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Newsletter

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Getting in early for MTD

HMRC is on track to meet the April 2026 delivery date when Making Tax Digital (MTD) will be mandated for the first tranche of self-employed taxpayers. Although you may be tempted to put off setting up new working practices, there could be some advantages in joining early.

Phase one users

Self-employed taxpayers and landlords will have to use MTD from April 2026 if their turnover exceeds £50,000. Only self-employment income and rental income is included for this purpose, with income from other sources – such as employment income, partnership income and investment income – ignored.

Some taxpayers in the correct income bracket are currently excluded from joining the pilot scheme, for example partners in a partnership and those with jointly owned property

Taxpayers with income of between £30,000 and £50,000 will not be mandated until April 2027. Although free to join early, they might prefer to wait a year.

Some caveats

The pilot scheme is live again after pausing in 2023, but it comes with some warnings, including:

- There is currently little MTD software available; just six suppliers to choose from, including two free offerings.
- Anyone using spreadsheets for record keeping will probably want to wait for bridging software to become available so that the spreadsheets can be linked directly with HMRC's systems.
- The new late filing penalty regime will immediately apply.

Some taxpayers falling into the correct income bracket are currently excluded from joining the pilot scheme, for example, partners in a partnership, those with jointly owned property or those claiming the married couple's allowance.

Advantages

One obvious advantage to joining MTD early is that users will get the chance to test a full cycle of submissions before MTD becomes mandatory. Early users will receive considerably more support during testing than those who are subsequently mandated. Early adopters will have access to a dedicated HMRC support team, with this team not limited to just dealing with MTD-related queries. They will also deal with wider self-assessment issues, so the wait times common with HMRC helplines can be avoided.

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Understanding adjusted net income

The personal savings allowance (PSA) and dividend allowance are often misunderstood because any income covered by the two allowances still counts towards a taxpayer's adjusted net income figure.

A small amount of dividend or savings income can therefore have a significant impact on your tax position.

Income levels

The key income thresholds are:

- **Net income of £50,270:** Go just a pound or two over this threshold and the PSA is reduced from £1,000 (for a basic rate taxpayer) to £500 (higher rate taxpayer). Also, the transferable marriage allowance will no longer be available.
- **Net income of £60,000:** At this level of income, a taxpayer may start to incur the high income child benefit charge. Although only a small additional amount of tax is going to be due if the threshold is exceeded by just a few pounds, it might mean having to file a self-assessment tax return for those otherwise paying tax through PAYE.
- **Net income of £100,000:** The personal allowance is tapered away once income exceeds £100,000, resulting in a high marginal income tax rate of 60%.
- **Net income of £125,140:** Entitlement to the PSA ceases altogether once income exceeds this amount.

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Implications

It is important that savings and dividend income is accurately reported to HMRC, even if it is covered by the PSA or dividend allowance, because there could be tax implications you have not considered. Reporting an estimated figure on the assumption it will make no difference to your tax position could lead to a subsequent unexpected tax bill.

If a self-assessment tax return is not required, taxpayers can report details of their savings and dividend income to HMRC using their personal tax account.

Mitigation

There are two straightforward ways to mitigate the impact of having too much savings and/or dividend income. You could move savings and investments across to individual savings accounts where income will be exempt, or make pension contributions.

Careful planning is required where pension contributions are concerned because contributions must be paid before the end of the relevant tax year.

Scottish tax rates and thresholds differ.

TAX

CGT private residence relief

You are probably aware that the sale of a main residence is generally free of capital gains tax (CGT), but, when CGT does come into play, the rules can be complex.

Relief generally

For full relief, a property must be:

- your only or main residence throughout the period of ownership; and
- occupied subject to certain permitted periods of absence.

The permitted periods of absence include absences (for whatever reason) totalling up to three years, periods up to four years when employed elsewhere in the UK, and any periods (without limit) when employed overseas.

Normally, to qualify as a permitted period of absence, the period should be both preceded and followed by a period of occupation.

Nomination

If you have two (or more) properties, you can nominate which one should be treated as your main residence. Of course, there is no point nominating a property if it is not occupied.

What catches many people out is that a nomination can only be made during the two-year period from when you first have more than one residence. This is a particular problem on marriage (or registration as a civil partnership) with each person owning a residence.

After that, a nomination can only be made if a new two-year period begins following a change in your combination of residences.

