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This issue:

- preparing for a no-deal Brexit – customs and tariffs;
- Getting the most out of personal tax returns;
- changes to accounting for leases – corporation tax;
- employment tax impacts of lease changes;
- tax and the mobile workforce;
- permanent establishment risk when expanding into new territories; and
- delays in processing R&D

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Preparing for a no-deal Brexit – customs and tariffs

If the UK leaves the EU without a deal on 31 October 2019, trade between the UK and EU would revert to World Trade Organisation (WTO) terms. This means the movement of goods between the UK and EU would be subject to customs duty and controls.

We set out below the top five steps businesses should take to prepare for a 'no deal' Brexit from a customs and tariffs perspective. Note these do not apply if you only import directly from the Republic of Ireland into Northern Ireland – the UK government has announced it will not apply customs duties or controls to goods crossing the land border.

1. Apply for an Economic Operator Registration and Identification (EORI) number if you don't have one

An EORI number is needed to import from and export to the EU after Brexit. In mid-August, HM Revenue & Customs (HMRC) announced that it would automatically allocate EORI numbers to businesses with a history of trading with the EU. However, some businesses may not have been issued with a number automatically.

If you wish to take responsibility for importing goods into an EU country (perhaps to save your customers from having to comply with customs formalities) you are also likely to need an EORI number issued by an EU country.

2. Apply to HMRC to use transitional simplified procedures (TSP) when importing into the UK

TSP allows your business to defer payment of customs duty and submission of import declarations when you import goods into the UK after Brexit.

You can only apply if your business is established in the UK, currently imports from the EU (TSP is not available if you only import from outside the EU) and meet certain other conditions.

For most goods ("standard" goods), under TSP you will only need to make a simplified import declaration in your own records when you import goods. You will then make a supplementary import declaration and pay any duty in the following calendar month (provided you have a duty deferment account, which you will also need to apply for).

3. Consider customs processes and how you will submit customs declarations

Customs declarations must be submitted to HMRC for each consignment imported to or exported from the UK. You will either need to use a customs agent to make these declarations, or acquire the special software and training needed to do this yourself.

4. Determine your commodity codes and the tariffs payable on your imports and exports
The classification of your products will determine what tariffs are paid when you import goods into the UK, or your goods are imported into the EU. It is vital that the goods are correctly classified, which means determining the correct ten digit commodity code.

The tariffs payable on import into the EU are determined under the EU's Common External Tariff. The UK government has announced a temporary import tariff that will apply when goods are imported into the UK under a 'no deal' Brexit. This eliminates or reduces duties on many goods in order to protect consumers.

5. Consider whether any customs reliefs or special procedures could help your business
You can apply for certain customs reliefs that could eliminate or mitigate the tariffs you face. These include:

- transit relief (for goods moving from the EU to the UK and then shipped back to the EU);
- customs warehousing (to avoid double taxation on goods bound for the EU);
- processing relief (for manufacturing in UK using EU components, where the finished product is exported to the EU); and
- temporary admission (for goods moving temporarily into the UK from the EU, or vice versa).

As well as these five points, businesses should also consider:

- changes to the VAT treatment of their cross-border trade;
- whether their international trade could be impacted by the loss of the EU's Free Trade Agreements (FTAs);
- whether their imports or exports need to comply with any licensing requirements; and
- which party in their supply chain will be responsible for import formalities and paying duties.

Getting the most out of personal tax returns

It's self-assessment tax return season once again and with penalties of up to 100%, the current penalty regime imposed by HMRC encourages individuals and their advisers to ensure tax returns are correct, and that the right level of tax is paid.

While the focus tends to be on ensuring all sources of income and gains are properly reported, it is really important that any interactions between advisers and clients at this time of year cover more than just the necessities. A good conversation can reveal a wealth of information that could potentially create tax savings now or in the future.

Identifying potential claims for tax relief
Perhaps a business invested in has gone into administration or shares are held in a company and these are now worth next to nothing. Maybe a loan was made to a business and it is now irrecoverable or a lender has called in a personal guarantee given in respect of a business loan. Where any investments are held that are now worth less than their original cost, realising these now can create losses for use against gains in the same year or at any time in the future. There are a variety of situations where a capital loss claim can be made on a tax return, banking a capital gains tax reduction of up to 28% in the future. The time limit for claiming a capital loss is four years from the end of the tax year in which the loss was made.

