

Overview

Darling's last stand

The last Pre-Budget Report before the election was billed as the Chancellor's chance to say how the huge financial deficit would be closed.

In that respect it was a bit of an anti-climax. It was fiscally neutral with any tax raised being spent on social or environmental measures. He indicated when and by how much he expected the deficit to come down but without giving any real idea of where the necessary spending cuts would fall. Indeed he confirmed that Government spending would be maintained for next year.

The tax on banker's bonuses which had been widely trailed was duly announced. Much of the other pre speech speculation was wide of the mark, however. The political content of the tax changes was less than expected and the speech was received in a fairly low key manner – the biggest cheer of the day was reserved for the cut in bingo duty!

The Chancellor said that it was important not to stifle the economic recovery by cutting spending too soon. That is a widely held view but it remains to be seen whether or not the financial markets will have confidence in his medium term plan of campaign without a few more specifics.

It is perhaps too much to expect bravery from a politician in a pre election period.

Bob Wheatcroft

Rates and Allowances for 2010/11

The Pre-Budget Report contained few surprises with regard to rates and allowances for the tax year 2010/11. The announcements are summarised below.

Income Tax

The main rates of Income Tax will remain at 20% for basic rate taxpayers and 40% for higher-rate payers. As previously announced, a new additional rate of 50% will apply to income exceeding £150,000.

Allowances and thresholds will remain frozen at current levels. The basic Personal Allowance for 2010/11 will therefore be £6,475, but the 2009 Budget announcement regarding the abatement of the Personal Allowance for those with income in excess of £100,000 is still due to take effect from April 2010.

National Insurance

Again, the rates and thresholds for payment of National Insurance Contributions will remain unchanged in 2010/11. The 0.5% increase in National Insurance planned to take effect from April 2011 will now be a 1% increase.

Tax Credits and Child Benefit

The child and disability elements of the Child Tax Credit, all elements of the Working Tax Credit, Child Benefit and Guardian's Allowance are all due to increase with effect from April 2010.

VAT

As expected, the standard rate of VAT will revert to 17.5% with effect from 1 January 2010.

Stamp Duty Land Tax

As previously announced, the SDLT holiday for residential properties with a value up to £175,000 will end on 31 December 2009.

Inheritance Tax

The Inheritance Tax Nil Rate Band

Inheritance Tax is chargeable at 40% on the value of a chargeable transfer which exceeds the Nil Rate Band. In 2007 it was announced that the Nil Rate Band for 2010/11 would increase to £350,000 however the 2009 Pre-Budget Report has stopped this planned increase. The Nil Rate Band for 2010/11 will instead be frozen at the current year's rate of £325,000.

Inheritance Tax – Anti Avoidance

Anti avoidance legislation has been introduced to prevent the future use of two Inheritance Tax planning schemes. One of these schemes involves the purchase of a life interest in a Trust, the other involves placing assets into a Trust in which you retain a future interest. The legislation will impose a future Inheritance Tax charge for persons who enter into these schemes on or after 9 December 2009.

Furnished Holiday Lettings

As announced in the Budget the furnished holiday lettings rules are to be repealed from April 2011, following which the tax treatment of such lets will mirror 'regular' lettings.

In the current tax year income from 'Furnished Holiday Lettings' is treated differently to other rental receipts. The rules provide that such income is deemed to be trading income, giving advantageous treatment in terms of losses, use of the income as relevant for pension premiums, and beneficial Capital Gains Tax treatment.

From April 2010 this change will affect the way losses from the letting the property can be used for loss relief purposes. From this date any losses carried forward will be available for offset against the property business. The lettings will cease to benefit from the Capital Gains Tax relief such as entrepreneurs' relief, roll-over relief and relief for gifts of business assets. Furthermore, capital allowances will not be available for expenditure incurred after this date on plant and machinery for use within the let property.

It also appears likely that the beneficial treatment of such properties for Inheritance Tax purposes will also be much more difficult to obtain in the future.

