Peat House Newham Road Truro Cornwall TR1 2DP
Telephone: 01872 276116 Telefax: 01872 222172
www.rrl-truro.co.uk

ROBINSON
REED
LAYTON
CHARTERED
ACCOUNTANTS
and
CHARTERED
TAX ADVISERS

2009 Pre-Budget Report Summary

Chancellor Alistair Darling presented his Pre-Budget Report on Wednesday 9 December 2009.

Mr Darling spoke of the Report taking place at 'a critical time for our economy' and that the task was 'to secure the recovery and promote long-term growth'.

This summary concentrates on the tax measures which are being introduced:

- a 1% increase in the NIC rates payable by employers, employees and the self-employed from April 2011
- freezing the personal allowances and tax bands at the 2009/10 amounts for most taxpayers
- the introduction of a 50% additional rate of tax for those with the highest income levels
- changes to the complex rules for the Special Annual Allowance charge which affect those with substantial income, making significantly higher pension contributions in anticipation of the removal of higher rate tax relief which will occur in 2011
- the deferral for a further year of the planned increase in the small companies corporation tax rate, maintaining the current rate of 21% for a further year
- the standard rate of VAT will return to its former rate of 17.5% on 1 January 2010
- a temporary bank payroll tax of 50% is to apply to certain bonuses (in whatever form).

You will find further details in the following summary.
Please contact us if you have any questions

Personal Tax

Allowances and rates

There will be no increase in the under 65 personal allowance for 2010/11 which will remain at the current £6,475. The basic rate limit will also be maintained at the current £37,400. Therefore an individual will continue to pay 40% tax rather than the basic rate of 20% when their total income exceeds £43,875.

The 10% starting rate for savings income band (frozen at £2,440) is only available where an individual's non savings income (broadly earnings, pensions, trading profits and property income) does not exceed the starting rate limit.

Comment

The government had previously announced that where the RPI (measure of inflation) is negative that allowances and tax bands would be frozen.

Changes for 2010/11

The government had previously announced that the personal allowance would be subject to an income limit of £100,000. An individual's personal allowance will be reduced by £1 for every £2 of adjusted net income above the income limit.

Adjusted net income for these purposes is broadly all income after adjustment for pension payments, charitable giving and relief for losses.

A new rate of income tax of 50% will be introduced from 6 April 2010. This will apply to taxable income above £150,000.

Dividend income is currently taxed at 10% where it falls within the basic rate band and 32.5% where liable at the higher rate of tax. A new rate of 42.5% will be introduced for dividends which fall into the income band above £150,000.

Example

The effect of the changes can be illustrated as follows:

	2009/10		2010/11	
		tax		tax
	£	£	£	£
Non dividend income	200,000		200,000	
Personal allowance	(6,475)		Nil	
Taxable income	193,525		200,000	
Taxable at 20%	37,400	7,480	37,400	7,480
Taxable at 40%	156,125	62,450	112,600	45,040
Taxable at 50%			50,000	25,000
Total tax liability		£69,930		£77,520

National Insurance Contributions (NICs)

The NIC rates and limits are broadly frozen for 2010/11 at the 2009/10 figures. There are two exceptions to this in that the lower earnings limit, linked to the state retirement pension, will increase from £95 to £97 per week and there will be an increase in the NIC rate which applies to Volunteer Development Workers. All other rates will be held at the 2009/10 levels.

An increase in the rates of NIC is proposed from April 2011. A further 1% will apply to the rates applicable to employers, employees and the self-employed. The main rate of Class 1 (employee) NIC will be 12% and the Class 4 rate will be 9%. The employer rate will increase to 13.8%. The additional rate of Class 1 and 4 contributions payable will be increased from the current 1% to 2%.

In order to protect those at the lower end of the earnings scale the government has announced that the primary threshold and lower profits limits will be increased by £570. Those paying the standard employee rate and earning below £20,000 will pay less NIC overall as a result of the change.

