Demystifying tax – making the most of allowances, reliefs and business finance

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Wesleyan Bank acts as a broker and a lender

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Businesses are set to bounce back after the financial challenges caused by the pandemic. According to the Bank of England[1], the UK economy is expected to expand by 7.25% in 2021 – the fastest rate of growth in more than 70 years.

The rebound is predicted because of the resilience and adaptability shown by businesses during the COVID-19 crisis which now puts them in a strong position to take advantage of growing customer demand. Announcements at this year's Budget underpin this optimism with new tax initiatives launched to reinvigorate the economy, rebuild cash flow and support investment.

In this guide, Wesleyan Bank aims to demystify tax benefits and reliefs by addressing the confusion around which schemes are available, their qualifying criteria and how alternative finance can also enable businesses to flourish in a post-pandemic environment.

1 **BBC News - UK economy set to grow at fastest rate in more than 70 years**

Tax relief schemes

Are you taking advantage of new tax incentives?

To drive growth the Chancellor, Rishi Sunak, has launched several new and extended tax incentives to support more longstanding tax allowances and reliefs.

One of the headline schemes introduced in the 2021 Budget is the "super-deduction". This incentive is designed to help businesses generate investment while being given the opportunity to optimise tax and cash flow savings. The scheme is already attracting keen interest as a survey by Make UK, the manufacturers' organisation, found that more than a fifth (22%) of members would bring forward or increase investment as a direct response to the move.[2]

The new super-deduction scheme means companies can claim a 130% deduction from their corporation tax (CT) bill for investment in 'plant and machinery' made between 1 April 2021 and 31 March 2023. Using the scheme means a deduction in CT of £24.70 is made for every £100 invested compared with the previous rate of £3.43 (or 18%) in every £100.

HMRC has agreed an extensive list of qualifying 'plant and machinery' which covers items such as:

- Production machinery
- Factory tools
- Computer equipment
- IT Software
- Furniture
- Commercial vehicles (not cars)

Where items fall outside of the main 'plant and machinery' list, they may qualify for the 'Special Rate' (SR) allowance. This gives relief at 50% of the qualifying cost in the first year with the balance going into the normal special rate pool to be written down at the usual 6% rate in future years.

Items included under the SR include long-life assets and items which are integral to a building such as:

- Air-conditioning and air-cooling systems
- Hot and cold water systems
- Electrical systems, including lighting systems
- External solar shading
- Lifts, escalators and moving walkways
- Space and water heating systems

There are some exceptions within these new allowances, such as leased items or integral features and plant and machinery installed in a building which is let. Second-hand items will continue to attract an 18% allowance.

There is no limit of capital investment under the super-deduction or SR allowance, although relief is capped at 50% and the assets must be tracked until they are disposed of, so the correct value and balancing charge is applied.

Super-deduction tax – not so super?

Analysis of the super-deduction proposals have left commentators questioning whether some of the actual benefits of the scheme might be limited.

Stuart Adam, a senior research economist of the Institute for Fiscal Studies has said, "It looks like the size of the super-deduction has been chosen precisely to offset the effect of the corporation tax rate rise. The tax rate is going up by 30%, it is going to be 130% of what it is. And so by giving a super-deduction of 130% of investment, it turns out that those two effects offset each other almost exactly."[3]

The Treasury has issued a factsheet to help businesses understand more about super-deduction allowances and see examples of the savings you could make which can be viewed on the **HM Treasury website**.

2 **Process Engineering – Make UK survey predicts 'superdeduction' investment boost for manufacturers**

3 **SKY News – Why Rishi Sunak's 'super deduction' isn't as great as it sounds**

Make the most of established taxable allowances

You can reduce your tax bill by leveraging the available capital allowances, many of which can be claimed over one or several years on most assets you buy for use within the business. While your accountant can advise on specific items, as general guidance capital allowances cover:

- Equipment
- Machinery
- Business vehicles such as cars, vans, lorries etc.

There are several well-established allowances which businesses are already able to take advantage of in reducing tax expenditure.