Individuals with furnished holiday lettings should be considering how this change will affect them and whether they should be examining planning strategies to mitigate the effect of some of these changes.

Offshore Evasion

Legislation is being brought forward to ensure that individuals who fail to declare offshore tax liabilities will face the tough penalties attracted by deliberate tax evasion. There will also be a new requirement to notify HMRC when opening offshore bank accounts in certain jurisdictions, supported by a separate penalty regime. Evading tax offshore could therefore result in combined penalties of up to 200 per cent of the unpaid tax.

HMRC is gaining access to data from over 300 financial institutions on UK taxpayers with offshore accounts. The 'New Disclosure Opportunity' gives those with undeclared offshore assets a final opportunity to come forward to pay tax, interest and a reduced penalty. The deadline for notifications is 4 January 2010 - if offshore tax evaders do not come forward now, they can expect much tougher penalties in the future.

Equitable Liability

Under Self Assessment, there is a statutory requirement to file a return, the information on which is used to assess the tax due for the period. HM Revenue & Customs is able to issue estimates of the tax due in the absence of a return.

Once issued, the determination of tax due can only be replaced by the taxpayer filing a tax return within five years from the statutory filing date or 12 months from the issue of the determination.

By concession, HMRC has only collected the sum which would have been due if the return had been filed on time, providing the taxpayer brought his tax affairs up to date and could show the correct amount of tax due.

This concession is now to be legislated for. The measure does not alter the statutory deadlines for filing a return and penalties and interest will continue to apply where deadlines are not met and tax is not paid when due.

Capital Gains Tax: Private Residence Relief and Adult Placement Carers

Where an individual has used part of their main residence for their business there is a restriction which prevents a claim for Private Residence Relief on that part of the home used in the business. However, as a concession HMRC has announced that where part of the home is set aside for use under a local authority adult placement scheme, legislation will be introduced to ensure that the carer's entitlement to full relief continues despite their business as a carer.

Shared Lives Carers

Legislation will be introduced in Finance Bill 2010 to establish a new income tax relief for qualifying Shared Lives carers. The new relief will be similar to the current Foster Care relief. The relief will consist of a tax-free allowance. Carers whose Shared Lives earnings are less than the tax-free allowance will not be taxed on their income from providing Shared Lives care.

This will apply to Shared Lives carers (including adult placement carers, Staying Put carers and those receiving a Scottish Kinship Care Allowance), who:

provide accommodation, care and support for up to three individuals who have been placed with them under a local authority Shared Lives placement scheme; and

share their home and family life with the individuals placed with them under the Shared Lives scheme.

Corporation Tax

The planned increase in the small companies' rate from 21% to 22%, scheduled to take effect from April 2010, is now deferred until April 2011.

Capital Allowances

Presumably in an attempt to prove his green credentials, the Chancellor announced that new electric vans will qualify for 100% first year allowances. This will have effect from 1 April 2010 (for companies) and 6 April 2010 (for unincorporated businesses) subject to the State aid rules. Second hand vans will not qualify. Electric cars and cars with Co2 emissions of not more than 110g/km already qualify for 100% capital allowances.

There were several anti avoidance measures announced regarding capital allowances. The first one is designed to stop companies in tax motivated transactions which acquire an interest in an "excess of allowances". This is defined as where the tax written down value exceeds the balance sheet value. This happens frequently in the commercial world and the Budget notice states that only tax motivated transactions will be affected. Rules already announced in July 2009 were designed to restrict the utilisation of losses by groups of companies that are created by an excess of capital allowances. The change in the Pre-Budget Report is to extend these rules to include the situation where an unincorporated shareholder sells a company with an excess of allowances to a group in a tax motivated transaction.

There were also a couple of anti avoidance measures involving the leasing of plant and machinery. These will have effect from 9 December 2009 and are aimed to ensure that:

- lessor companies are unable to generate tax losses using arrangements intended to result in tax relief in excess of the value of taxable income; and
- businesses are prevented from turning a timing advantage into a permanent tax reduction by ceasing to be within the charge to tax following the sale of the right to income from a lease of plant and machinery.

