



The Post Election Budget 2010

Tuesday 22 June 2010

Budget Summary

George Osborne presented his first Budget on Tuesday 22 June 2010.

For the first time, forecasts were published in advance of the Budget. The Office for Budget Responsibility was formed in May 2010 to make an independent assessment of the public finances and the economy in advance of each Budget and Pre-Budget Report.

Within the framework of these forecasts George Osborne stated that a tough but fair Budget was needed. Many fundamental announcements have been made which affect the taxation of most individuals. These are in addition to changes already made by the previous government, such as the 50% tax rate and changes to the tax relief available for pension contributions.

Our summary focuses on the issues likely to affect you, your family and your business. To help you decipher what was said we have included our own comments.

If you have any questions please do not hesitate to contact us for advice.

EXECUTIVE SUMMARY

The main taxation changes were:

Personal and Employment Tax

- Personal allowance to increase by £1,000 from 5 April 2011.
- Higher rate tax threshold will be reduced so that higher rate and top rate taxpayers will not benefit from the increased personal allowance.
- Employers' NIC threshold to increase above inflation as previously announced.
- Up to £5,000 exemption from Employer's NIC for each of first 10 people employed by new businesses located (broadly) outside South East.
- The treatment of rents from furnished holiday lets to continue as business income for 2010/11.

Business Tax

- Main corporation tax rate to reduce by 1% every year for four years to 24%.
- Small companies rate to be cut to 20% from 1 April 2011.
- Thresholds for small company's rate and main rate of corporation tax to remain unchanged.
- Annual investment allowance reduced from £100,000 to £25,000 from 1 April 2012.
- Reduction in capital allowances from 20% to 18%, and from 10% to 8%, from 1 April 2012.
- Taxation of foreign profits, intellectual property and R&D to be reformed to make UK more business friendly.

Capital Gains Tax (CGT)

- Rate of CGT to increase to 28% for higher rate and top rate income taxpayers (basic rate taxpayers rate to remain at 18%) with no tapering based on length of ownership.
- New CGT rate to be introduced for gains made from midnight.
- Entrepreneurs' relief will apply to first £5m of qualifying gains made from midnight.

VAT and Other Matters

- 20% main VAT rate to be introduced on 4 January 2011, with continued exemptions for essential goods.
- Insurance premium tax rates to increase from 5% to 6% and from 17.5% to 20%.
- Introduction of a bank balance sheet levy, initially at 0.04% from January 2011, increasing to 0.07%.

The key theme of this Budget was that "we are all in this together". Businesses have a number of reasons to feel more cheerful, but will be eagerly awaiting the outcome of various consultations. Entrepreneurs and those people with furnished holiday lets will be extremely relieved!

No further changes were announced for Inheritance Tax in spite of the political promises made by the Conservative party.

HMRC's new penalty regime is continuing to be strengthened with the introduction of a £100 penalty for late submission of tax returns, even if there is no tax due.

For further details please contact Jonathan Crowther (Pershore) or Sandy Lewis (Ledbury).

PERSONAL AND EMPLOYMENT TAX

The personal allowance

For those aged under 65 the personal allowance will be increased by £1,000, from £6,475 to £7,475 for 2011/12.

Comment

By increasing the personal allowance by £1,000 the government states that 880,000 people will be taken out of tax altogether.

However, there was no mention of a transferable personal allowance for married couples or civil partnerships.

For 2010/11 onwards those with adjusted net income over £100,000 have their personal allowance withdrawn 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.

Tax rates

There are no changes announced to the main rates of tax for the current or future years. In particular, the new 50% rate (42.5% for dividends) remains for those with taxable income above £150,000.

To ensure that the majority of higher rate taxpayers will pay the same total level of income tax and National Insurance Contributions (NICs) as previously planned, the government will reduce the basic rate limit by £2,500, and the upper earnings and profits limits for NICs by £1,650, based on current estimates of the Retail Prices Index. These changes will take effect for 2011/12.

The existing basic rate limit is £37,400. The exact figure of the basic rate limit for 2011/12 will be confirmed in the autumn.

The higher rate threshold (the point at which 40% tax begins to be paid) will remain frozen until 2013/14.

Trust rate

For 2010/11, the trust rate, which mainly applies to discretionary trusts, was increased from 40% to 50% and the trust dividend rate from 32.5% to 42.5% and these changes remain.