If no nomination is made, the question of which property is your main residence will be determined by HMRC according to the facts.

Reoccupation

Reoccupying a property prior to sale can be particularly beneficial if it converts unoccupied periods into permitted periods of absence.

However, a period of reoccupation must be genuine; it isn't sufficient for you to just spend a week at the property. It will be necessary to make the property your actual main residence again, with official bodies notified of the change of address.

TAX

Furnished holiday lettings uncertainty

The advantageous tax regime for furnished holiday lettings is due to be abolished from April 2025, but guidance has not yet been issued, and the new government adds to the uncertainty.

The most pressing concern for many owners will be whether full relief for their interest costs is going to cease from 6 April 2025 (1 April 2025 for companies). Currently, higher and additional rate taxpayers benefit from 40% or 45% tax relief respectively (higher relief ranges from 21% to 48% for Scottish landlords), rather than just the 20% basic rate tax reduction which is given to buy-to-let landlords.

The March Budget announcement amounted to just a couple of short paragraphs, and there has been no sign of the promised draft legislation, including an anti-forestalling provision. An additional hindrance is that HMRC has rejected a suggestion to introduce a brightline test which would clearly set out the distinction between property letting and trading activities: they consider the test unnecessary.

TAX

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The way ahead – outcomes from the general election

In her first speech as Chancellor of the Exchequer Rachel Reeves outlined her plans to 'rebuild Britain' and reiterated the government's commitment not to increase national insurance, income tax rates and VAT.

Central to Labour's bid to stimulate investment in industry and economic growth is reform of the planning system and meeting targets for house building, in line with their manifesto and election campaign promises.

The Chancellor promised, as part of a broader plan for reform, to turn attention to the pensions system "to drive investment in homegrown businesses and deliver greater returns to pension savers". What measures she might have in mind may become clearer in her first Budget expected in the autumn. No tax changes are expected before the Budget.

The Labour Party's election manifesto and announcements over the past few months give an idea of what can be expected from the new government.

Income tax – Income tax thresholds and the personal allowance will remain frozen until April 2028, continuing the previous government's policy. This will bring more people into the higher and additional tax rates.

Capital gains tax (CGT) – The only guarantee given is that CGT will not be charged on the sale of a main residence. There have been mixed messages about CGT rates.

Non-doms – The last government announced changes to the non-dom tax regime but they have not been legislated. Labour wants to abolish non-dom status for tax and replace it with a modern scheme for people who stay in the UK for only a short period. The new rules can be expected to incorporate this aim.

Inheritance tax – Labour's election manifesto promised an end to "the use of offshore trusts to avoid inheritance tax". There has been speculation that business and agricultural property reliefs might also be targets for reform.

VAT – A key policy of the new government is the imposition of VAT on private school fees from an early date, most likely to be September 2025. Parents should start planning now for increased fees or a transfer to a state school. The business rates exemption for private schools will also be removed.

Business taxes – Within six months, the government is expected to set out key policies for the next five years with the aim of helping "businesses to plan investments with confidence".

Also expected is clearer guidance on what expenditure qualifies for full expensing and the annual investment allowance.

Labour has promised not to increase corporation tax but will review tax breaks for businesses. It has also said it will replace business rates with a new system that will put online retailers on a par with high street businesses.

Labour promised an end to "the use of offshore trusts to avoid inheritance tax". Business and agricultural property reliefs might also be targets for reform.

Employment – Labour has pledged the early introduction of a "new deal for working people". Expected measures, some or all of which will be preceded by consultation with businesses, include the abolition of age differences in minimum wage rates, a ban on zero-hours and 'fire and rehire' contracts, the repeal of some trade union laws and giving employees rights to parental leave, sick pay and protection from unfair dismissal from day one.

Further ahead – The government faces spending pressure in several areas including the NHS and defence. Its funding plans rely on economic growth. If that does not materialise, future tax increases may become inevitable.

BUSINESS

Rejected VAT registrations

HMRC rejected over 50,000 VAT registration requests last year, amounting to 17% of all applications. Some are refused because of suspected connection with VAT fraud, but others are turned down due to mistakes in completing the registration form.

Traders are not helped by the difficulty of getting through to a VAT helpline – the average wait is over 25 minutes and, often when the call is answered the officer cannot deal with the query but only directs the caller to guidance on the HMRC website.