Research & Development (R&D) tax relief made more widely available

R&D tax relief will be available to companies regardless of whether or not they have, or retain an interest in, the intellectual property developed through the R&D process. This applies to 'SME' companies for their accounting periods ending after 9 December 2009. SMEs will be able to take advantage of this change whether they

claim under the SME R&D scheme or the large-company R&D scheme (which is available for those whose R&D is grant-funded and never required the IP to be owned by the company).

This will help university spin outs which in the past have been excluded from relief if IP remains with the university.

Companies in this field may wish to consider extending their accounting periods to take advantage of this relief sooner.

www.armstrongwatson.co.uk/r-and-d

10% rate on income from UK patents

From April 2013 a reduced rate of corporation tax of 10% will apply to income arising from new UK patents. Details of this are not expected to come until late 2010 (as the legislation will be introduced in Finance Act 2011) and so it is not yet clear whether this rate will apply only to royalties or also to sale of goods protected by patents.

In any event we would expect to see an increase in the number of new patents registered in the UK as many businesses have been reluctant to register patents due to the costs involved. This relief should negate that financial issue; however, enforceability of patents will remain a commercial issue.

EIS / VCTs

Although no specific proposals were made it is understood that the scope of EIS and VCT tax relief is going to be restricted so that they only apply to smaller companies. These remain very valuable reliefs and importantly there will not be any change to the relief that investors can claim. EIS therefore remains a valuable tool in:

- planning for relief from income tax, capital gains tax and inheritance tax; and
- for companies to use when seeking investment.

EMI share options

Changes may be made to the rules relating to Enterprise Management Incentives (EMI) share option schemes to ensure that the European Commission approves the schemes for State Aid purposes.

Film Tax Credits

Film production companies making films with production spends spread across two or more accounting periods have been unfairly restricted in the maximum tax credit claimable. This anomaly has occurred when the proportion of UK spend has increased in the second accounting period.

The legislation is to be amended to ensure that, where the proportion of UK spend increases in the second accounting period, film production companies will not be restricted in their claim for tax credits. This applies for accounting period ended on or after 9 December 2009.

Sale of Lessor Companies

Sale of Lessor Companies: Alternative Treatment

This only affects companies carrying on a business of leasing plant or machinery.

When a lessor company changes hands there is a tax timing benefit for the selling group. Schedule 10 of FA 2006 imposes a tax charge which prevented this loss of tax, but because of the challenging economic times the measure has affected normal commercial transactions.

The Pre-Budget Report has announced that from 9 December 2009 the lessor company can elect for an alternative treatment, removing the need to calculate an immediate charge, this is done by isolating the profits of the business following the sale of the company.

Sale of Lessor Companies: Consortium Arrangements

When the lessor company is owned by a consortium of companies it was previously possible to structure the arrangement to avoid the above tax charge, this is now being prevented by altering the definition of a company owned by a consortium to include those owned indirectly.

Employee Benefit Trusts (EBTs)

Surprisingly, despite all the noises made by HM Revenue & Customs recently in respect of EBTs, there was no announcement in the Pre-Budget Report in relation to either the PAYE/NIC aspects of EBTs or the Inheritance Tax position.

Therefore, EBTs remain a useful tool to extract surplus cash and assets from a company, to improve a shareholder's Capital Gains Tax or Inheritance Tax position of their shareholding or to provide tax efficient loans to employees.

Of course, changes may occur in the next Budget, rumoured to be in February, so now may be the time to undertake such planning.

Employment Tax

Main points

- Significant increases to the rates at which employers and employees pay National Insurance.
- Significant changes to the amounts on which employees pay tax on company car and fuel benefit and on which employers pay Class 1A National Insurance. The cost to employers is increased further by the increase in the rate of Class 1A National Insurance from 6 April 2011.