Comment

The government had previously announced that NIC rates were to increase by 0.5%. This further increase of 0.5% will represent a significant increase in costs for employers.

Furnished Holiday Lettings (FHL)

Unlike general property rental businesses, FHL are treated as a trade for certain taxation purposes, which is generally more preferential in terms of loss reliefs and CGT reliefs. The government had previously announced that it would repeal the FHL rules with effect from 2010/11 but until then it would relax the rule that FHL had to be situated in the UK. Properties situated in the European Economic Area (EEA) qualify as FHL provided they meet the other conditions.

The government has confirmed that FHL will cease to be treated as a trade which will impact for loss relief, capital allowances, pension contribution and CGT purposes. These changes take effect from 1 April 2010 for companies and 6 April 2010 for individuals.

From April 2010 those letting furnished holiday accommodation will be able to claim a 10% 'wear and tear' allowance which is generally 10% of the rent less rates. They will also be entitled to claim Landlord's Energy Savings Allowances on qualifying energy saving capital expenditure incurred on the property. These allowances are currently available against general property income.

Comment

This change had been previously announced when the FHL rules were extended to include properties situated in the EEA.

Tackling offshore evasion

HMRC will be consulting on a package of deterrents and new tools to help them tackle offshore tax evasion. This includes a notification requirement for certain offshore bank accounts and a new tough approach to penalties for offshore non compliance.

Disclosure of tax avoidance schemes (DOTAS)

HMRC have issued proposed rules on the options to strengthen and improve the system under which they receive information about avoidance schemes. The intention is to ensure they continue to receive information early and that they have sufficient powers to penalise those who do not comply with the rules.

Personal Tax continued

Shared Lives carers

From 6 April 2010 income tax relief will be introduced for Shared Lives carers who provide accommodation, care and support for up to three individuals placed with them under a local authority Shared Lives Placement Scheme. The Shared Lives carers must share their homes and family life with the individuals placed with them.

Special Annual Allowance charge – new limits for 2009/10

The Special Annual Allowance (SAA) charge was introduced by some very complex rules in Finance Act 2009. The current rate of the SAA charge is 20% on excess pension contributions. The aim of the charge is to discourage individuals from making significantly higher pension contributions in anticipation of the removal of higher rate tax relief which will occur in 2011. The main features of the charge are:

- It applies for 2009/10 and 2010/11 to individuals with relevant income in excess of £150,000 in either of those years or the two preceding years and where increased pension contributions have been paid after 22 April 2009.
- The total pension contributions paid exceed £20,000 (the 'SAA threshold'). A higher threshold of up to £30,000 may be possible depending on the level of contributions in previous years.
- The SAA threshold is reduced by the amount of so-called 'protected' contributions which are sums being paid at least quarterly under arrangements put in place before 22 April 2009.

It is now proposed to lower the threshold for triggering the SAA charge by reducing the relevant income limit to £130,000 with effect from 9 December 2009. Individuals will be affected by this if their relevant income in 2009/10 or either of the two preceding years exceeds £130,000. For 2009/10 only, protected contributions will include any contributions paid up to and including 8 December 2009.

Example

Mary has relevant income of £140,000 in 2009/10. She makes regular monthly contributions of £2,000 under arrangements which have been in place for several years. She made a one-off contribution of £5,000 in September 2009 and another of the same amount in March 2010. Her basic SAA for the year is £20,000. In her case all the regular contributions plus the September payment are protected and so her SAA reduces to nil.

The contribution made in March will be caught and will be subject to the 20% charge which is payable by Mary.

Comment

This will potentially catch a significant number of individuals. It is important to review the level of relevant income for 2007/08 and 2008/09. If in either year the figure is over £130,000 and below £150,000 the new rules will apply irrespective of the income level in 2009/10. If in either year the figure exceeds £150,000 the existing rules will bite.

The rules will catch one-off contributions made by employers as well as lump sum payments made by the scheme member. In either case the charge is on the individual.

