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## news letter

### *What's in Store?*

Welcome to our autumn newsletter. Please give us a call if you have any questions on anything we have included.

eBay has been a huge success. But what are the tax implications of selling those unwanted items online? Read our article to find out.

For employers, terminating an employee's contract is never easy. The tax rules can sometimes add to the headache. See 'The End of the Road?' for clarification on the current position.

We report on the important changes to the BACS system being made at the end of the year. Is your business ready? We also include a summary of the most popular excuses your customers give for late payment of your invoices.

Finally, London is running out of phone numbers. From this autumn 020 3 will be added to 020 7 and 020 8 as a third prefix.



### Arctic Systems - A Winter's Tale...

From time to time a tax case hits the headlines. Such is the fate of Mr and Mrs Jones and their company Arctic Systems. The case is still progressing through the courts and is now on its way to the Court of Appeal. We would not normally bring you news without a happy (or unhappy) ending but wanted to update you on the story so far.

Mr and Mrs Jones owned and ran an IT company. They were the founder shareholders. He was a director and she was the company secretary (but not a director). There were no other employees. Mr Jones was responsible for earning all the income of the company whilst Mrs Jones dealt with the administration and worked on average a few hours each week. Mr Jones drew a very modest salary and the balance of the profit was paid out to the couple as dividends - each taking 50%.

The Revenue argued that the corporate structure whereby Mr Jones earned all of the income whilst a substantial part of the profits was paid to his wife as a dividend was an 'arrangement'. Therefore they had the power under the 'settlements' legislation to treat the dividends paid to Mrs Jones as belonging to Mr Jones for income tax purposes. As she was not a 40% taxpayer whilst he was, additional tax could be collected.

The case potentially has far reaching implications for many husband and wife companies but the position is far from clear leaving a whole host of questions unanswered. You can rest assured that we will be keeping a very close eye on developments. In the meantime please get in touch if there are any issues you would like to discuss with us now.

AUTUMN 2005

## eBay

eBay, the online auction website, has been hugely successful. At any one time it has well over 100 million registered users (10 million in the UK). It has been used increasingly by businesses with stock to shift or out of date equipment to unload. However until recently, only individuals were allowed to register with the inevitable result that many businesses registered and traded as individuals.

UK businesses can now officially join eBay and can also sign up for a PayPal account allowing them to send and receive credit and debit card payments online. Don't forget that anything sold on eBay should be reflected in the business books in the normal way.

Private sellers registering on eBay can sell unwanted items online. Are there tax considerations? ..... it all depends.

Sales of high value items such as paintings and antiques may incur capital gains tax (CGT) but generally only if the amount generated exceeds £6,000. Sets or collections of items may be liable to CGT if the total proceeds exceed £6,000.

There are so called 'power sellers' who buy goods specifically to sell them online and in some cases give up their day jobs to concentrate on this. These individuals are trading and should be paying tax on their profits.

Not surprisingly the Revenue is keen to catch up with these people and ensure they are complying with the law and paying any tax that is due. eBay has met with the Revenue to discuss the way forward. There are no specific measures yet in place to tackle the problem but it is likely that this will change.

## Service Charge Optional

The tax and national insurance (NI) treatment of tips, gratuities and service charges in the catering and related industries is notoriously complex. The Revenue is well aware that tax and NI is not always properly accounted for and has started to look into this matter. We summarise briefly the correct tax and NI treatment below.

Where the customer pays a tip direct to the employee the responsibility for dealing with that tip rests with the employee. They should declare the amounts received to the Revenue and usually the tax will be collected through the employee's PAYE code. The employer has no PAYE responsibility and there is no NI due.

If the employer leaves the tax position to the employee to sort out, it is prudent that this is reflected in the contract of employment, so that it is clear that the responsibility rests with the employee and not the employer.

