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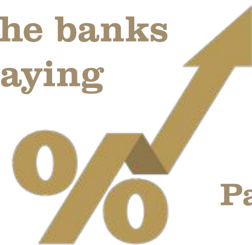

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# Navigating Uncertain Times

**As we come into Autumn, we can reflect on a Summer which saw a warm, dry May and June give way to one of the wettest Julys on record.**

Jonathan Ridley
Tax Partner (Editor)
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Our farming team were out in force at the Cumberland Show in June, which gave us a welcome opportunity to catch up with some familiar (and in some cases sunburnt!) faces. Ice cold beers and ice creams were the order of the day, all in stark contrast with Penrith Show in July where tea and scones took centre stage as we and our visitors took shelter from the torrential rain. The July rain 'up North' even managed to thwart England's attempt to regain the Ashes – the wait goes on.

Whilst unpredictable weather is a challenge that farmers are accustomed to facing, it has been far from the only area of uncertainty for our clients in 2023. Inflation has proven to be more stubborn than had been hoped, with the associated high input and labour costs continuing to place a strain on business cashflow. The Bank of England continue to raise the base rate in a bid to bring inflation back down to their target of 2%, but in doing so they are tightly squeezing those with borrowings on variable rates or on fixed term deals coming to an end.

A further Basic Payment Scheme (BPS) reduction this year, coupled with a lack of clarity over replacement subsidy schemes and the claiming process, does nothing to help cashflow or confidence, and is a source of frustration for many.

However, as always at Dodd & Co, we will be doing our best to help our clients navigate these uncertain times, and 'cash' is a bit of a theme in our Autumn newsletter. We look at strategies for managing cashflow, what you should be considering if you are fortunate enough to have some cash to invest, how this Government (or the next one!) might look to collect more cash from capital taxation, the end of tax credits, and some VAT tips.

We hope you find this newsletter useful, and as always if you have any questions do not hesitate to get in touch with your usual Dodd & Co contact. ■

# Capital Taxes - Ripe for Reform?

**As we hurtle towards another election, are we about to face any significant changes to capital taxes?**

If you have been following any of the Conservative party chatter, you won't have missed the increasing clamour from Tory politicians for the abolition of Inheritance Tax (IHT). Perhaps changing economic conditions and an upcoming election will make all politicians weigh up whether existing capital taxes are fit for purpose?

After all, Capital Gains Tax (CGT) has existed since 1965 and IHT since 1986. Tax rates and allowances have been tinkered with, but capital taxes have remained broadly static for forty years.

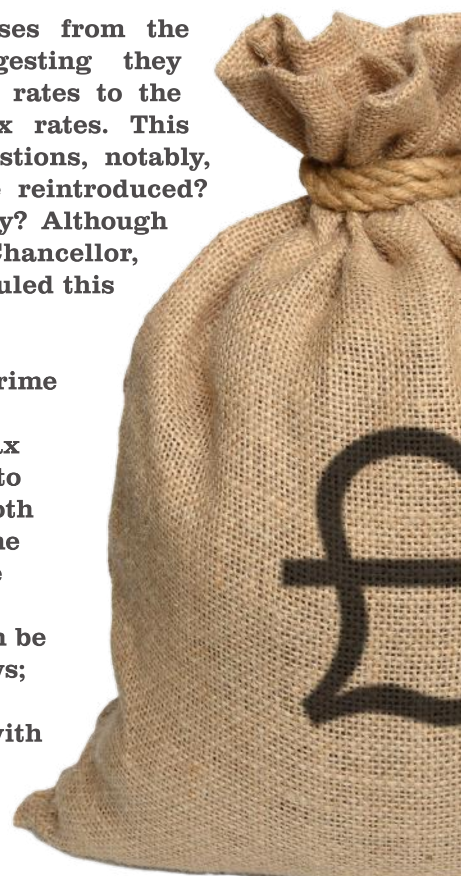
The gradual eroding of the value of the IHT nil rate band now means many more people pay IHT. It is also worth noting that if you have significant wealth, it is largely a choice as to whether to pay IHT. After all, problem assets can be disposed of in lifetime, perhaps with a CGT charge, whilst assets qualifying for relief can be kept until death. IHT is probably not collecting tax from the intended people now and is perhaps ripe for reform.

Obviously, CGT is also tied up with IHT, the tax-free uplift to market value on death for CGT purposes being one example.

