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BUSINESS NEWSLETTER

We hope you enjoy reading this newsletter and find it useful. Please contact us if you would like to discuss any matters further.

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This month's newsletter covers :
Important announcements from HMRC in the last month and some of the most common queries we hear from personal tax clients and sole traders at this time of year:
This article covers:

1. The delay of Making Tax Digital for Income Tax Self-Assessment announced by HMRC.
2. Allowable expense sole traders can claim back tax on.
3. What HMRC 'Payments on Account' mean and an illustration of how these work in practice.

Making Tax Digital for Income Tax Self-Assessment (MTD ITSA): delayed!

What is MTD ITSA?

Under MTD for ITSA, businesses, self-employed individuals and landlords will keep digital records, and send a quarterly summary of their business income and expenses to HMRC using MTD-compatible software. In response they will receive an estimated tax calculation based on the information provided to help them budget for their tax. At the end of the year, they can add any non-business information and finalise their tax affairs using MTD-compatible software. This will replace the need for a Self-Assessment tax return.

The government has announced a further delay to the introduction of Making Tax Digital for Income Tax Self-Assessment (MTD ITSA). Why this change and what is the new timeframe?

In a statement released on 19 December, the government has finally acknowledged that MTD ITSA is a significant change for all concerned, and that launching during an economic crisis is not ideal. MTD ITSA will now be delayed until April 2026, with the self-employed and landlords with turnover in excess of £50,000 joining first. Those with income over £30,000 but not exceeding £50,000 will not need to join until April 2027. A start date for general partnerships has not yet been announced. Prior to this announcement, the mandatory use of software to remain compliant was set for April 2024.
The government will now review the needs of smaller businesses before asking those earning less than £30,000 to join. Previously MTD ITSA was going to be mandatory for the self-employed/landlords earning over £10,000. Given the expected additional costs and administrative burden for small businesses this will undoubtedly be a very welcome change. However, HMRC will have its work cut out when operating different systems for self-assessment customers so further delays could be on the cards.

Note. This does not affect the move to tax year basis periods, which will be effective from 2024/25 after next year's transition.

What can you do to prepare for the introduction of MTD ITSA

Despite the pushing back of this significant change to how self-employed/landlords record their income and expenses; it is important that those impacted turn their attention towards what they need to do to stay compliant when MTD ITSA goes live. Getting the right system in place for both compliance and your needs is the first step to preparing for Making Tax Digital.
The good news is there are plenty of software options on the market for both the self-employed and individuals that are compliant for MTD ITSA. If you wish to discuss these options, please get in touch with OCL and speak with one of the team.

One of our upcoming articles will also cover some of the available software options to assist with MTD ITSA compliance and record keeping.

Approaching deadline for capital allowances 'super-deduction' for limited companies:

For two years from 1 April 2021 until the end of March 2023, any investments your business makes in main rate (main pool) plant and machinery will qualify for a 130% capital allowance deduction. The final deadline to take advantage of this super deduction is just a few months away. If you are considering a capital equipment purchase for your business, it's worth taking note of this deadline and the tax saving opportunity the super deduction represents. Please get in touch with one of our team if you need to discuss further.

Income tax relief: How you can reduce your tax by claiming on business expenses

As a sole trader or freelancer, it's crucial to understand your basic allowable expenses—even if you're using an accountant to help with your tax return.

You can claim tax back on some of the costs of running your business—what HMRC calls allowable expenses. These appear as costs in your business accounts deducted from the profit you pay tax on.

Expenses can reduce the average sole trader's tax bill—often significantly.

For example, if your turnover is £80,000 and you claim £20,000 in allowable expenses, you only pay tax on the remaining £60,000—a substantial saving.

You can also use simplified expenses.

These flat rates allow you to quickly calculate tax relief on vehicles, working from home and living on your business premises. It can make working your expenses significantly easier.

On the Gov.uk website, you can find the most common expenses you can claim for self-employed and the most common expenses you can claim for if you rent out a property.

Self-employed allowable expenses list

Below we cover some of the things you can claim for. To reiterate, we assume you're using cash basis accounting, as the rules for traditional accounting can be slightly different.

You can add these figures to your self-assessment tax return.

Office equipment and tools

You can claim expenses for business equipment such as laptops, PCs, printers, and computer software that your business has used for less than two years.

You can't claim tax back on small tools.