However in many situations the employer will collect the tips, particularly where tips are added to the credit card bill or where the employer makes a service charge. If the employer organises the distribution of tips to staff, the employer has an obligation to operate PAYE on payment of the tips to the employees. In addition NI (both employers' and employees') is due. The plus about this route is that the tips can count towards the employer's requirement to pay the National Minimum Wage.

A *tronc* is a special arrangement used to pool and distribute tips. It is usually operated by a *tronc*master who is responsible for operating a PAYE system independently of the employer's scheme. NI will not be due so long as there is no contractual entitlement to a share of the tips and the employer does not determine, directly or indirectly, their allocation.

The Revenue has published a revised guide on the subject - booklet E24(2005). Please talk to us if you have any questions on anything we have raised in this article.

## Charity News

The Charity Commission is seeking to make life easier for charities by improving its online services. The Commission now allows organisations wishing to apply for registration as a charity to make their application via an online registration service.

All charities with income over £250,000 should have been issued with a password enabling them to register to use the new online services. This allows them to:

- update their entry in the register of charities so that the information available to the public is as up to date as it can be and
- complete and submit their annual return online.

Other longer term plans include looking at ways of allowing annual accounts to be completed and submitted online. In the meantime charities registering to use the online services are able to send annual accounts as an email attachment.

Further information is available on the Charity Commission website at [www.charity-commission.gov.uk](http://www.charity-commission.gov.uk)

In a further recent move, the charity regulators in England and Wales and Scotland have signed a new agreement to reduce overlap of regulations and to help achieve greater consistency in the charity sector across the UK.





## *The Cheque's in the Post*

The DTI estimates that at least 10,000 businesses fail each year because of late payment of their invoices. This will come as no surprise to those of you who regularly hear 'the cheque's in the post' as an excuse for late payment of an invoice. British businesses are now waiting an average of 61 days for payment.

It is a subject we have covered in previous newsletters but the problem doesn't go away. The Better Payment Practice Group has recently provided an undated list of the most common excuses for late payment and suggestions for dealing with them. Not rocket science we admit but a useful reminder nonetheless.

### **Excuse**

### **Action**

The director who signs the cheques is on holiday

Try to find out what provision has been made for paying salaries and other important bills. Often signed cheques will have been left. Stress to the person you are dealing with how important your account is.

The computer is down

Be persistent in your questioning and if there is a real problem suggest a manual cheque instead.

The cheque's in the post

Ask for postage details as a starting point.

Waiting for funds from a large customer

Ask who, and when payment is expected. Ask whether they can arrange credit with their bank on the security of the debt so that you can be paid.

We've lost your invoice

Offer to fax or email a copy immediately. Then if payment is not forthcoming you'll know it was a delaying tactic.

## *An End to VAT Reclaims on Employee Mileage?*

Customs are expected to issue revised guidance on procedures for reclaiming (input) VAT on employees' mileage expenses. This follows an ECJ ruling (European Commission vs United Kingdom) that businesses should not reclaim the VAT element of reimbursed employee mileage allowances because EU law says that businesses must have a valid VAT invoice to support the claim for input VAT recovery.

The system used by many UK businesses where employers pay employees for their business mileage using a mileage rate will have to change, although the detail and timescale has not yet been announced. Typically a business paying an employee 40p a mile for 100 miles, being £40, would recover input VAT of £1.79. This is the VAT element of the fuel costs of say 12p per mile.

Suggestions are that businesses may have to stop claiming back VAT on mileage payments altogether, or may have to introduce a system where the business itself pays for the fuel and employees repay the business for the private miles they travel. Fuel cards or business credit cards could be used but this would create additional administration for the business and potential benefit in kind issues for the employee.

Businesses that purchase fuel using fuel cards or company credit cards (where the business meets the cost of all fuel provided to an employee) and where the VAT fuel scale charges of between £35 and £68 per quarter apply to cover the private use, will not be affected by any changes.

There is an argument that says you should work on the basis that late payment of invoices unlike death and taxes is not inevitable.