It is hard to see why someone selling a farm with a £1million gain, giving the money to their daughter, and then dying the following day is landed with a CGT charge of £200,000 (assuming no reliefs), and then the resulting sum facing a 40% IHT charge on death, another £320,000. This leads to tax of £520,000 or 52%.

Contrast this with leaving the farm to the daughter on death, no IHT due to Agricultural Property Relief; a sale the following day would result in no CGT, so the daughter gets the full £1 million, in her pocket at an effective tax rate of 0%!

It is hard to defend this difference and to a large extent it often clouds commercial logic to sell or transfer assets earlier.



We have heard noises from the Labour Party suggesting they might increase CGT rates to the same as income tax rates. This raises plenty of questions, notably, would indexation be reintroduced? Would rebasing apply? Although Labour's shadow Chancellor, Rachel Reeves, has ruled this out.

In fact, our current Prime Minister had already asked the Office of Tax Simplification (OTS) to suggest changes to both IHT and CGT whilst he was Chancellor of the Exchequer. The OTS' recommendations can be summarised as follows;

For CGT, align with income tax rates, remove the CGT rebasing on death,

reintroduce indexation or rebase assets to a more recent date.

For IHT, the CGT uplift on death was on the list of things to remove, along with a change to the trading/investment business test, increasing the trade element from more than 50% to more than 80%.

Perhaps a more radical approach was proposed by the All Party Parliamentary Group for Intergenerational Fairness (yes, there is such a thing!)

This Group recognised the low tax take from IHT and suggested scrapping it. Yes, that approach is back where we started this piece, with politicians calling for it ahead of an election. It proposed CGT at lower rates, perhaps 10% or 20% but levied on almost all capital disposals, with either the lower rate applying to business transfers or holdover relief still being maintained. In the latter case, tax is only paid when the assets are sold and not reinvested in business assets.

So, is the climate for fundamental changes to capital taxes now more favourable than it has been in the last 30 years? In my opinion, yes, but will any politicians be brave enough to have a radical rethink of capital taxes policy, delivering something that is fairer but potentially raises more tax revenue?

We might get a hint of future Conservative tax policy at the Autumn statement on 22 November. We should also get an idea of Labour's tax policies in advance of the next general election, so it will be interesting to see whether any of them pay any attention to the reports generated over the last few years.

# Revenue is Vanity, Profit is Sanity, but Cash is King...

**After a turbulent few years, are we starting to see things levelling off? Perhaps. But inflation remains high, interest rates continue rising, and income is starting to be squeezed.**

For many, the 22/23 year may appear better than ever. High milk and livestock prices have been able to cover, and exceed, increases in input prices, resulting in record profits for some. However, these profits mean there may be larger than usual tax bills on the horizon. And despite the accounts looking good, you may worry how you will pay this additional tax.

Profit does not equate to cash. From an accounting perspective, stock values and depreciation affect profit but not cash, while asset financing and loans affect cash but not profit. And in what is a very seasonal industry, any month can look entirely different to the next. As I write this, I hope that most readers will have received the first 50% of their BPS payment (albeit down on last year). Similarly, Arla customers should see their half-year payment in September. Both of these measures are designed to help with cashflow.

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However, with BPS reductions and now falling milk and auction prices, you will need to balance your income against inputs and be conscious of timing. You will also need to consider changes to your debt obligations. High inflation has brought with it a series of base rate rises. For those with debt on variable rates, or coming to the end of fixed terms, repayments may increase significantly. Ultra-low rates are likely to be a thing of the past, making it more important than ever to have an open conversation with your lending providers, and to think carefully about how you will fund future projects. As a team we are experienced in cashflow planning if this is something you need to complete.

All these factors result in a perfect storm for cashflow and tax planning, and many of our clients will feel a real need to plan ahead. With Cloud Accounting packages we can now review your real-time information ahead of the year end, and provide you with an insight into where you are headed.

If you feel in any doubt, your Dodd and Co team are here to help.

## Q. I am thinking of purchasing a new vehicle for my business – what do I need to consider?

**A.** The VAT rules for reclaiming VAT on vehicles can be confusing and will depend upon the type and specification of the vehicle. HMRC does not allow VAT recovery on cars (unless they are 100% used for business such as a pool car; this is a difficult criterion to meet). VAT can be reclaimed in full on commercial vehicles provided there is only very limited private use (perhaps less than 5%, or a handful of trips a year). If private use is any greater than that, then some VAT should be disallowed.

