TOP TEN TAX CHALLENGES

2022

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INTRODUCTION

As most business owners and high-net-worth individuals know, the tax landscape is changing all the time and there are new targeted taxes on the horizon too. To help you stay one step ahead, our tax team is sharing the 10 top tax challenges for 2022.

Read on to discover if one or more of these tax challenges applies to you.

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1 TAX IN UNCERTAIN TIMES

As well as being aware of tax changes that have already been announced, business owners and individuals must consider the impact of new targeted taxes and stay alert to areas that could be ripe for reform.

For business owners, planning for known Corporation Tax increases seems straightforward enough. However, their impact and the new Health and Social Care Levy, which is due to take effect in April 2022, could erode profits quickly if they are not factored into pricing and other decisions ahead of time.

"Preparing for tax changes isn't a side issue, it's integral to the delivery of products or services that generate a healthy return for the business and its shareholders."

Protecting your wealth

For individuals, especially those with a high-net-worth, the importance of protecting wealth for the benefit of the family as a whole has been accentuated during the pandemic. Changes to capital taxes, including the Capital Gains Tax (CGT) and Inheritance Tax (IHT) regimes, can't be ruled out and should be factored into any decision making. Being aware of what could change, as much as what is changing, remains a key challenge.

Areas ripe for reform

Some areas of the tax system are also ripe for reform, particularly where working practices have changed significantly during the pandemic, due to the rise of home working and/or increased global mobility.

Establishing a fair and equitable tax system which reduces the impact of differing employment statuses is another area where reform is anticipated to support workers in the rapidly growing gig economy.

In the short term, business owners and individuals should be prepared for more surprises. Chancellor Rishi Sunak has already demonstrated a willingness to enact measures out of cycle, so more of the same is possible. For business owners, staying in touch with trusted advisers is vital to weigh up the commercial impact of known and unknown fiscal changes, while taking full advantage of opportunities, reliefs and allowances. For individuals, protecting family wealth will require even more forethought and strategic planning to balance risks and rewards in a climate of uncertainty.

In the longer term, who knows where the UK's tax system will end up? With a mounting debt burden, an ageing population and more price competition from overseas, almost anything is possible.

Predicting the direction of travel for corporate and individual taxation has probably never been more challenging. However, having a framework of a plan can help you react quickly and mitigate the impacts of changes.

Andrew England, Partner at Menzies LLP

PERSONAL WEALTH AND TAX

Important to plan ahead

There is a tremendous amount of uncertainty about capital taxes at the moment – capital gains tax (CGT), inheritance tax (IHT) and a potential wealth tax. While changes in these areas of taxation are by no means certain, it has become even more important for individuals, particularly those who have accumulated significant personal wealth, to plan ahead.

The reasons for the uncertainty are clear

Recent reviews of both the CGT and IHT regimes carried out by the Office of Tax Simplification (OTS), combined with speculation about how the Government might be intending to pay for the pandemic, have raised concerns that punitive tax changes could be on the way. The Government's decision to establish a Wealth Tax Commission to consider a new capital tax on personal wealth, has raised concerns further.

Recent speculation about changes to the CGT regime have led some people to sell assets earlier than originally planned, only to find that nothing has actually happened. Responding to the latest review by the OTS, the Treasury has agreed to a series of reforms, including a move to simplify how CGT is reported and paid through the introduction of a Single Customer Account. However, the main focus of these reforms is simplification and improving guidance, rather than raising taxes.

Following two comprehensive OTS reviews, reform of the IHT regime can't be ruled out. Since the last report by the OTS was published in July 2019, there has been widespread speculation that far-reaching changes could be on the way.

The introduction of a new wealth tax also remains a possibility. In this case, however, it would most likely take the form of a one-off tax, based on assets owned at a defined date in the past. At present, there is no indication that The Government is seriously considering implementing a wealth tax.

Changes to reliefs and the regime for lifetime gifts can't be ruled out in the future. If any of these changes do go ahead, they could have a major impact on some individuals and their families.

David Truman,
Partner at Menzies LLP

TAX AND GLOBAL MOBILITY

As a result of Brexit and the pandemic, more people than ever before are working from overseas.

For many businesses, the pandemic has proved that employees can work successfully from another country. This has given employers access to a wider pool of talent, while removing the costs involved in bringing international workers into the UK. However, when managing workers based overseas, failing to ensure compliance with local tax regulations could incur expensive penalties, particularly if they are allowed to accumulate over time.

Brexit-related changes to areas such as immigration and social security rules have also created new challenges for employers, when moving people between the UK and the EU.