Other points

- HMRC is considering the policy and practicalities of allowing large connected employers to combine or pool their PAYE references, thereby reducing their administration time and costs.
- HMRC and the Department for Business, Innovation and Skills are to consult in the New Year on proposed changes to the National Minimum Wage Regulations to tackle the problem of arrangements commonly called "travel schemes".
- Changes may be made to the rules relating to Enterprise Management Incentives (EMI) share option schemes to ensure that the European Commission approves the schemes for State Aid purposes.
- Restriction on the tax exemption for workplace canteens.

National Insurance Contributions (NIC) rates and thresholds

No major changes were made to the previously announced rates and thresholds for 2010/11 but the previously announced 0.5% increase in NIC from 2011/12 has been doubled to 1%.

The main rates of Class 1 and 4 NIC from 6 April 2011 will be 12% and 9% respectively, Class 1 employer rate 13.8% (including Class 1A and 1B), and the additional rate of Class 1 and Class 4 NIC, payable on earnings above the annual earnings limit, will be 2%.

The primary threshold and lower profits limit will be increased by an extra £570 for 2011/12 to compensate lower earners, meaning people earning £20,000 or less will be no worse off as a result of the 1% increase to the main rate of NIC.

Car and car fuel benefit

Company car drivers who are provided with cars which are wholly electrically propelled will not have to pay tax on the car and fuel benefit. This measure is to take effect from 6 April 2010 for a period of five years. The benefit will also be exempt from employer Class 1A National Insurance, resulting in savings for both employee and employer.

From 6 April 2010, the lower threshold (the CO₂ emissions figure which sets the 15 per cent rate) for all other cars will be reduced from 135 to 130 g/km.

From 6 April 2011:

- there will no longer be any reductions for alternative fuels (hybrids, bi-fuels and cars manufactured to run on E85 – types H, B and G)
- the diesel surcharge will apply to all diesels (including type L diesels approved to Euro IV emissions limits and first registered before 1 January 2006)
- the £80,000 limit for the price of a car for car benefit purposes will no longer apply
- the lower threshold (the Co₂ emissions figure which sets the 15 per cent rate) will be reduced from 130 to 125 g/km

From 6 April 2012 the current graduated table of company car tax bands will be extended down and all Co₂ emissions thresholds moved down by 5g/km so that the 10 per cent band will apply to company cars with Co₂ emissions up to 99g/km. Qualifying Low Emissions Cars (QUALECs) will therefore no longer exist as a separate category.

The effect of the above changes is that the car benefit figure, on which employees pay tax and employers pay Class 1A National Insurance, will increase year on year for most employees and employers over the next few years. The only way of reducing these increased costs appears to be by adopting an increasingly green fleet policy, which can take time and is not always practical. The costs for employers are further increased from 6 April 2011 by the increase in the rate of Class 1A National Insurance from 12.8% to 13.8%.

Company car drivers who are provided with fuel for private use will see a significant increase in the tax charge on the 'benefit' from 6 April 2010. The fuel multiplier on which the appropriate emissions based percentage is applied is to increase from £16,900 to £18,000. In many cases the tax cost of the 'benefit' may be more than the cost of the private fuel used and relinquishing the 'benefit' can result in substantial cost savings for both the employer and employee.

Employers will also see a significant increase in employer Class 1A National Insurance on car fuel benefit. The employer Class 1A National Insurance cost will also be increased further from 6 April 2011 by the increase in the rate from 12.8% to 13.8%.

Van and van fuel benefit

Company van drivers who are provided with electric vans will not have to pay tax on the van benefit. The van benefit legislation will be amended to include a definition of an electric van for this purpose. This measure is to take effect from 6 April 2010 for a period of five years. The benefit will also be exempt from employer Class 1A National Insurance, resulting in savings for both employee and employer.

With the exception of the exemption for electrically propelled vans, no change has been announced to the flat rate figure of £3,000 on which van benefit is charged.

The flat rate figure on which van fuel benefit is charged is to be increased from £500 to £550 from 6 April 2010.

