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Budget update

2012/13

21 March 2012

Safety in numbers

HAZLEWOODS

DRIVING LIFELONG PROSPERITY

Contents

INTRODUCTION

George's Budget Bet for Growth

So, another Budget, more paper waving, cheering and jeering, but most of the announcements had already been leaked by the Government in the week before, so what were they all getting so worked up about?

Growth forecasts were slightly increased to 0.8% for the current year, with predictions of 2.0% and 2.7% in 2013 and 2014 respectively. Borrowing is £11 billion lower than was forecast last November, which will be used to repay debt, therefore reducing interest costs.

Announcements were made about reducing welfare costs by £10 billion by the year 2016, providing assistance to double exports to £1 trillion, overhauling the planning regulations to make them simpler and providing extra funding to help construction firms finance new houses.

Tax avoidance has been high on the Government's agenda for a while now and the Chancellor called it "morally repugnant" in his speech today. With that in mind, consultation will take place on a general anti avoidance rule aimed at putting a stop to aggressive and contrived tax planning arrangements. The aim is to introduce this as legislation in the Finance Act 2013.

One of the most publicised areas of tax avoidance recently has been in respect of Stamp Duty Land Tax (SDLT). The Chancellor, therefore, attacked this with some vigour, introducing a new 7% rate for residential properties above £2m, imposing a super charge of 15% on residential properties over £2m being purchased in a "corporate envelope" and blocking a number of specific SDLT avoidance schemes. Furthermore, profits made on the disposal of offshore companies holding residential properties will be subject to capital gains tax from 2013. Consultation will also begin on an annual charge for residential properties already contained within a corporate.

Companies came in for some good news, with the main rate of corporation tax to be reduced by 2%, rather than the anticipated 1%, so that the rate applying from 1 April 2012 will be 24%, with the intention to lower it to 22% by 2014. The indication from the Chancellor was that he would like to align this rate with the current small companies rate of 20%.

Small companies may also benefit by reducing their administrative costs, with the proposal put forward that companies with turnover less than £77,000 will be able to prepare accounts on a cash basis.

The proposed erosion of Child Benefit was revised, so that it is tapered down once one member of the household has income of more than £50,000, with it disappearing completely once income exceeds £60,000. It is understood the mechanics of this will be that Child Benefit will still be received, but will then be repaid through PAYE or self assessment from the parent earning in excess of the thresholds.

This seems contrary to independent taxation and will be seen by many to be unfair. Households with two working parents earning £50,000 each, ie a household income of £100,000 will continue to receive Child Benefit, whereas households with only one parent earning £60,000 will lose their Child Benefit completely. This needs to be reconsidered before its implementation in January 2013.

Better news came in the form of increased personal allowances for income tax. These are to be £8,105 from April 2012, increasing to £9,205 in April 2013. The aim is to remove a further two million people from the tax net. However, all things come at a price, with the additional personal allowances available for individuals over 65 being frozen and effectively tapered away over time. Due to there being no inflationary increases, it is anticipated this will generate an additional £3.29 billion in tax revenues over the next five years.

The Chancellor then spent some time debating the merits of the 50% tax rate for incomes above £150,000. Unsurprisingly, HM Revenue & Customs have informed the Treasury that tax receipts are down by £3.6 billion, predominantly due to the fact that some £16 billion of income was 'brought forward' and self assessed in the year before the introduction of the 50% tax rate. So, he announced the top rate would be 45% from April 2013.

Bearing in mind the Chancellor's comment about changing income reporting practices to avoid the 50% tax rate, this seems a bizarre decision. Those who can alter the timing of their income will do precisely that for the next tax year, reducing their income when the 50% rate is in place, before then taking a huge amount of income on or after 6 April 2013 when the 50% rate is gone! The deferral of the reduction just seems to exacerbate the problem already experienced.

Despite this reduction, the Chancellor estimates that, even after this reduction, the tax revenues generated from his cuts for the wealthiest will generate five times more than is currently the case.

