

Emergency budget 2010

Emergency budget report - 22 June 2010...

On 22 June George Osborne delivered his Emergency Budget on behalf of the new Coalition Government. The emphasis was on tough choices and the Chancellor promised that he was not going to hide away the details of his announcement in the press releases that historically follow. Normally, once the Chancellor has sat down, we then have to review a great number of press releases and budget notes, some containing measures which were not even hinted at in the main speech. It would seem that this time the Chancellor has indeed covered most of the key changes in his speech. The expected capital gains increases were delivered along with the widely anticipated increase in VAT - although this announcement was met with much noise from the other MPs.

This publication contains a summary of the key announcements and how they may affect you.

Capital gains tax

As expected, there are changes to Capital gains tax (CGT).

For individuals with total income and capital gains above £37,400 for the tax year 2010/11 (after annual exemptions, losses and other appropriate reliefs), the CGT rate increased from midnight on 22 June 2010 to 28%, up 10%. Those whose income and gains are less than £37,400 continue to pay CGT at 18%.

For trustees and personal representatives of deceased persons, the new 28% rate of capital gains tax applies from 23 June 2010. The current annual exemption of £10,100 for gains in 2010/11 remains, and will increase in future.

Perhaps a little surprising was the inclusion of a substantial increase in the lifetime limit of entrepreneurs relief; from £2m (as introduced with effect from 6 April 2010, having been £1m before) to £5m from 23 June 2010. This may help serial entrepreneurs who have already utilised the £1m or £2m limit and will substantially extend the benefit to those selling businesses or other qualifying assets from 23 June onwards by preserving an effective 10% rate of tax on these gains.

We have experienced a period of uncertainty since May when an increase in capital gains tax was announced but without any detail. For basic rate taxpayers, the retention of the 18% rate of CGT will be welcome news. For those realising gains (which will render them higher rate taxpayers), the top CGT rate of 28% is not as high as was feared. For higher rate taxpayers, a capital gain on the sale of an investment asset will still face lower rate of tax than any income that asset generates, since the income may be taxed at 40 or 50%. Ensuring that capital gains qualify for entrepreneurs relief will become even more important for business owners now that the relief affords an 18% tax saving. The relief can apply for gains up to £5m – a maximum lifetime tax saving of £900,000 compared with £80,000 per person when the relief was first introduced.

Change in VAT rate

As was widely anticipated, the current standard rate of VAT is to increase to 20%.

The increase is effective from 4th January 2011. As a consequence, the VAT fraction will change from 7/47ths to 1/6th from that date. This will have a knock on effect in areas such as Flat Rate Scheme rates, Motoring Fuel Scale Charge rates etc. As with previous 2008/2009 rate changes, transitional procedures will need to be observed - mainly devised to forestall certain VAT avoidance measures by business.

There were no changes to the zero-rate, reduced rate or VAT exempt categories of transactions. This means that the taxation of many basic foodstuffs, children's clothing, books, newspapers, health and education, domestic fuel and power and all other supplies falling outside the standard-rating remains unchanged.

There are no changes to the Cash Accounting or Annual Accounting schemes.

There is a minor change to the threshold for businesses exiting the flat rate scheme. Currently a business must leave the scheme if its annual turnover exceeds £225,000. From 4th January, this level will increase to £230,000 in order to reflect the increase in the VAT rate. The threshold for businesses eligible to join the scheme remains at £150,000.

Insurance premium tax will increase in line with VAT increases.

It is likely that many businesses will be encouraging consumers to buy before the traditional January sales to beat the VAT increases. If you are a VAT exempt business, or you are otherwise unable to reclaim VAT on your expenses, you may want to see what expenditure you can advance prior to the VAT increase. Make sure however that the anti forestalling rules don't apply and consider other taxes prior to taking any action.

This is another good reason to get your tax return information to Sagars in good time – if we are able to prepare your tax return before 4 January 2011 we can bill you at the 17.5% rate of VAT rather than the new rate of 20%.

VAT Anti-forestalling legislation

From 22nd June, any arrangements that purport to apply the 17.5% VAT rate to goods or services to be delivered or performed on or after the rate change date of 4th January 2011 will be subject to a supplementary charge of 2.5%. This measure is likely to apply only to those transactions where artificial steps have been taken to apply the former

17.5% rate where the increased rate would otherwise have applied. The measure is likely to be similar if not identical to that introduced prior to the VAT rate increase on 1st January 2010. The anti-forestalling element will apply only to such transactions where the value of the supply is £100,000 or more.

Furnished holiday lets

The Chancellor announced that the advantageous rules for furnished holiday lets (FHLs) will remain in place. This clarifies an area of uncertainty that has been hovering since last December when it was announced that the favourable rules would end from 6 April 2010.

This means that if you own a qualifying FHL property, you can claim capital allowances on assets in the property, offset any losses against other income and potentially claim inheritance tax relief on their value. Since 6 April 2009, the rules have been extended to include properties in the European economic area.

The government will consult on amendments to the current rules to take effect in 2011/12 and it is anticipated that they will increase the number of days a property must be let before it qualifies.

This is really good news for anyone who owns (or is considering acquiring) a FHL. It ends months of uncertainty about the future tax treatment of FHLs which may have meant that some investors have either looked to sell or refrained from acquiring other such properties.

Corporation tax changes

The Chancellor declared significant changes to corporation tax.