## Q. But what is classed as commercial, there are so many variations?

**A.** There are! A van is a commercial vehicle regardless of shape or size. A double cab pick-up can be classed as a commercial vehicle when capable of carrying a 1 tonne payload. A car-derived van on the other hand will look like a car from the outside but will function like a van on the inside – there must not be any rear seats or seat fixings, any side windows must be opaque and fixed, and there must be a payload area with floor panel in the rear.

## Q. The dealer tells me that VAT is recoverable?

**A.** That might be so, however the devil is in the detail so it's always worth checking before committing to the purchase.

Contact Jo Coleby, VAT Technical Manager jo.coleby@doddaccountants.co.uk

## Q. Will I receive a penalty if I file my repayment VAT return late?

**A.** On 1 January 2023, HMRC introduced two new penalty schemes – one for late filing and one for overdue payment. Before 1 January 2023, if a repayment return was filed late HMRC could not issue a default surcharge (as default surcharges could only be charged on amounts due to HMRC). As of 1 January 2023, the late filing of a repayment return will incur a penalty point. Fines of £200 per late return will then be issued by HMRC upon reaching your penalty point threshold.

## Q. I am considering using my land to generate new diversified income, will there be any VAT implications?

**A.** With an increase in uncertainty and financial pressure on farmers, innovation and diversification has never been so important. Farming businesses intending to use their land to generate new diversified income will need to identify the nature and the VAT treatment of the supplies it will make and consider the impact on future VAT recovery. Some common examples of diversification include furnished holiday lettings, milk vending machines, campsites, renewable energy, and letting out a cottage on the farm.

Whilst many of these may generate further taxable income, the receipt of any exempt income (such as the income from letting out a cottage as someone's main residence) could lead to a restriction in the amount of VAT reclaimable. This is a particularly important consideration when, for example, a residential property is under renovation as it may not be possible to automatically reclaim all the VAT on those costs.

Always explore VAT implications before starting your new diversification journey.

By Jo Coleby

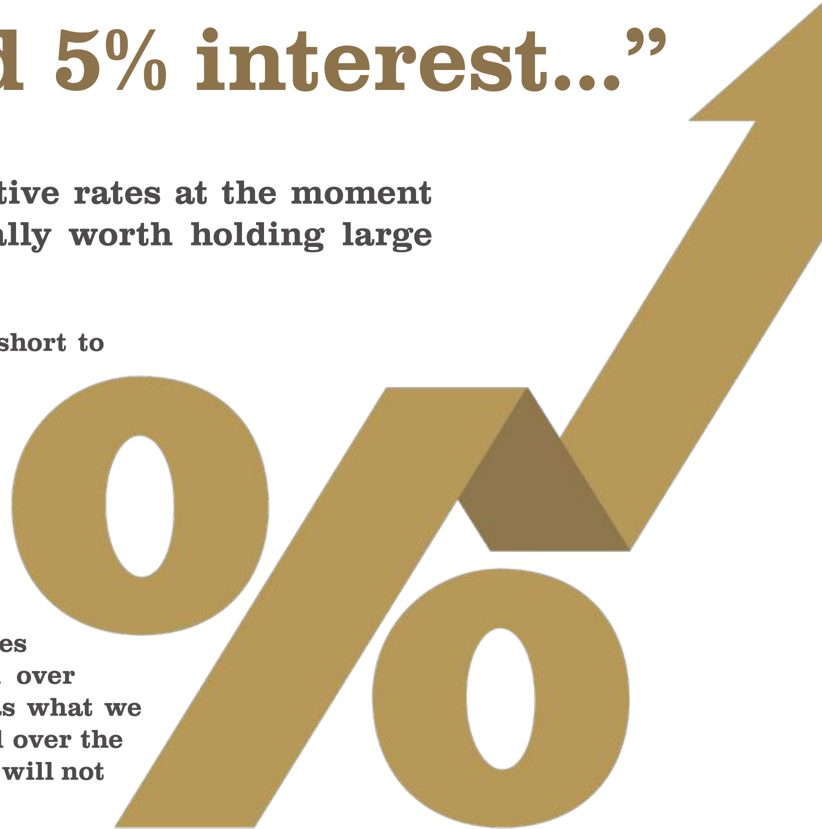
## Q. I have recently opted to tax my land but have not received anything in writing from HMRC, should I be worried?

