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## **NEWSLETTER SEPTEMBER 2010**

### **PAYE TAX DEMANDS – SOME PRACTICAL GUIDANCE**

Our readers will no doubt be aware of the recent publicity in the media relating to letters which are being sent by HM Revenue & Customs (HMRC) to many individuals (and which will continue to be sent until Christmas) concerning underpayments of PAYE. It is estimated that some 1.4 million individuals have paid too little tax, with around 4.3 million being owed a refund. However, the average amount of underpaid tax is far greater than the average amount of refunds due.

Understandably, accusing fingers have been pointed at HMRC and this situation has been described by many as “tax chaos”, a “tax fiasco” and “yet another blunder by the tax authorities”. In this article we do not attempt to apportion blame but we do attempt to establish the facts and to explain how this situation arose. More importantly, however, we try and provide some practical advice and guidance for those who have received or may yet receive a letter concerning the underpayment or overpayment of tax.

#### **The background**

At first sight this situation appears to be entirely the fault of HMRC and many argue that this matter could have been avoided had appropriate measures been taken some years ago concerning computer software and checking systems.

The facts are relatively straight forward. The United Kingdom tax system is extremely complex, especially when compared with a number of other countries. In the past numerous governments have promised to simplify the system but, in the main, it has continued to grow like Topsy, and in certain areas has almost spiralled out of control. However, little has been done to correct the situation although, once again, we have been promised a radical overhaul of the system by the present coalition government.

Our complex tax system, coupled with drastic changes in work patterns over past years, has resulted in numerous instances where a person’s PAYE code, one of the cornerstones in computing an individual’s taxable income, is inaccurate. This may occur, for example, if an individual moves jobs, is provided with a company car or other benefits, works for only part of the year or has several sources of income. In addition, some employers may have used incorrect tax codes in past years which has resulted in an underpayment of tax.

Unfortunately a number of the above changes in circumstances remained hidden, as HMRC’s computer software was not sufficiently powerful to detect such changes and amend an individual’s PAYE code.

Enter the supercomputer which HMRC has recently installed. This computer was given the task of trawling through millions of individuals’ records and in so doing it detected a huge number of coding errors which had never been picked up in the past. Hence the avalanche of letters that are being received and will be received in the near future by many individuals.

The important point to note is that in the vast majority of cases tax is legitimately owed by many individuals (although, in a number of cases individuals will be owed a tax refund). The reason why this situation has become headline news is that large sums (on average approximately £1,400) are now being pursued by HMRC.

It should be noted that HMRC has little room for maneuver in relation to the letters being sent out for underpaid tax because it is obliged by law to collect any tax due. In addition, interest is due on any tax which is due. However, Dave Harnett, the head of HMRC, announced when he appeared before the Commons Treasury Select Committee that, as a concession, interest would not be charged for those individuals who owed more than £2,000 (see below).

It is also unfortunate that there is little likelihood of the government bailing out individuals by changing the law, as in the present economic climate the government is intent on collecting whatever revenues it can legitimately obtain.

#### **Action to be taken**

If you receive a letter from HMRC relating to underpaid tax you should contact us and we will investigate this matter and deal directly with HMRC on your behalf.

If the calculations are correct after we have checked them do not pay immediately. There may be a route to take if the circumstances warrant it. If you can prove that you had given the tax authorities and/or your employer the correct information concerning your affairs and there have been no changes to your circumstances during the past year you may be able to get the amount due cancelled.

The rules state that the tax authorities must act on relevant information within a year and make any necessary changes to your tax code. If they did not do so you may have grounds for the amount of tax owed to be cancelled. In practice this means that all your correct information must have been received by HMRC by 6 April 2009 as the errors discovered date back to April 2008.

The claim you may be able to make in the above circumstances is under an Extra Statutory Concession known as ESC A19. However it must be stressed that it is expected that only a small minority of individuals will be successful in pursuing this route.

#### **Payment of amounts due**

But what happens if you do owe any tax? As already mentioned, the average tax owed is approximately £1,400, with many sums being considerably in excess of this figure. However, a number of individuals may not be able to lay their hands on this amount immediately.

Remember that the letters being sent out at present are not demands. Individuals will be sent formal demands in January 2011. If the amount of tax due is less than £2,000 then the underpaid tax will be collected over 12 months starting in April 2011 by an adjustment being made to your PAYE code. In other words you will pay the amount due by instalment, either weekly or monthly, through your reduced wage or salary. Although the thought of not having to pay the whole amount immediately might be welcomed, remember that for an individual owing the average tax due this will mean that their net pay will be reduced by some £100 a month.

If you feel that the repayment of tax by this method will cause you financial hardship you can apply to have the repayments spread over a longer period. In addition, HMRC has announced that those individuals who owe less than £300 will not be pursued for payment of tax due.

However, if the amount due is more than £2,000, then the whole sum must be paid in one go. The individual will receive a second letter from HMRC informing him or her when the amount has to be paid. As stated earlier in this article, HMRC will not charge interest on these overdue sums.

