



Pre Budget Report
24 November 2008

PRE - BUDGET NEWS 2008

Introduction

Against a background of economic instability, with the world looking at a global recession, Alistair Darling delivered his Pre-Budget Report. The atmosphere was more akin to a budget, and certain measures will have immediate effect. VAT will be reduced from 17.5% to 15% from next Monday 1 December 2008, and this cut will last for 13 months. It will be a nightmare for businesses to implement and its effect will only be with the end user. There is a question as to how much impact it will have, given the price cuts that retailers have been delivering recently. But it should help retailers, if only to reduce the amount that they have to pay over to HMRC.

Borrowing will increase to a peak of 57% of GDP in 2013/2014, to finance this and other measures and giveaways. Higher taxes will be paid through increased National Insurance, a new 45% higher rate, restriction of the benefit of personal allowances to those on higher incomes, amongst other measures. The increases in taxes generally start from April 2011, although some start sooner.

For specific advice, contact any of the Dodd & Co tax team on 01228 530913 or 01768 864466 or reply to this e mail and someone will get back to you.

Income Tax

	2008-09 £	2009-10 £
Personal Allowance – under 65	6,035	6,475
Personal Allowance – 65 – 74	9,030	9,490
Personal Allowance – 75 and over	9,180	9,640
Married Couples Allowance – under 65	Nil	Nil
Married Couples Allowance – 65 – 74 born pre 06/04/35	6,535	6,865
Married Couples Allowance – 75 and over	6,625	6,965
Earned income – Basic Rate (20%) Band – income to	34,800	37,400
Earned income – Higher Rate (40%) income over	34,800	37,400

National Insurance

Per Week	2008-09 £	2009-10 £
Class 1 – Employment Income		
Lower earnings limit – No NIC paid at this limit - credit given	90	95
Secondary limit – NIC starts to be paid	105	110
Upper earnings limit – main rate limit	770	844
Upper accruals point – no further credit given but NIC paid	770	770
Class 2 rate	2.30	2.40
Small earnings limit (annual profits)	4,825	5,075
Class 4		
Lower profits limit – per year	5,435	5,715
Upper profits limit – per year	40,040	43,875

There are no changes to the rates of National Insurance in 2009-10.

From 2011-12

All rates of National Insurance will be increased by 0.5%.

Higher Earning Individuals

Changes To Take Effect In 2010-11

The personal allowance will be restricted for those earning over £100,000. For every £2 earned above £100,000 the allowance will be restricted by £1 until it is reduced to half the basic personal allowance. This means that if the basic allowance for 2010-11 is set at £7,000 (for example), individuals earning over £107,000 will receive half the personal allowance (£3,500).

Those whose income exceeds £140,000 will have the remaining half of the allowance reduced so that for every £2 of income over £140,000 £1 is taken off the remaining allowance. This means that, with the same figures as above, individuals earning over £147,000 will not get the benefit of any personal allowance.

Changes To Take Effect in 2011-12

A higher tax rate of 45% will be levied on earned income and savings income over £150,000.

The rate for dividend income above £150,000 will be 37.5%. This equates to tax of 30.56% on net dividends.

Trusts

These higher rates will also be the trust tax rates from 6 April 2011. The 37.5% rate will apply to dividend income and the 45% rate will apply to all other income.

Tax Credits Rates

The main change for families claiming child tax credits is that the child element of the award is increasing above indexation to £2,235 per child from April 2009, an increase of £150 from £2,085 in 2008/09.

The other elements of the tax credits award for both child tax credits and working tax credits are increasing in line with inflation. The disregard for changes in income during the year remains at £25,000.

A further positive announcement for families is that the increase to the child benefits rates will be paid from 5 January 2009 instead of 6 April 2009. The new amounts payable will be £20.00 per week for the first or only child and £ 13.20 per week for subsequent children.

Corporation Tax

There were no radical changes or surprises in relation to corporation tax.

Rates of corporation tax

As expected, the small companies rate of corporation tax of 21% will continue for another year, with the increased rate of 22% being introduced in April 2010.

