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NEWSLETTER

Lockdown

Coronavirus restrictions are now expected to be relaxed on 19 July and provided that does not change, I shall re-open my office to visitors. I shall also follow government guidance on whether masks should be worn.

VAT

A business has to register for VAT as soon as sales exceed £85,000 in any consecutive twelve months. The important point here is that it is <u>any</u> twelve month period, not just the business's accounting year, as people often assume. When sales are getting close to the threshold, therefore, they need to be checked at the end of every month.

The Adjudicator

The Adjudicator's Office was set up more than 20 years ago as an independent body to consider complaints against what was then the Inland Revenue, now HMRC. Anyone who has complained to HMRC and is not satisfied with their response can refer the matter to the Adjudicator, who can recommend redress, including compensatory payments, if the complaint his upheld.

In the early years, I was impressed by their ability to impartially consider a complaint, reach the correct conclusion and make appropriate recommendations. Since then, however, their standards have fallen considerably, as illustrated by their behaviour in a recent complaint I made, after issuing their initial report.

1. I sent them a letter listing 9 brief points, in the same order as the report, which were factually incorrect or required further clarification. Their 4 page reply considered those points in a completely random order, different to both the original report and my letter, making it very difficult to follow or even to tell whether they had addressed every point. I later requested that they apologise for such a badly written letter.

2. They replied in the all-too-common modern form of non-apology, saying sorry for how I felt rather than sorry for what they had done. The letter also included an inaccurate summary of my initial complaint, including something which I had definitely not complained about.

3. I wrote back and asked them to provide a proper apology and withdraw their statement that I had complained about something which I had not. Their reply claimed that, because they were not directly quoting my words, it did not matter that what they said had a different meaning to what I had complained about! Their second attempt at an apology followed the same format as the first, so was still unsatisfactory.

4. My next request for a correction and apology was addressed directly to the Adjudicator herself, Helen Megarry, but I have no evidence that she read it and the reply came from someone else. All I have received is another evasive reply.

5. I have written back with my criticisms, but I do not expect a reply. It seems that they are too arrogant to ever admit to any mistakes, misunderstandings or misquotes. Often they do not even bother to sign their letters. As they no longer act with honesty and integrity, I have lost all faith in their ability to properly scrutinise the actions of HMRC. When their first reaction to criticism is to become defensive and pretend that they did nothing wrong, there is really no difference between the Adjudicator and HMRC.

Subcontractors

Subcontractors who work in the building industry suffer a 20% tax deduction on their earnings, so are used to claiming a tax refund when their tax returns are filed. That may not be the case for 2020/21, if the subcontractor had time off because of coronavirus and claimed the SEISS grants from the government. Those grants are taxable, so total earnings may be almost as much as before, but tax deductions will be much lower. That could mean that the subcontractor gets a much smaller refund than usual, or even has tax to pay.

Pass it on

Please feel free to copy or pass on this newsletter to friends and business acquaintances. Anyone who would like to be added to the mailing list should e-mail me at the address above.

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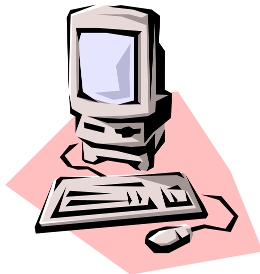

Mortgage Applications

Before granting a loan, mortgage lenders want to see evidence that the borrower will have sufficient income to be able to meet the monthly repayments. For employed people, they will accept payslips and P60s but, for the self-employed, things are not so straightforward. Lenders generally calculate an applicant's income as the average profit for the last three years, but that apparently simple calculation can cause confusion and difficulty on all sides.

1. Borrowers often assume that their profit is the same as the "wage" which they draw from the business each week or month to live on. That is not correct. Profit is the business income minus the business expenses, which is something completely different in all but the simplest businesses. For instance, when a business is starting up, customers may take some time to pay, so the "wage" the proprietor can take will be lower than the profit, because not all of the income is yet in the bank. Conversely, many businesses in the last year will have taken bouncebank loans, allowing owners to maintain the same level of drawings, although profit is lower.

2. Lenders have lost sight of how to properly assess the profits of a business. In the past, they would use the accounts which I produce, which are always prepared to show a "true and fair" view of the profit. That profit is then adjusted on the tax return to claim all of the available tax allowances, producing the lowest possible profit and tax liability.

   The taxable profit can be substantially different to the accounts profit, mainly because of the treatment of purchases of equipment and machinery. In the accounts which I prepare, those items are written off over five years, to reflect the time they will be in use in the business before they wear out and need to be replaced. For tax purposes, on the other hand, the whole of the cost can be written off in the year of purchase, leaving a much lower profit for that year.

   Imagine a small business with a steady income, which spends £15,000 on new equipment every five years. The accounts show a profit of £30,000 every year and the owner applies for a mortgage where that level of income is needed for approval. The lender requests the last three years' tax assessments but, because new equipment was purchased in the second year, the profits for tax purposes are £33,000, £18,000 and £33,000. Because the average of those figures is only £28,000 and they fluctuate so much, the application fails.

   It does not take an accountant to see that this is a ridiculous state of affairs, and that it would be much more reasonable to use the profit from the accounts, which is computed on a consistent basis and not distorted by the vagaries of the tax system. All of the lenders, though, have adopted the dogmatic view that only the taxable profit can be the "right" profit. That attitude seems to have been born of an ignorance of the tax system at the top of those organisations, or an unwillingness to give their staff proper training in understanding a profit and loss account and balance sheet. A proper review of the accounts could also provide other information valuable to the lender, such as whether the applicant is consistently spending more than the profit, thus getting deeper and deeper into debt.

   Furthermore, the lenders do not seem to appreciate the scope for applicants to manipulate the tax return figures to improve the chances of the mortgage being approved. For instance, a self employed applicant who has spent a lot on equipment could initially submit a return without claiming the available tax allowances, in order to show a higher income. After the mortgage has been approved, the tax return can be amended to claim the allowances and reduce the tax bill. Which version of the return then shows the "right" profit?

3. Accountants can be left in an impossible situation, unable to satisfy the needs of both client and lender. Clients are usually keen to have the lowest possible tax bill, so expect the accountant to claim all available tax allowances, leaving a low profit. If the client applies for a mortgage a year or two later, that low profit could lead to a refusal, but it is then too late to amend the tax return.