Stationery and communications

As well as the usual paper, envelopes and pens, you can also claim back tax on postage and printing, including the costs of printer ink and cartridges that you use as part of your business.

With more businesses now trading online, this allowance also applies to electronic communications – so you can claim tax back on your business phone, mobile and internet bills.

Phone and internet

If you use your phone, mobile and internet for personal and business use, you'll need to demonstrate a realistic way of dividing the costs and can only claim tax back on the part for business use.

If you can't show this, you can't claim any tax back.

Professional and financial services

If you get advice from an accountant, lawyer or other professional as part of your business, you can claim tax back on their fees.

You can also claim allowable expenses for hiring surveyors and architects for your business, just not for personal home improvements.

If you have a business bank account, you can claim tax relief on bank, overdraft and credit card charges or interest on business loans.

You can also claim tax back on hire purchase, lease, or other financial payments for equipment you use in your business.

Pension contributions

Contributions to your pension are not a business expense, so they don't affect your self-employed profits. However, you are eligible for tax relief on any contributions you make, which your pension provider will automatically claim.

Staff and employee costs

You can claim tax relief on employee and staff salaries, bonuses, pensions, benefits, staff and employee costs, agency fees, subcontractors, and employer's National Insurance contributions.

Travel costs

There's a host of allowable expenses you can claim for if you must travel for business, including train, bus, taxi, airfares, and accommodation costs.

But these only apply if the primary reason for your journey or stay was for business.

If you take a trip that combines business and pleasure, you can only claim tax relief on costs that you can show are separate from the private part of your journey.

If you can't split up the costs, you can't claim tax relief on any part.

Car and vehicle costs

If you use a vehicle as part of your business, you can claim tax relief for expenses such as petrol, insurance, and repairs.

Mileage allowance

As a self-employed person, you can add up all your motor expenses for the year and work out the separate business element of the total cost.

However, keeping track and working this out takes time and effort.

Instead, you can claim mileage allowance, a simplified expense that lets you calculate the costs for running your vehicle.

Other vehicle-related areas you can claim expenses on include:

- Parking
- Breakdown cover
- Hire charges.

Again, tax relief only applies to these if they are business rather than private expenses.

You can't claim tax back on parking or other fines incurred while driving. There's no tax relief for breaking the law.

Food and clothing

Everybody needs food and clothing but claiming for them on expenses depends on what you're using them for.

Clothing

Generally, you can't claim for clothing if it's something you'd wear as part of an everyday wardrobe. So, even if you've bought a suit for work, you can't claim for its cost.

But, if you must buy a uniform that identifies what you do or needs special protective clothing to do your job, you can claim for that.

You can't claim for non-uniform items such as shoes and socks.

If you're an entertainer, and the clothes you're buying are a costume for a stage, TV or film performance, then you can claim tax relief on those.

Clowns, magicians, acrobats and Elvis impersonators – we bet HMRC enjoys reading your clothing claims!

Laundry

If you wear a uniform or special protective clothing, you can claim expenses if you wash, repair, or replace it.

Food

You can only claim money back on food and drink if it's a business expense, meaning it must be outside your usual working routine, such as a business trip.

Stock and materials

You can claim tax back on:

- Items that you resell, e.g. stock
- Raw materials that you use to make goods for sale
- Direct costs from producing goods.

Marketing and advertising

You can claim tax back on the costs of advertising and marketing your business, including costs for hosting and maintaining your company website.

But beware, you may think that treating a customer or supplier to lunch is 'marketing', but HMRC considers it as 'entertaining', which you can't claim tax back for.

If you're a member of a professional trade body or organisation as part of your business, you can claim tax relief on your membership fees. Subscriptions to trade or professional journals are also allowable expenses, so claim for those too.

What are payments on account?

These are advance payments you make twice a year towards your Self-Assessment tax bill.

HMRC estimate how much tax you owe for the upcoming year based on your previous year's tax bill. You pay this estimate over two instalment dates for the purpose of spreading out your tax payments throughout the year.

HMRC designed this process to help taxpayers stay on top of their payments as well as avoid paying tax in arrears.

You can calculate your upcoming payment on account by halving your previous year's tax bill. Your actual tax bill won't necessarily match the estimate, as business income generally fluctuates from year to year.

So If your payments on account don't cover your total tax bill for the year, you must make an additional 'balancing payment'.