**A.** From 1 February 2023, HMRC stopped acknowledging option to tax notifications. Opting to tax is a two-stage process – firstly making the decision to opt to tax, and secondly making the correct notification to HMRC within 30 days of the decision being made. Permission to opt is not normally needed. Making a valid option to tax is critical in most commercial transactions. It is therefore imperative that once submitted, this signed document (and related information) is retained alongside the automated email response from HMRC (this will act as HMRC acknowledgement).

## Q. Is this still the case if the option to tax was not submitted within 30 days?

**A.** No. HMRC may require additional information and written confirmations before accepting the effective date of the option to tax. In this case, we would expect HMRC to confirm the option to tax in writing.

# "But Sarah, the banks are paying around 5% interest..."

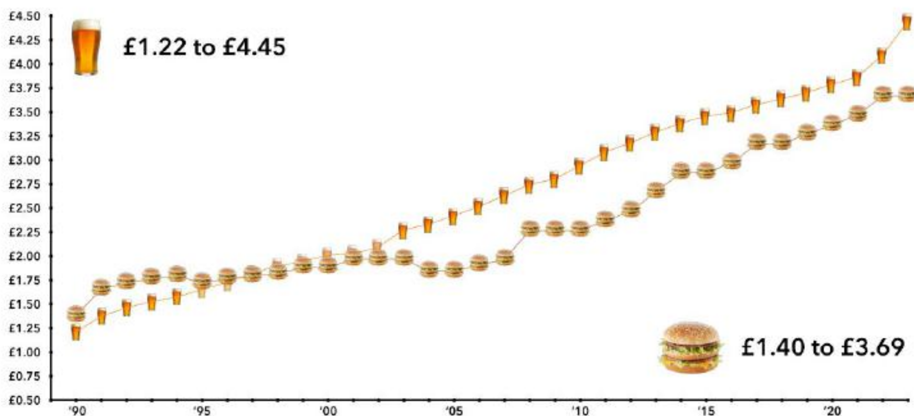


**Whilst banks are paying very attractive rates at the moment (key word being 'moment'), is it really worth holding large sums of money in cash at present?**

The answer, if monies are not required in the short to medium term i.e., less than 5 years, would be no.

If monies are required in the short to medium term i.e., less than 5 years, holding cash is a sensible route to ensure capital is protected from market fluctuations and not at risk of falling.

High street banks are paying over 5% interest rates at present, the highest rates we have seen in over 15 years. However, money is only as valuable as what we can purchase with it and whilst inflation is well over the government target of 2%, what we can buy today, will not be the same as what we can buy in 5 years' time.




The Bank of England had no other choice but to raise rates to try and tackle the fastest soaring inflation we have seen in some time, and to help the economy recover.

Inflation is by definition the decrease in the purchasing power of money, and is reflected in the cost of goods and services we buy on a regular basis.

As an example, in January 2023 the inflation rate was 10.1%. If a cash account is paying an interest rate of 5%, the 5.1% difference is the rate at which the money is losing its real value and the purchasing power it has. So, if you had large sums of money in cash, you can see the inflationary risk of