Income shifting - Husband and wife companies

Buried in the small print of the press releases, there was a welcome announcement for husband and wife companies which explained that the government has decided not to introduce the new "income shifting" rules in the foreseeable future. This means that family companies can continue to take advantage of the tax planning arrangements that were formally approved by the House of Lords in the "arctic systems" case.

Loss carry back

A temporary measure is introduced with effect from today, whereby companies with a trading loss in an accounting period ending after 23 November 2008 (but before 24 November 2009) will be able to carry this loss back 3 years and potentially obtain a repayment of corporation tax. A very similar measure was introduced in the last recession, but this time the relief is not as generous because the carry back is capped at £50,000 in relation to carrying the loss back more than one year (whereas the full amount of the loss could be carried back when the three year loss carry back relief was last introduced).

Derelict land - land remediation relief

Companies that incur expenditure in bringing long term derelict land back into use will be able to obtain additional tax relief as a result of the land remediation relief rules being extended to cover a wider range of expenditure. In future, the following expenditure will qualify for an additional 50% enhanced tax relief providing certain conditions are met:

- the removal of buildings or other structures or machinery bases
- the removal of reinforced concrete pilecaps and basements
- the removal of underground pipes (or other apparatus) for the supply of electricity, gas, water, telecommunications, or for drainage or sewerage.
- the removal of post-tensioned concrete heavyweight construction

Included within the required qualifying conditions are that the land has to have been derelict since 1 April 1998 and must also have been derelict at the time it was acquired by the claimant. Given the government's desire to encourage both consumers and businesses to spend, it is slightly surprising that this new relief is not being introduced until next April.

Corporation Tax / Continued

International

The government is going to try and stem the recent trend of international groups moving their headquarters offshore, by introducing next April an exemption from UK tax for dividends that are received from overseas companies. Improvements to the Controlled Foreign Companies (CFC) rules are also to be introduced in subsequent years.

Anti-avoidance

As usual, the government took the opportunity to announce a number of new anti-avoidance provisions to counter tax avoidance arrangements involving leasing and film schemes.

Trading Loss Carry Back – Sole Traders and Partnerships

The Chancellor used his Pre Budget Speech to announce that he was extending the loss carry back rules for companies, but he did not mention the position for sole traders and partnerships.

A welcome sight in the press releases was therefore the notification that all sole traders and partnerships who suffer a loss in their accounting period ending between 6 April 2008 and 5 April 2009 will also be able to change the way they obtain tax relief on the loss incurred.

The current rule is that established businesses have been able to carry losses back to set against taxable income in only the previous tax year.

The new rules announced today will allow the losses to be carried back for as many as three tax years, the losses being claimed against the latest years first. These new rules will however be restricted so that a maximum of £50,000 of losses can be carried back for more than one year.

To illustrate, assume a previously successful business has been hit hard by the credit crunch and in the accounting year ending on 31 December 2008 the business will suffer a loss of £120,000. The business generated profits of £60,000 in 2007, £40,000 in 2006 and £30,000 in the 2005 accounting year.

The business owner can claim for £60,000 to be set against the taxable profit they earned in the year ending 31 December 2007. This will reduce the tax liability for that year to nil, and a tax repayment can be claimed.

Under the previous rules no further loss claim could be made, and £60,000 of losses could only be carried forward and utilised against future accounting profits. This gives no immediate benefit for the business owner as no tax repayment can be claimed for a large part of the losses.

However, the announcement made today will enable the business owner to carry back up to a further £50,000 of losses to the two previous years.

In this example this will result in £40,000 of losses being set against the taxable profit for the December 2006 accounts, meaning all of the tax paid in that year can also be reclaimed, with a further £10,000 being set against the profits from the December 2005 accounting period.

Trading Loss Carry Back – Sole Traders and Partnerships / Continued

A total of £110,000 of losses will therefore get relief immediately, with only a small balance of £10,000 being carried forward to reduce the tax payable on future profits.

