) issued a statement to remind auditors of charities that they are required to carry out their audit in compliance, not only with the FRC's ethical and auditing standards, but also applicable legal and regulatory requirements.
Attention is drawn to:

Key Points from FRC's Statement.

- Any person appointed as an auditor or independent examiner for a charity has a duty to report matters of material significance which they become aware of during their appointment to the relevant UK charity regulator.
- The guidance explains those matters which the UK charity regulators consider to be of material significance and provides some further explanation of each of the matters.
- The statutory duty to report is not a new duty but this guidance is the first guidance to be issued jointly by the three UK charity regulators on the subject.
- Under charity law, the term 'material significance' is used to determine which matters should be reported. Material in this context has a different meaning to that which auditors and independent examiners will be familiar with in accounting terms. In this case, it means matters which are of material significance to a UK charity regulator in carrying out its functions.
- The matters in Table 1 below are always considered reportable as matters of material significance by UK charity regulators. This list is effective for all audits or independent examinations which are conducted and/or reported after 1 May 2017 (regardless of the accounting period being examined).
- A matter of material significance becomes reportable as soon as the auditor or independent examiner:
  - becomes aware of it, or
  - in the case of an auditor, makes a modified auditor's opinion or an auditor's report with an emphasis of matter paragraph or a paragraph highlighting a material uncertainty relating to going concern, or
  - in the case of an independent examiner, issues a qualified independent examiner's report i.e. a report which identifies one or more concerns about the charity's accounts.

  Auditors and independent examiners may decide that other matters not included in this list are, in their judgement, of such a nature that they consider them reportable as a matter of material significance. In this case, in making their report they should identify the matter(s) reported as of material significance.

Table 1: Reportable matters of material significance:

Matter	Title	Each matter is prefaced by the following statement - 'During an audit/independent examination'
1	Dishonesty & Fraud	matters suggesting dishonesty or fraud involving a significant loss of, or a material risk to, charitable funds or assets.
2	Internal Controls & Governance	failure(s) of internal controls, including failure(s) in charity governance that resulted in, or could give rise to, a material loss or misappropriation of charitable funds, or which leads to significant charitable funds being put at major risk.
3	Money Laundering & Criminal Activity	knowledge or suspicion that the charity or charitable funds including the charity's bank account(s) have been used for money laundering or such funds are the proceeds of serious organised crime or that the charity is a conduit for criminal activity.
4	Support of Terrorism	matters leading to the knowledge or suspicion that the charity, its trustees, employees or assets, have been involved in or used to support terrorism or proscribed organisations in the UK or outside of the CCNI EG058 November 2017 10 UK, with the exception of matters related to a qualifying offence as defined by Section 3(7) of the Northern Ireland (Sentences) Act 1998.
5	Risk to charity's beneficiaries	evidence suggesting that in the way the charity carries out its work relating to the care and welfare of beneficiaries, the charity's beneficiaries have been or were put at significant risk of abuse or mistreatment.
6	Breaches of law or the charity's trusts	single or recurring breach(es) of either a legislative requirement or of the charity's trusts leading to material charitable funds being misapplied.
7	Breach of an order or direction made by a charity regulator	evidence suggesting a deliberate or significant breach of an order or direction made by a charity regulator under statutory powers including suspending a charity trustee, prohibiting a particular transaction or activity or granting consent on particular terms involving significant charitable assets or liabilities.
8	Modified audit opinion or qualified independent examiner's report	on making a modified audit opinion, emphasis of matter, material uncertainty related to going concern, or issuing of a qualified independent examiner's report identifying matters of concern to which attention is drawn, notification of the nature of the modification/qualification/emphasis of matter or concern with supporting reasons including notification of the action taken, if any, by the trustees subsequent to that audit opinion, emphasis of matter or material uncertainty identified /independent examiner's report.
9	Conflicts of interest and related party transactions	evidence that significant conflicts of interest have not been managed appropriately by the trustees and/or related party transactions have not been fully disclosed in all the respects required by the applicable SORP, or applicable Regulations.

RELAXATION TO SUBSTANTIAL SHAREHOLDING EXEMPTION

SSE has been a very useful relief where a trading company or the holding company of a trading group which had held at least 10% of the ordinary shares in a “subsidiary” for at least 12 months, disposed of some or all of its shareholding in the subsidiary.

For the relief to apply, the subsidiary itself has to have been a trading company or the holding company of a trading group for at least 12 months.

Prior to the recent changes in Sections 27 and 28 Finance (No2) Act 2017, it was necessary, after the disposal, for the holding company either to be a trading company or the holding company of a trading group or for it to be liquidated shortly after the disposal.

The changes mean that this will no longer be necessary.

