Client Bulletin

June 2022

NATIONAL INSURANCE CHANGES

Class 1

The calculation of Class 1 National Insurance contributions is complicated for 2022/23 by the in-year change to the primary threshold. This is the point at which employees start paying National Insurance contributions on their earnings.

From 6 April 2022 until 5 July 2022, the primary threshold is set at £190 per week (£823 per month). This is equivalent to £9,880 per year. However, from 6 July 2022, the primary threshold is aligned with the personal allowance, set at £12,570. As a result, from 6 July 2022 the primary threshold is £242 per week (£1,048 per month).

As the increase in the primary threshold does not take effect until part way through the tax year, the annual threshold for 2022/23 is £11,908. This is of relevance to directors who have an annual earnings period regardless of their actual pay interval. The annual primary threshold of £11,908 is equivalent to £229 per week.

For 2022/23 employees pay primary Class 1 contributions at the main rate of 13.25% on earnings between the primary threshold and the upper earnings limit (set at £967 per week; £4,189 per month; £50,270 per year) and at the additional rate of 3.25% on earnings in excess of the upper earnings limit.

The secondary threshold is set at £175 per week (£758 per month; £9,100 per year) for 2022/23. This is the point at which employer's Class 1 National Insurance contributions start. The threshold remains the same for the full tax year; unlike the primary threshold it does not change on 6 July 2022.

Higher thresholds apply where the employee is under 21, an apprentice under the age of 25 or armed forces veteran in the first year of their first civilian employment since leaving the armed forces (all set at £967 per week, £4,189 per month; £50,270 per year) or a new Freeport employee where the employer has physical premises in a Freeport Tax Zone (set at £481 per week; £2,083 per month; £25,000 per year).

The secondary Class 1 rate is 15.05% for 2022/23.

It is important that the thresholds used are those that apply at the time that the payment is made; the higher primary threshold should not be used where payment is made before 6 July 2022.

We can help you check you are calculating Class 1 contributions correctly for 2022/23.

Employment Allowance

Eligible employers can claim the National Insurance Employment Allowance which reduces the amount of employer's Class 1 National Insurance that they pay. The allowance is not available to employers whose secondary Class 1 liability in 2021/22 was £100,000 or more. Personal companies where the sole employee is also a director are not able to benefit from the allowance either (although it can be claimed by family companies with at least two employees).

The allowance is set at £5,000 for 2022/23. It can be claimed through the payroll. Where the employer's Class 1 liability for 2022/23 is less than £5,000, the allowance is capped at the liability for the year.

We can help you claim the employment allowance to reduce your National Insurance bill.

Class 4

Class 4 National Insurance contributions are paid by the self-employed where their profits are more than the lower profits limit. This is aligned with the annual primary threshold, and is set at £11,908 for 2022/23. Contributions are payable at the main Class 4 rate (10.25% for 2022/23) on earnings between the lower profits limit and the upper profits limit, set at £50,270 for 2022/23, and at the additional Class 4 rate of 3.25% on earnings in excess of the upper profits limit.

We can help you calculate your Class 4 National Insurance liability.

Class 2

Currently Class 2 contributions are payable by the self-employed where profits exceed the small profits threshold, set at £6,725 for 2022/23. Where profits are less than this, Class 2 contributions can be paid voluntarily to maintain the earner's contribution record.

However, new legislation provides for regulations to be made to align the starting point for Class 2 contributions with that for Class 4 (£11,908 for 2022/23) and also for regulations to be made, with retrospective effect no earlier than 6 April 2022, for self-employed earners with profits below the new threshold and at least equal to the small profits threshold to be treated as if they have paid a Class 2 contribution. This will provide them with a qualifying year for zero contribution cost.

At the time of writing the regulations to give effect to this measure had not yet been made.

We can help you understand your Class 2 liabilities and the impact of your contribution record on your state pension entitlement.

TAX-EFFICIENT PROFIT EXTRACTION

Optimal salary for 2022/23

Where a business is operated as a personal or family company, profits will need to be extracted from that company if they are to be used in a personal capacity. There are various ways of extracting profits, but from a tax perspective, not all extraction methods are equal.

A popular and tax efficient strategy is to take a small salary and to extract any further profits as dividends where these are needed outside the company.