The business owner will need to weigh up whether this is the best use of the losses, and the tax team at Dodd & Co can use their Know How to help with this decision. For example the business owner would only have paid tax at a rate of 20% on a large part of his profits in 2006 and 2005, whereas he may anticipate a higher profit in future years which could lead to him paying tax at a rate of 40%. It is therefore necessary to weigh up whether a 20% tax repayment now is more attractive than a 40% reduction in tax in future years.

Please contact us if you would like to discuss how these changes affect you.

Cars and Capital Allowances

The government has confirmed their intention, which was outlined in the budget earlier this year, to provide tax relief (in the form of capital allowances) based on a vehicle's CO₂ emissions. In addition, the government has confirmed that the restriction on a business' access to a full deduction for lease payments, will also be based on the vehicle's CO₂ emissions. These new rules will apply to businesses from 6 April 2009 and companies from 1 April 2009.

Currently, the capital allowance treatment for cars is based on the vehicle's cost, and whether it is higher than £12,000. Where a vehicle's cost is less than £12,000, the cost is added to the business' capital allowance pool and tax relief is available at 20%, with no restriction. In instances where a vehicle's cost is greater than £12,000, the capital allowances of the vehicle is calculated independent of the general pool, with an annual restriction of £3,000 being applied. This means that where the vehicles cost is greater than £12,000, the capital allowances available for that vehicle can never exceed £3,000 in a year.

On disposal of a vehicle, which costs greater than £12,000, a balancing allowance is allowed in the year of disposal where the proceeds received are less than the tax written down value. A balancing allowance applies where the proceeds are greater than the tax written down value.

From April 2009, the rules that restrict a vehicle's capital allowances where the cost is greater than £12,000 have been abolished. In addition the rules which require a vehicle to be held in a separate capital allowance pool, will be removed. However, cars owned by sole traders / partnerships, that are used privately, will continue to be held in a separate pool.

These rules have been replaced with a CO₂ format and will attract writing down allowances at the following rates:

Greater than 160 g/km	10%
Less than or equal to 160 g/km	20%
Less than or equal to 110 g/km	100%

Cars and Capital Allowances / Continued

This could result in businesses taking longer to receive similar allowances under the current regime, where the vehicle's CO₂ emissions are greater than 160 g/km.

Expensive vehicles which are currently in a separate pool will continue to stay in their own pool for a period of up to 5 years (or until disposed of), at which time they will then be transferred to the general pool and receive writing down allowances at 20%.

The disallowance of leases payments has historically been dependant on the vehicle's list price, however, from April 2009, the government will introduce a flat rate scheme where only vehicle's with CO₂ emissions of greater than 160 g/km will have a 15% disallowance applied against their lease costs.

Existing leases will not be affected by the introduction of the new rules.

Expenditure incurred by businesses on motorcycles will qualify for the Annual Investment Allowance and therefore potentially receive 100% allowances in the year that they are acquired.

VAT Rate Cut to 15%

The Chancellor's decision to cut the standard rate of VAT from 17.5% to 15% was no surprise to many, as it was leaked well in advance of the Pre Budget Report. However, the last time the VAT rate was changed was seventeen years ago, and therefore many businesses are concerned about how the rate change will affect them on a practical level.

Businesses will have to make their own decision on whether to cut prices to customers or leave their prices unchanged and increase their profit margins. However, the Chancellor indicated that the spirit of the cut was to help increase consumer demand and start customers spending.

The cut will be effective from 1 December 2008, and will be withdrawn in January 2010. The new rate is likely to cause real headaches for many VAT registered businesses. Many firms will find that their bookkeeping and computer systems will struggle to cope with the change in the rate of VAT, and some will find it a challenge to understand the relatively complicated rules about what VAT rate to charge on supplies which straddle the month end. Others will be concerned about the cost of changing price lists and reconfiguring tills. Businesses which use cash accounting or retail schemes are likely to have particular difficulties in implementing the new VAT rate and should seek advice as soon as possible.

