

## In this issue:

Pensions: how flexible is  
flexibility?

LLP employment status options

A tax-efficient exit strategy

Tightening the net on  
tax evasion

Individual protection for  
your pension

## Pensions: how flexible is flexibility?

**With great fanfare, the Government is introducing the pension changes that from 6 April 2015 will give you complete flexibility when you access your pension savings from a money purchase pension scheme after age 55.**

The main change is that people will be able to draw as much or as little as they wish, without having to buy an annuity. Of course the option of annuity purchase will still be available and may well be the answer for many people. Regardless of what you choose, you will be able to receive 25% of your pension savings as a tax-free lump sum.

At present, once you start drawing funds directly from your pension, you cannot make any further pension contributions. But from 6 April 2015, you will have a limited ability to make contributions into a money purchase pension. The limit will be £10,000 a year (in addition to any carried forward unused pension relief from previous years) rather than the full £40,000 that is available to others. And unlike this £40,000 standard annual allowance, you will not be able to carry forward the special annual allowance of £10,000; if you don't use, you will lose.

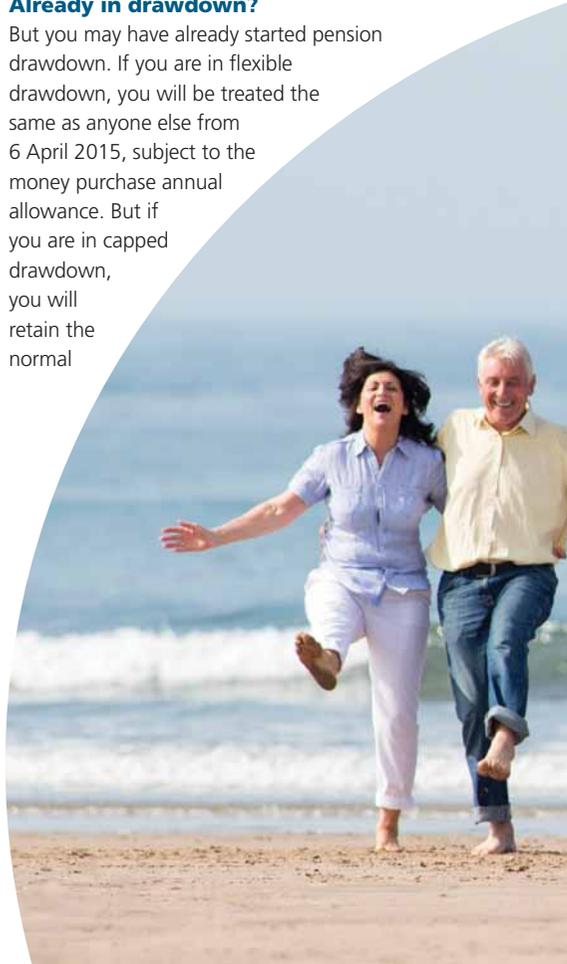
The reason for this restriction in an otherwise very liberal regime is to stop people of 55 or more from making £40,000 pension contributions and then immediately paying themselves the £40,000 from the pension. That way they would have avoided all national insurance contributions as well as tax on the £40,000.

Even if you are subject to the money purchase annual allowance, the normal £40,000 annual allowance will still be available to cover savings into defined benefit schemes (e.g. those that provide benefits based on the employee's final earnings). For example, if you have £7,000 of

pension savings subject to the £10,000 limit, then £33,000 of the normal annual allowance will be available. If you go over the £10,000 limit, then the excess will be subject to an annual allowance charge and your normal allowance will be £30,000.

### **Already in drawdown?**

But you may have already started pension drawdown. If you are in flexible drawdown, you will be treated the same as anyone else from 6 April 2015, subject to the money purchase annual allowance. But if you are in capped drawdown, you will retain the normal



annual allowance assuming your income remains within the capped drawdown limits. One way of protecting your normal annual allowance could be to start capped drawdown now while it is still available, but to do this you must be 55 before 6 April 2015.

You might be tempted to draw all your funds from the pension as quickly as you can. Leaving aside the question of your future income needs, you should always take tax advice before deciding how much to draw from your pension.

Any drawings above the tax free lump sum will be subject to income tax. Whatever you leave in the pension plan is free of tax on any investment income and capital gains and will only become taxable when you draw it.

And the Chancellor has announced another reason why you should consider not drawing all of your pension funds. They won't be subject to inheritance tax on death, although those who inherit them will have to pay income tax when they draw them out after 5 April 2016 and 45% in 2015/16.

The detailed rules are complicated, so please contact us for advice.