So, despite the advance leaking of details to the press, there were still a few surprises in the Chancellor's speech and, of course, lots of detail he didn't mention that will take some time to sift through. It was nice not to have any bad news about growth forecasts or borrowing and positive that there are tax reductions coming through. With more cash in the back pocket, hopefully more will be spent and the country will grow as a result. In the week after the Cheltenham Festival, it is certainly a gamble, let's hope it pays off!

INDIVIDUALS

Increased personal allowance

The personal allowance will increase by £1,100 from £8,105 to £9,205 in 2013-14. This is in line with the Government's much publicised intention to eventually allow individuals to earn £10,000 per year tax free.

The basic rate band will be decreased by £2,125 from £34,370 to £32,245 in 2013-2014, effectively meaning that those already paying higher rate tax do not benefit from the increased allowances.

The national insurance upper earnings limit will remain aligned with the threshold at which income is taxed at 40%, and will therefore reduce by equivalent amounts, although no announcement has been made about the lower earnings limit.

Additional personal allowance freeze

From 6 April 2013 age related allowances will be restricted and ultimately withdrawn altogether. Individuals born after 5 April 1948 will only qualify for the standard personal allowance with no access to the increased age related allowances currently in existence.

For those born between 6 April 1938 and 5 April 1948 the allowance of £10,500 will be frozen at that level, and for those born on or before 5 April 1938 the frozen amount will be £10,660. When the personal allowance aligns with these amounts, age related allowances will be abolished altogether.

For those with large incomes, such that the age related allowance is already tapered to nil, the change will actually be of benefit. However, for those on smaller incomes who benefit from the age related allowance, the lack of inflationary increase will amount to an increase in tax liability.

Child Benefit restriction

From 7 January 2013 Child Benefit will be withdrawn for families where at least one earner is in receipt of income in excess of £50,000.

Following the previous heavily criticised proposals, the Government has at last announced how Child Benefit will be withdrawn for high earners. Instead of a reduction in payments to the carer, Child Benefit will be clawed back from the highest earner in a household, by an annual income tax charge.

For each £100 earned over £50,000 1% of the Child Benefit allowance will be charged to the taxpayer, so that individuals with income of at least £60,000 will repay all of their Child Benefit. This will either be collected through the self-assessment tax return or via the PAYE code for those in employment.

These provisions emphasise even further how family businesses can plan their remuneration structure to ensure that tax liabilities are minimised and access to state benefits are maximised.

INDIVIDUALS (cont)

Enterprise Investment Scheme (EIS) and Venture Capital Trusts (VCT)

Simplification of the rules

The measures announced aim to simplify the rules of the schemes making them easier for companies, VCTs and investors to use.

Proposed amendments:

For EIS:

- Relax the rules defining when a person is connected to a company through an interest in its capital by disregarding loan capital;
- Widen the definition of shares which qualify for relief, which includes shares to carry a preferential right to a dividend; and
- Remove the £500 minimum investment limit.

These changes will apply to shares issued on or after 6 April 2012.

For VCT:

- Remove the £1 million limit for VCT investment by companies not in partnership.

This change will apply to shares issued on or after 1 April 2012.

Increase to EIS thresholds

Proposed amendments to increase:

- Employee limit to fewer than 250 employees (currently 50 employees);
- The size threshold to gross assets of no more than £15 million before investment and £16 million after (currently £7m and £8m respectively); and
- The maximum amount that can be invested in an individual company, to £5 million (currently £1m).

Subject to approval, these changes will apply to shares in investee companies that are issued on or after 6 April 2012.

Legislation will also increase the annual amount that an individual can invest under the EIS to £1 million and will apply from the 2012-13 tax year.

BUSINESS

Corporation Tax

Main rate of corporation tax

The main rate of corporation tax will reduce by a further 1% to 24% from 1 April 2012.

From 1 April 2013 the rate will be 23% and from 1 April 2014 will be 22%.

Company Cars

Company car benefits

The appropriate percentages, applied to the list price to calculate car benefits, are normally announced approximately two years in advance, in order to give certainty to industry. The rates up to and including 2013-14 have previously been announced.

For 2014-15 there will be an increase of 1% for all bands where cars emit more than 75g of CO_2/km.

The 3% diesel supplement will be removed from April 2016.

