

Pre-Budget report for 2008 – 24 November 2008

Chancellor Alistair Darling has announced the government's Pre-Budget report for 2008. The report is in effect a mini-Budget designed to help the government's finances cope with impending recession and the effects of international financial crisis. The key features are summarised in the following paragraphs.

Income tax rates and allowances

- For 2009/10, the main rates of income tax will be the 20% basic rate and the 40 per cent higher rate.
- The basic personal allowance for 2008/09 was increased above indexation from £5,225 to £6,035. For 2009/10 the allowance will be increased by £130 above indexation from £6,035 to £6,475. The basic rate limit for 2009/10 will be increased by £800 above indexation from £34,800 to £37,400.
- The personal allowance for those aged 65 to 74 will be increased from 2009/10 from £9,030 to £9,490. The personal allowance for those aged 75 and over will rise from £9,180 to £9,640.
- The starting rate limit for savings income will increase from £2,320 to £2,440 in 2009/10.
- From 2010/11, the basic personal allowance will be subject to income limits of £100,000 and £140,000. Where an individual's gross income before personal allowances and any other deductions is below or equal to the £100,000 income limit, they will continue to be entitled to the full amount of the basic personal allowance. If an individual's gross income is above the income limit of £100,000, the amount of their allowance will be reduced by £1 for every £2 above the income limit up to a maximum of one half of the basic personal allowance. If an individual's gross income is above a second income limit of £140,000, the amount of their allowance will be further reduced by £1 for every £2 above the income limit up to a maximum of the full amount of the basic personal allowance.
- A new 45% rate of income tax will apply to taxable non-savings and savings income above £150,000 on and after 6 April 2011.
- A new 37.5% rate of tax will apply to taxable dividend income above £150,000 on and after 6 April 2011.
- The dividend trust rate and the trust rate of tax will be increased to 37.5% and 45% respectively from 6 April 2011.

National Insurance rates and limits

- For 2009/10 the Upper Earnings Limit (UEL) for primary Class 1 National Insurance Contributions (NICs) will be aligned with the level at which people start to pay higher rate income tax. The new limit will be £844 per week, with an annual equivalent of £43,875.

- From 2011/12 the NICs primary threshold will be broadly aligned with the income tax basic personal allowance.
- From 2011/12 the main rate of Class 1 and Class 4 NICs will be increased by 0.5% to 11.5% and 8.5% respectively.
- From 2011/12 the Class 1 employer rate of NICs will be increased by 0.5% to 13.3%. The increased rate will also apply to Class 1A and Class 1B contributions.
- From 2011/12 the additional rate of Class 1 and 4 NICs, which is paid on income above the UEL, will be increased by 0.5% to 1.5%.

Corporation tax rates

- The planned increase of the small companies' rate (SCR) of corporation tax from 21% to 22% from 1 April 2009 has been deferred until 1 April 2010.
- Legislation will be introduced in Finance Bill 2009 to maintain the SCR for all profits, apart from ring fence profits, at 21% from 1 April 2009 and set the fraction used to smooth the difference between the main rate of CT and the SCR (marginal SCR) at 7/400. Profits limits will remain the same.
- The SCR for ring fence profits will remain at 19% from 1 April 2009 and the marginal small companies' relief fraction for ring fence profits will remain at 11/400.

Business taxation

- **Losses** - The provisions under which businesses may carry trading losses back against profits of earlier years to get a repayment of tax are being extended for a one-year period. The new rules apply for company accounting periods ending in the period 24 November 2008 to 23 November 2009. For unincorporated businesses, the measure will have effect in relation to trading losses for tax year 2008/09. Broadly, the period is being extended from the current one year entitlement to a period of three years, with losses being carried back against later years first. The amount of losses that can be carried back to the preceding year remains unlimited. After carry back to the preceding year, a maximum of £50,000 of the balance of unused losses is then available for carry back to the earlier two years.
- **Business expenditure on cars** - Budget 2008 announced the abolition of the current rules for "expensive cars", replacing them with an environmentally based pooling system. It has now been confirmed that the rate of writing-down allowance will be based on the CO2 emissions of the car. In addition, the restriction on allowable lease rentals for businesses that lease or hire cars will also be based on the CO2 emissions of the car. The new rules will generally have effect on and after 1 April 2009 for businesses in the charge to corporation tax, and on and after 6 April 2009 for businesses in the charge to income tax.