The practical problems are not restricted to the income side of business' VAT affairs. Many firms will find that when they do their next VAT return, they will have some purchase invoices which show VAT at 17.5% and others which show VAT at 15%. Care will have to be taken to ensure that VAT is reclaimed at the correct rate.

However, one benefit that many may not be aware of is that the cut in the rate of VAT will also cut fuel scale charges. The quarterly scale charge for cars with CO₂ emissions of 120g/km or less will fall from £20.55 to £18.00 as a result of the reduction in the VAT rate, and the scale charge for the most polluting vehicles will fall from £71.94 to £63.00.

HMRC has promised to operate a light touch for businesses' first return using the new rate, but it is still vital to try to avoid any errors. To try to help answer some of the queries that businesses will want to ask, we have put together a list of FAQ's, but if you would like to discuss how the change in VAT rate affects your business, contact Faye Armstrong on 01228 530913 or email faye@doddaccountants.co.uk.

VAT Rate Cut to 15% / Continued

FAQs

What is the new VAT fraction?

The old 7/47 will be replaced by 3/23.

What date is the new rate effective from?

The new rate of VAT applies to all standard rated supplies made on or after 1 December 2008. However, there are some transitional rules, as explained below.

What happens if I make a supply in November but raise an invoice in December?

Goods

You should charge the rate of VAT that is in force at the date the goods are “removed” from your premises. However:

- If somebody removed goods from your premises between 18 November and 30 November,
- But they have not paid you by 1 December,
- Then you can raise an invoice dated 1 December and charge them VAT at 15%.

Services

You should charge the rate of VAT that is in force at the date the services are provided to your customer. However:

- If you finished supplying the services between 18 November and 30 November,
- But the customer had not paid you by 1 December,
- Then you can raise an invoice dated 1 December and charge VAT at 15%.

Continuous Services

Some services such as construction services are supplied over a long period of time. The VAT is accounted for on these services when a VAT invoice is raised. If a VAT invoice is raised for these services on or after 1 December 2008, then as long as you have not received payment for them by that date, VAT should be charged at 15%.

I use the flat rate scheme – will my flat rate percentage fall?

HMRC have reduced some flat rate percentages as a result of the reduction in the standard rate of VAT. See our special page about the flat rate scheme for more details of which rates have fallen, along with details of the changes to the tests for joining and leaving the scheme.

Flat Rate Scheme Simplification

The over complicated rules which governed when a business could join the flat rate scheme were simplified in the Pre Budget Report.

In the past, businesses had to pass two income tests before they could join the scheme – one looked at their income from standard rated and zero rated supplies, and the other looked at their total business income. These confusing tests are to be simplified, and from 1 April 2009, businesses will be able to join the flat rate scheme provided that they expect their income from standard rated and zero rated supplies to be less than £150,000 in the next year.

The test for deciding whether a business has to leave the scheme have also been simplified, and from 1 April 2009, businesses will be able to stay on the scheme as long as they expect their flat rate income, that is the income that they apply the flat rate percentage to, to be less than £225,000 in the next year.

Reductions in the flat rate percentages for many businesses were also announced in the Pre Budget Report. These will be effective from 1 December 2008, and aim to ensure that businesses on the flat rate scheme do not lose out from the reduction in the standard rate of VAT. The rate for those in the hotel sector fell from 9.5% to 8.5%, whilst the rate for business services not listed elsewhere fell by 1.5% to 9.5%. A full list of the new flat rate percentages is available on HMRC's website.

HMRC's New Business Payment Support Service

From 24 November 2008 the Revenue have introduced a new Business Support Service designed to meet the needs of businesses affected by the current economic conditions.

If you are concerned about being able to meet tax, National Insurance or other payments owed to HM Revenue & Customs, or you anticipate that payments becoming due in the future will cause you problems, you can get in touch with the Revenue to discuss payment options. This is intended to help you deal with temporary cashflow difficulties.