From 1 April 2011 the small companies rate of tax will reduce by 1% to 20%. At the same time, the main rate of corporation tax will reduce by 1% to 27%. In each subsequent year, the main rate will reduce by a further 1% until it reaches 24%.

The small companies rate applies to a standalone company with profits up to £300,000 whilst the main rate applies for those with profits above £1,500,000 and a marginal rate operates for those with profits in between. As the main rate falls each year, the marginal rate will also fall (it's currently 29.75% but will end up at 25%).

Lower corporation tax bills will be welcomed by companies, although some of the other announced changes (such as capital allowances and VAT) may counter some of the benefits to owner managed businesses. Given the maximum rate of income tax is now 50%, this may create a further incentive for unincorporated businesses to consider incorporation again.

Capital allowance changes

It was announced that from April 2012 the Annual Investment Allowance (which allows many businesses to benefit from 100% tax relief on plant and machinery acquired for business use) will reduce from its recently increased level of £100,000 to £25,000.

At the same time, the writing down allowance on plant and machinery pools which was recently reduced from 25% to 20%, will decrease again to 18%. Long life assets, integral features and cars with CO₂ emissions above 160g/km will decrease from 10% to 8% per annum. A hybrid rate will apply for periods straddling before and after April 2012.

The only positive news was for anyone buying new zero emissions goods vehicles for use in their business. If acquired in the five years from 1 April 2010 (6 April for unincorporated businesses), they

can attract 100% tax relief on acquisition.

Many smaller businesses will find that the proposed annual investment allowance still provides full tax relief for capital expenditure and these new rules may not have much effect.

However, any business which has to purchase equipment above the £25,000 level will find that their tax relief on such expenditure is slowed, which may well counter any corporation tax reductions if they are operating via a company. If you spend £100,000 per annum on plant and machinery, from 2012 your tax relief may reduce from the full £100,000, to £38,500 in year 1 and 18% reducing balance on the remaining £61,500 thereafter. An unincorporated business may find the additional tax cost from reduced allowances to be significant particularly if they are paying tax at 50%.

Anti avoidance

Very rarely does a budget pass without a raft of anti avoidance measures aimed at closing down obscure and highly technical loopholes that have been exploited.

This emergency budget included the announcement that a general anti avoidance rule was being considered and promised further changes to be implemented from April 2011 to counter tax avoidance using employee trusts (mainly "EBT" and "EFRBS" type arrangements).

It is intended that inheritance tax will be included within the "DOTAS" rules which require notice of any tax avoidance schemes to be given to HM Revenue and Customs.

Tax relief for new businesses

Start up businesses outside of the South East will benefit from a £5k exemption from employer National Insurance for each of the first 10 employees during the first 12 months of employment. Further details are to be announced.

This may prove to be a helpful incentive for new businesses taking on employees, provided the rules are easy to apply and don't require businesses to spend large sums of money getting advice on how to take advantage of it.

Pensions

The Chancellor acknowledged that the changes which have been implemented (and those planned to take place from 6 April 2011) in relation to the tax relief on pension contributions are complex and unwieldy. In view of this, although without giving too much away, the Chancellor stated that the government would be working with the pensions industry towards an alternative more straightforward regime that will yield a similar level of tax revenue to the current legislation, due to take effect next year.

Also with effect from budget day those aged below 75 will not be required to purchase an annuity or secure an income until they reach 77 (rather than 75). The rules are due to be finalised next year so if someone is near the age of 75 but has not yet taken action, they can delay doing so until the new rules are introduced.

The upshot is that we are now unclear about the rules governing tax relief on pension contributions made on or after 6 April 2011. The regime that applies until 5 April 2011 appears to be here to stay so anyone wanting to add to their pension may consider doing so before 6 April 2011 under the current regime, provided they are aware of any high earner tax charge that may be suffered.

Personal taxation

From 6 April 2011 the personal allowance for those aged under 65 will increase by £1,000 to £7,475.

The basic rate limit will be restricted so that anyone paying tax at 40% will not benefit from this additional allowance and there may be changes to align NIC contributions for employees and employers with the personal allowance.

For those on modest incomes, the additional £1,000 tax free income per annum will be welcome. Perhaps of more interest is the promise to work towards increasing the personal allowance to £10,000 in future which would take a significant number of people out of the tax net entirely.

What didn't happen...

We've provided a summary of the key announcements included in the budget.

However, a few other areas were subject to a great deal of pre-budget speculation and seem to have escaped inclusion for now - the most notable omission perhaps being Principal Private Residence Relief.

Given the recent issues surrounding MPs expenses, it was widely anticipated that the tax relief applying to private residences may be reformed, at least to restrict the ability to obtain relief on "second homes".

www.sagars.co.uk

Sagars LLP, Gresham House, 5-7 St Pauls Street, Leeds LS1 2JG
T: 0113 297 6789 F: 0113 297 6790

The briefing is for general information only and does not constitute specific advice. You should not rely on this information to make (or refrain from making) any decisions. You should ALWAYS obtain detailed professional advice in relation to your own particular affairs.

Sagars LLP is registered to carry on audit work and regulated for a range of investment business activities by the Institute of Chartered Accountants in England and Wales.

An independent member of HCWA with associated firms throughout the United Kingdom and Worldwide.

Sagars LLP is a limited liability partnership registered in England and Wales with registered number OC310488