Small Business Tax & Finance

Supplement to the April 2008 edition

Budget Summary

What was said and, more importantly, what was not said!

As now seems to be traditional, some of the most important Budget decisions were not announced in the Chancellor's speech and were not covered in HMRC's Budget Notes. Most significant of all, of course, was the decision to delay implementation of the 'income shifting' legislation until April 2009. Hopefully by then it will be appreciated that the proposed scheme really was unworkable and the files will be left to gather dust in some far corner of HM Treasury's doubtless capacious muniments room.

Secondly, paragraph 4.42 of the Budget Report confirms that: 'The Government does not see the need for any change to the taxation of life insurance bonds as a result of CGT reform.' The point here, of course, is that whereas from 6 April 2008 capital gains on investments in quoted securities and unit trusts will be charged at a flat rate of 18%, higher rate taxpayers will continue to pay an effective 40% tax on gains arising within single-premium life assurance policies and other 'insurance bonds'. Life assurance bonds are now looking to become a singularly tax-inefficient investment vehicle.

Thirdly, the Government has decided to withdraw the VAT Staff Hire Concession, with effect from 1 April 2009 (paragraph 4.54 of the Budget Report). This concession allows employment businesses, supplying temporary staff, to charge VAT only on their own fees, and not on wages, *etc*, paid direct by the client to individual workers. This concession has been under review for some time, because HMRC considers it has been exploited for tax planning purposes.

Postponement of income shifting legislation

Paragraph 4.69 of the Budget Report reiterates that: 'The Government firmly believes it is unfair that some individuals can arrange their affairs to gain a tax advantage by shifting part of their income to another person who is subject to a lower rate of tax', but then goes on to say that:

> 'The Government considered the responses received to the recent consultation and believes that a further period of consultation will ensure that the legislation in this area provides clarity and certainty for businesses and their advisors. The Government now intends to introduce legislation through Finance Bill 2009 and will not enact legislation effective from 6 April 2008.'

The bad news for IT contractor and similar personal service businesses is in the next paragraph of the Budget Report (4.70), which warns that: 'The Government is concerned at the growing use of structures, such as "umbrella companies" or overarching contracts of employment with employment businesses, to obtain tax relief for travel expenses that would not be available to other workers. It will monitor the use of these structures and, if necessary, consider action in the future.'

The Chancellor's Budget Speech

In fact, the Chancellor said very little about tax in his Budget Speech. He alluded to measures previously announced, such as the reductions in the basic rate of income tax and the main rate of corporation tax (but not, oddly enough, the increases in the small companies rate), but new announcements were limited to:

A promise of 'further steps to help small companies simplify their tax calculations' – consultation has been opened by posting an on-line questionnaire at *www.hm-treasury.gov.uk/budget/budget_08/bud_bud08_index.cfm*, which will remain open until Wednesday, 30 April 2008. The review will focus on companies with fewer than ten employees and an annual turnover of less than £750,000 and ask whether the range of adjustments which such companies have to make between their statutory accounts and the figures to be reported on their Tax Returns could be reduced, and whether simplification could be achieved by aligning their tax obligations with those of comparable unincorporated businesses.

'Reforming capital allowances for business cars to increase the incentive to move to lower emitting cars' – this was a reference to the consultation process which began at Budget 2006 and a 'consultation update' was published as part of the Budget 2008 pack, with comments invited by Friday, 16 May 2008. The central proposal is that, from April 2009, writing-down allowances for cars with CO_2 emissions above 165 g/km (according to the consultation update) or 160 g/km (according to the Budget Report) will be reduced to 10%. This will replace the existing restrictions on capital allowances for cars costing more than £12,000 (and the existing restrictions on lease rental payments will be replaced by restrictions on lease rental payments for cars above the 160 / 165 g/km threshold). Cars below the emissions threshold will continue to qualify for writing-down allowances at 20% (the new 'main rate' for plant and machinery, which takes effect from April 2008). The 100% first-year allowance for very low emission cars will continue to be

Income Tax Rates and Allowances

The income tax rate bands and personal allowances have been uprated for 2008/09, as follows:

Rates of income tax	*2008/09* £	*2007/08* £
10% starting rate on income to:		2,230
10% starting rate for savings income only to:	2,320	
22% basic rate on income to:		34,600
20% basic rate on income to:	36,000	
40% higher rate on additional income		

