BUSINESS UPDATE
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Solving partnership problems

Partnerships can carry on for years without anyone even thinking about the partnership agreement. Then a problem arises and the partners discover that the agreement is inadequate, out-of-date or – worst of all – might not even exist. A well-designed partnership agreement can help solve a number of difficulties.

The basic problem is that the provisions of the Partnership Act 1890 apply where there is no specific agreement to the contrary. For example, under the Act, it is not possible to expel a partner, an individual partner can dissolve the partnership, and the death or bankruptcy of a partner will automatically dissolve the partnership.

An out-of-date or non-existent partnership agreement could make it difficult to deal with the problem of an under-performing partner. A well designed partnership agreement might give the majority the right to expel an individual partner or at least the power to alter a partner's status, maybe changing them to a salaried partner.

Different problems can arise if a partner leaves of their own accord. It might be desirable to be able to place an outgoing partner on 'gardening leave' to protect the partnership's business interests. Once a partner has actually left, a restrictive covenant can prevent them from soliciting the partnership's clients. But covenants must be carefully constructed or they could turn out to be unenforceable.

Partners' retirement can raise other issues. A recently retired partner may have made a significant contribution to the partnership's value, so the partnership might want them to benefit from a sale of the business if it were to take place within a given period after their retirement.

Partnership agreements should be up-to-date with changes in the law generally – especially discrimination law. Agreements should therefore provide for parental leave, comply with sex discrimination legislation, and take account of the recent changes regarding age discrimination – particularly the recent abolition of the default retirement age of 65.

Firms that have grown in size may be especially vulnerable. An agreement that worked for a small three or four person partnership may no longer be appropriate. Decisions that could once be taken by all the partners may now have to be delegated to an individual or to a small group.

Every partnership should have a proper partnership agreement and then review it regularly.

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HMRC fails the grade on guidance

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Taxpayers can avoid a penalty for filing a tax return late if they have a 'reasonable excuse'. But HM Revenue & Customs (HMRC) has come under fire for giving taxpayers guidance on what 'reasonable excuse' means that is at odds with the interpretation given by tribunals. HMRC is also being criticised for delays that allow penalties to mount up.

The term 'reasonable excuse' is not defined in the legislation. In a number of recent cases, tax tribunals have criticised HMRC's guidance, which states that taxpayers would have a 'reasonable excuse' when some unforeseeable and exceptional event beyond their control has prevented them from filing the return on time. The tribunal says that HMRC's official interpretation is too narrow, in particular its view that the event need not be 'exceptional'.

Employers face a different problem. If they file their end-of-year returns late they are charged a penalty of £100 per 50 employees for each month or part month that the return is outstanding. However, HMRC does not send out the penalty notice until four months after the filing date of 19 May, which means that employers might accumulate a minimum £500 penalty before realising there is a problem.

How to delay tax payments

For many taxpayers the problem is not so much making the return as it is paying the tax due. If you know that you will be unable to pay a tax bill (including VAT), you might be given more time to pay. You must contact HMRC's business payment support service before the tax payment is due.

If you can pay your tax on time, make sure you actually do so. Payments to HMRC by bank transfer are not within the banks' faster payments system and so still take three working days. For VAT, you should consider using direct debit as it gives you another three days before HMRC takes the payment from your bank account, on top of the seven extra days allowed if you file your VAT returns online.

Although HMRC expects taxpayers to get returns and payments in on time, its attitude to dealing with taxpayers' correspondence is more relaxed. Bulk post issued by HMRC often arrives many days or even weeks after it is dated and letters to HMRC go astray all too frequently. Such problems only reinforce the need to get your tax right and avoid lengthy enquiry correspondence. If you would like further advice on tax deadlines and paying your tax, please get in touch.

Did you know that the Government recently announced the location of 11 new enterprise zones, completing the total of 22 across England? The new locations include sites in Cornwall, Kent, Oxfordshire, Hereford and Warrington. The advantages of relocating your business to an enterprise zone or setting up a new business within a zone, include a business rate discount worth up to £275,000 over five years, simplified planning regulations and Government support to ensure that super-fast broadband is rolled out within the zones. In addition, certain designated areas will benefit from enhanced first-year capital allowances for investment in plant and machinery.

Escaping employee tax status

Some people have tried to avoid being taxed as employees by setting up sham contracts.