PAYE Scheme Pooling

HMRC is considering the policy and practicalities of allowing large connected employers to combine or pool their PAYE references, thereby reducing their administration time and costs. HMRC has already carried out informal discussions about PAYE pooling with selected employers and representative bodies. Following on from this HMRC expects to publish draft PAYE Regulations for formal consultation early in 2010 in order to seek wider views and comments.

National Minimum Wage and "Travel Schemes"

HMRC and the Department for Business, Innovation and Skills are to consult in the New Year on proposed changes to the National Minimum Wage Regulations to tackle the problem of arrangements commonly called "travel schemes". Travel schemes" take advantage of the tax and National Insurance expenses rules relating to travel to a temporary workplace. Where temporary workers paid through such arrangements are paid at or near the NMW, such arrangements are potentially exploitative as they can impact adversely workers' entitlements to earnings related social security benefits.

Enterprise Management share option schemes

Changes may be made to the rules relating to Enterprise Management Incentives (EMI) share option schemes to ensure that the European Commission approves the schemes for State Aid purposes.

Restriction on the tax exemption for workplace canteens

This will only affect employees and employers who use the exemption in conjunction with salary sacrifice or flexible benefit arrangements. Such arrangements are intended to allow some employees to purchase canteen meals out of gross pay and

hence obtain a significant tax advantage over the majority of employees who purchase meals using their net pay. The legislation will not affect general canteen subsidies that are available to all employees, for example where the employer provides a subsidy that is reflected in lower canteen prices. The legislation will take effect from 6 April 2011.

Bank Payroll Tax

A new Bank Payroll Tax (BPT) of 50% is to be introduced, payable by the bank, on bonuses over £25,000 paid to employees. The bank is also liable where an intermediary provides the bonus. The tax is effective immediately until 5 April 2010, for all discretionary and contractual bonus awards, with an exception for contractual obligations already existing.

For the purposes of BPT, banking employment is one where the duties are wholly or mainly concerned with activities regulated by the Financial Services and Markets Act 2000.

BPT is payable 31 August 2010.

Stamp Duty Land Tax

As previously announced, the SDLT holiday for residential properties with a value up to £175,000 will end on 31 December 2009.

SDLT avoidance disclosure

SDLT avoidance schemes are to be disclosed to HMRC on residential property with values over £1,000,000.

This will come in from April 2010 and will follow the same format as the current disclosure requirement for commercial property with values over £5,000,000.

Interestingly these rules will involve a 'grandfathering' provision which will exempt current structures from the disclosure requirement. The implication here is that HMRC is happy that it has sufficient details of current schemes to be able to target those that do not work. This implication ties in with recent commentary that HMRC is looking to challenge schemes based on sub-sale relief which have made up a significant part of the SDLT avoidance market.

Structures involving an indefinite deferral of an SDLT trigger should remain as robust planning tools.

VAT

VAT will return to 17.5% on 1 January 2010. The grace period for certain businesses trading across the midnight deadline to charge the lower rate has been confirmed as until either when they close, or if earlier, 6.00am.

The rates used in the Flat Rate Scheme were changed on 1 December 2009 to reflect the change in the standard rate of VAT to 15%. HMRC has taken the opportunity to re-align some of the flat rate schemes' percentages under the guise of the re-introduction of the 17.5 per cent rate. Particular sectors adversely affected are:

- agricultural services
- post offices
- businesses supplying forestry and fishing rights.

Do not assume that other flat rate percentages return to pre 1 December 2008 levels.

It should also be noted that as of 1 January 2010 the package of changes to simplify and modernise the VAT system for cross-border trading and to counter fraud will come into effect across the European Union. The package includes:

- new time of supply rules for services
- European Sales List (ESL) reporting for supplies of cross-border services and changes to ESLs for goods
- a new electronic refund procedure for VAT incurred in other EU Member States.

These items were discussed in Budget 2009 and reported in budget notices BN75, BN76, and BN77 respectively.

Climate Change Levy

Legislation will be introduced in Finance Bill 2010 to amend the reduced rate of climate change levy from 20 to 35 per cent.