The rates applicable to dividends remain 10% for income up to the basic rate limit and 32.5% above that

Personal allowances		
Personal allowance	5,435	5,225
Registered blind person	1,800	1,730
Age-related allowances		
Personal allowance – 65 to 74	9,030	7,550
Personal allowance – 75 plus	9,180	7,690
Married couple's allowance:		
either spouse born on or before		
– 5 April 1935	6,535*	6,285*
– 5 April 1933		6,365*
– 5 April 1934	6,625*	
– minimum amount	2,540*	2,440*
Income limit	21,800	20,900
Clawback	£1 in £2	£1 in £2

* Denotes allowance given as a 10 per cent credit

Company Car Fuel Benefit Charge		
Multiplier	£16,900	£14,400
Construction Industry Scheme (CIS)		
CIS deduction rate	20%	20%
– for 'unverified' subcontractors	30%	30%
Official rate of interest		
For the tax charge on staff loans	6.25%	6.25%
– on living accommodation	6.25%	6.25%
Pension Schemes		
Annual allowance	£235,000	£225,000
Lifetime allowance	£1,650,000	£1.6 million
Capital Gains Tax		
Annual exemption	£9,600	£9,200
– most trusts	£4,800	£4,600

National Insurance Contributions and Tax Credits

For details of **National Insurance contributions** and **Working and Child Tax Credits** for 2008/09, see the Pre-Budget Supplement (published with our November 2007 edition). For details of the **annual pensions and benefits uprating** for 2008/09 and of **Pension Credit** payments for that year, please turn to pages 99 and 102 respectively of our February 2008 edition.

available until March 2013, but from April 2008 the maximum qualifying emission will be reduced from 120 g/km to 110 g/km.

A transitional relief for charities, so that their Gift Aid repayments for donations made in 2008/09, 2009/10 and 2010/11 will continue to be calculated as if the basic rate of tax was still 22 per cent. This transitional relief will apply equally to Community Amateur Sports Clubs (CASCs). On Budget Day HMRC also published a paper *Gift Aid: Administrative Changes and Proposals*, setting out a number of relaxations to the requirements relating to Gift Aid administration and the correction of errors identified by the audit process.

An increase in the maximum investment qualifying for relief under the Enterprise Investment Scheme (EIS), from £400,00 to £500,000. The Government also wishes to make the Enterprise Investment Scheme more 'user friendly' and to this end HM Treasury and HMRC published a Consultation Document on Budget Day, with a closing date of Friday, 20 June 2008.

An increase in the maximum employee shareholding qualifying for relief under the Enterprise Management Incentive (EMI) Scheme, from £100,000 to £120,000. (It was later announced that, to comply with EU State Aid guidelines, the EMI is to be restricted to companies with fewer than 250 employees – this will not affect existing share options or new options granted on or before 5 April 2008.)

The usual clutch of 'further measures against tax avoidance to ensure fairness for all taxpayers'.

Making permanent the lower (5%) VAT rate for over-the-counter sales of smoking cessation products, which was due to expire on 30 June 2008.

A deferment of stamp duty on a shared ownership home until the purchaser owns 80 per cent of the equity.

A 'major reform' of Vehicle Excise Duty, to be implemented in stages from April 2009, to encourage the manufacture and use of cars with lower CO_2 emissions.

Plus, of course, warnings of a 'green tax' on plastic carrier bags, increases in the excise duties on tobacco products and alcoholic drinks, but a postponement of the planned increases in fuel duties from April to October 2008.

Business Tax Changes

Two minor amendments to the new capital allowances régime for plant and machinery, which comes into force this month (April), were announced on Budget Day:

Under the new régime, a trader will have a 'main pool' of plant and machinery qualifying for writing-down allowances at 20% and a 'special rate pool' of items qualifying for writing-down allowances at 10%. The change announced on Budget Day is that, if the unrelieved expenditure in either pool is £1,000 or less, the trader will be able to write it off immediately. This will be available to write off small pools of pre-April 2008 expenditure brought forward, but will also be a permanent feature of the new régime. It will be available to sole traders, partnerships and companies. However, there will be no facility to write off small balances in 'single asset pools'.