The IR35 legislation was introduced to tax income from 'disguised employment' at a rate similar to any other employment income. It has been particularly devastating for freelance contractors who often have little choice but to operate through an intermediary company.

However, contractors have been successfully fighting back by using 'IR35 friendly' contracts so that arrangements with clients are outside the scope of IR35. One of the most important factors in such a contract is the right of substitution. Whereas an employee is obliged to perform work personally, in a contractor/client relationship the contractor will normally be free to provide a substitute if they are ill or on holiday.

But the problem is that actual working practices must match those stated in the contract – so a substitution clause must be a genuine right. The most recent case to be heard, involving Autoclenz Ltd, reinforces this position as it was heard in the highest court in the land – the Supreme Court.

The case concerned car valets who actually wanted to be treated as employees so that they would be entitled to various employment rights. The valets' contracts stated that they were self-employed and contained an express term allowing them to appoint a substitute. However, the court concluded that the contracts did not reflect the true relationship between the parties, and that the valets were in reality employees.

To rely on a substitution clause the right should ideally be included in the original contract, and you, as the contractor, should be responsible for the substitute's recruitment, their work and their remuneration. Although it is unlikely that a client will permit unfettered use of substitutes, the fewer restrictions placed on their use the better. Bear in mind that just because the right to use a substitute has never been exercised does not mean that it does not exist. If contractors engaged on similar terms have supplied a substitute then this indicates that the right is genuine.

Although substitution clauses are important in establishing self-employed status, there are many other factors to consider. The goalposts for contractors are constantly moving, so contact us if you need advice.

Did you know that the amount of tax debt or underpaid tax that HM Revenue & Customs (HMRC) can collect via PAYE if you are employed has increased from £2,000 to £3,000? HMRC can now use this collection method for the majority of tax debts, including tax credits. If you owe tax for 2010/11 and didn't complete a tax return, then you should receive a tax calculation from HMRC. Underpayments up to £3,000 will automatically be collected through your tax code for 2012/13. If you complete a tax return and have PAYE income, then you will have the option of having underpayments up to £3,000 collected in the same way.

New proposals aid non-dom investment

A new tax relief for non-domiciled individuals who invest in UK business will have no upper limit and be simple to claim, according to a recent Government consultation document.

In the March 2011 Budget the Chancellor announced that from April 2012 non-domiciled individuals who are taxed on the remittance basis will not be taxed on overseas income and capital gains brought into the UK for commercial investment. The Government has now published more details, although these might change before they become law.

Under the proposals, tax-free remittances will be allowed for investment in any company carrying out trading activity, or developing or letting commercial property. The only exclusions will be leasing and residential property letting, although building and developing residential property will be permitted. The investment will have to be in a company, but no decision has yet been made on whether the relief will be confined to investment in companies not listed on a recognised stock exchange. It will be possible to invest in shares or loans.

Investment of overseas income and capital gains held in offshore trusts or other investment vehicles will also attract relief. Another unexpected feature is that the investment can be in a company incorporated and trading outside the UK, as long as it has a permanent establishment in the UK. Furthermore, investors can be connected with the company and draw 'commercial remuneration' for any work they do, for example, as directors.

There are to be some anti-avoidance rules. They are directed mainly at preventing non-domiciliaries taking out their investment to enjoy in the UK. When they dispose of an investment, the original amount invested will have to be taken out of the UK within two weeks of the disposal, or reinvested in a qualifying business in the same period. The relief will have to be claimed in the investor's tax return.

Also starting in April 2012 will be the increased £50,000 annual charge for non-domiciled individuals who claim the remittance basis and have been resident in the UK in 12 or more of the 14 previous tax years. This charge will not be affected by the new relief for business investments. Those who decide not to pay the charge will pay tax on all their worldwide income and capital gains in the year they arise.

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Surviving the social media whirl

Many businesses are using social media, such as Facebook, LinkedIn and Twitter, to interact with customers and promote their goods and services in an up to date and customer-friendly way.

Social media can provide a wide range of opportunities for businesses to communicate with customers, suppliers, employees and the public. But the very flexibility and freedom of social media carry risks as well, so it is important for employers to have a robust social media policy and a well thought-out strategy.

First you need to be clear what you want to achieve and how social media are relevant to your business goals and marketing strategy. Are you aiming to improve your brand presence, for example, or to increase traffic to your company website? Do your research by checking out all the potential sites you might use. Try to understand your target audience. You can also join groups and Twitter chats relevant to your business.