The optimal salary will depend on personal circumstances and whether the employment allowance is available. However, it is beneficial to pay a salary that is at least equal to the lower earnings limit for National Insurance of £6,396 for 2022/23 to ensure the year is a qualifying year for state pension purposes (unless the recipient already has the 35 qualifying years needed for a full state pension).

Where the employment allowance is not available (as is the case for a personal company where the sole employee is a director), the optimal salary for 2022/23 is equal to the annual primary threshold of £11,908, provided that the director has at least £11,908 of his or her personal allowance available to shelter the salary from tax.

Where the employment allowance is available, the optimal salary for 2022/23 is equal to the personal allowance of £12,570, as long as this has not been used elsewhere.

We can help you determine your optimal salary for 2022/23 depending on your personal circumstances.

Dividends

Once the optimal salary has been paid, if further profits are available and are required outside the company, it is more tax-efficient to take these as dividends. Remember, dividends can only be paid if there are sufficient retained profits from which to pay the dividend, and must be paid in proportion to shareholdings (although the use of an alphabet share structure can provide valuable flexibility).

Dividends can be paid tax-free where they are sheltered by any remaining personal allowance or by the dividend allowance (set at £2,000 for 2022/23. Thereafter, they are taxed at 8.75% where they fall within the basic rate band, 33.75% where they fall within the higher rate band and at 39.35% where they fall within the additional rate band.

Using an alphabet share structure and paying dividends to family members to utilise unused dividend allowances and basic rate bands can efficient.

We can help you formulate a tax-efficient dividend policy for your company.

MAKING TAX DIGITAL

MTD for VAT

All VAT-registered businesses are now within MTD for VAT and VAT-registered businesses with turnover below the VAT registration threshold of £85,000 which have not already signed up to MTD for VAT voluntarily must comply with the requirements from the start of their first VAT accounting period beginning on or after 1 April 2022. Under MTD, records must be maintained digitally and VAT returns must be filed digitally using MTD-compatible software.

If you are new to MTD for VAT, we can help you meet your obligations.

Basis period reform

MTD for Income Tax will apply to businesses and landlords in relation to their trading and property income where their gross income from these sources is more than £10,000 for the tax year from 6 April 2024. Ahead of its introduction, the rules on basis periods are being reformed.

Currently, the current year basis applies to unincorporated businesses under which once the business is up and running it is taxed on the profits for the accounting period that ends in the tax year (so, for example, the profits for the year to 31 December 2022 are taxed in 2022/23). Different rules apply in the opening and closing years of the business.

However, from 2024/25, profits will be taxed on a tax-year basis, so that the profits for 2024/25 will be those for the period from 6 April 2024 to 5 April 2025. Where the accounting period is different to the tax year, apportionment will be needed to arrive at the profits for the tax year.

To move from the current year basis to the tax year basis, 2023/24 will be a transitional year.

We can explain what the change in the rules will mean for your business, and what you need to do to prepare. We can also help you get ready for MTD for ITSA.

CAPITAL ALLOWANCES

Annual Investment Allowance

The Annual Investment Allowance (AIA) allows businesses to deduct qualifying expenditure up to the available limit when calculating profits, providing immediate tax relief for the expenditure. The AIA is available to unincorporated businesses and to companies.

The temporary limit of £1 million, which has applied since 1 January 2019, comes to an end on 31 March 2023. From 1 April 2023, it is due to revert to its permanent level of £200,000. Transitional rules apply where an accounting period spans 31 March 2023, and these can operate harshly.

If you are planning significant capital expenditure, we can help ensure that you optimise the relief and don't fall foul of the transitional rules.

Super-deduction

Companies can claim a super-deduction for most expenditure that qualifies for main rate capital allowances where that expenditure is incurred between 1 April 2021 and 31 March 2023. The main exclusion is expenditure on cars. The super-deduction provides an enhanced deduction of 130% of the expenditure.

If you run your business as a company, time is limited to take advantage of the super-deduction (which provides a better rate of relief than the AIA).

We can help you plan your capital expenditure to make best use of the available reliefs.

50% first-year allowance

Companies can also benefit from a 50% first-year allowance for qualifying expenditure incurred in the period from 1 April 2021 to 31 March 2023 which would otherwise qualify for special rate writing down allowances of 6%.

The allowance is beneficial where the AIA limit has been used up.

We can help you plan your capital expenditure to take advantage of the time-limited reliefs.