National Insurance Contributions (NICs)

The NIC rates and limits were broadly frozen for 2010/11 at the 2009/10 figures.

Changes to the rates of NIC and thresholds are proposed from April 2011. As announced by the previous government the NIC primary threshold (the point at which NICs are payable) will increase and 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%.

The upper earnings limit and the upper profits limit will continue to be aligned with the income tax higher rate threshold (which is being reduced in April 2011).

The government will introduce two measures for employers:

- the level at which employers start to pay NICs will increase by £21 per week above indexation from April 2011
- a three-year scheme will be introduced to exempt new businesses in targeted regions from up to £5,000 of Class 1 employer NICs, for each of the first ten employees hired in their first year of business.

Comment

Whilst the government needs the additional income from the rise in the NIC rates, there is a clear attempt to avoid a 'jobs tax'. In addition, there is an intention to prevent those on low incomes from suffering from the NIC rises.

Tax credits

A whole series of changes are announced to the tax credits system. From April 2011:

- the second income threshold for the family element of the Child Tax Credit will reduce from £50,000 to £40,000
- the first and second withdrawal rates for tax credits will increase to 41%
- the baby element will be removed from the Child Tax Credit and, from April 2012, the 50 plus element will be removed from the Working Tax Credit
- the level of in-year rises of income that will be disregarded from calculations of tax credit entitlement will decrease from £25,000 to £10,000 and, from April 2013, this will be reduced to £5,000.

In April 2011, the child element of the Child Tax Credit will increase by £150 above indexation and, in April 2012, it will increase by £60 above indexation.

From April 2012:

- the period for which a tax credit claim and certain changes of circumstances can be backdated will be reduced from three months to one month
- a disregard of £2,500 will be introduced in the tax credits system for in-year falls in income.

Comment

Tax credits were a core feature of the previous government's strategy for helping low income families. Whilst the new government wishes to continue with the principle:

'Spending on tax credits has increased from £18 billion in 2003 to £30 billion this year. This is unsustainable.'

Sandy Lewis says middle income earners will be hit most by these new proposals.

Child Benefit

From April 2011, both rates of Child Benefit will be frozen for three years.

Comment

There had been much discussion whether Child Benefit would survive, particularly for those on higher incomes.

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

Some time ago the Labour government announced its intention to remove higher rate relief on the pension contributions of those with high income, broadly £130,000 or more.

This announcement has led to complex rules being introduced from April 2011 onwards, with even more complicated anti-forestalling rules for the years 2009/10 and 2010/11.

Whilst there are no changes to the rules for 2009/10 and 2010/11, the government is looking at simpler ways of achieving a similar result from 2011 via consultation with interested parties.

Provisional research suggests an annual allowance in the region of £30,000 - £45,000 might deliver the necessary tax yield. Relevant issues for the government to consider include:

- options to ensure that basic rate taxpayers are not subject to the restriction and to support cases caused by one-off 'spikes' in pension accrual
- how pension accrual in defined benefit schemes would be valued
- whether and how there could be flexibility for individuals over paying any charges that arise
- how compliance and delivery would operate in practice.

Requirement to buy an annuity

From April 2011 the rules that create an obligation to purchase an annuity by age 75 will be replaced with age 77. A consultation on the detail of this change will be launched in the near future.

Furnished Holiday Lettings

The tax treatment of Furnished Holiday Lettings (FHL) has been advantageous for many years. Provided that certain conditions are met, FHL are treated as a trade. This can be preferable to the tax regime for normal let property in a number of specific areas, as the rules and reliefs for trades are often more generous.

The government has announced that these rules will continue unchanged for 2010/11, with a consultation into possible future changes starting in the summer.

Business Tax

Corporation tax rates

The main rate of corporation tax which generally applies to companies with profits of more than £1.5 million is to reduce from 28% to 27% from 1 April 2011. There will be further graduated reductions so that the main rate will be 24% by 1 April 2014.

The small profits rate of corporation tax which generally applies to companies with up to £300,000 of profits is to reduce to 20% also with effect from 1 April 2011.

The effective marginal corporation tax rate for profits between £300,000 and £1.5 million is expected to be 28.75% from 1 April 2011 (assuming there is no change to the basis upon which the marginal relief calculation is computed).