In some circumstances it is possible to convert capital losses into income tax losses and claim relief against income tax for the year of the loss and the previous one. Income tax relief can also be claimed on a tax return for interest costs on a loan taken out for the purpose of investing in, or for onward lending to, certain businesses. Time limits for claiming relief against income tax are much shorter so it's important to identify these as soon as possible. With income tax rates of up to 45%, claims like these can have a significant impact on an individual's tax liability. It is crucial to know that these types of claims and reliefs are available so they don't go unclaimed.

Other common tax saving measures
It is important to discuss other tax efficient measures that are widely available; for example income tax relief on pension contributions and gift aid donations, the use of ISAs and making the most of annual exemptions and personal allowances.

Planning ahead
Perhaps selling a property, a business or an investment is on the agenda for the future; where these thoughts are discussed at an early stage between an individual and their adviser, there is a good chance that any tax liability arising can be reduced or wiped out completely with some common and straightforward tax planning.

This year's tax return conversation is a good opportunity to discuss both current and future potential tax savings.

Changes to accounting for leases – corporation tax

A new accounting standard, IFRS 16, will change how companies account for leases and many companies will be required to capitalise operating lease assets. The new standard will have the greatest impact on businesses with large portfolios of short-leasehold property, such as retailers, pubs/ restaurant chains, or other sizable assets under operating leases.

Companies preparing accounts under IFRS or FRS 101 will be impacted for accounting periods starting after 1 January 2019, while companies who prepare accounts under FRS 102 will not be impacted until 2022 /2023.

Before the changes to the accounting standard there were three types of leases:

- **finance lease:** substantially all the risk and reward transfers to the lessee. Finance lease assets should be capitalised on the balance sheet while depreciation and finance charges are expensed through the Profit and Loss (P&L). Finance lease assets do not qualify for capital allowances, although the company should be entitled to tax relief as the depreciation and finance charges are expensed to the P&L;
- **operating lease:** significant risk and reward remains with the lessor. The lessee recognises the lease expense in the P&L with no balance sheet impact. Tax relief should be available on the P&L cost; and
- **hire purchase:** is a lease under which the company can acquire the legal ownership of the asset. The cost is capitalised on the balance sheet with depreciation and interest charges being expensed through the P&L. Capital allowances can be claimed on qualifying hire purchase assets, all depreciation is disallowed and interest expensed to the P&L should be deductible.

The new standard removes the distinction between finance and operating leases and, as a result, operating leases should now be capitalised. The accounting and tax treatments for hire purchase assets remain unchanged.

The main tax implication of the new standard is that companies may be required to recognise a deferred tax liability on transition and large corporates would need to consider the impact of the changes on the corporate interest restriction calculation. However, companies should review their reporting systems now to ensure they can differentiate between hire purchase assets and other leased assets to ensure the correct tax treatment.

Employment tax impacts of lease changes

Benefit in kind taxation

When an employer provides assets for employees to use personally, a Benefit in Kind (BIK) may arise. The employee is subject to income tax at the employee's marginal rate and class 1A National Insurance Contributions (NICs) are due by the employer. These benefits are reported annually on forms P11D which must be submitted to HMRC by 6 July following each tax year.

Where these assets are leased, usually the employer engages in the contracts directly with the provider, settling any leasing costs directly. Under the new accounting standards, employers may be tempted to move the leased contracts to the employees so that the company does not have to account for the leases on the balance sheet. This impacts the BIK treatment and may give rise to additional employee class 1 NICs. If the employer reimburses the lease charges to the employees, this is treated as salary reportable through the payroll.

It is important for the company to understand how benefits in kind should be reported before moving the leasing contracts, and consideration should be given to how the tax impact on the employees can be best managed.

Where income tax was previously due on a BIK reported on a form P11D, it may have been collected via an adjustment through the individual's PAYE code. If the benefits are now going to be reportable via the payroll because of the contract changes, then the tax code for the employee may need to be updated, which can be quite frustrating for the employee.

Impact on tax reliefs

Tax reliefs including Enterprise Investment Scheme (EIS) and Enterprise Management Incentives (EMI) may be affected in some cases by the accounting changes due to the specific criteria for qualifying companies, which include a limit on the balance sheet amounts.