SAA rates for 2010/11

The current rate of the SAA charge is 20% on the excess contributions. For 2010/11 the rate will be that necessary to reduce the tax relief on the excess to the basic rate. Bearing in mind that the top rate of tax will be 50%, some of the charge could be at 30% and some at 20% depending on the effective rates at which pension contributions are being relieved.

Removal of higher rate relief for pension contributions from 6 April 2011

Further detail has been provided on the plan to remove higher rate relief on the pension contributions of those with high income. However some of the detail is still subject to consultation. The rules will apply to those whose gross income exceeds £150,000 and in calculating this limit account will be taken of employer pension contributions.

There will be an income 'floor' of £130,000 (excluding employer pension contributions). Any individual with income below this limit will not be affected at all by the rules. If the income exceeds £130,000 then the amount of any employer contribution must be added to establish if the £150,000 limit is exceeded.

Comment

The basis of this calculation will be very important for many family companies where annual employer pension contributions have been a feature of remuneration planning.

Refunded pension contributions

When a registered pension scheme repays contributions to members who leave having completed less than two years service, they are required to pay a tax charge to recoup the tax relief given on the original contributions. That charge is currently 20% on the first £10,800 of refunded contributions and 40% on any balance. Where a refund is made on or after 6 April 2010 the 20% rate will apply to the first £20,000 of refunded contributions and any balance will be taxed at 50%. The charge is levied on the pension scheme.

Lump sums from Employer-Financed Retirement Benefit Schemes (EFRBS)

In certain situations a lump sum, gratuity or other benefit may be paid by an EFRBS to an entity other than an individual. In those cases there is a tax charge payable by the recipient which is currently 40%. That rate will increase to 50% for benefits paid after 6 April 2010.

Business Tax

Corporation tax rates

The small companies corporation tax rate which applies to companies with up to £300,000 of profits is currently 21%. An increase to 22% was originally planned to take effect from 1 April 2010 but was deferred. This has now been deferred for a further year until 1 April 2011.

Business Payment Support Service (BPSS)

The service launched by the 2008 Pre-Budget, which enables viable businesses to negotiate more flexible payment arrangements to meet business tax liabilities including PAYE, will continue to be available for the foreseeable future.

The service supplements the existing Time to Pay (TTP) arrangements which may be negotiated by all taxpayers. However from April 2010 a new requirement will apply where a business seeks a TTP arrangement and the liability is worth £1 million or more. Such a business will need to provide an 'Independent Business Review' in support of the request and this is expected to be implemented from April 2010.

Capital allowance boost for low-carbon transport

A 100% first year allowance will be available for capital expenditure on new electric vans from 1 April 2010 for companies and 6 April 2010 for an unincorporated business. This proposal is subject to European State Aid rules.

Reduced corporation tax for innovation companies

A reduced corporation tax rate of 10% is to apply from April 2013 to income arising from patents. It is intended that there will be a consultation with business in time for the Finance Bill 2011. It will apply to patents granted after the legislation is passed.

Comment

This proposal is to be known as the 'Patent Box' and is designed to ensure that the UK remains an attractive location for innovation, by offering stronger incentives.

Venture Capital Schemes

Certain changes to the qualifying conditions for the Enterprise Investment Scheme (EIS) and Venture Capital Trusts (VCTs) are being made to ensure that both schemes continue to meet European State Aid requirements.

In summary the proposed changes are:

- to qualify a company must not be in difficulty
- to qualify a company need only have a permanent establishment in the UK rather than carrying on a qualifying trade wholly or mainly in the UK
- a VCT's shares must now be traded on an EU regulated market rather than being restricted to an official UK list
- rules governing the amount of a VCT's investment which must be held as equity are changed.