## LLP employment status options

**The tax rules for limited liability partnerships (LLPs) were tightened from 6 April 2014, and since then it has been much more difficult for fixed salary members to retain their self-employed status.**

Making a cash call has proved to be by far the most popular route to retaining such status. The basic idea is that a member can avoid being taxed as an employee if they have made a sufficient "capital contribution" to



includes fixed sums such as salary, and variable sums which are not based on the profits of the LLP as a whole – such as payments based on personal or team success. Drawings paid on account of a genuine share of overall profits are not included provided the

the partnership, so that there is a real risk resting on the success or failure of the LLP. The amount required is the equivalent of at least 25% of the member's expected "disguised salary" for a particular tax year.

**Capital contribution** – This is what members have contributed in accordance with the LLP agreement, and it must be of a permanent nature. The contribution cannot include a current account balance, any amounts that are not payable until a future date, undrawn profits (unless converted into capital), amounts held in a tax reserve, or any other amounts where there is no intention that the investment will be of a permanent nature. However, a long-term loan held on terms comparable to capital will count, because the only real difference is in the description used.

**Disguised salary** – This is the element of the member's pay that is not profit-related. It

drawings are subject to clawback if the expected profits do not materialise.

For existing LLP members, the 25% test must be considered at the start of each tax year and also if there is any change in circumstances.

New members have a two-month grace period in which to meet the 25% test; this is so that they have enough time in which to arrange any necessary loan finance. Their disguised salary is scaled up to the whole year for the purposes of the calculation.

But be warned – even if an LLP has sorted everything out for the current year, funding arrangements will still need reviewing in advance of 5 April 2015 if payments to members are set to increase.

We can offer advice on this potentially tricky area should you need it.

# A tax-efficient exit strategy

**A company's ability to buy back its own shares can be a very useful, if sometimes overlooked, facility.**

Such a strategy means that the remaining shareholders do not have to find the purchase funds. The normal tax treatment is that the shareholder is treated as receiving a distribution which is subject to income tax. However, where an unquoted trading company is involved, there is the possibility of having the share buy-back instead treated as a capital transaction subject to capital gains tax (CGT). If the disposal qualifies for entrepreneurs' relief, then the tax rate will be only 10%. Of course the company and the transaction must meet various conditions, in particular:

- The person disposing of the shares must normally have owned them for at least five years.
- The shareholder must either sell all of their shareholding or the shareholding must be substantially reduced. In this context, 'substantially' means their holding after the purchase is not more than 75% of what it was before. Any shares held by associates are included in the calculations.
- The shareholder must not be connected with the company after the buy back. 'Connected' here means having a shareholding of more than 30%, and

again the inclusion of associates complicates things.

- The share purchase must be for the purpose of benefiting the company's trade. Despite the other shareholding conditions, HM Revenue & Customs (HMRC) may only agree that this condition has been met if the entire shareholding is bought back.

Common examples are where shareholders disagree about the company's management or where an unwilling shareholder wishes to end their association with the company. HMRC might allow an exception where the company does not have the resources for a complete buy back at the time of purchase. The trade benefit condition will also not be met if the shareholder remains as a director or is subsequently appointed as a consultant.

Where the company cannot afford to buy back shares in a single transaction, a solution might be a contract with multiple completion dates. If the deal is properly structured, it should meet the CGT treatment conditions and the whole disposal can then qualify for entrepreneurs' relief. However, the payments for the shares will then be staggered. In some cases, CGT treatment is not always beneficial, especially for small amounts where shareholders are basic rate taxpayers. However, CGT treatment is mandatory if the conditions are met, so get in touch with us if you need advice.



## Tightening the net on tax evasion

**In a further crackdown on offshore tax evasion, HM Revenue & Customs (HMRC) has been consulting on a new criminal offence and tougher civil sanctions.**

The proposed powers will complement HMRC's existing offshore evasion strategy. This provides incentives for taxpayers to disclose their liabilities voluntarily, and it is coupled with tough penalties where taxpayers fail to comply. It is backed up by a wide and increasing range of international information exchange agreements between many of the world's tax authorities.

The Government has already recovered £1.5 billion from offshore evaders over the past two years and it has signed agreements with 44 jurisdictions to automatically share information on financial accounts. However, there are many jurisdictions from where HMRC finds it difficult to obtain information. To compensate, HMRC wants to increase the costs of being caught.

Tax evaders can already be prosecuted but HMRC has to prove that the taxpayer intended to act fraudulently – and that is a high bar. The proposal is for a strict summary liability offence, under which the act of evading tax itself is criminal, regardless of the reasons why the taxpayer failed to comply.

This offence would be limited to individuals' conduct in relation to their personal tax affairs and where it causes 'significant revenue loss.' For example the consultation asks whether it should be restricted to failure to declare income and gains from savings and investments or cover the non-declaration of all offshore income and gains. Another question is whether conviction should carry a custodial sentence of up to six months in the most serious cases.