Impact on market value for employment-related securities

Company valuations may also be impacted and while the equity valuation should remain unchanged, enterprise values may increase under IFRS 16. Companies issuing equity to employees may need to think further on how market value is identified for tax purposes.

Tax and the mobile workforce

Workplace agility has changed how and where employees carry out their duties with technology driving these opportunities. Cross border workers are more common and can even arise inadvertently under working from home policies. However, employers must be mindful of the tax implications for both their employees and the business where employees carry out duties in another country.

Even without a UK business presence, businesses with foreign employees visiting the UK may have a PAYE obligation from day one if they don't have a Short Term Business Visitors Arrangement. A host employer could be identified if the employee is on a client site, or the employee could be obliged to process UK payroll taxes on behalf of their employer.

Residency, along with foreign work days, can impact how much salary is processed through foreign and local payrolls and frequently employers can be left footing an employment tax liability in another jurisdiction when the same income is being taxed in the home country. Obtaining credits for foreign taxes paid can be cumbersome and lengthy. One solution in the UK is an "Appendix 5" arrangement where credit for foreign taxes paid can be obtained within the UK payroll process itself. In the absence of an Appendix 5 arrangement claims can be made for overpayment relief or through the self-assessment system.

EU co-ordination and reciprocal agreements allow for social security liabilities in just one country for mobile employees; employees can apply for a certificate to remain liable to social security in their home country which exempts them from foreign social security. If the UK leaves the EU without a deal, then current certificates for UK workers in the EU, EEA and Switzerland will remain valid until their end date. After this time, social security may be payable in both the UK and the foreign state. HMRC advises they are working to protect UK nationals working in EU member states by negotiating reciprocal agreements during the transition period.

Finally, a single employee can create a tax presence for a business who otherwise has no other operations in a particular country. Concluding contracts or even the use of a regular home office could create a permanent establishment in another country for tax purposes.

Permanent establishment risk when expanding into new territories

Since the Brexit referendum in June 2016, there has been an increased focus on how local businesses can compete and trade on a global scale. From our experience, many local companies have incorporated subsidiaries in the Republic of Ireland or elsewhere in the EU.

When your business is expanding overseas, you should be aware of the potential tax pitfalls or compliance requirements you may need to consider. Usually the place where a company is incorporated determines its tax residency and it is subject to corporate tax on its worldwide income in that jurisdiction.

However, where a UK resident company undertakes trade in an overseas jurisdiction it may create a permanent establishment or branch there and be liable to overseas corporation tax in respect of its activities in that jurisdiction.

A permanent establishment may arise either where there is a fixed place of business or where an agent acting on behalf of the company has and habitually exercises authority to do business on behalf of the company. This agency rule can prove quite troublesome, especially when a company deploys its sales team in the first instance to test the water in that market. Your local sales processes should be reviewed to ensure that no overseas permanent establishments arise.

Delays in processing Research and Development (R&D) credits

HMRC are currently experiencing significant delays in processing R&D Small and Medium-sized Enterprise (SME) tax credit claims and Research and Development Expenditure Credit (RDEC) claims. They had announced a recovery plan with a target date of 30 September 2019 to get through the backlog, with current statistics showing HMRC are currently processing SME R&D tax credit claims submitted in May 2019 and RDEC claims submitted as far back as December 2018.

Businesses have raised concerns that claims they submitted in late 2018 have still not been processed and this is having an impact on their resources to continue with R&D activities. Responding to these concerns, HMRC have provided some further details on their recovery plan. The plan includes having additional staff to process the R&D claims as well as moving the processing of the claims to colleagues in the customer services group.

HMRC guidance states that their approach for handling R&D SME tax credit claims would previously have been to deal with them within 28 days, where they would have either paid the payable tax credit or contacted the company regarding the claim. An SME making an R&D claim can expect all of the corporation tax issues to be dealt with by the R&D specialist unit. It should be noted that claims made by a larger company, or companies that form part of a group, should expect the processing of the claim to take slightly longer than the standard turnaround time.

So what does this mean for businesses considering making an R&D claim? With many companies having a September or December year end, an influx of further R&D claims is expected. Businesses should be proactive in engaging with their specialist R&D consultants now to ensure that their claims are submitted ahead of their corporation tax return submission deadline, thus ensuring the cash flow benefits of the incentives are attained as soon as possible.

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