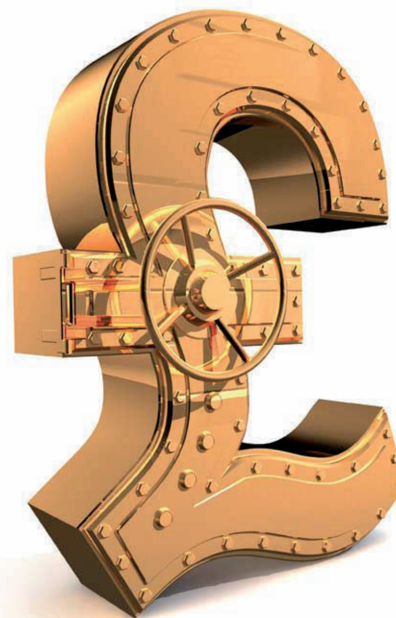
In addition a new 'small enterprise' definition is to be incorporated into legislation to ensure that the schemes remain targeted on the small enterprises for which they are intended and do not benefit larger enterprises.

Controlled Foreign Company (CFC) reform

The government remains committed to the reform of these rules and has announced that proposals will be issued in the New Year.

Worldwide Debt Cap for large groups

Further amendments have been proposed to the debt cap legislation which comes into force for periods of account beginning on or after 1 January 2010 for large groups. The amendments eliminate various anomalies which have been identified in applying the rules and include additional provisions relating to the allocation of disallowed finance costs.



Bank payroll tax

A temporary bank payroll tax of 50% is to apply to certain bonuses (in whatever form). The tax will apply to the amount of the bonus which exceeds £25,000 for any individual employee. The tax will apply to banks, building societies and other related financial businesses.

It is to apply to all discretionary and contractual bonus awards made after the announcement of the measure on 9 December 2009, except for contractual bonus entitlements which existed at the time of the announcement, where the payer has no discretion as to the amount of the bonus. The initial charging period will run until 5 April 2010. However the government has indicated that this period of charge could be extended until other relevant provisions of the Financial Services Bill come into force.

This one-off tax is payable on 31 August 2010. It will not be deductible in calculating the institution's profit or loss for corporation tax or income tax purposes.

Comment

This intervention is designed to tackle certain remuneration practices that are considered to have contributed to the excessive risk taking in the banking industry.

Employment

Workplace canteens

Legislation will be introduced to restrict the existing tax exemption for workplace canteens. However this will only affect employees and employers who use the exemption in conjunction with salary sacrifice or flexible benefit arrangements.

These arrangements allowed 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 canteen subsidies that are available to all employees. This will take effect from 6 April 2011.

Company cars

From 6 April 2012 the CO_2 emissions bands used to work out the taxable benefit for an employee who has the use of a company car will be shifted down by 5gm CO_2 per km. In addition, the current graduated table of company car tax bands will be extended down to a 10% band. This will mean that a 10% band will apply to company cars with CO_2 emissions up to 99gm CO_2 per km.

As a result 'qualifying low emissions cars' will no longer exist as a separate category.

Comment

Whilst a welcome move there are very few cars that might appeal to company car drivers that fall into this new band.

Changes to fuel benefit tax

From 6 April 2010 employees who receive free private fuel from their employers for company cars or vans will pay more income tax on this benefit.

For company car drivers the existing figure used as the basis for calculating the benefit will be increased from £16,900 to £18,000. For company van drivers the benefit will be increased from £500 to £550.

Comment

As a result of these increases employers will suffer additional Class 1A National Insurance Contributions.

Electric cars and vans

Employees who are provided with a company car for their private use, which is propelled solely by electricity, currently pay tax on the benefit which is based on 9% of the list price of the car. From 6 April 2010 this percentage will be reduced to 0% therefore reducing the benefit calculation and tax liability to nil. This will apply for five years.

In a similar vein, employees who are provided with a company van for their private use, which is propelled solely by electricity, currently pay tax on a flat rate benefit of £3,000. From 6 April 2010 this benefit will be reduced to nil thereby eliminating the tax liability. This will also apply for five years.

Comment

As a result of these changes employers will eliminate their Class 1A National Insurance liabilities on cars and vans provided to employees this way.