HMRC expects that it will continue to investigate most cases, which will still be settled through civil means. The consultation on tougher civil sanctions looks at extending the scope of the existing penalty regime for offshore non-compliance. For example inheritance tax could be included. Other proposals would aim to deter taxpayers from deliberately moving offshore assets between jurisdictions to continue evading tax. Under consideration are a penal offshore surcharge, extension of the 20-year assessing time limit, and increasing the levels of offshore penalties to reflect the number of times a person has deliberately moved offshore assets to continue evading tax.



# Individual protection for your pension

**The reduction in the pension lifetime allowance from £1.5 million to £1.25 million from 6 April 2014 was accompanied by some complicated transitional arrangements.**

Before 5 April 2014, you had the option of protecting your pension savings by applying for fixed protection 2014. This allowed you to fix your lifetime allowance at £1.5 million, but you would lose the benefit of this protection if you were to make any future contributions to a money purchase pension scheme, or if you were to build up new benefits in a defined benefits scheme above a restricted set amount, or if you joined a new pension scheme. However, you can now apply for a new facility called individual protection 2014.

You can only use individual protection 2014 if your pension savings on 5 April 2014 were valued at over £1.25 million. Your allowance will then be fixed at the value of your pension savings on 5 April 2014 – subject to a maximum of £1.5 million. The good news is that you can continue to make future contributions and accrue further pension benefits without losing protection.

The value of any further pension savings above that level will then be subject to the lifetime allowance charge that applies when pension savings exceed the lifetime allowance. The charge is at the rate of 55% if pension benefits are taken as a lump sum, and 25% if taken as pension income – and the income will also be taxed. There is no downside to applying for individual protection 2014 if you qualify, because it can be held alongside fixed protection 2014.



You can have individual protection 2014 alongside enhanced protection (this was available when the lifetime allowance was first introduced) and fixed protection 2012 (available when the allowance was previously reduced). But you cannot have it if you have primary protection, which was also available when the lifetime allowance was first brought in. You can lose enhanced protection and fixed protection 2012 in the same way as fixed protection 2014 – for example, if you are not careful in opting out of automatic enrolment into a workplace pension scheme.

Individual protection 2014 is a very useful back-up. And you have until 5 April 2017 to make an application. This is an extremely complicated area, so please contact us for advice.

# Wake up to auto-enrolment

**Automatic enrolment of employees into pension schemes has passed the two year mark. The time to ignore it has now passed...**

About 4.7 million people have been automatically enrolled into a workplace pension since the system started in October 2012, according to The Pensions Regulator (TPR). However, by the end of September, fewer than 34,000 employers had completed their automatic enrolment declaration of compliance. The Government started with the largest employers – who generally have the appropriate administrative resources – yet there have been glitches: TPR enforcement action meant one company in the FTSE 250 had to pay over £140,000 in back contributions after missing their staging date for the introduction of automatic enrolment.

It is now the turn of employers with 60 or fewer employees. Back in July TPR said that "... there are considerable challenges over the next 12 months and beyond, particularly as we start to see employers for whom making pension provision for their employees will be a new and previously untested process."



One lesson from the first phase of automatic enrolment is that planning is vital: the staging date is set in stone. TPR recommends that your business's automatic enrolment timetable should begin a year before your staging date.

The payroll system is a key factor. It is essential to collect the correct employer and employee contributions and pay them when due. Supplying accurate employee data to your pension provider is also vital, as is meticulous record keeping. A payroll failure in any of these areas means a possible TPR intervention with financial penalties of £50,000 or more. Don't assume that your existing payroll system will necessarily handle automatic enrolment. One of the problems faced by the FTSE 250 company mentioned above was that their payroll system suffered from "design flaws resulting in significant delay in achieving compliance". To avoid such problems and make auto-enrolment a smooth process for you and your employees, ask us about your payroll system options now.

**Farries, Kirk & McVean**  
Dumfries Enterprise Park  
Heathhall  
Dumfries DG1 3SJ  
Tel 01387 252127  
Fax 01387 250501  
Email [info@fkmvc.co.uk](mailto:info@fkmvc.co.uk)

**Also at**  
12 Murray Street, Annan  
Tel 01461 202489  
38 Drumlanrig Street, Thornhill  
Tel 01848 330850  
87 High Street, Lockerbie  
Tel 01576 203099  
73 High Street, Dalbeattie  
Tel 01556 611544

**Partners**  
R W Mitchell BA CA  
C Paterson BCom CA  
G M McGill BA CA  
R B Palmer BA CA

Registered to carry on audit work in the UK and regulated for a range of investment business activities by The Institute of Chartered Accountants of Scotland.