The new régime also provides that the 'designated integral features' of a building (electrical and cold water systems, *etc*) shall qualify for writing down allowances at the lower 10% rate. It was announced on Budget Day that where more than half of any 'integral feature' is replaced within a twelve month period, the expenditure shall count as capital and not as revenue expenditure on repairs. The yardstick for the 'more than half' test will be the replacement cost of the asset, at the beginning of the relevant twelve-month period.

Enhanced Capital Allowances Later this year new categories will be added to the lists of technologies qualifying for Enhanced Capital Allowances. They will include waste water recovery and re-use systems, compressed air master controllers and air flow controllers, heat pump dehumidifiers and white LED lighting.

Small Companies Rate Budget Note BN 4 states that, with effect from 1 April 2008, in applying the 'control' test to ascertain whether two or more companies are 'associated' for the purposes of the small companies rate, the rights and powers of business partners will be disregarded, unless 'tax planning arrangements' have been made to exploit the relief.

National Insurance Contributions

On Budget Day HMRC published a Consultation Document entitled *Improving the Collection of National Insurance Contributions from the Self-Employed*. This proposes that the Self Assessment statements sent to taxpayers should include a notification of any Class 2 arrears. Alternatively, where not paid by monthly direct debit, Class 2 contributions could simply be charged half-yearly on the taxpayer's Self Assessment Statement of Account and paid along with his income tax and Class 4 contributions. The closing date for comments is Friday, 6 June 2008.

Residence and Domicile

The Budget made a series of significant changes to the new rules, announced in last October's Pre-Budget Statement to take effect from 6 April 2008, for determining residence status and for taxing the foreign income and capital gains of individuals who are not domiciled, or not ordinarily resident, in the United Kingdom:

Residence status Two changes to the new rules for 'counting days' for the purpose of determining whether an individual is resident or ordinarily resident in the United Kingdom were announced by BN 102. First, a day will now be counted only if the individual is present in the United Kingdom at midnight on the end of that day – in other words, days of arrival will be counted but not days of departure.This means that the exemption for passengers in transit between two places outside the United Kingdom will now only be relevant where the stopover spans midnight.

The second change is that the exemption for passengers in transit will not now be restricted to people who do not leave that part of an airport or port which is open only to international travellers. Indeed, the exemption will be available to passengers who arrive at one airport and then travel across England to leave by another, or (say) arrive by Eurostar and leave by ship from Southampton. However, the exemption will be restricted to individuals who are indeed merely in transit and who do not, for example, attend a business meeting whilst in the United Kingdom.

Remittance basis Last October, the Chancellor announced that from 6 April 2008 any non-domiciled or not ordinarily resident individual who elected to use the remittance basis would not be entitled to claim either personal allowances or the capital gains tax annual exemption unless his unremitted overseas income and gains totalled less than £1,000. BN 103 doubles that *de minimis* limit to £2,000.

BN 104 explains further changes to the detailed rules for identifying remittances and BN 106 deals with employees, who are resident but not ordinarily resident, or not domiciled, and receive shares or share options as part of their remuneration package.

£30,000 annual forfait BN 107 announces that the forfait will not be payable by children and young people (those who have not attained the age of 18 by the end of the relevant year of assessment). It also redefines the forfait as 'a tax charge on unremitted income and gains rather than a stand-alone charge' – this will allow it to be allocated to particular items of income or gains, which could then be remitted without further liability

Corporation Tax Rates and Bands

For the Financial Year 2008 (the year beginning 1 April 2008) the main rate of corporation tax is reduced from 30% to 28%, but the small companies rate rises from 20% to 21%. The consequent changes to the marginal relief calculations are as follows:

	Financial Year 2008	*Financial Year 2007*
Main rate of corporation tax	28%	30%
Small companies rate	21%	20%
Profit limit	£300,000	£300,000
Marginal relief to	£1.5 million	£1.5 million
Marginal relief fraction	7/400	1/40
Effective rate on profits in marginal relief band	29.75%	32.5%

Thus the effective rates of tax on a company's profits are:

Nil to £300,000	21%	20%
£300,001 to £1.5 million	29.75%	32.5%
Over £1.5 million	28%	30%

The Chancellor confirmed that the main rate of corporation tax will remain 28% for the Financial Year 2009 (the year beginning 1 April 2009). The small companies rate will rise to 22% with effect from 1 April 2009.