This was a particular problem where, after the disposal of a trading subsidiary, the holding company was a singleton company, and therefore not the holding company of a trading group and did not carry on a trade itself. The company may, for example, have held one or more properties which it rented out, perhaps to its former trading subsidiary.

The relaxation also applies to qualifying institutional investors.

Another piece of good news is that the relaxation is effective in relation to disposals made on or after 1 April 2017 (Section 27 Finance (No2) Act 2017).

EMPLOYMENT CORNER

Budget Round-up

The last Budget did not contain many employment tax measures – but those which were included are significant. The Budget really concentrated on issues which affect the rest of the UK rather than those which specifically affect Scotland – with the exception of the Personal Allowance.

The rise in Personal Allowance to £11,850 was to be expected and is in line with the Government's aim to increase it to £12,500 by 2020, which will help many low paid workers to pay less tax or be removed from tax altogether. The National Living Wage (payable to those aged 25 and over) has risen by 4.4% from £7.50 to £7.83 from 1 April 2018, which should mean that full time workers will be around £600 per annum better off. It should also be noted that as non-savings, non-dividend income tax raising is now devolved to Scotland, each increase in the Personal Allowance also puts more pressure on the Scottish Government to fill the gap in revenues between what is raised in Scottish Income Tax and the reduction in Barnett Formula Block Grant.

The Higher rate threshold rise to £46,350 provides a further widening of the differential between Basic and higher rate taxpayers north and south of the Scottish border. If Scottish thresholds were to stay the same in 2017/18, this would represent a £670 difference in the tax Scottish higher rate taxpayers pay compared to English (assuming they have a personal allowance).

Charging electric vehicles at work

Charging electric vehicles at work will not attract a benefit in kind charge from 2018/19. This will no doubt encourage many employers to purchase hybrid and all-electric fleet vehicles. Currently, the fuel scale change is an expensive luxury for most employees with company cars. This in contrast to the additional 1% levy from 2018/19 on diesel vehicles which do not meet emissions targets, making driving diesel company cars ever more punitive.

Apprenticeship Levy

Although the Chancellor stated that 3 million new apprenticeships will have been conceived by 2020, it was disappointing to note that no measure of understanding appears to have been developed about the success or otherwise of the bedding in of the Apprenticeship Levy, which many employers view as "just another tax". Having different apprenticeship schemes and access to funding in Scotland and England is also causing concern for some employers and needs to be examined as a priority to ensure all employers have equality of access to funds.

The Taylor review, the gig economy and employment status
Whilst the Chancellor's speech doffed its hat to the notion of fairness in the workplace, no measures to tackle this in line with the Taylor Report recommendations, the gig economy or erosion of the tax base by non-alignment of self-employed National Insurance with employed NICs were brought in. Mr Hammond had tried to align NICs in the Spring Budget but was forced to withdraw the measure due to heavy opposition. The Government did announce its intention to publish a consultation to assist it in responding to the Taylor report which combines an assessment of how to make tests for employment status and tax "clearer".

Tax avoidance
Further to existing measures to tackle tax avoidance schemes and disguised remuneration, the Government will now legislate to:

- introduce the close companies' gateway, to tackle disguised remuneration avoidance schemes used by close companies to remunerate their employees, and directors, who have a material interest. This change will have effect on and after 6 April 2017
- require all employees, and self-employed individuals, who have received a disguised remuneration loan to provide information to HMRC by 1 October 2019.

With effect from 22 November 2017, Part 7A of Income Tax (Earnings and Pensions) Act 2003 applies regardless of whether contributions to disguised remuneration avoidance schemes should previously have been taxed as employment income, and also ensures that liabilities arising from the loan charge are collected from the appropriate person where the employer is located offshore.

"Off-payroll" reform: possible extension to the private sector of IR35
New regulations effective from April 2017 were introduced obliging public sector engagers to examine engagement relationships to determine whether individuals hired to work there were taxed as employees even if working through an intermediary. A consultation was published in early 2018 to determine if these obligations are to be extended into the private sector.

Travel and subsistence
Following the call for evidence on the taxation of employee expenses published on 20 March 2017, existing concessionary travel and subsistence overseas scale rates will now be given a statutory basis from 6 April 2019. In addition, from the same date, employers will not to have to check receipts when making payments to employees for subsistence using benchmark scale rates for meal allowances and overseas scale rates. In both cases, employers will only be asked to ensure that employees are undertaking qualifying travel. The abolition of receipt checking does not apply to amounts agreed under bespoke scale rates or industry wide rates.

Consultation on extending the scope for employees and the self-employed to claim tax relief on self-funded training
Another measure which arose following the call for evidence on the taxation of employee expenses published on 20 March 2017 was that the government also intends to consult in 2018 on whether to extend the scope of tax relief currently available to employees and the self-employed for work-related training costs. A paper was published on 1 December 2017.