The number for the new support line is 0845 302 1435. You can call this number to discuss your payment options and arrange for the payments to be made over a longer period if necessary. The Revenue will not charge additional late payment surcharges on payments included in the arrangement, although interest will continue to be payable on those taxes where it applies from the due date of payment.

The information you will need to supply if you contact the Revenue are:

- your tax reference number
- details of the tax that you are or will have trouble paying
- basic details of your business's income and outgoings

Assistant For SME's

There is a variety of measures that should be of assistance to small and medium sized businesses.

Early in 2009 the Government will launch a **Small Business Finance Scheme** – a temporary scheme to enable up to £1bn of lending by banks that will be supported by Government.

The Government will also make available a **capital fund of £50 million providing equity** or quasi-equity to SME's that are overleveraged.

The **RDA's will launch loan funds**, similar to that already launched by Advantage West Midlands, to provide transition funding for viable SME's facing financial difficulties.

The **Empty Property rate Relief** will be extended, to give exemptions to rates on empty properties with a rateable value up to £15,000 – the Government claim that this will exempt about 70% of empty properties from business rates.

Where there has been a rating review, and backdated rates liability agreed, those back rates have in the past been payable immediately. They will now be able to be paid in interest free installments over 8 years.

Income Shifting, transferring profits between, usually, a husband and wife, has been on the Government's agenda for some time – for example, the Arctic Systems Case. The Government promised a review in this pre- budget report. This review has been temporarily shelved, "given the current economic challenges".

Tax Relief For Large Pension Contributions

Tax relief on contributions to a pension scheme is restricted by reference to two limits. The "Lifetime Allowance" (LTA) refers to the total value of your pension fund and the "Annual Allowance" (AA) refers, as the name suggests, to the amount you contribute in one year.

The LTA was set in 2006 and was due to rise to £1.8 million in April 2010. The AA will rise to £255,000.

The Chancellor announced in his Pre-Budget Report that these limits will remain the same for the five years commencing April 2011. The freezing of the LTA will affect other limits that are set by reference to the LTA. The commutation limit for example is 1% of the LTA, so this could affect those wishing to take a small pension fund as a lump sum.

Duties

Whilst the reduction in the rate of VAT is a temporary measure there has been a compensatory increase in the rates of duty on fuel, alcohol and tobacco, but this appears to be a permanent increase. The tobacco duty is set to increase (by 2% for cigarettes and 4% on other tobacco products) and this is effective from tonight (24 November 2008), but the increase to the alcohol duty (by 8%) and the fuel duty rates will not take effect until 1 December 2008. The unleaded and diesel increase will be 2p per litre, with a further increase to both of 1.84p per litre from 1 April 2009.

The chancellor also announced a reform to the rates of Air Passenger Duty (APD) levied on all flights from the UK. The new rates will be spread over 4 bands and will be based upon the distance travelled (to the capital city of the destination country) in miles from the UK (London) during a flight. There will still be two rates of duty based upon the class of travel. The new rates will be effective for those planning to travel on or after 1 November 2009 (and will include those who have already booked their tickets).

There was also an announcement that the proposed increases in vehicle excise duty rates would be capped and be introduced over the next two years in an attempt to ease the burden on motorists. Vehicles with CO₂ emissions under 141g/km will see no increase in their duty on 1 April 2009 (and reductions from 2010/11), but those over 140g/km CO₂ emissions will see a rise of £5 with effect from 1 April 2009 (with further rises of up to £30 from 2010/11).

Giveaways For Pensioners

The Basic state pension will increase to £95.25 per week in April 2009. from £90.70 – this is the October 2008 inflation increase. In addition, each pensioner will receive a one off payment of £60 in January 2009, to effectively give all pensioners the benefit of the increase from January.

The Pensioners Credit minimum income guarantee also increases, to £130 for individuals and £198.45 for couple for 2009/10.

The Savings Gateway – For Those On Benefits And Receiving Credits

The Government will add 50p to every £ saved under a new Savings Gateway Scheme. It will be introduced in 2010 and should be easy to use and understand. The Government expect 8 million people to be able to qualify to use the scheme.



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