Businesses that have incurred plant and machinery expenditure this year, but too soon to qualify for the super-deduction tax relief (i.e. before 1 April 2021), could gain some benefit from the Annual Investment Allowance (AIA). The AIA was first introduced in 2008 and since then many businesses have taken advantage of the 100% tax deduction available for expenditure on fixtures, fittings, plant and machinery.

The scheme has been given a boost following the temporary rise from £200,000 to £1m of allowable expenditure which was due to end in December 2020, but has subsequently been extended until 1 January 2022.

The main AIA categories are:

- Office equipment including computer hardware and certain types of software, and office furniture
- Parts of a building referred to as integral features
- Certain fixtures, such as air conditioning, fitted kitchens, or bathroom fittings
- Lorries or vans used for moving purposes
- Machines used for business purposes
- Agricultural machinery including tractors
- Machines used for providing entertainment, such as arcade game machines.

If you are looking at purchasing specific items which fall under the criteria matching the SR rate and you are spending up to £1m, the AIA may be more attractive as it provides 100% rather than the SR rate of 50%. Your financial advisor will be able clarify which scheme is best for your circumstances.

Offset the tax and spread the cost

To capitalise on emerging revenue opportunities and kickstart their recovery, many businesses are planning to purchase specialist equipment and technology or refurbish their existing premises. But this can be cost prohibitive if they elect to pay for all new investments upfront in one lump sum. In addition to receiving up to 100% tax relief from the AIA, you may also wish to consider spreading the cost over a term of up to five years with an asset finance loan.

Tailored asset finance solutions from traditional high street lenders or alternative finance providers enable businesses to spread the cost of new investments over time to support their growth aspirations. As well as allowing SMEs to retain cash in their business, flexible asset finance loans may make it possible to achieve a quicker return on investment.

Building for the future with research and development

Research & Development (R&D) tax credit has been available to SMEs for over 20 years, but despite this it could rank as one of the most misunderstood corporation tax reliefs. Its name leads many to believe that it only applies to those businesses working in science. However, it is actually intended to reward and incentivise innovation across any sector.

With the Government setting a target of R&D investment being 2.4% of GDP by 2027, more companies need to join around 60,000 SMEs who according HMRC statistics shared in £5.3bn of tax relief during the last year.[4] Some 66% of claims came from the manufacturing, professional, scientific, technical and information and communication sectors taking advantage of the 230% they can claim on their qualifying R&D costs. Loss-making companies can in certain circumstances surrender their losses in return for a payable tax credit.

To be recognised as an SME for R&D tax credit purposes a business must have fewer than 500 employees and a turnover under £175m, which allows for 33% of costs spent of qualifying R&D can be claimed back as tax relief. If a company is outside of this criteria it must claim under the large company scheme.[5]

To make a claim, HMRC defines the work has having a technological advance where a new product or service, or an enhancement to an existing solution, has been created or includes something which is new or improved. It can also cover projects which have not been successful because the hoped for outcome is beyond any current understanding or expertise.

So, in terms of sectors and projects this may include:

- Manufacturing – developing prototypes; material testing; product enhancements; and improving processes
- Engineering – for sectors including building; automotive; electrical; environmental; and transportation. It may involve creating new designs, or the use of new materials, improving the design of machinery or components or streamlining through automation
- Architecture and construction - designing or building non-typical structures, retrofitting safety features to meet new regulations; and designing for improved energy consumption; water conservation; and helping to meet other environmental considerations
- Software development- advancing Artificial Intelligence (AI) systems; developing using untested methodologies; creating more efficient algorithms; game design; and firmware development.

In making a claim for the R&D credit is it important to have an accurate record of costs incurred in relation to the specific project which should comprise:

- Staff salaries
- Sub-contractor costs
- Contract workers
- Consumables
- Software licence costs

What you cannot include are items such as:

- Normal operating costs
- Recruitment costs event for those working in R&D
- Staff costs of those not directly involved in the specific R&D project
- Costs involved for items used in production

Claims, supported by the relevant technical and financial information, must be made within two years of the work. An SME can claim up to £20,000 plus 300% of its total Pay as you Earn (PAYE) and National Insurance Contributions (NICs) liability for the period.