Real Time Information - A Post Implementation Review
HMRC has now published its assessment of the implementation of RTI, at https://www.gov.uk/government/publications/real-time-information-programme-post-implementation-review

EMPLOYMENT CORNER – RANGERS FALLOUT

Tax advisers generally, together with employers with similar Employee Benefit Trust (EBT) arrangements, have been waiting for seven years for the final judgement on RFC 2012 Plc (in liquidation) (formerly The Rangers Football Club Plc) v Advocate General for Scotland ("The Rangers Case") to emerge. It is therefore pleasing to have a final, binding decision which delivers certainty for employers and their tax advisers. Having followed the debate through two tribunal hearings and a Court of Session hearing, it is clear the unanimous Supreme Court judgement handed down by Lord Hodge, which has been the best part of four months in the making, has also been a difficult and complicated process.

BDO, liquidators to Rangers Football Club, will be liable for any PAYE and NICs deemed to be due under this ruling. It is unlikely the players who were the original beneficiaries of the EBT could be asked to pay any back taxes by HMRC.

It is important to note that since the 'Rangers' EBT was first set up, tax practice and attitudes to tax avoidance have moved on. The introduction of the DOTAS rules, changes to penalty regimes and more recently the introduction of accelerated payment notices and follower notices have changed the climate. Additionally, all the main professional bodies for tax advisers have agreed to revised Professional Conduct in Relation to Taxation rules, which establish standards in relation to tax planning.

Tax advisers should be aware this verdict has opened up an opportunity for HMRC to issue “Follower Notices”, which would entitle it to pursue income tax and NICs from employers who have operated similar schemes to that of Rangers, using this case as the trigger. If they have not done so already, firms should look to review any cases where EBTs were being used, and bear in mind it is the particular avoidance mechanism which is in point – this is not sector- specific. There are likely to be a number of football and rugby clubs which are caught, but businesses in other sectors could also have structured remuneration in a very similar way and are thus also likely to be scrutinised by HMRC.

To recap, in the Rangers case, the fact pattern[1] is that Murray Group Management Ltd (MGM) established a Principal Trust for the benefit of its employees and the employees of any group company including MGM which entered into a deed of adherence. The trustee of the Principal Trust then set up a series of sub trusts for the benefit of employees’ families. MGM paid contributions to the Principal Trustee with a direction that a sub-trust be established and funded for the family of a particular employee. The employee was appointed protector of the sub-trust, and the sub-trust trustee would lend the employee money that had been advanced to the sub trust from his employer. At the time, EBTs were used for many different purposes, the most common of which were to assist with some aspects of pension funding and as a vehicle for supporting share-based remuneration.

However, their use for structuring bonus payments caught HMRC’s attention as an avoidance mechanism, and as such the 2011 Finance Act removed the relevant tax advantages under the disguised remuneration rules.
The three key issues being reviewed by the Supreme Court were whether the £47+ million paid from offshore EBTs to over 80 players and staff did in fact constitute earnings under ICTA 1988 and ITEPA 2003; whether the deeming provisions within the legislation were sufficient to capture the payments as earnings; and whether each recipient was sufficiently close to the funds that this meant they had been placed unreservedly at their disposal.

Lord Hodge agreed with the First Tier Tribunal dissenting judge Dr Poon’s assessment that “the legislative code for emoluments has primacy over the benefits code in relation to loans”. This appears to have been a crucial deciding factor in this case, and the main reason for the Supreme Court’s decision that the three key issues pointed towards earnings from an employment, making the payments liable to PAYE and NICs.
No doubt the repercussions of the Rangers case will continue to unfold over time, but meanwhile, the way in which employees are remunerated will need to be revisited (if employers have not already done so). Those finance, tax and HR departments who have waited to see the outcome of the case before acting would ideally need to liaise on a suitable replacement for the tiered remuneration strategies where EBTs have historically been used, to ensure the contractual rights of employees are not negatively affected by any changes.

It is likely that HMRC will use the purposive view taken by the Supreme Court of the legislation as an opportunity to question almost any EBT based arrangements or even those which closely resemble them, such as Employer Financed Retirement Benefit Schemes (EFRBS). The trusts in question will also need to be reviewed and appropriate consideration given to winding up the trusts and re-distribution of funds. If there are still any remaining EBTs which have not been brought to HMRC’s attention under the DOTAS or HMRC’s EBT settlement opportunity, then alternative forms of disclosure will now need to be prepared.

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[1] Supreme Court summary: https://www.supremecourt.uk/cases/uksc-2016-0073.html

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