In both 2015-16 and 2016-17 the percentages will increase by 2%, to a maximum of 37% (the current maximum is 35%).

From April 2015 the five year exemption for zero carbon and lower rate for ultra low carbon emissions cars will come to an end. The percentage for zero emission and all low carbon cars emitting less than 95g of CO_2/km will be 13% in 2015-16 and will increase to 15% in 2016-17.

Company car fuel benefits

Where employees are provided fuel for private use by their employer, the appropriate percentage is applied to a fixed sum. This increases by £1,400 to £20,200 (from £18,800) for the tax year 2012-13.

There is further commitment to increase the percentage by 2% above the rate of inflation for the tax year 2013-14. The actual figure will be announced once the September 2012 inflation figure is known.

The environment and capital allowances

The Government will extend the 100% writing down allowance for cars used in business for a further two years to 2014/15. From April 2013, however, only vehicles with carbon dioxide emissions of 95g/km or less will be eligible; a reduction from 110g/km under previous legislation.

BUSINESS (cont)

Similarly, to encourage investment in lower emission cars, from April 2013 capital allowances will only be available at the main rate of 18% on vehicles with carbon dioxide ratings of 130g/km or less. Vehicles that do not qualify will form part of the special rate pool that is written off at only 8% each year. This measure will significantly delay the relief available to businesses for all but the most fuel efficient cars.

For leased cars 15% of the rental costs are currently disallowed if the emissions exceed 160g/km. From April 2013 this will be the case for all rental cars where the emissions exceed 130g/km.

Enterprise Management Incentives (EMI)

To assist small and medium sized enterprises recruit and retain high caliber employees, there will be an increase in the value of the share options that may be held by an employee to £250,000; an increase of £130,000.

In addition, it has been announced that from April 2013 there are proposals to extend Entrepreneurs' Relief to cover shares obtained under EMI.

OTHER ISSUES

Stamp Duty Land Tax (SDLT)

Residential properties above £2 million

SDLT on the purchase of a residential property will be charged at 7% of the chargeable consideration, where this is more than £2 million.

This measure will apply for **new** transactions entered into from 22 March 2012.

Contracts that have been entered into before 22 March 2012, but complete after this date, will not be affected, and the old rate of 5% will apply.

Properties acquired by companies (and other non-natural persons)

Where a UK residential property, for consideration in excess of £2 million, is acquired by a non-natural person[1], a higher rate of SDLT at 15% will be charged. These structures have been used as a way of avoiding SDLT on future purchases.

In addition, there will be an introduction of an annual charge in 2013 on such property owned by the same sorts of non-natural persons, which the Government hopes will result in a reduction in the number of high value properties owned in such structures.

The measure will apply from 21 March 2012.

Where transactions which are already in progress and contracts have been signed, on or before 21 March 2012, the higher rate will not apply.

[1] Non-natural persons include companies, collective investment scheme (including unit trusts), and partnerships in which a non-natural person is a partner. There are exclusions from the charges for property developers and corporate trustees in certain circumstances.

SDLT avoidance

Users and promoters of tax avoidance schemes that seek to avoid paying SDLT on the purchase of an interest in land, will be affected by a change in legislation.

The measure will amend the SDLT sub-sales rules, involving sub-sales and an option to purchase land, to make it clear that the grant or assignment of an option cannot satisfy the requirements of the sub-sale rules and, therefore, renders the planning ineffective.

This measure will apply for transactions on or after 21 March 2012.

OTHER ISSUES (cont)

Inheritance Tax (IHT)

Changes to the spouse exemption where one spouse is not UK domiciled

HM Revenue & Customs (HMRC) have at long last proposed updating the position regarding differently domiciled spouses. There will be consultation on this, but if this is implemented, it will bring the exemption limit up to date. For couples, where their estates are not large, the proposed changes will enable them to simplify their affairs.

Where both spouses are domiciled in the UK, transfers between them are usually exempt from IHT, but transfers from a UK domiciled spouse to a non-domiciled spouse have until now only been exempt up to £55,000. That figure hasn't changed since IHT was introduced in 1984.