HMRC has produced a comprehensive guide to R&D relief which is available online. Your accountant or an R&D tax specialist will also be able to guide you on whether you qualify to make a claim.

4 **HM Revenue & Customs – Research and Development Tax Credits Statistics September 2020**

5 **New Civil Engineer – Many civil engineering firms are missing out on vital tax-free innovation funding**

Open up the Patent Box

One relief which can bring benefits for some organisations is the UK Patent Box which is available to companies who generate profits from their own patented inventions or their intellectual property (IP).

To qualify companies must own, or exclusively license, the patent/IP or have the responsibly for their development. A claim can also be made if a company holds exclusive UK rights for a patent which has been developed by someone else, providing that they have the rights to develop and exploit the patented invention.

The relief, although separate, can be combined with the R&D tax credit and benefit those active in product or service development.

Business tax

Corporation tax hike to take effect in 2023

Payable by limited companies who must have registered with HMRC within three months of starting to trade, corporation tax (CT) is paid on trading (gross) profits made from sales to customers in the UK and overseas, investment profits and capital gains from the sale of property or investments.

Businesses must ensure that their CT calculation is accurate and filed on time. This must be done within nine months of your end of financial year and tax due paid at nine months and one day of that year-end. Any late payments attract interest.

The current CT rate is 19%, however it is set to rise on to 25% on 1 April 2023 as the government aims to generate an extra £17bn of revenue by 2025/26.

To lessen the impact, companies with profits of not more than £50,000 will stay at the current rate and there will be a tapering of the rate for companies with profits falling between £50,000 and £250,00. The new higher 25% rate will only be applied to businesses with taxable profits in excess of £250,000.

Corporation tax finance

Cash is king and there are times when most businesses will feel the pinch of an upcoming tax bill. Covering your corporation tax bill with an unsecured loan that can be paid back over a 12 month period is a convenient way to spread the cost of the tax owed. It could enable you to free-up funds to be funnelled back into the most profitable areas of your business, helping to increase your bottom line over the year.

All systems go for Making Tax Digital

The pandemic has increased the digitalisation of business life. One government initiative which had started a phased rollout over the coming years is the launch of 'Making Tax Digital' (MTD). It intends to make the whole process of tax returns and payment quicker and easier.

MTD is a digital tax account. As well as being the way to submit returns and paying tax bills, it gives individuals and businesses real-time information at any point in the financial year about their tax position, providing month-by-month comparisons or future liability predictions. MTD will also reduce errors and provides a digital audit trail should any issues arise.

HMRC will be carefully monitoring compliance and has recently hired 1,000 new investigators who are part of a nationwide clampdown.

VAT was the first to move and for companies with a taxable turnover over £85,000 MTD is already a reality as returns can no longer be submitted via HMRC's online gateway or spreadsheet file. All returns must be completed using approved accounting software with an application programming interface (API).

The next stage means that by April 2022 all those under that threshold (£85,000) will have to submit their returns digitally.

In summary the key dates for MTD are:

- April 2022: VAT-registered businesses with a taxable turnover below £85,000. It is already implemented for those with a taxable turnover above £85,000
- April 2023: Self-employed businesses and landlords income tax with annual income above £10,000 with the first return due in the fourth month of your accounting period, followed by a need to file every three months making a total of five returns a year. The initial plan allows for voluntarily payments throughout the year to be made on account
- April 2024: Companies pilot scheme for corporation tax submissions with all businesses using by April 2026.

To meet these deadlines and to prevent issues arising it is advised that you talk to your financial advisors and agree on when is the right time is for you to implement MTD.

Is your software MTD compliant?

You may have to undertake a review to determine whether an investment in new IT or accounting software is needed so you can comply with MTD. To help, HMRC has published on its website a comprehensive list of the recognised software you will need to file under MTD.

If you do have to make an investment it may be possible to spread the cost with an unsecured loan. Specialist commercial lenders can offer flexible finance plans (typically from one to five years) covering hardware, software including other equipment upgrades and additional licences midway through a contract term, without any increase to your monthly repayments.

