

2007 BUDGET REPORT

SUMMARY OF TAX ISSUES



Capital Gains Tax

There are no major changes in the capital gains tax rules.

The Chancellor has increased the capital gains tax annual exempt amount for individuals from £8,800 to £9,200 and for most trustees, the exempt amount has

increased to £4,600.

In his 11th and probably his last budget speech, Gordon Brown set tight spending limits for the future. He also announced a number of taxation changes, details of which were contained in numerous press releases published after his speech finished.

The tax allowances for 2007/08 had been announced in his pre-budget report, but the Chancellor made the headlines by announcing a cut in the basic rate of income tax and in the main rate of corporation tax from April 2008 (ie from 2008/09 onwards). However, he drew less attention to the withdrawal of the 10% income tax band (from 2008/09) and the proposed increase in corporation tax for smaller companies (from 2007/08).

Income Tax Rates and Allowances

Generally, income tax allowances for 2007/08 have increased in line with inflation, although the increase in tax credits varies.

The Chancellor announced that the basic rate of income tax will be reduced from 22% to 20% from 2008/09. He also advised that the starting rate of income tax of 10% will be removed for computing tax on earned income and pensions from April 2008. However, the 10% rate will still be available for investment income (including dividends) and capital gains.

The basic rate limit will increase in real terms by £800 in 2009/10.

The Chancellor promised that child tax credits, working tax credits and personal allowances for older people will be increased by more than inflation from April 2008, to help to alleviate the withdrawal of the starting income tax rate.

National Insurance Contributions

The Chancellor announced an increase (from April 2008) in the upper earnings limit for national insurance of £75 per week (£3,900 per year) above the normal inflation adjustment. The limit will be further increased in April 2009 and will be aligned to the higher rate tax threshold.

Inheritance Tax

There were no major announcements affecting the IHT rules. However, the Chancellor did announce that the IHT 'nil rate' limit for 2010/11 will be £350,000. The nil rate limit for 2007/08 will be £300,000.

Child Benefits

The Chancellor announced an increase in the weekly rate of child benefit for the eldest child to £20, but this increase will not apply until April 2010.

Savings and Investments

The Chancellor confirmed that the annual limit on investments in Individual Savings Accounts (ISAs) will be increased from April 2008 to £7,200, with an increase in the cash limit to £3,600. The previously announced changes have been confirmed, including:

- bringing Personal Equity Plans (PEPs) within the ISA wrapper; and
- removing the distinction between mini and maxi ISAs.

Venture Capital Schemes

The Chancellor announced a number of changes to the 'qualifying company' rules to take effect from 6 April 2007. This will affect individuals investing under the Enterprise Investment Scheme (EIS) or in Venture Capital Trusts (VCTs). It will also affect companies using the Corporate Venturing Scheme (CVS) and companies intending to award employee share options using Enterprise Management Incentives (EMIs).

The main changes are that from 6 April 2007:

- The target company must have raised no more than £2 million under the EIS, VCT and CVS schemes in the previous 12 months; and
- The company raising money must have fewer than 50 full-time employees (or their equivalents) at the date the shares or securities are issued.

This will mean that for VCTs, in particular, it will be more difficult to locate suitable investments.

Business Tax

The Chancellor announced a number of changes that will affect businesses, including the following:

- The main corporation rate will decrease from 30% to 28% from April 2008;
- The small companies' rate of corporation tax will increase from 19% to 20% from April 2007. There will be a further increase to 21% from April 2008 and another increase to 22% from April 2009;
- The temporary 50% rate for first year capital allowances will be extended for small enterprises until April 2008;
- From April 2008 there will be a new £50,000 'annual investment allowance' for expenditure on plant and machinery, although the details have not been settled;
- Capital allowances for industrial buildings and agricultural buildings are to be phased out between 2008 and 2011 and there will be a restriction on balancing allowances and charges;
- There are changes proposed to the rate of capital allowances on certain assets. For example, the rate of writing down allowance for plant and machinery will reduce from 25% to 20% from 2008/09 and there will be a new 10% rate of allowance for building fixtures; and
- There will also be some changes to the tax relief system for research and development expenditure.

The increase in the rate of tax for small companies will impact on many small businesses. It will also deter (as it was intended), businesses incorporating for purely tax reasons.

Alternatively Secured Pensions

As forewarned in the pre-budget report, the Chancellor confirmed a tightening of the rules on Alternatively Secured Pensions (ASPs). This includes the introduction of a requirement to draw a minimum income from an ASP fund and a tax charge where ASP funds, remaining on the death of a member, are transferred to the pension fund of other members in the scheme.

Tax Avoidance

The Chancellor confirmed previously announced changes to the capital gains tax rules to prevent individuals using tax schemes that create artificial capital losses to set against their gains, thereby reducing tax liabilities. The new rules will allow HM Revenue & Customs to restrict loss claims where the loss arose from 'an arrangement' which had a tax advantage as its main purpose.

There was also a proposal to change the tax treatment of commissions related to individuals on personal life policies. In future these will be taxable where they arise from a life policy costing more than £100,000, where there is a chargeable event within three years of the investment.

There are a number of proposals to stop companies obtaining tax advantages in certain circumstances. This includes:

- A measure to stop companies benefiting from buying loss making companies; and
- A change in the rules regarding Employee Benefit Trusts (EBTs), to stop companies obtaining a tax deduction before benefits are paid to employees.

There will be a tightening of the tax and national insurance (NI) rules to prevent individuals avoiding tax and NI by using managed service companies.

Film and Other Partnership Loss Relief

The restriction to 'sideways' loss relief announced on 2 March 2007 has been confirmed, although the Treasury has advised that these new rules are not intended to apply to 'old style' section 48 and section 42 film partnership losses.

Pre-Owned Assets Tax

The Chancellor has announced a relaxation in the time limit for making claims under the 'pre-owned' asset regime. It will now be possible to make a late claim that assets should be treated as falling within the IHT net, rather than incurring an annual income tax charge.

Taxation of Non-UK Dividends

The Chancellor announced a limited relief for individuals in receipt of dividends from non-resident companies. In certain cases a tax credit of 10% will be allowed, although this will only apply where overseas dividends do not exceed £5,000.

Overseas Homes Owned Via Companies

The Chancellor has promised to relax the rules to prevent a tax charge on individuals who own a residential property abroad through a company.

In many countries it is normal practice for residential property to be owned via a company. However, without this relaxation, a tax charge would normally arise if the property is used by the owner or his/her family. The tax is based on the notional benefit of using the property. Unfortunately, many owners of property were not aware of this tax charge.

The change (which acts retrospectively) means that there is no tax charge, provided the company is owned by individuals and certain other conditions are met.

Value Added Tax

The registration threshold for Value Added Tax (VAT) purposes has increased from £61,000 to £64,000 with effect from 1 April 2007.

The deregistration threshold has increased from £59,000 to £62,000 from the same date.

Tax Returns

The Chancellor announced a number of changes to deadlines and other administration arrangements for personal tax returns.

We will provide further information on this, and the other matters in this newsletter, over the coming months.

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