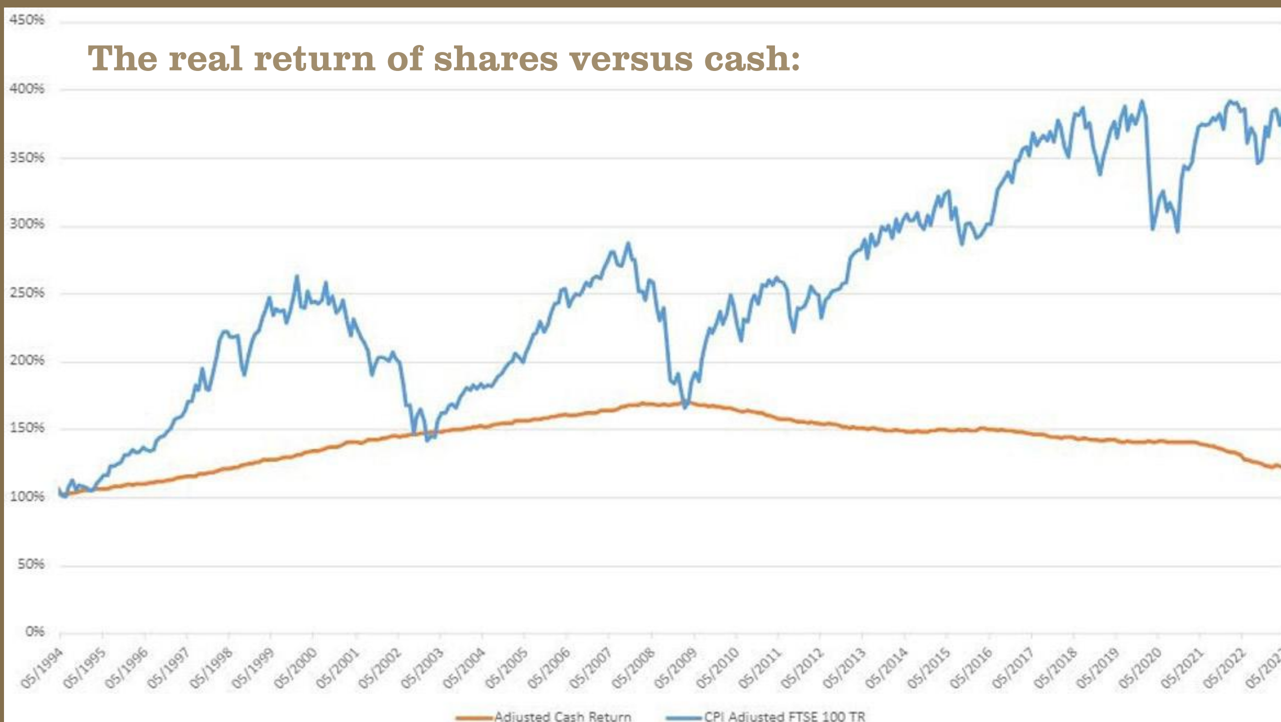
holding this over the medium to longer term.

In addition, interest rates will likely peak in the near future, meaning the rate you are getting now, will not be available once inflation is back under control.

## "So Sarah, what can I do?"

Depending on your wider circumstances, you could look to invest part of your cash holding to try and maintain the future purchasing power of the money, ensuring enough is retained as an emergency fund. This would include contributing monies into a carefully picked account based on circumstances, goals and tax position, and using an investment strategy based on your risk views and investment objectives. We would ensure you were in a diverse strategy across various asset classes, inclusive of shares, bonds and other assets, to help spread the risk.

Of course, there is no guarantee that investing this way in stocks and shares can do better than cash, as unfortunately we do not have a crystal ball (I wish). However, past performance has shown that over the longer term, markets do consistently outperform cash.




Source: ASPIM and Bloomberg, 05/1994 to 05/2023

If you would like to know more about making your cash work harder for you, where a tailored financial plan can be designed, please do not hesitate to get in contact, as we would love to help make your goals and dreams a reality.

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# Bringing the Curtain Down on Tax Credits

Working Tax Credits and Child Tax Credits were first introduced in April 2003 as a means tested benefit to provide financial help to those eligible to claim. However, after 20 years the current system is coming to an end with a potential move across to Universal Credit as the alternative.

Families or individuals who are currently receiving tax credits should soon receive a migration letter explaining the change and what they need to do if they intend to apply to move across to Universal Credit. It is important to apply before the deadline in the letter otherwise the tax credits payments will stop but there will not then be the opportunity to take advantage of the migration across.

There are independent benefits calculators online that can be used to check how your payments will be affected and what they may change to under Universal Credit instead of tax credits. https://www.gov.uk/benefits-calculators

Sometimes claimants will be entitled to the same amount they received from their previous benefits, and sometimes they will be eligible for more or less under Universal Credit. If the amount you are entitled to on Universal Credit is less, a top up amount is available. This is known as Transitional Protection. You can get the Transitional Protection if you have received a Migration Notice letter from DWP and you make a claim by the deadline date on your letter.

Another significant difference is that if you claimed tax credits in the past it did not matter if you had savings in excess of £16,000 providing the other qualifying conditions were met. However, this can prevent a successful claim for Universal Credit. It has been announced that for one year only, having savings over £16,000 will be disregarded when the migration across takes place, but it will then be necessary for claimants to review their savings on a timely basis, as after 12 months the Universal Credit payments will stop if you still have savings of over £16,000.

If you have any questions concerning the end of tax credits and the migration across to Universal Credit please get in touch.

By Rachel Coates

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