Other Business Measures

The government has announced the following measures.

- An extension to the temporary exemption from business rates for empty properties. For 2009/10 properties with a rateable value of up to £15,000 are exempt. The relief will be extended to 2010/11 for empty commercial properties with a rateable value of up to £18,000.
- An additional £500 million of lending available to small and medium-sized enterprises through a 12 month continuation of the Enterprise Finance Guarantee. This provides targeted support for viable businesses with less than £25 million turnover that have no or insufficient security.
- Creating a new Growth Capital Fund to support growing companies seeking to borrow amounts between £2 million and £10 million. Further details will be announced in 2010.
- Further investment in the Strategic Investment Fund and UK Innovation Investment Fund.

Capital Taxes

Inheritance tax (IHT) nil rate band

The nil rate band for 2010/11 will be frozen at the current level of £325,000.

Comment
The original intention of the government was to increase the nil rate band to £350,000.

IHT avoidance

Legislation, effective from 9 December 2009, will be introduced in Finance Bill 2010 to counter two tax avoidance schemes that have been designed to avoid IHT charges on property in trusts. The measures will have effect for:

- transfers into a trust where the settlor retains a future interest, or where a future interest in a trust is purchased, on or after 9 December 2009
- interests purchased in trusts on or after 9 December 2009.

Capital gains tax (CGT) and principal private residence relief (PPR)

PPR is not available on any part of a house which is used exclusively for the purposes of a business or vocation. On disposing of the house the appropriate proportion of the gain relating to the part occupied as the only or main residence is eligible for PPR.

Where a person cares for an adult under a local authority placement scheme, their contract with the local authority may require them to set aside one or more rooms exclusively for the use of the adult in care. In such a case, PPR may not be available on that part of the property. Finance Bill 2010 will remove this possible restriction.

The measure will have effect for disposals on or after 9 December 2009.

Standard rate of VAT

As previously announced the temporary reduction in the standard rate of VAT to 15% will end on 31 December 2009.

The Pre-Budget Report confirms arrangements to smooth the transition for businesses back to the 17.5% standard rate.

- There will be a 'period of grace' for businesses trading across the midnight deadline to charge the lower 15% rate until they close (or until 6 am on 1 January 2010, whichever is earlier).
- Shops will be able to add the extra VAT to prices at the tills for up to 28 days, giving them extra time to complete the re-pricing of their stock.

VAT Flat Rate Scheme changes

The Flat Rate Scheme provides an optional simplified VAT arrangement for businesses with a turnover up to £150,000. The percentages were re-calculated in December 2008 to reflect the temporary reduction in the standard rate of VAT. The flat rate percentages have now been re-calculated to reflect the reversion of the standard rate of VAT to 17.5%. The new rates will be implemented on 1 January 2010.

Changes also include technical adjustments to reflect more up to date business patterns. This means that, for some sectors, the rates will not simply return to the level set prior to December 2008. Virtually all sectors will face an increase because of the increase in the standard rate, although increases in some sectors will be larger than others.

Miscellaneous

Spotlights on avoidance

HMRC's internet publication, 'Spotlights', which highlights avoidance schemes, will be expanded to include more general 'buyer beware' messages. These will provide taxpayers with an indication of the type of arrangements to avoid. It will continue to highlight specific avoidance schemes that in HMRC's view are ineffective or have unintended adverse consequences in order to deter taxpayers from buying into high risk avoidance.

Equitable Liability Extra Statutory Concession

A concession has existed for taxpayers in receipt of a determination of income or corporation tax who are out of time to file their tax return and who can demonstrate that the sums charged are excessive.

By concession HMRC only collected the sum that would have been due for the period had the taxpayer filed the return on time. Legislation will be introduced to permit HMRC to continue to apply this treatment provided certain conditions are met.

Comment
HMRC's original intention was to remove this concession but not introduce relieving legislation. After pressure from professional bodies, HMRC have changed their mind.

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