The proposal is for non UK domiciled spouses to be able to elect to be treated as UK domiciled for IHT purposes which would mean unlimited IHT exempt transfers between spouses. If they do not make an election, the exemption will be increased to the nil rate band, which is currently £325,000.

Changes to IHT charges in trusts

The Government will be consulting on changes to the way that trusts, which are subject to IHT, are taxed on their 10 year anniversaries and when property is transferred out of the trust. At present, the calculations are unwieldy and complex, and anyone who is not a specialist finds the calculations extremely difficult. Any simplification here will be welcome.

Anti-avoidance measures

There is a proposal to close a tax avoidance scheme where UK domiciled individuals could avoid IHT by purchasing an interest in an offshore trust. HMRC have attempted to close this scheme twice before, so we will have to wait to see the draft legislation before we can comment as to whether this scheme will finally close.

Update on previous announcements

The nil rate band remains frozen at £325,000 until 2015. Thereafter it is intended that it will rise in line with the Consumer Price Index (CPI).

For deaths on or after 6 April 2012, there will be a reduced rate of tax of 36% where the deceased has left 10% or more of their net estate to a charity.

VAT

Registration/deregistration

The registration and deregistration thresholds are increased by £4,000 to £77,000 and £75,000 respectively with effect from 1 April 2012.

Fuel scale charge

The figures for the amount of output VAT to account for in respect of fuel provided for private motoring are shown on our "Tax Facts" card. The figures are based on carbon dioxide (CO_2) emissions, and come into effect in the first VAT return period beginning on or after 1 May 2012.

"Addressing borderline anomalies"

A Consultation Document (closing date for responses – 4 May 2012) has been published in which HMRC set out their proposals for aligning the VAT treatment of similar products which are currently taxed differently, and for closing perceived loopholes which they believe can be used to avoid VAT.

In all cases, HMRC's proposed measures will come into effect on 1 October 2012, and will be accompanied by anti-forestalling provisions to prevent artificial prepayment arrangements being put in place prior to that date.

The areas covered are the following:

- *Approved alterations to protected (listed) buildings*

  The present VAT zero-rating is to be removed from:
  - the supply of building services and associated building materials in the course of an approved alteration of a protected building
  - the first sale or grant of a long lease in a "substantially reconstructed" protected building (except where the building is reconstructed from a "shell").

  The VAT treatment of alterations to protected buildings is therefore aligned with the treatment of repairs to such buildings, and indeed with that applicable to alterations to other types of building.

  Transitional arrangements applying until 20 March 2013 will protect zero-rating for contracts already in place on Budget day.

OTHER ISSUES (cont)

- *Hot food and premises*
  Measures are to be introduced to clarify the definitions of "hot takeaway food" and food for consumption "on the premises", such that the following supplies will be standard-rated:
  - the sale of all hot food, with the exception of freshly baked bread
  - food sold for consumption in areas adjacent to the food retailer (e.g. tables/ chairs outside) or shared with other retailers (e.g. a food court).

- *Self storage and hairdressers chair rentals*
  The following supplies are to be added to the list of items which are not covered by the general VAT-exemption for supplies of land:
  - the provision of self-storage facilities
  - the provision of salon space by a salon to a self-employed stylist

  Suppliers of this type of service will no longer be able to argue that they are providing a "licence to occupy land" to avoid charging VAT.

  Accordingly supplies of self-storage facilities will become subject to VAT. The new measures are a direct response to two recent cases where HMRC have been defeated at the First Tier Tribunal.

  As far as chair rentals are concerned, HMRC have always regarded the supply as being the taxable provision of salon "facilities".

- *Holiday caravans*
  Zero-rating will no longer apply to the sale of a caravan which is not designed and constructed for "continuous year round occupation". A caravan will only be considered to be thus designed and constructed if it is manufactured to British Standard BS 3632 or equivalent which applies to residential caravans.

- *Sports nutrition drinks*
  VAT law states that the sale of "beverages" should be standard-rated. HMRC propose to introduce a new category into the list of food / drink items which override the general zero-rating provisions to ensure that sports nutrition drinks are taxed at the standard rate in the same way as other "beverages".