### **NIC – MIND THE GAP**

As many of our readers will be aware, if an individual has not paid enough National Insurance contributions (NICs) in a particular tax year then that year will not count towards that individual's basic State Pension and certain bereavement benefits. The year in question is referred to as a "gap" year.

However, it is often possible for the individual to make a voluntary payment of NIC in relation to the gap year in order for that year to count when computing any State Pension or bereavement benefit that is due.

HM Revenue & Customs (HMRC) may send the individual a "Gap in your National Insurance Record" letter telling him or her that the year won't count towards State Pension or bereavement benefit. The letter explains how you can pay voluntary NICs to make the year count.

However, readers should note that HMRC has changed its approach to the sending out of gap letters and has stated as follows:

"In response to customer feedback the letters will be better targeted this year, therefore, not everyone who has a gap in their National Insurance contributions record will receive a gap letter. If you have a gap in your record and don't receive a letter you can still pay voluntary contributions."

The following is an extract from the advice given by HMRC in relation to the issuing of gap letters.

#### **Who will get a gap letter?**

Subject to certain exceptions, letters will be issued to people who are aged 35 or over at 6 April 2010 and who have not already built up the 30 'qualifying years' needed to get a full basic State Pension.

#### **If you don't get a gap letter**

If you think you have a gap in your National Insurance contributions but don't get a letter, you may still want to pay voluntary contributions in some circumstances.

People who reach State Pension age on or after 6 April 2010 need only 30 qualifying years to get a full basic State Pension and most can easily build these up without having to pay voluntary National Insurance contributions for years where they have gaps. However, eligibility for bereavements benefits (payable, if someone dies, to their spouse or civil partner if under State Pension age, and based on the deceased's National Insurance contributions) is different to eligibility for basic State Pension so you may want to pay voluntary contributions to protect your spouse or civil partner's entitlement to these.

#### **How to check if you have a gap in your National insurance record**

You can contact the HMRC National Insurance Helpline on Tel 0845 915 5996. They can check your record for the last six tax years and tell you if there is a gap. If there is, they'll tell you whether it is possible to make it up and how to pay."

## MOVING BANK ACCOUNTS – SOME PRATICAL ADVICE

In today's financial climate many of us are constantly looking for the best deals and this may well include any arrangements we have with our bank. For example, the majority of the main high street banks are now offering free banking, provided that the account remains in credit.

Those individuals (or businesses) who are not satisfied that they are getting the best deal from their existing bankers may be looking to switch accounts to another bank. At first sight this can seem a daunting task, especially for those of us who have a variety of direct debits and standing orders on their accounts and who receive credits paid directly into their account by a third party.

Indeed, in the past some banks have taken advantage of this situation and have not assisted to any great degree those who wished to move accounts. Often this was because some account holders would simply give up and remain with their bank because they could not face the upheaval of moving.

To a large degree this situation has changed due to complaints received from account holders who wished to move their account but were not assisted by their existing bank. Indeed many of the banks now have specialist teams and systems that will facilitate any moves.

Set out below are some points that should be considered should you wish to transfer your account to another bank.

- Open your new bank account.
- Inform your existing bank that you wish to close your account.
- Send letters to any persons or organisations that pay money into your account, giving them details of your new account and instructing them to pay any future payments into this account. Make sure you inform them as to the date when these new instructions will operate from or whether this is immediate. (Some banks provide pro forma letters that you can use to carry out this exercise.)
- Request a list of direct debits and standing orders from your existing bank and contact the persons or individuals to whom payments are made. In relation to direct debit payments, give these persons details of your new bank and ask that their records are amended by a certain date or immediately. (Some banks will contact those organisations to whom direct debits are made on your behalf.)

In relation to standing order payments you should cancel the existing standing orders and create new standing orders.

- Request your existing bankers to cancel all direct debit and standing order payments. Make sure you do this in writing.
- Finally, ask your existing bank to close your account and transfer any balance to your new account and send you a closing statement.

## REGIONAL EMPLOYER NICs HOLIDAY FOR NEW BUSINESSES

As outlined in this year's emergency Budget, HM Revenue & Customs (HMRC) has now launched a new regional NIC initiative. This initiative exempts businesses from paying National Insurance contributions (NICs).

The Regional Employer NICs Holiday is available to new businesses for a limited period and subject to meeting certain conditions. New businesses may be able to qualify for a reduction of up to £5,000 of the employer NICs that would normally be due - for each of the first ten employees they take on. This means a potential aid to business of up to £50,000.

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<sup>i</sup> *The articles in this newsletter are of necessity summaries of the topics covered. The publisher has taken all due care in the preparation of this publication. No responsibility for loss occasioned to any person acting or refraining from action as a result of any material in this publication can be accepted by the authors or the publishers. The publisher accepts no responsibility for the content of any material provided by third parties or for the content of any hypertext site referred to in this publication. The Publisher accepts no responsibility for the content of any website of other document referred to in this publication.*