Failure to register for VAT promptly when a business exceeds the £90,000 past or future turnover threshold is likely to result in penalties and hampers trading because the business cannot issue VAT invoices.

Getting it right

One reason for rejecting an application is because HMRC thinks the information given is incorrect. You must ensure that details of the type of business entity, its owners or directors, contact details, HMRC reference number and financial information are accurate and consistent with information HMRC might already have or that is held at Companies House. You have to give details of your bank account, which must be in the name of the business being registered.

Especially important are a full description of the business activities and the reason you want to register. You must state if you expect regular VAT repayments – HMRC will check your application particularly carefully. Seek professional help if you have any doubts.

BUSINESS

Opting out of the cash basis – pros and cons

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Cash basis accounting is now the default method for self-employed individuals and partnerships, but you can opt out and carry on using the accruals basis instead.

HMRC introduced the change as a way to simplify accounting for small businesses. But in fact the new system appears to be aimed at facilitating the introduction of Making Tax Digital (MTD) for income tax. MTD is set to start in April 2026 for individuals with qualifying income over £50,000 and April 2027 for qualifying income over £30,000. No start date has been announced for MTD for partnerships.

Drawing up accounts based on cash in and out is certainly simpler, making it easier to provide the quarterly accounting information that MTD will require. But annual profits may fluctuate wildly when expenses are paid in a different accounting period from the receipt of the related income, and stock and work in progress are not taken into account. That may result in years when taxable income unexpectedly jumps into a higher tax band than if it accrued more evenly. It also makes budgeting and cash flow challenging and makes it harder to work out how profitable your business really is.

Time payments with care

However, by the same token and with care, you may be able to plan your payments and receipts to ensure you stay below a relevant income tax threshold. You could buy stock and pay your suppliers early if you think your profits may be more heavily taxed in this tax year rather than next, or delay payments in the converse situation.

On the income side, although you might not be able to persuade your customers or clients to pay you early, you could postpone income by delaying invoicing, or even ask a customer to hold off paying your invoice until after the year end.

PENSIONS

Top-up your missing NICs online

The government has recently launched a new digital service which should make it easier for people to check for any gaps in their national insurance contribution (NIC) record. They can then pay securely through this service.

The full annual amount of new state pension now stands at just over £11,500, following two years of healthy percentage increases. However, this full amount is only paid to those with 35 qualifying years on their NI record.

Digital service

The new service – known as Check Your State Pension Forecast – lets most people:

- view gaps in their NI record;
- see how much their state pension could increase if gaps are filled (not everyone will benefit from filling gaps);
- see the cost of achieving the potential increase; and
- pay voluntary contributions to fill gaps.

People can access the Check Your State Pension Forecast service via their personal tax account or using the HMRC app. Anyone with gaps can choose which years they would like to fill. After making a secure payment through the service, confirmation will be sent that the payment has been received. A person's NI record will then be updated.

Cost

To add a year costs £907, and this will boost current annual pension entitlement by some £329, a very respectable return for someone who enjoys many years of retirement.

The normal time limit for someone to fill gaps is six years. The deadline for filling gaps in the 2018/19 tax year is therefore 5 April 2025.

Short-term extension

However, transitional arrangements running until 5 April 2025 mean that people can currently look further back to fill gaps – as far back as the 2006/07 tax year. On top of that, gaps for the years 2006/07 to 2017/18 can be filled at a reduced annual cost of £824, improving the return even further.

NEWS IN BRIEF

News round up

British savings bond

The 'new' three-year fixed rate bond pays interest of up to 4.15%. Although there is security for investment of up to £1 million, the interest rate is not competitive when returns of over 5% are currently available on easy-access accounts.

Push back on remote working

Companies pushing for a return to office-based working will be emboldened by a recent employment tribunal ruling. The case of a senior manager who wanted to work at home was rejected on the basis that there are weaknesses with remote working.

Four-day week trial expanded

Following results from a 2022 trial of four-day working, which has seen around 54 of the 61 companies and local councils taking part retaining the practice, a new pilot is set to allow firms that sign up to the three-month project to try flexible start and finish times, compressed hours and nine-day fortnights. The pilot is due to start in November.

Advisory fuel rates

The 1 June 2024 update sees the rate for fully electric cars cut from 9p to 8p per mile. Petrol and diesel rates are all increased by 1p (2p for the over 2,000cc petrol rate), but LPG rates are unchanged.

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