Following Royal Assent of Finance Bill 2010, secondary legislation will be introduced to require relief claimants affected by the change in the reduced rate to give their energy suppliers fresh certificates confirming their new relief entitlement.

Hydrocarbon Oils Duty Rates

The current 20 ppl duty differential for biodiesel and bioethanol will cease from 1 April 2010, and duty will thereafter be charged at the same rate as main road fuels. It was announced in Budget 2009 that main road fuels will be increased on 1 April each year from 2010 to 2013 by 1 ppl above indexation.

A relief scheme will be introduced so that producers can continue to benefit from a 20 ppl duty differential in relation to biodiesel produced only from waste cooking oil.

The scheme will allow producers to offset an allowance of 20 ppl against duty that is payable.

With effect from 1 January 2010 the rates will be as follows

Category of business	Appropriate percentage
Accountancy or book-keeping	13
Advertising	10
Agricultural services	10
Any other activity not listed elsewhere	10.5
Architect, civil and structural engineer or surveyor	13
Boarding or care of animals	10.5
Business services that are not listed elsewhere	10.5
Catering services, including restaurants and takeaways	11
Computer and IT consultancy or data processing	13
Computer repair services	9.5
Dealing in waster or scrap	9.5
Entertainment or journalism	11
Estate agency or property management services	10.5
Farming or agriculture that is not listed elsewhere	6
Film, radio, television or video production	11.5
Financial services	12
Forestry or fishing	9.5
General building or construction services*	8.5
Hairdressing or other beauty treatment services	11.5
Hiring or renting goods	8.5
Hotel or accommodation	9.5
Investigation or security	10.5
Labour-only building or construction services*	13
Laundry or dry-cleaning services	10.5
Lawyer or legal services	13
Library, archive, museum, or other cultural activity	8.5
Management consultancy	12.5
Manufacturing fabricated metal products	9.5
Manufacturing food	8
Manufacturing that is not listed elsewhere	8.5
Manufacturing yarn, textiles, or clothing	8
Membership organisation	7
Mining or quarrying	9
Packaging	8
Photography	10
Post offices	4.5
Printing	7.5
Publishing	10
Pubs	6
Real estate activity not listed elsewhere	12.5
Repairing personal or household goods	9
Repairing vehicles	7.5
Retailing food, confectionary, tobacco, newspapers, or children's clothing	3.5

Category of business	Appropriate percentage
Retailing pharmaceuticals, medical goods, cosmetics, or toiletries	7
Retailing that is not listed elsewhere	6.5
Retailing vehicles or fuel	6
Secretarial services	11.5
Social work	10
Sport or recreation	7.5
Transport or storage, including couriers, freight, removals, and taxis	9
Travel agency	9.5
Veterinary medicine	10
Wholesaling agricultural products	7
Wholesaling food	6.5
Wholesaling that is not listed elsewhere	7.5

Pensions

Further restriction of tax relief on pensions

The Chancellor announced that employer pension contributions will be included in higher-rate tax relief restrictions. He confirmed he would restrict higher-rate tax relief on pension contributions for people with incomes over £150,000 from April 2011 - a move he originally announced in his Budget in April. However, he outlined today that employer pension contributions will now be included in the restrictions and that the earning point at which individuals will be affected will reduce to £130,000.

He is now effectively saying anyone earning above £130,000 is going to see their tax relief restricted to basic rate. The Government predicts the new rules will affect an extra 85,000 people, 300,000 compared to 215,000 originally. But Standard Life believes the new restrictions could affect 150,000 additional people.

Changes to expected rollout of "personal accounts"

As part of measures to save £5bn from spending programmes the Chancellor announced a phasing-in of the roll-out of pension personal accounts - although no detailed timetable was put forward. However, earlier reports that the 2012 deadline would be set back by a year have been denied by the Department for Work and Pensions.

Personal Accounts are aimed at ensuring low-paid workers not in a company pension scheme have an income in retirement on top of the basic State Pension. Under the proposal, employers would be forced to contribute to Personal Accounts unless they choose to opt out and implement alternative pension measures for staff.