While the flexibility provided by remote working has been positive for many, it's vital that employers understand the wider tax implications involved in managing global teams and plan ahead.

Andy Brookes,
Senior Manager at Menzies LLP

Optimise your tax position

Each location will have a unique set of tax rules and exemptions, so it's important that employers make the most of any opportunities to optimise their tax position. For example, when bringing workers into the UK for less than 24 months, they may be able to claim Temporary Workplace Relief to offset their travel and subsistence costs. UK workers that are sent abroad temporarily may be eligible to remain under the UK social security regime. It is therefore important to consider whether bilateral social security agreements exist between the UK and the other country or whether the other country is within the EU and EEA.

When sending workers on international assignments, employers should ensure that their internal tax and mobility policies are well drafted, thereby reducing ambiguity and managing employee expectations.

It's worth bearing in mind that remote workers represent a new category of worker, and local rules surrounding employment rights, tax, social security, corporation tax and VAT may evolve further. Businesses should take action now to manage their remote population, understand their current obligations and watch out for changes in the future.

CORPORATE TAX INCREASES AND CASH MANAGEMENT

From April 2023, the rules around Corporation Tax are set to become more complicated. As well as increasing the likelihood of businesses needing to pay a higher rate of corporate tax, some may also need to make earlier payments to HMRC. These changes could make it more difficult for businesses to plan ahead in order to mitigate any negative impacts on their cashflow.

The Government's planned changes to corporate taxes will involve the introduction of two rates:

- 19% for companies with annual taxable profits of £50,000 or less
- 25% for companies with annual taxable profits of over £250,000
- A marginal rate of tax will apply for profits between £50,000 and £250,000

The limits above are 'group' limits and further changes are being introduced which will need to be taken into account, bringing back the old associated company rules. These rules could also impact both the tax rate and whether a company falls into the quarterly instalment regime for tax payments. The changes are likely to make it more challenging for organisations to calculate which of these two bands they fall into and when they need to make tax payments to HMRC.

To optimise their tax position and manage the potential cashflow impact of these reforms, there are a number of things decision makers can do. They should review their business structures, as it may be possible to reduce the number of associated companies, plan the timing of their expenditure carefully to maximise tax reliefs, such as the capital allowances super-deduction, and therefore reduce tax or increase losses.

If losses do arise, businesses should consider the benefits of carrying forward any unused tax losses to reduce further tax, rather than claiming a repayment of tax at the current 19% tax rate. This is because the future tax saving may outweigh an immediate cash refund.

Through effective forward planning, businesses can avoid getting caught out by the forthcoming changes to corporate tax and keep their cash position under control.

**Lucy Mangan,
Partner at Menzies LLP**

GREEN TAX FUTURE

The majority of businesses know that improving their sustainability credentials is crucial to their future success.

While the Chartered Institute of Transport and Logistics (CILT) has emphasised the need for a climate change tax policy roadmap, the future landscape for this area of tax is currently uncertain. For example, the Enhanced Capital Allowances for energy-saving or environmentally beneficial technologies regime, which came to an end in March 2020, used to enable businesses to claim enhanced relief on their qualifying plant and machinery spending. While businesses will still be able to take advantage of the super-deduction on capital allowances until April 2023, further grants and reliefs will be required to incentivise green investments in the longer term.

A key area for businesses to watch is changes in tax policy, aimed at helping employers to reduce their 'Scope 3' carbon emissions. These are emissions associated with a company's value chain, including its suppliers' distribution activities and its fleet, or business travel. Decision makers should be aware of current and future tax incentives aimed at making it more tax-efficient for employers and employees to transition to sustainable company fleets.'

Due to be introduced in April 2022, the plastic packaging tax could impact businesses in a variety of industries, such as logistics and food manufacturing. It will apply at a rate of £200 per metric tonne for UK businesses that manufacture or import 10 tonnes of plastic packaging per year and

will apply to packaging that contains more plastic by weight than any other single material. With similar taxes likely to be introduced in the near future, businesses should consider the impact this, and other new green taxes could have on their supply chain.

Until there is a clear green tax roadmap in place, it will be challenging for businesses to plan their spending on green investments. However, with reform in this area almost certainly on the way, organisations must stay alert to changes and react to fiscal changes as and when they arise.

Being aware of the reliefs available to support businesses in making green improvements and staying abreast of tax changes on the horizon will enable them to plan their spending more effectively.

Andrew England,
Partner at Menzies LLP

TAX AND THE SELF-EMPLOYED

Chancellor Rishi Sunak has made it crystal clear that it is his intention to change the way self-employed people are taxed, so those affected need to be ready.