VAT

Government support packages have been a vital lifeline to ease the pressure on SMEs' finances during the pandemic. However, the decision to allow VAT payments to be deferred until 2022 will only offer temporary respite from liabilities which ultimately will have to be repaid in full.

Businesses who have opted into the Government's Time to Pay arrangement can split their VAT bill into smaller, interest-free payments over the course of 11 months. This means that VAT liabilities due between 20 March and 30 June 2021 do not need to be paid in full until the end of March 2022.

Just because you can put off paying your VAT bill doesn't mean you should. Whilst SMEs have been granted an extension of time this does not equate to a cancellation of the debt. Furthermore, many SMEs who choose to delay could end up being burdened with a sizable bill when their March 2022 VAT liability is due as normal.

To avoid increased costs and worry in the future, it might make sense to pay your VAT now. Specialist commercial finance providers offer flexible funding solutions to enable businesses to spread the cost of their VAT bills over a 3-12 month period and retain greater control over their finances. This could help to ease any cash flow concerns and assist SMEs to smoothly manage future peaks and troughs.

Self-assessment tax - don't forget your personal tax entitlements

It's imperative to ensure that your business can benefit from the available tax credits and allowances, but equally important that you apply the same rigour to your own tax return. Whether you are self-employed, a partner in a firm or a company director, 31 January and 31 July are key deadlines for settling your self-assessment tax liability.

The need to file a self-assessment tax return can also be eased by using these top tips to keep organised and could help to minimise your tax bill:

- Keep your financial records in order with detailed and accurate financial records of all earnings and business expenditure with an up-to-date file of invoices and receipts. In addition, make sure you record any gift aid donations. Once you have completed the tax return don't throw away these records as they have to be kept for seven years.
- Claim all the tax breaks you are entitled to including professional membership fees and subscriptions, specialist equipment, as well as sales and marketing promotional materials. In addition, you can claim business mileage or fuel, excluding commuting to your normal place of work.
- Don't miss out on pension tax relief particularly if you are in a 'relief at source' arrangement and/or have a personal pension plan. A higher rate taxpayer will need to make a claim via the tax return.
- Appoint an experienced accountant or tax advisor so you are taking advantage of all of the tax-efficient options for your circumstances and they can advise on dates to pay tax so as not to miss any deadlines, what financial records you need to keep and ensuring you claim all the tax reliefs available.

Deferral isn’t the only option

On 24 September 2020 as part of the Government’s Winter Economy Plan, it was announced that taxpayers with up to £30,000 of self-assessment liabilities due on 31 January 2021, whether deferred from July 2020 or otherwise due by 31 January under self-assessment, could make payment in 12 monthly instalments under the Time to Pay arrangements. This means the final payment would not be due until January 2022.

To avoid increased costs in the future, you can still choose to pay your tax bill now as you normally would. In fact, HMRC are encouraging businesses and self-employed workers to behave as ‘good citizens’ and pay the tax they owe on time thereby helping the Government.

If you do choose to make the payment, you may wish to spread the cost over the remaining months of the year in order to retain working capital in your business. Alternative finance providers offer unsecured loan facilities which allow you to spread the cost of tax liabilities in a flexible way, over a term of six or 12 months. Some specialist lenders also offer an optional deferred repayment for the first month, further easing the burden on your finances.

Spread the cost of your tax liabilities and unlock your cash flow for business growth

Business and personal tax liabilities can put a considerable amount of pressure on your cash flow, even when you have planned for them, resulting in a shortage of available working capital which can limit growth potential.

Wesleyan Bank offers flexible corporation tax, VAT and self-assessment tax solutions through short-term unsecured loans. Tailored financial plans with set monthly payments enable businesses to manage their cash flow throughout the year and smooth over any peaks and troughs in their finances.

In a world that has become increasingly unpredictable, gaining better predictability over your monthly expenditure will enable you to navigate current and future challenges with a clear perspective and a degree of peace of mind.

To enquire about these loans:

- bankcommercialsales@wesleyan.co.uk
- 0800 980 9348

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