From April 2009 the special rules that restrict the amount of capital allowances for cars costing more than £12,000 will be abolished.

Qualifying expenditure incurred on or after 1 or 6 April 2009 on cars will be allocated to one of the two general plant and machinery pools. The pool that is appropriate will depend on the car's CO2 emissions. Expenditure on cars with CO2 emissions over 160g/km will be dealt with in the special rate pool and will attract WDAs at 10%. Cars that have an element of non-business use will continue to be dealt with in a single asset pool to enable the private use adjustment to be made, but for expenditure incurred from April 2009 onwards the rate of WDA will be determined by the car's CO2 emissions.

Motorcycles are to be excluded from the definition of cars and will not, therefore, be subject to the new rules. Expenditure incurred on motorcycles on or after 1 or 6 April 2009 will qualify for Annual Investment Allowance.

- **Income shifting** - The income shifting legislation that caused much concern in the last pre-budget report will not be included in Finance Act 2009. This is good news, especially for contractors. And with the next pre-budget report likely to be in the run-up to the next general election, perhaps we will not see its reappearance in the near future.
- **Foreign dividends** - An exemption for foreign dividends for large and medium sized businesses has been confirmed. This will be introduced in 2009.
- **Plant and machinery leasing** - Anti-avoidance measures are being introduced to counter avoidance involving a leaseback following the sale or lease of plant or machinery. The new rules will ensure that a business entering into such arrangements does not gain more relief than it would have done had it obtained loan finance, and that tax is not avoided when a lessor grants a long funding lease. The new provisions will also ensure that when a long funding lease ends, the lessee has obtained an appropriate amount of relief. The measure will have effect for leasebacks entered into, and long funding leases granted or ending, on or after 13 November 2008.
- **Land remediation relief** - The existing land remediation relief rules, which give bodies liable to corporation tax a deduction of 150% for qualifying expenditure on removing or mitigating the effect of contamination, are to be amended to give greater clarity on what categories of expenditure qualify for relief, whilst at the same time giving companies greater certainty about whether their expenditure will qualify for relief. The measure will have effect for expenditure incurred on or after 1 April 2009.
- **HMRC Business Payment Support Service** - HMRC will provide a new service for businesses in temporary financial difficulty and unable to pay their tax bills to spread payment of their bills over a timetable they can afford. The service will cover all taxes paid by business, including corporation tax, VAT, PAYE, income tax and National Insurance Contributions.

- **Business rates** - Small firms are to get a temporary increase in threshold for empty property relief. For 2009/10 empty commercial properties with a rateable value below £15,000 will be exempt from business rates.

Personal taxation

- **Pensions** - The lifetime allowance (LTA) was set at £1.5 million when it was introduced in April 2006 and it was set to rise in stages to £1.8 million in 2010/11. The annual allowance (AA) was set at £215,000 in April 2006 and was set to rise to £255,000 in 2010/11. The government has now confirmed that the 2010/11 LTA of £1.8 million and the AA of £255,000 will continue to apply, with their rates held constant, for a further five tax years, i.e. up to and including the tax year 2015/16.
- **Individual Savings Accounts (ISAs)** - The list of investments that can qualify for the ISA regime is being extended from 16 December 2008 to include bonds which are issued by Multilateral Institutions (as defined by the Organisation for Economic Cooperation and Development(OECD)).
- **Savings Gateway** - A new state supported saving scheme - known as the Savings Gateway - will be launched, in which the government will contribute 50 pence for every pound saved. It will start in 2010 and is targeted at 8 million people on low incomes.
- **Disabled company car drivers** - Legislation will be introduced in Finance Bill 2009, effective on or after 6 April 2009, to extend the special treatment to allow disabled company car drivers driving an automatic car to use the lower list price of an equivalent manual car to work out the benefit charge. They can already use the CO2 emissions of an equivalent manual car to measure the benefit.
- **Employment-related securities** - Legislation will be introduced in Finance Bill 2009 to simplify certain tax rules that apply to employment-related securities or shares (ERS) acquired by employees for less than market value. An outdated anti-avoidance provision relating to transactions between associated persons will also be removed. The ERS changes will have effect for transactions occurring on or after the date that Finance Bill 2009 receives Royal Assent. The repeal will have effect on and after the same date.