Comment

The Chancellor stated that there is to be reform of corporation tax over a five year period to promote UK competitiveness. These headline rate reductions are an initial step towards this goal. The previous government had intended to increase the small profits rate of corporation tax from its current rate of 21% to 22%.

Capital allowances on plant and machinery

Two key areas of change to capital allowance rates are to take effect from April 2012.

The first measure will reduce the maximum Annual Investment Allowance. This is available to most businesses and provides immediate 100% tax relief on the purchase of qualifying plant and machinery. The allowance is currently £100,000. It is to decrease to £25,000.

The second measure reduces the rates of writing down allowances per annum on expenditure not relieved by other allowances as follows:

- from 20% to 18% on expenditure allocated to the main plant pool
- from 10% to 8% on expenditure allocated to the special rate pool.

Transitional rules will apply for chargeable periods which span 1 April 2012 for businesses within the charge to corporation tax and 6 April 2012 for businesses within the charge to income tax.

Comment

The delayed start date for the proposed reduction in capital allowances from April 2012 makes sense as it will help to offset the loss of corporation tax revenue to the Exchequer when the reduction in corporation tax rates kicks in.

Consortium Relief

Those aspects of corporation tax group relief rules that cover consortium relief will be amended to allow EU and EEA-resident companies engaged in UK consortia to pass on relief for the losses of those consortia to their UK resident group companies. At the same time, the government is strengthening rules designed to ensure that access to consortium relief is given only in proper proportion to the member company's involvement in the consortium. Legislation will be in the Finance Bill and both changes will have effect from the day on which draft legislation is published.

Income tax deducted at source

Current rules require certain persons (mainly individuals and unincorporated bodies) to deduct income tax at source on certain payments such as interest and patent royalties and to then pay it over to HMRC. A change to HMRC powers is proposed to enable regulations to be made relating to when and how such a person should remit and report the payment.

Previous announcements to go ahead

The following proposals announced by the previous government are to be implemented:

- the introduction of a new 100% first year allowance for capital expenditure on new zero-emission goods vehicles for expenditure incurred on or after 1 April 2010 and before 1 April 2015 for companies and on or after 6 April 2010 and before 6 April 2015 for unincorporated businesses.
- the removal of the condition that required intellectual property derived from research and development expenditure to be owned by the small and medium enterprise company seeking the tax relief claim. The change will have effect for any expenditure incurred in an accounting period ending on or after 9 December 2009.

Small business tax

The government remains committed to a review of IR35 and small business tax and will release further details shortly.

CAPITAL GAINS TAX

Capital gains tax (CGT) annual exemption

Despite rumours that the annual exemption might change for 2010/11, it remains at the level set previously (£10,100).

CGT rates

Legislation will be included in Finance Bill 2010 to introduce a new rate of CGT of 28%. For individuals, the rate of CGT remains at 18% where total taxable gains and income, after taking into account all allowable deductions including losses, personal allowances and the CGT annual exemption, are less than the upper limit of the income tax basic rate band (£37,400). The new 28% rate will apply to gains or any parts of gains above this limit.

Where Entrepreneurs' Relief applies for individuals or trustees the rate remains at 10%.

The new rate of CGT will apply from 23 June 2010.

Gains arising in 2010/11, but before 23 June 2010, will continue to be liable to CGT at 18% and will not be taken into account in determining the rate(s) at which gains of individuals arising on or after 23 June 2010 should be charged.

Gains on disposals before 23 June 2010 which have been deferred until 23 June 2010 or later under certain CGT reliefs (eg gains deferred under the Enterprise Investment Scheme) will be liable to CGT at the time the deferral period ends. The gain becomes liable to tax in the same way as gains arising on disposals on or after this date at either 18% or 28%.

In working out the CGT due, taxpayers will be able to deduct losses and the annual exemption in the way which minimises the tax due.

Comment

The CGT changes were not as bad as first mooted. However Richard Beard has expressed disappointment that there is no relief for assets held for a long period of time.

Example of Capital Gains Calculation

In 2010/11 David's taxable income, after all allowable deductions and the personal allowance, is £27,400. The upper limit of the income tax basic rate band is £37,400. David has the following capital transactions:

- May 2010 he sells an asset and realises a chargeable gain of £17,000.
- November 2010 he sells another asset, realising a chargeable gain of £25,100.