Other Matters

- ***Freight transport services performed wholly outside the EU***

The temporary arrangements under which supplies of freight transport and related services taking place wholly outside the EU are not liable to UK VAT when performed for UK businesses and charities are to be formalised.

- ***Invoicing rules***

  Minor changes to simplify the UK VAT invoicing rules are to be introduced from 1 January 2013 to conform with the EU Invoicing Directive

- ***Providers of education***

  The VAT exemption for providers of education, in particular at university degree level, is to be reviewed in Finance Bill 2013 to ensure that commercial universities are treated fairly.

- ***Charitable buildings***

  Measures will be introduced in Finance Bill 2013 to remove charitable buildings from the scope of the VAT reduced rate for the supply and installation of energy-saving materials .

Confirmation of previously announced measures

- ***Cost sharing exemption***

  A VAT exemption for services shared between VAT exempt bodies including charities and universities will be introduced in Finance Bill 2012.

- ***Status of public bodies***

  Finance Bill 2012 will include provisions to amend UK law to ensure that there is clear transposition of EU agreements relating to the VAT treatment of public bodies carrying out their statutory duties in competition with the private sector.

- ***VAT grouping extra statutory concession***

  Finance Bill 2012 will include provisions to bring a long standing concession on the valuation of certain reverse charges applicable to VAT groups into law.

- ***Low value consignment relief***

  VAT relief will no longer apply to low value imports from the Channel Islands, with effect from 1 April 2012.

- ***Online registration and online filing***

  An online system for VAT registration, de-registration, and changes to business details will be introduced with effect from 31 October 2012. From the same date, certain VAT forms will be removed from the law.

- ***Overseas traders***

  The VAT threshold for businesses not established in the UK will be removed from 1 December 2012. From this date, such businesses will need to register for VAT as soon as they make any taxable supplies in the UK.

OTHER ISSUES (cont)

Patent Box & Research & Development ('R&D') tax incentives

The Budget confirmed that improvements to R&D tax incentives that had previously been announced will feature in the 2012 Finance Bill and will be effective from 1 April 2012. These include:

- An increase in the rate of enhancement of tax relief for qualifying R&D expenditure from 100% to 125%. This means that £100 of eligible R&D costs will give a tax deduction of £225;
- The current cap on the amount of payable credits that can be claimed (limited to the PAYE and National Insurance paid by the company in the period) will be removed; and
- The £10,000 minimum qualifying expenditure for a claim will be removed

The Chancellor also confirmed that legislation will be tabled in Finance Bill 2012 to introduce new tax incentives for companies making profits from UK and European patents. The draft legislation for these tax incentives had previously been published in December 2011 after consultation with industry and professionals.

The Patent Box will complement the existing tax incentives for Research and Development and will effectively allow eligible claimant companies to apply a corporation tax rate of just 10% to its profits within the Patent Box. The new tax incentives will be phased in over a four to five year period from 1 April 2013 and according to Treasury figures, the Patent Box is expected to deliver total annual tax savings to UK business of almost £1 billion.

Some key features of the Patent Box proposals are as follows:

- it will apply to existing patents as well as new patents;
- it will apply to worldwide profits generated from qualifying patents;
- there is a mechanism for it effectively to apply to profits arising during the 'patent pending' period, provided appropriate action is taken in advance;
- it is not sector specific; any company with qualifying IP will be eligible;
- it will apply to profits from products incorporating patented technologies, only one patent is required for the whole of the profits on the product to come within the Patent Box
- it will include not only profits from sales of patented products but also other forms of patent profits, for example royalties from exclusive licences, sale of the patent, damages for infringement etc
- patented tools and patented processes used in the production process can effectively be included; the attributable profits are identified via a notional royalty

It should be noted that the Patent Box tax incentives will not apply automatically; they must actively be claimed through the company's corporation tax self assessment return.

There is also a beneficial interaction with R&D tax incentives; the more expenditure identified as qualifying R&D, the more profits will qualify for the 10% Patent Box tax rate.

The Patent Box tax savings may be optimised with some advance planning. If you would like further details, please contact David Clift on david.clift@hazlewoods.co.uk.

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