



IR35: working in the public sector

Changes to the tax rules for personal service companies in the public sector have led to anger and some confusion.

Since 6 April 2017, it has been the duty of public sector organisations to determine the IR35 status of people they engage through an intermediary. Where a public service organisation considers the IR35 rules apply to a personal service company or other intermediary, they must deduct income tax and national insurance contributions from fees paid to the intermediary.

Contractors have complained that some public sector organisations are adopting an overly cautious approach. The changes affect anyone working for a public authority, including local authorities, hospitals, schools, the BBC and Channel 4, and police and fire authorities. If the engagement is through an agency, the agency must deduct employment taxes, but the public sector organisation has to inform the agency whether the employment status test is met.

Whether an engagement falls within IR35 depends on several factors, such as who decides how the work is carried out. HM Revenue & Customs (HMRC) introduced a new Employment Status Service (ESS) tool in March, which anyone can use to test the status of a contract. If a contractor thinks a public authority is wrongly deducting tax, they could use the ESS and show the results to their client. HMRC says it will stand by the result given by the ESS, unless a compliance check finds that the information provided was not accurate.

Another change that applies from 6 April 2017 is that the 5% deduction allowed to intermediaries for 'notional expenses' will no longer be available in the public sector. This change was introduced in 2016/17 and has affected people such as locum doctors, who take on engagements all over the country.

Please contact us for advice on how these changes may affect you.

New cash basis for property income

Many more small businesses can now use the simplified cash basis of calculating profits following a big increase to the entry limit.

For property letting businesses, the cash basis has become the standard method for individuals, unless the landlords opt out or has rental income above the threshold.

Under the cash basis, a business records income when it is received and outgoings when they are paid. You therefore do not pay tax on income you have not received.

From 6 April 2017, the cash basis will be available to self-employed individuals (and partnerships of individuals) with annual turnover up to £150,000. Previously, small businesses could only use the cash basis if their turnover was below the VAT registration threshold – £85,000 in 2017/18.

The cash basis will not suit some small businesses, however. If you need to obtain finance, a lender will probably want to see a profit and loss account, which provides a more accurate picture of the business. Loss relief against other income of the same or previous year is not allowed under the cash basis and interest is only allowable up to £500.

You can also use a simplified basis for business vehicle costs, whereby you record your business miles and claim a flat rate of 45p per mile for the first 10,000 miles and 25p thereafter.

Landlords can opt out of the cash basis separately for their UK and overseas property businesses. The £500 cap for loan interest does not apply to property letting, but in 2017/18 you can only deduct 75% of finance costs from rental income. The remaining 25% is relieved by means of a basic rate tax reduction. If you think you may be affected, please get in touch.

Challenging a will

Challenging a will is never easy, with several recent decisions involving charitable legacies simply confirming the right of a person to leave their money to whom they like.

Proving undue influence or lack of mental capacity is rarely successful, and it can be extremely expensive and time consuming. Mediation should normally be tried before resorting to the court. Neither route is helped, of course, by the main witness being dead. A spouse, civil partner or close relative can claim for reasonable financial provision. But adult children who are financially secure will struggle to succeed with a financial provision claim.



Tax restriction starts to bite landlords

If you are a buy to let landlord, you will almost certainly be aware that the restriction on tax relief for finance costs started to bite from 6 April this year.

For the current tax year, only 25% of finance costs are subject to the basic rate restriction. For example, if your buy to let finance costs are £20,000, then £15,000 can be deducted as an expense in calculating property income. Tax relief for the other £5,000 will be given as a basic rate tax reduction of £1,000.

For new buy to lets, using a limited company will bypass the restriction. However, there are other important tax issues to consider before going down this route. As for incorporating an existing property business, this might be an option if you have not owned the property for too long – otherwise the capital gains tax (CGT) cost could be excessive. And don't forget the stamp duty land tax cost.

Another option might be to sell off some properties in order to pay off some or all of the finance on the ones you retain. Although there will be the CGT cost, you might find yourself having to do this anyway if you cannot re-mortgage in the future because of the tighter lending restrictions that now apply. Replacing buy to let finance with a mortgage on your own home is also a possibility given that residential mortgage rates are generally much lower. The interest should still qualify for tax relief.

Warning – two pensions-related changes

There are a couple of recent tax changes which might affect you. One should, in theory, already be in place, but the other will not apply until next year.

Restriction on pension contributions

The amount you can contribute to a pension once you have started drawing flexibly is set to be further reduced from £10,000 a year to £4,000 a year. The restriction, known as the money purchase annual allowance (MPAA), was due to come in on 6 April 2017. The measure was withdrawn from the pre-election Finance Act, along with other controversial clauses, but is expected to return after the election. The MPAA can be triggered with a flexi access drawdown from a crystallised fund or withdrawals from an uncrystallised fund. However, simply designating funds for flexi-access drawdown does not trigger the MPAA, nor does taking just the tax-free pension commencement lump sum. It is also possible to take a non-flexible annuity or withdraw a small pot of up to £10,000 without triggering the MPAA.

Self-employed class 2 national insurance contributions (NICs)

The self-employed will not have to pay class 2 NICs from 6 April 2018, but it could actually cost you an additional £592.80 a year. Currently, class 2 NICs at the rate of £148.20 a year can be paid on a voluntary basis if profits are below a small profits threshold of £6,025 in order to maintain your contribution record. This could be quite important given that 35 years of contributions are required to qualify for the full amount of the new state pension. From 6 April 2018, class 4 NICs will be restructured so that you will be deemed to have paid NICs where your profits fall between £5,876 and £8,164 a year (at current limits). If profits are below this level, the only way you can maintain your contribution record as a self-employed person will be to pay the voluntary class 3 NICs.