David has no allowable losses to set against these gains, and the annual exemption for 2010/11 is £10,100. Neither of the gains qualify for Entrepreneurs' Relief.

David's taxable income is £10,000 less than the upper limit of the basic rate band (£37,400 - £27,400).

David sets the annual exemption against the later gain (because part of that gain is liable to tax at the higher CGT rate), which leaves £15,000 taxable (£25,100 - £10,100). The first £10,000 of the £15,000 is taxed at 18% and the remaining £5,000 is taxed at 28%.

The £17,000 chargeable gain David realised in May 2010 before the change of rates on 23 June 2010 is taxable at 18%.

Trusts

For trustees and personal representatives of deceased persons, the CGT rate will be 28% for gains arising on or after 23 June 2010, except where Entrepreneurs' Relief applies.

Entrepreneurs' Relief

Subject to a number of conditions, gains on disposals of entrepreneurial businesses by individuals and certain trustees qualify for Entrepreneurs' Relief. The relief is given by reducing the qualifying gains by 4/9 and the balance is then charged at an 18% rate of tax. This results in the qualifying gains being taxed at an effective rate of 10%.

The changes to the CGT rates from 23 June 2010 would mean that the 4/9 reduction no longer achieved an effective rate of 10%. Finance Bill 2010 will include provisions to charge gains on qualifying disposals on or after 23 June 2010 at a 10% rate of tax. The previous 4/9 reduction will cease to apply from this date.

Finance Bill 2010 will include provision to increase the amount of gains that can qualify for Entrepreneurs' Relief to £5 million (previously £2 million) from 23 June 2010.

Where individuals or trustees make qualifying gains above the previous £2 million limit before 23 June 2010 (£1 million before 6 April 2010) no additional relief will be allowed for the excess above the old limit. If they make further qualifying gains on or after 23 June 2010, they will be able to claim relief on up to a further £3 million of those additional gains (or up to £4 million where the earlier £1 million limit applied), giving relief on accumulated qualifying gains up to the new limit of £5 million.

In determining at what rate(s) an individual should be charged to CGT on any other gains, those gains qualifying for Entrepreneurs' Relief are set against any unused basic rate band before non qualifying gains.

Comment

The increase in the Entrepreneurs' Relief limit to £5 million was unexpected but welcome.

VAT AND OTHER MATTERS

VAT: change of standard rate

It is proposed to increase the standard rate of VAT from 17.5% to 20% with effect for any supply made on or after 4 January 2011. The rate change does not affect either zero-rated supplies nor those supplies subject to VAT at the 5% reduced rate.

Comment

An increase in the standard rate was widely forecast. Unsurprisingly, draft legislation has also been issued setting out anti-avoidance measures to deal with transactions aimed at forestalling the increase in rate.

VAT Flat Rate Scheme

The VAT Flat Rate Scheme simplifies VAT for businesses with an annual turnover (VAT exclusive) of up to £150,000. The percentages used in the scheme will change from 4 January 2011 to reflect the increase in the standard rate of VAT.

VAT: detailed changes

As previously announced changes will be made early next year to:

- the VAT recovery on mixed use assets
- the place of supply rules for natural gas, heat and cooling
- the definition of aircraft that can be supplied at zero rate
- certain postal services provided by Royal Mail.

Tackling tax avoidance

The government will take a more strategic approach to the risk of avoidance to prevent increasing complexity and reduce the need for frequent legislative change. In this context, the government is tackling long-standing avoidance risks in a way that makes it clear what result the legislation intends to achieve.

The government intends to examine whether the option of a General Anti-Avoidance Rule should form one element of its strengthened defences.

The government will also continue to shut down avoidance schemes as they emerge.

Inheritance tax (IHT)

The government will consult on bringing IHT on trusts within the Disclosure of Tax Avoidance Schemes regime.

Bank levy

A bank levy based on banks' balance sheets will be introduced, following consultation, effective from 1 January 2011. It is proposed that the levy will be set at a rate of 0.07%, with a lower initial rate of 0.04% in 2011.