(though the legislation will include 'ordering rules that determine that untaxed unremitted foreign income or gains will be treated as remitted before income or gains upon which the £30,000 has been paid'), and may facilitate claims for tax credit relief claims in the individual's home country.

In his Budget Speech the Chancellor stated that 'there will be no further changes to this régime [*the tax régime for non-domiciled individuals*] for the rest of this Parliament or the next' – the last three words were met by much laughter from the Opposition Front Bench!

Inheritance Tax

As previously announced, the inheritance tax nil rate band will be increased from £300,000 to £312,000 with effect from 6 April 2008.

As readers will be aware, legislation announced as part of last October's Pre-Budget Report will allow any part of the nil rate band not used by an individual to be 'transferred' to his widow or her widower (or to his or her civil partner), to be set against the survivor's estate at death. This will apply where the surviving spouse or civil partner died or dies on or after 9 October 2007.

If (say) a man leaves part of his estate to his wife and part to his son, but the part bequeathed to his son is clearly well within the nil rate band, it may not be necessary to agree valuations of the assets left to the son. However, on the widow's later death, a valuation of those assets as at the date of the husband's death may become necessary, in order to calculate the unused part of the husband's nil rate band. Strictly speaking, section 274, *Taxation of Capital Gains Act 1992* would then require the value agreed for inheritance tax purposes to be used as the base cost for capital gains tax – even if the son had in the meantime sold the asset and agreed a capital gains tax computation with HMRC. To avoid this problem, it was announced on Budget Day that section 274 will be disapplied where the valuation of an asset does not have to be ascertained for inheritance tax purposes on the first death.

Trusts and the transitional period The *Finance Act 2006*, which introduced a new inheritance tax régime for trusts, provided a 'transitional period' to allow trustees to rearrange their trusts in the light of the new rules, before those rules came into full force and effect. On Budget Day it was announced that the 'transitional period', which was due to expire on 5 April 2008, will now be extended to 5 October 2008. The *Finance Act 2008* will also clarify the rules governing the situation where, within the transitional period, an existing interest in possession (IIP) is replaced by a transitional serial interest (TSI) for the same beneficiary.

Value Added Tax

The VAT registration and deregistration thresholds have been uprated as follows:

	From 1 April 2008	*Previously*
Registration threshold	£67,000	£64,000
Deregistration threshold	£65,000	£62,000
For acquisitions from other EU Member States	£67,000	£64,000

New fuel scale charges The VAT scale charges for taxing private use of road fuel on which input tax has been reclaimed will be amended with effect from the trader's first prescribed accounting period beginning on or after 1 May 2008. The new charges are set out in BN 76 and represent substantial increases for all cars, except those with a CO_2 emissions rating of 120 g/km or less.

VAT Returns: correction of errors At present, a trader who discovers errors in his past VAT Returns may correct the position by declaring the under- or overpayment as an adjustment to the VAT Return for the period in which the mistakes were discovered, providing the net under- or overpayment does not exceed £2,000. Otherwise, full details of the errors must be reported on Form VAT 652 or by letter. For errors declared on Returns for accounting periods beginning on or after 1 July 2008, the £2,000 limit will be increased to the *greater* of £10,000 and 1% of turnover for the return period (sales and other outputs, excluding VAT, as shown in Box 6 of the VAT Return), capped at £50,000.

Closing date for old claims Following the decision in *Fleming (trading as Bodycraft)* and *Condé Nast Publications* (see page 111 of our March edition), the Government is belatedly providing a statutory transitional period for claims for the repayment of output tax overpaid for accounting periods ended before 4 December 1996, and for the payment of input tax underclaimed for accounting periods ended before 1 May 1997. The transitional period will end on 31 March 2009.

Option to tax land and buildings An option to tax land and buildings can be revoked after twenty years – as the option was introduced in August 1989, the earliest date an option can be revoked is 1 August 2009. A Treasury Order will be made shortly to provide the necessary legislation and also to make a number of improvements to the 'option to tax' scheme. These will come into force on 1 June 2008 and include the introduction of an opportunity to make an early revocation during a 'cooling-off' period – for details, see BN 79.

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