The warning came when the Chancellor introduced the Coronavirus Job Retention Scheme and Self-Employment Income Support Scheme (SEISS) in March 2020 – a move which was widely welcomed at the time. Referring to the differential in NIC rates payable by individuals according to their employment status, he said: “If we all want to benefit equally from state support, we must all pay in equally in future.”

It seems likely that a further increase in NICs for the self-employed is likely in the near future, on top of the planned rise of 1.25% from April 2022.

Andy Brookes,
Senior Manager at Menzies LLP

Other changes

Other fundamental changes affecting the way self-employed individuals are taxed are expected, following publication of the Taylor Review. Depending on their way of working and terms of employment, an individual’s employment status could be assessed differently in the future, potentially making them liable for PAYE. This could have a significant impact on income levels for some self-employed individuals and it is important to plan ahead.

It’s unclear how much longer smaller companies can avoid the impact of HMRC’s IR35 rule changes for the private sector. Medium-sized and large companies were required to comply with the rule changes in April 2021. If the rule changes are extended to small businesses, the end employer will become liable for each contracted worker’s tax payments if they do not apply the rules correctly. As a result, they might view the risks attached to employing such workers differently in the future.

Other planned administrative changes will impact self-employed individuals in the next few years, in particular Making Tax Digital (MTD). From 6 April 2024, self-employed individuals and landlords will be required to file quarterly updates regarding their business profits digitally. Some businesses are already filing MTD updates for VAT and additionally will be required to file quarterly updates for income tax, which creates further compliance for taxpayers. Further proposed changes affecting the ‘basis period’ of a business for accounting purposes, bringing it into line with the tax year, could further accelerate the timing of tax payments for self-employed individuals. However, it should be noted that both MTD and the proposed changes to the basis period could bring benefits too, such as simplification and improved cashflow visibility.

More change in this area of taxation is likely in the future, so it is important for self-employed individuals to seek the support of a trusted adviser to guide their decisions and forward planning.

QUALIFYING FOR R&D TAX RELIEF

Many businesses do not claim research and development (R&D) tax relief, despite the fact that their problem-solving activities often meet HMRC's eligibility requirements.

Many different kinds of businesses, from food and drink manufacturers to architectural practices, are developing products and processes that advance science or technology. Despite this, there is still a common misconception that research and development (R&D) is a 'scientific' activity, that takes place in the laboratory and is conducted by those in 'white coats'. For this reason, many organisations don't realise that investment in problem-solving activities could be eligible for R&D tax credits.

Since its introduction in 2000, the Government's R&D tax regime has seen little change, adopting a light touch to encourage more UK businesses to make claims and promote innovation. However, the Chancellor's Autumn 2021 Budget statement included a number of reforms, due to take effect from April 2023. These included expanding the regime's qualifying expenditure to include data and cloud computing costs.

With a number of important reforms to the R&D tax regime on the horizon, it's vital that organisations speak to a reputable adviser to find out if they should be taking advantage of this valuable incentive.

Anthony Lalsing,
Partner at Menzies LLP

Measures were also introduced to ensure that R&D activity carried out in the UK is incentivised. For tech startups and other SMEs that currently subcontract their R&D activity overseas, this will require them to carefully weigh up the cost savings associated with using overseas labour, versus the benefits of claiming R&D tax incentives.

Maintaining a healthy cashflow will be key for businesses over the coming months as they navigate the road to recovery. Those not currently claiming R&D tax relief should seek expert advice on how to maximise the value of the available reliefs against the commercial costs of running their business.

MANAGING CROSS BORDER PAYMENTS

Many businesses trade internationally, whether that means selling products or services to global customers or transacting with other group companies. But are the tax implications being properly considered in relation to these activities?

Cross-border payments have become more prevalent, as companies can more readily connect with global customers and suppliers, and it is important that businesses assess the tax consequences of these transactions. For example, UK-based businesses may suffer 'withholding taxes' in many jurisdictions, and they need to understand when these taxes may arise, the tax treaty position with the relevant country, and any relief that might be available in the UK. Going through this exercise in advance allows for the tax implications to be clarified and included within a contractual agreement, otherwise unforeseen tax costs could potentially wipe out any profit on a transaction.

UK-based businesses could be liable for 'withholding taxes' in many jurisdictions and they need to fully understand the implications of this. Failing to do so could leave them in a situation where they are contractually obliged to provide services at a price that delivers little or no profit.