Disclaimer

This summary is published for the information of clients. It provides only an overview of the main proposals announced by the Chancellor of the Exchequer in his Budget Statement, and no action should be taken without consulting the detailed legislation or seeking professional advice. Therefore no responsibility for loss occasioned by any person acting or refraining from action as a result of the material contained in this summary can be accepted by the authors or the firm.

Summary of Rates and Allowances

Indirect Tax

Value Added Tax

With effect from 4 January 2011 the standard rate of Value Added Tax will increase to 20 per cent.

VAT	April 2010-11	4 January 2011
Standard rate	17.5%	20%
Reduced rate	5%	5%

Budget also announces that sectoral rates for the VAT Flat Rate Scheme (FRS) will be updated. Details of new sectoral rates will be available on the HMRC website.

Insurance Premium Tax

With effect from 4 January 2011 the standard rate of Insurance Premium Tax will increase to 6 per cent and the higher rate will increase to 20 per cent.

IPT	April 2010-11	4 January 2011
Standard rate	5%	6%
Higher rate	17.5%	20%

PERSONAL TAX AND BENEFITS

Income Tax

Budget announces that in 2011-12, the income tax personal allowance for under 65s will be increased by £1,000 in cash terms, taking it from £6,475 in 2010-11 to £7,475 in 2011-12.

National Insurance Contributions

Employee and employer rates				
	Employee (Class 1 primary)		Employer (Class 1 secondary)	
Earnings per week	April 2010-11	April 2011-12	April 2010-11	April 2011-12
Below primary threshold / secondary threshold	Nil	Nil	Nil	Nil
Above primary threshold / secondary threshold*	11%	12%	12.8%	13.8%
Above upper earnings limit	1%	2%	12.8%	13.8%

* Reduced rate for married women between primary threshold and upper earnings limit is 4.85 per cent for 2010-11 and 5.85 per cent for 2011-12. The reduced rate applies to women married before 6 April 1977 who have elected to pay a reduced rate of class 1 contributions.

Self employed rates				
	Class 2 (per week) *		Class 4	
Profits per year	April 2010-11	April 2011-12	April 2010-11	April 2011-12
Below small earnings exception	Nil	Nil	Nil	Nil
Small earnings exception to lower profits limit	£2.40	Not available **	Nil	Nil
Lower profits limit to upper profits limit	£2.40	Not available **	8%	9%
Above upper profits limit	£2.40	Not available **	1%	2%

* Class 2 NICs are paid at a weekly flat rate of £2.40 by all self employed persons. Those with profits less than, or expected to be less than, the level of the small earnings exception may apply for exemption from paying Class 2 contributions.

** The exact figure for class 2 for 2011-12 will be determined by data available in the autumn.

State Pension

The Government will uprate the basic State Pension by a triple guarantee of the highest of earnings, prices or 2.5 per cent from April 2011.

Child and Working Tax Credit rates

The child element of the Child Tax Credit will increase by £150 above CPI in April 2011. The baby element of the Child Tax Credit will be removed from April 2011.

Child and working Tax Credits rates		
£ per year (unless stated)	April 2010-11	April 2011-12
Income thresholds and withdrawal rates		
First withdrawal rate	39%	41%
Second income threshold	50,000	40,000
Second withdrawal rate	6.67%	41%
Income disregard	25,000	10,000

Child Benefit

From 2011-12, both rates of Child Benefit will be frozen for three years.

Corporation Tax

Corporation tax on profits	April 2010-11	April 2011-12
£0-£300,000	21%	20%*
£300,001-£1,500,000	Marginal rate	Marginal rate
£1,500,001 or more	28%	27%

* The small profits rate was due to rise to 22 per cent in 2011-12, as announced originally at Budget 2007 and deferred to 2011-12 at 2009 Pre-Budget Report.

Capital Gains Tax

Capital gains tax	April 2010-11	23 June 2010-11
Standard rate	18%	18%
Higher rate*	n/a	28%
Entrepreneurs' relief rate	10%	10%
Annual Exempt Amount	£10,100	£10,100
Entrepreneurs' relief lifetime limit of gains	£2,000,000	£5,000,000

* for higher and additional rate tax payers

Landline duty

Landline duty will not be implemented.

Landline duty	As of April 2010, from 1 October 2010	As of June 2010, from 1 October 2010
Rate per fixed line	50 pence	N/A