

Budget 2007

The Highlights

Gordon Brown, the longest serving Chancellor of the Exchequer in 200 years, presented his eleventh – and probably final – Budget on 21st March. Mr Brown has been quoted as saying that there are two types of Chancellor – those who fail and those who get out in time. It would appear that he will fall into the second category.

Companies

This was a mixed Budget for companies, with larger companies gaining and smaller companies losing out.

When the present Government came to power in 1997, Mr Brown lowered the rate of corporation tax but over the last decade rates in other countries have fallen significantly. The average rate in the EU is now around 25% and the rate in Ireland is 12.5%. This is beginning to make international companies question whether the UK is still the best place to do business and several high profile companies have recently relocated. Mr Brown has been under pressure to reduce the rate of corporation tax and he has now announced that the rate will fall from 30% to 28% from 1 April 2008. While this reduction is welcome, further reductions may be necessary to persuade businesses to remain in the UK.

For small companies, however, the rate of corporation tax will increase in stages from the current level of 19% to 20% from 1st April 2007, 21% from 1st April 2008 and 22% from 1st April 2009. The thinking behind this measure is difficult to understand – it will discourage rather than encourage enterprise in small businesses, a sector the Government has consistently said that it wished to support.

The Chancellor announced improvements in the allowances companies can claim for expenditure on research and development (R&D) from 2008/09. Small and medium size enterprises (SMEs) spending more than £10,000 will benefit from an increase in the amount they can claim from 150% of the actual expenditure to 175% and large companies will see an increase from 125% to 130%. In a further relaxation of the rules, companies with fewer than 500 employees will now be able to claim the SME rates of R&D tax relief. The facility to claim the relief by way of partial repayment of PAYE liabilities will remain. An opportunity to remove the £10,000 hurdle and to simplify the definition of R&D (a regular issue in claims) has again been missed.

Businesses

Another shock was the announcement that capital allowances are to be reformed. The details will be in the Finance Bill (due to be published on 29th March) but we know that the main features will be:

- Phasing out of Industrial Buildings Allowances and Agricultural Buildings Allowances over the next four years (with the immediate scrapping of balancing events)
- A £50,000 annual investment allowance for investment in plant and machinery allowable at 100%
- Reduction of writing down allowances from 25% per annum to 20% per annum (10% for certain equipment installed in buildings)
- An extension of the 50% first year allowance for small enterprises for a further year
- A payable tax credit for investment in certain “green technologies” from 2008/09

These changes will impact on manufacturing businesses, agriculture, any business investing significant amounts in equipment and the commercial property sector.

The VAT registration threshold will rise to £64,000 from 1st April and the deregistration limit will rise to £62,000. The VAT scale charge on motor vehicles owned by businesses is being recast so that it is based on CO₂ emissions for VAT periods beginning on or after 1st May.

Individuals

As with company tax rates, the Chancellor has given with one hand and taken with the other. The 10% band for the first £2150 of income is being withdrawn from 6 April 2008 and from the same date the basic rate of income tax will fall from 22% to 20%. This will hit those on low incomes and intriguingly the 10% rate will remain for those with investment income; this seems an odd measure for a Labour Chancellor.

There will be an alignment of the upper national insurance limit with the start of higher rate tax band. This will increase the amount of earned income on which employees and the self employed pay national insurance.

Pensioners will see their tax free allowances grow steadily so that by 2011 those over 75 will pay no tax on income of up to £10,000.

The investment limits for Individual Savings Accounts (ISAs) will rise from £7,000 to £7,200 but with an increase in the permissible cash element from £3,000 to £3,600.

In an unexpected announcement, the Government has confirmed that people who own property outside the UK through an overseas company will not have to pay tax on the "benefit in kind" of living there. Unusually, this announcement is fully retrospective and anyone who has paid tax in the past will be able to reclaim it.

Individuals receiving dividends from foreign companies will, in most cases, benefit from a notional 10% tax credit from 6th April 2008.

The inheritance tax (IHT) allowance rises to £300,000 from 6th April and will rise in stages to £350,000 in 2010/11.

There were changes to the Enterprise Investment Scheme, Corporate Venturing Scheme and to Venture Capital trusts which will limit the amount that companies can raise through these tax favoured schemes to £2 million per annum.

A new targeted anti avoidance rule (TAAR) has been introduced for certain capital gains tax transactions and while H M Revenue & Customs (HMRC) have said that this will only be applied to certain types of blatant avoidance, the rules are widely drawn and could theoretically catch some routine tax planning. Clarification has been sought. There are dangers in legislation which is drawn widely but partially disapplied by concession: the courts can only rule on the basis of the law as enacted and concessions can be withdrawn if HMRC – or Government – decide that a form of planning is no longer acceptable.

Guilty Pleasures

Duty on beer was increased by 1p a pint, on cider by 1p a litre (5p for a 75cl bottle of sparkling cider), on wine by 5p for a 75cl bottle and on sparkling wine by 7p for a 75cl bottle. The duty on spirits remained unchanged. The rate of duty on tobacco products increased in line with inflation.

Motorists will pay an extra 2p a litre from 1st October and those driving new cars with CO₂ emissions over 226 g/km will see their vehicle

excise duty rise to £300 this year and £400 next year.

Other Measures

In an attempt to block a perceived avoidance measure, the Government is mounting an attack on Managed Service Companies (MSCs). These have become popular with workers in the construction industry and enable workers to receive their income as a mixture of salary, dividends and expenses. The new measure is designed to put workers in such companies in the same position for tax and national insurance as employees of the company for which they actually carry out the work. Further measures are planned to avoid the non payment of tax due by allowing HMRC to pursue people other than the individual worker.

The Government has also continued its crackdown on VAT "carousel" fraud.

Summary

The 2007 Budget delivered an odd mixture of measures with some clear winners and some unexpected losers. Many small businesses will find that they have lost out at the expense of larger businesses.

Looking back over the Chancellor's eleven Budgets it is striking that the measure that the tax profession feared most from Mr Brown – a severe hardening of the IHT regime – has never materialised, though the substantial changes to the trust tax regime in 2006 reduced the IHT efficiency of many trust arrangements.

The main features of his Chancellorship will probably be remembered as a sustained – and arguably successful – assault on tax avoidance and an increase in both the volume and complexity of legislation: the volume of tax legislation has doubled in the last decade. He has also more than doubled the amount of income tax, IHT and CGT collected and has tripled the amount of stamp duty and stamp duty land tax.

If you would like to receive a copy of our Budget tax rates card, our quarterly newsletter or would like to talk about some specific tax planning, please contact us: the details are given below.



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