Nick Farmer,
Partner at Menzies LLP

Tax issues from cross-border payments

There are a number of other tax issues that may arise from cross-border payments, and these typically vary depending on the nature of the transactions. For instance, if services have been delivered on the ground in another country, it needs to be identified if a permanent establishment has been created, giving rise to local corporate income tax or if local payroll taxes are due. Other indirect taxes should also be considered, such as VAT or local sales taxes, customs duties, as well as other state and local taxes that may arise in a particular territory.

Another important area of taxation related to cross-border payments is 'transfer pricing'. This affects groups that are transacting between related companies in different countries and requires the transactions to be priced on an arm's length basis. In order to improve transparency in this area, the UK Government has consulted on plans to introduce transfer pricing reporting for corporate tax returns. This will make it easier for HMRC to review any inter-company, cross-border transactions that are taking place and assess whether sufficient tax is being paid.

Cross-border payments may also include passive income flows, such as in relation to interest, royalties or dividends. Such payments also often incur withholding taxes, and it is important to review how these arise under the terms of a tax treaty. In this respect, it should be noted that now the UK is outside the EU, withholding taxes are more likely to arise on payment flows from EU companies, and can also arise on interest or royalty payments being made from the UK.

The international tax landscape is constantly changing, and this is clearly evidenced from the OECD Base Erosion and Profit Shifting (BEPS) initiative, that has recently secured a global minimum effective tax rate of 15 per cent for the largest companies.

For all companies that are trading internationally, with third parties or other group companies, it makes sense to take advice about the tax implications of cross-border payments, and preferably before arrangements are set in stone.

VAT AFTER BREXIT

Brexit has transformed the VAT landscape for businesses moving goods between the UK and the EU.

The end of free trading means that for some businesses exporting goods to the EU, it may be worth registering for VAT outside of the UK. If they decide that this is the right solution for their business, they should choose their location carefully, taking account of local VAT regimes.

Full customs controls from 1st January 2022

Throughout 2021, measures have been in place to help businesses transition to the post-Brexit trading environment by delaying submissions of customs declarations and payments of customs duties.

As well as understanding areas such as the correct procedure for dealing with a certificate or origin, businesses may be able to take advantage of other new regimes, such as the EU Import One Stop Shop (IOSS) scheme, which will prevent the need for multiple VAT registrations for online business to customer sales throughout the EU. With proposals underway to introduce separate VAT rates for different member states, they may also need to adjust the prices of their goods accordingly, to keep costs competitive.

When accounting for VAT in the post-Brexit world, UK businesses are in uncharted territory. By being prepared to flex their approach as rules become clearer, they can find the most tax-efficient solution and optimise profits as they do so.

As well as developing a clear understanding of HMRC's guidance for businesses trading internationally, it's vital that decision makers review their supply chains carefully and take steps to mitigate the financial impact of VAT changes on their business model.

Andrew Norman
Director at Menzies LLP

HOW TO PROTECT YOURSELF

In an uncertain tax climate, it is more important than ever that business owners and individuals who have accumulated personal wealth, have a plan for their future.

For business owners, it is important to consider what will happen to the business when they retire and/or on their death. This shouldn't be left to chance. Will the business close, or will someone take over and will this trigger a CGT or IHT liability? Failing to plan ahead could leave the individual concerned, or their family, with a higher tax liability when the time comes.

When planning for retirement, some individuals find themselves in the fortunate position that they have more money than they are ever likely to need. In this instance, they may wish to consider establishing a Family Investment Company or Trust. This is especially sensible if individuals are unable to gift their money today - perhaps their children have enough wealth already and their grandchildren are still too young. Transferring a chunk of wealth out of their estate, while retaining some control over what happens to it, could be an ideal, tax-efficient solution.

The best way to protect your wealth, for the benefit of you and your family, is to have a plan and keep it under review. Even if capital tax increases fail to materialise in the short term, they are unlikely to reduce, so assuming some increase in tax liabilities over time remains a sensible approach.

WHAT NEXT?

We are living in extremely uncertain times, but businesses and their owners, and other self-employed individuals, can't afford to do nothing.

It has probably never been more important to have a trusted team of tax advisers on your side, helping you to make the right decisions about how to structure your financial interests or ease pressure on cashflow in the year ahead.

If one or more of the above tax challenges could be an issue for you and/or your business in 2022, please get in touch.

Business owners must consider what will happen to the business when they retire and/or on their death. This shouldn't be left to chance. Without a plan, the individual concerned, or their family, could find themselves with a higher tax liability when the time comes.

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MEET THE EXPERTS

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