Currently, if an employee receives shares from his or her employer which are to be paid for in instalments, then sells the shares before all of the instalments have been paid, a tax charge can arise, even where the employee has made no profit overall on the shares. The first change will remove this tax charge. However, if the employee is released from any requirement to pay the instalments then a tax charge may still be imposed.

The second change removes a tax charge that can arise on the sale by an employee of nil or partly-paid shares, even where the employee has made no profit overall on the shares.

The third change covers the situation where an employee has received shares from his or her employer, and a scrip issue or bonus issue is made so that the employee receives new shares in proportion to their existing shareholding. Although the employee has received no extra value overall, because the value of their existing shares will have fallen, a tax charge can arise in some circumstances. Broadly, this change will ensure that the correct tax charge (which may be nil) will arise.

VAT

- **VAT rates** - The standard rate of VAT is being reduced from 17.5% to 15% from 1 December 2008. The rate will remain at 15% until 1 January 2010 when it will revert to 17.5%.

Zero rated supplies, such as basic foodstuffs, children's clothing and books; exempt supplies, such as education and health; and supplies subject to VAT at 5%, such as domestic fuel and power are not affected by this change.

Anti-forestalling legislation will be introduced in Finance Bill 2009 to ensure that businesses are not able to use artificial arrangements to reduce the VAT rate on goods or services to be provided after the VAT rate reverts to 17.5% where there is no current economic activity.

- **Bespoke retail schemes threshold** - This measure will increase (from £100 million) to £130 million the threshold above which a business may not use a published retail scheme to account for VAT on its retail supplies. The measure will have effect on and after 1 April 2009.
- **Flat rate scheme** - The entry and leaving tests for the flat rate scheme are being simplified from 1 April 2009. The entry test based on total business income will be removed altogether and the leaving test will be amended, so that businesses can determine their eligibility to use the scheme based upon the method they use to calculate their VAT while on it.

There are currently two tests to determine whether a business may use the scheme. Both entry tests must be met. The first test requires a business to check that its taxable turnover is less than £150,000. The second test requires a business to check that its total income is less than £187,500. The second test will be removed altogether. Eligibility to join the flat rate scheme will be determined solely by the turnover of the business.

Businesses must check the value of their income annually to determine if they are eligible to remain in the scheme. If annual income exceeds £225,000, a business must leave the scheme. "Income" for this purpose is not defined in VAT legislation. Therefore, in order to simplify the scheme, the leaving test will in future be calculated based on the method used by the business to calculate its VAT while on the scheme. Thus, if a business calculates its VAT liability on cash received, the leaving test will also be based on cash received; if liability is calculated on the basis of invoices issued, the leaving test will be based on the same method.

Tax credits and pensions

- The pension credit will be increased in April 2009 from £124 to £130 a week for individuals and from £189 to £198 for couples. State pensions to rise in line with inflation, from £90.70 to £95.25 for a single person. Pension and child benefit increases will take effect in January, three months early, and every pensioner gets a one-off payment of £60 from January while couples get £120.

Fuel and excise duty

- The differential first-year rates on new cars will go ahead in April 2010 - but controversial new rates for older cars will be phased in. Duty rates for all cars will increase by maximum of £5 from next year. In 2010 the maximum rise will be limited to £30 per car, rather than £90. Less polluting cars will see no increase, or a cut of up to £30.

Air passenger duty

- The chancellor said that changing APD into a "tax per plane" rather than a per person tax could harm the aviation industry which was facing "huge problems". Instead APD is to be reformed so that those who travel the furthest - and who have a bigger environmental impact - meet the cost.