Using social media can make staff more productive by helping them to gather instant information and feedback from customers and prospects, but without an effective strategy it can also be a waste of time and effort. Your staff should understand what you are trying to achieve from your social media strategy and a manager needs to monitor its effectiveness. Employees need training on ways to identify the best approaches to take, how to manage any negative coverage you receive, and on what is acceptable to post, both during and outside working hours. It is good practice for employees to have different profiles for their business and social use.

It is vital to let staff know that messages posted to social media sites will be monitored – and you need to have the technology to do this – and that employers can take disciplinary action against employees who post defamatory comments online that bring their company into disrepute, or disclose confidential information. A combination of training and enforcement should help you to make effective use of social media and protect your business from negative publicity.

A clear written social media policy, which you can incorporate into your staff employment contracts, will strengthen your position if you need to dismiss an employee as a result of unacceptable social media use. Please get in touch if you would like any further advice on these issues.

Had you heard that Companies House has announced that it will not, after all, require most of its filing services to be done electronically from March 2013? The reason given is the Government's desire not to add new regulations affecting small businesses, and Companies House points out that over 70% of filing services are already carried out digitally. The issue will be reconsidered in 2014 when the moratorium on new regulations ends. Although accounts will not have to be filed online using the iXBRL format, this will be of little benefit for most companies because this format is still required when submitting accounts to HM Revenue & Customs.

Swiss tax agreement

The new tax agreement between the UK and Switzerland will let UK taxpayers keep Swiss bank accounts out of sight of HM Revenue & Customs, but they will suffer a withholding tax of up to 48% from 2013.

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People who have not paid tax on their Swiss investments in the past will also suffer a one-off deduction of about 19% to 34% of the account's value, depending on the age of the account and the amounts withdrawn since 2003. Alternatively, they will be able to avoid the charge by disclosing their tax liabilities.

Non-domiciled individuals, whose offshore income might not be wholly liable to UK tax, can opt-out of the initial charge on their whole account by self assessing their liability, which will then be taxed at 34%. There is no special opt-out from the withholding tax.

The agreement only covers UK tax liabilities. The US has adopted a different approach and non-domiciled individuals who are US citizens will still have to pay US tax on the whole of their income. From 1 July 2013, all foreign banks will have to disclose information about accounts held for US citizens or businesses, otherwise they will face financial penalties and sanctions on their operations in the US.

VAT on salary sacrifice schemes

Most employers offer their employees the option of sacrificing some of their salary entitlement in exchange for various employer-provided benefits. Following a recent tax case, there could now be a VAT complication.

The popularity of salary sacrifice is not surprising given the tax and national insurance contributions (NICs) savings that can be made. For example, salary might be sacrificed in return for childcare vouchers – saving both income tax and NICs. The range of benefits being offered is widening, and now includes pension contributions, staff meals, cycle-to-work schemes and bus travel.

HM Revenue & Customs (HMRC) previously accepted that the salary reduction was not consideration for the benefits received, and therefore output VAT was not due. However, following a decision by the European Court of Justice (ECJ), this treatment will change. The decision concerned AstraZeneca, whose employees sacrificed salary in exchange for shopping vouchers on which the company recovered input VAT. The ECJ decided that the salary sacrificed represented a supply, and that output VAT was therefore due.

Although the decision dates from 2010, HMRC will only be applying the change from the later of 1 January 2012 or, if the salary sacrifice was agreed before 28 July 2011, the date from when the current agreement ends – usually the date of the employee's annual salary/benefits review. From that date, where a benefit is liable to VAT then input VAT will be recoverable, but output VAT will be due on the higher of the amount of salary sacrificed and the value of the benefit. The change will affect cycle-to-work schemes, shopping vouchers, food and catering provided by employers (unless zero-rated), but not childcare vouchers because they are not subject to VAT.

The ECJ decision only applies where consideration is received in exchange for benefits, so it does not affect the treatment of benefits provided free to all employees, such as workplace gyms. The decision also does not alter the tax and NICs treatment of salary sacrifice schemes.

The big question for employers is who will bear the additional cost where output VAT is now going to be due – the employer or the employee? If the employer is not prepared to bear the cost, then schemes will need to be amended accordingly.

VAT is never easy, so please contact us if you need further advice.