The two deadlines for paying your Self-Assessment tax are:

- **Midnight on 31 January** (the same date your Self-Assessment tax return is due) for any tax you owe for the previous tax year (a balancing payment) and your first payment on account for the upcoming tax year.
- **Midnight 31 July** for your second payment on account for the upcoming tax year.

As a Self-Assessment taxpayer, you're required to make payments on account to HMRC unless you fall under one of the following two categories:

- Your last Self-Assessment tax bill was less than £1,000.
- 80% or more of your tax was deducted at source through PAYE.

An example of how payment on account works

Let's say you became self-employed in May 2020 and completed your first Self-Assessment return for the 2020/21 tax year.

Once you completed your return, HMRC calculated you owed £500 tax for the year, due by 31 January 2022. Your tax bill was under the £1,000 threshold, so you weren't required to make payments on account for the following tax year.

During the following tax year (2021/22), you recorded higher profits and your bill for the 2021/22 tax year came to £2,000.

Because this is above the threshold, the payment on account process was triggered for the 2022/23 tax year.

Therefore, in addition to the £2,000 tax payment owed for the 2021/22 tax year, your tax bill also included your first payment on account for the 2022/23 tax year of £1,000 (half your 2021/22 tax bill).

So, you paid a total of £3,000 on 31 January 2023.

Your second payment on account of £1,000 for the 2022/23 tax year was made on 31 July 2023.

Now, in total, you have paid £2,000 towards your 2022/23 tax bill.

When you submit your Self-Assessment tax return for the 2022/23 year, and your tax bill comes to £1,800, for example, you'll be owed a refund of £200 (the difference between the £2,000 you have paid on account and your actual tax bill).

In this case, your next payment on account for the following tax year, due 31 January 2024, would be £900 (half of your 2022/23 tax bill).

How and when to make payment on account payments

There are a few ways you can pay, just make sure you allow enough time for the payment to be processed before the deadline.

For same or next day payment choose either online banking, CHAPS, pay online with a personal debit card or corporate credit card (personal credit cards are not taken), or pay at your bank (you'll need a paying-in slip from HMRC to do this).

Allow three working days if you choose to pay by Bacs or cheque through the post.

A convenient way to ensure you don't miss your payment on account is to set up a direct debit with HMRC. By sending this form to your bank, you approve HMRC to collect however much you owe from your account. It will tell you in advance how much it will take and when.

Allow five working days to process a direct debit the first time you set one up.

If you prefer to make regular monthly or weekly payments towards your next tax bill, you can set up a Budget Payment Plan. How much you want to pay and how often is up to you.

The amount you have paid into your Budget Payment Plan will be used against your next tax bill, meaning you won't be left with a large balance to pay at the deadline.

If the amount in your plan doesn't cover your tax in full, you'll need to pay the difference.

If you miss a payment deadline, you'll be charged interest, and you may also have to pay a late payment penalty.

How to reduce payments on account

All business income can fluctuate from year to year.

If you know your tax bill is going to be lower than the previous year, say for example you have fewer clients or your tax relief has gone up, you can avoid overpaying tax by asking HMRC to reduce your payments on account.

You can choose to do this online or by post.

To do this online, sign into your online account. Select the option to view your latest Self Assessment return, and then select 'reduce payments on account'.

To apply by post, fill out the SA303 form on screen, print it, and send to the tax office.

Do think carefully before you reduce your payment on account because if it turns out you've underpaid, you'll have to pay interest on the outstanding amount, which can increase your tax bill significantly.

Payment on account refunds

If you have paid too much tax, you're entitled to claim a tax refund just like any other regular employee.

But as a Self-Assessment taxpayer, you claim a refund through the Self-Assessment process. This means any overpayments will be processed once you've submitted your next tax return.

Once HMRC has received your return, you'll be told if you have overpaid.

You'll be able to then choose how you want the money to be paid back to you, for example, by cheque or bank transfer. Alternatively, you can put it towards your next payment on account tax bill.

Final thoughts on payment on account

Now you understand how HMRC calculates payment on account, you should find it easier to anticipate your next tax bill.

For further support with this, OCL Accountancy will be able to help you, if you have one.

But, as always, it's best practice to submit your Self-Assessment tax return as soon as possible post tax year-end to give yourself enough breathing room to settle a balancing payment without incurring interest and late payment penalties.