For your part always make sure you:

- agree terms of payment in advance
- invoice promptly
- collect on time
- don't be embarrassed to discuss money!

## *London Gets New Phone Number!*

London is getting a new telephone number during the autumn of 2005. Some residential and business customers who put in a new line or apply for a new telephone number will be given an 020 3 prefix to meet the increasing demand.

However the new prefix will be an addition to the 020 7 and 020 8 prefixes so that existing London numbers will not change. Indeed new 020 7 and 020 8 numbers will continue to be issued throughout 2005 and beyond. However where an existing business applies for an additional line they may end up with two numbers with different prefixes. Some have complained that this is likely to be confusing.



## The End of the Road?

When an employment comes to an end it may be for a variety of reasons. Where it is not the employee's decision to go there is likely to be a financial package to soften the blow. The package may include salary, holiday pay, redundancy pay, payment in lieu of notice and compensation for loss of office.

Salary and holiday pay are taxable in full because they represent earnings and are taxable as employment income. Likewise certain benefits if they relate to the duties of the employment.

### The elusive £30,000 exemption

Other elements of the package may be eligible for a £30,000 tax exemption for termination payments so long as they are triggered by the termination and are not otherwise taxable.

So far so good, but the difficulty often lies in determining whether the £30,000 exemption is available or not. There is a growing body of case law on this point.

The critical question is whether the employee has the **right** under (or implied under) the terms and conditions of employment to the payment. If the answer is yes then the payment is taxable in full.

The 'right' need not be a contractual one and indeed any payment that the employee can 'reasonably expect' will be taxable in full. The exception to the rule is the right to redundancy pay both statutory and non-statutory. This is always treated as a termination payment. However care must be taken to ensure that any payment is a genuine redundancy payment and not, for example, a terminal bonus.

### Payments in lieu of notice (PILONs)

This is probably the most difficult area of all in determining the correct treatment. This is at least partly due to the fact that it is not a term recognised in tax law and means different things to different people.

We give you four scenarios where a payment is made in lieu of notice. See whether you think the payment would be taxable in full or eligible for the £30,000 exemption - answers at the end of the article.

- 1 Notice is given but not worked (often referred to as 'gardening leave') and salary for the period is paid as a lump sum.

- 2 The contract provides for PILONs to be provided as an alternative to notice. Would it make any difference if there was no contractual right but payment in lieu is customary?
- 3 The employer and employee agree at the time of termination that the employment is to be terminated without proper notice but a PILON will be made.
- 4 There are no contractual arrangements for a PILON. The employer terminates the contract and tenders a payment in lieu of proper notice.

As you can see this is something of a minefield. Add to that the fact that the national insurance treatment of the payments does not necessarily mirror the tax treatment and you realise the need for good professional advice. It is much easier to get the words and actions right before rather than after the event. If you need to terminate an employment speak to us sooner rather than later. After all the £30,000 exemption is valuable but don't assume it will automatically be available just by calling something a termination payment.



#### Answers

1&2 taxable in full, even if payment is just 'customary'.

3&4 so long as there is no existing agreement or understanding that a PILON would be made then such payments are eligible for the £30,000 exemption.

## Are you Ready for the Changes to BACS?

The current BACS (Bankers Automated Clearing Service) will be discontinued in December 2005. At the time of writing around one third of small businesses have yet to make plans to meet the deadline.

The replacement BACSTEL-IP is a completely new internet-based method for making submissions and collecting reports. The new system promises faster transactions than its predecessor. Banks and suppliers of BACS-approved software have already converted many

businesses but there are many that still need to upgrade their software and packages must be approved through the BACS approved software service (see [www.bacslimited.co.uk](http://www.bacslimited.co.uk)). There are more than 20 suppliers but your choice is likely to be heavily influenced by your business bank.

So if you don't want to be in the position of having to make wage and other payments by cheque or cash come the end of the year then you need to take action sooner rather than later.

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