

# BUDGET REVIEW

News and Information from Montague Brown, Registered Auditors & Accountants | Spring 2006



## Brown hails Britain's 'new economic stability'

Chancellor Gordon Brown delivered his tenth consecutive Budget to the House of Commons, amid growing speculation that it could be his last before he embarks on a political leadership campaign.

In a Budget focused largely on education, sport and the environment, the Chancellor presented a picture of economic stability for the UK, reporting that both inflation and economic growth are on target, at 2% and 2-2.5% respectively.

The Chancellor announced a number of measures aimed at encouraging innovation and enterprise. These include an extension of R&D tax credits so that companies with 500 employees can claim higher credit, and a major enhancement of the Enterprise Investment Scheme. The Chancellor also announced plans to

increase employer involvement in education, in a bid to match skills with the needs of businesses.

For the most part tax thresholds are increased in line with inflation. The Chancellor announced a nominal rise in the stamp duty land tax threshold to £125,000, and the inheritance tax threshold will also see a further increase to £325,000 by 2009/10.

One of the more radical announcements related to Vehicle Excise Duty, with the Chancellor revealing that the tax will rise to £210 for the most polluting cars, and will be phased out entirely for those producing the lowest emissions.

Other measures announced include the legislation for Real Estate Investment Trusts (REITs), and training to boost the careers of working women.

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## Personal Tax and Savings

The personal allowances for 2006/07 are £5,035 for those under 65 at 5 April 2007, £7,280 for those aged 65 to 74 and £7,420 for those aged 75 and over.

The married couple's allowance (MCA) is given to those couples in which at least one spouse or civil partner was born before 6 April 1935. This is worth £606.50 for 2006/07 where the elder partner is aged less than 75, and £613.50 where the elder partner is aged 75 or over.

The age-related element of allowances will be scaled back where income exceeds £20,100 (2005/06 £19,500). For MCA reduction this will be the husband's income for marriages before 5 December 2005. For marriages on or

after that date or for civil partners, it is the income of the higher earner that is taken into account.

### Pensions

As announced in the 2005 Pre-Budget Report, the rules for self-directed pension schemes are to be tightened to remove any tax advantages for investing in residential property and certain other assets such as fine wines, classic cars, art and antiques. The rule preventing recycling of tax-free lump sums will not apply where no more than 30% of the lump sum is recycled, and the upper threshold of £15,000 will be linked to the standard lifetime allowance.

**This newsletter highlights some of the key budget announcements that might affect you and your business.**

**Contact us for specific one-to-one advice on any of the measures.**

**We'd be delighted to help you.**

**Please contact us for further advice on how these changes affect you**

# Business Taxation

## Capital allowances for small businesses

The rate of first year allowance for capital expenditure by small businesses on plant and machinery is increased from 40% to 50% for the period of one year from 1 April 2006 for companies and from 6 April 2006 for businesses subject to income tax.

## Research and development (R&D) tax credits

The Government intends to provide additional support to firms with between 250 and 500 employees through the R&D tax credits system. Details of the proposals will be published later in the year following state aid discussions with the EC.

## Venture capital schemes

Changes announced include:

- For EIS investors, the annual investment limit for income tax purposes is doubled to £400,000
- Investors in VCTs will now only benefit from income tax relief at 30% (currently 40%)
- A reduction in the maximum size of companies able to raise money under the EIS, VCT and CVS schemes; this is reduced to £7 million before the investment and £8 million afterwards
- The minimum holding period for VCT investments is increased from three to five years.

## UK Real Estate Investment Trusts

Companies and groups can elect to join the UK Real Estate Investment Trust (REIT) regime with effect from 1 January 2007. The regime exempts qualifying rental income and gains on disposals of investment properties from corporation tax. Any other profits or gains made by the REIT will be subject to corporation tax.

### Business Tip

*An HMRC dispensation may reduce the amount of work required to complete forms P11D. You need not report expenses payments covered by a dispensation.*

## Corporation Tax Rates

Taxable profits	Financial year to 31 March 2007
First £300,000	19%
Next £1,200,000	32.75%
Over £1,500,000	30%
Small companies marginal relief fraction	
£300,000 – £1,500,000	$\frac{11}{400}$

# Personal taxation and pensions

## Income tax rates

	2006/07	2005/06
Starting rate band to	£2,150	£2,090
Tax rate	10%	10%
Basic rate band – next	£31,150	£30,310
Non-savings rate	22%	22%
Savings rate	20%	20%
UK dividend rate	10%	10%
Higher rate – income over	£33,300	£32,400
Tax rate excl. UK dividends	40%	40%
UK dividend rate	32.5%	32.5%

## Landlord's energy saving allowance

The allowance enables landlords to claim an income tax deduction against rental income for the cost of loft or cavity wall insulation in a dwelling they let. The Chancellor announced that with effect from 6 April 2006 the deduction will also apply to the cost of draught proofing and insulation for hot water systems.

## Computers and mobile phones

Employees with the private use of a computer provided by their employers have been exempt from tax on the first £500 of annual benefit in kind. This exemption is to be withdrawn, with effect from 6 April 2006.

In addition, the exemption on the private use of employer-provided mobile phones will be restricted with effect from 6 April 2006, to cover one phone per employee.

## Pensions – 'A' Day – 6 April 2006

As announced prior to today's Budget statement there are widespread changes which come into effect on 6 April 2006.

From 'A' day there is no limit on the amount that may be contributed to a registered pension scheme. The maximum amount on which an individual can claim tax relief in any tax year is the greater of the individual's UK relevant earnings or £3,600.

If total pension input exceeds the annual allowance of £215,000 there is a tax charge at 40% on the excess. This limit does not apply in the year that full pension benefits are taken.

Maximum age for tax relief	74
Minimum age for taking benefits	50
Lifetime allowance charge	– lump sum paid 55%
	– monies retained 25%
on cumulative benefits exceeding	£1,500,000*
Maximum tax-free lump sum	25%*

\* subject to transitional protection for excess amount

Under the original rules applying from 6 April 2006, those applying for Enhanced Protection under the new pension rules would have been denied that protection if they had an ongoing term assurance (life cover) policy written under pension rules (sometimes referred to as section 226A and section 621 policies) or belonged to schemes which include stand-alone entitlements to death benefits. Finance Bill 2006 will contain confirmation that the continuing existence of these arrangements will not deny Enhanced Protection.



## Duties

### Stamp taxes and duty

While the rates for stamp duty land tax (SDLT) remain unchanged, the threshold for paying SDLT on residential property is increased from £120,000 to £125,000 from 23 March 2006.

### Other duties or levies

From 6pm on 22 March 2006 tobacco duty rates will rise in line with inflation and a similar rate of increase will apply to duties on beer and wine, with effect from midnight on 26 March 2006. There is no increase in duty on spirits, cider and sparkling wine.

### > New VED rates for cars

Band	CO <sub>2</sub> emissions g/km	Petrol	Diesel
A	100 and below	£0	£0
B	101 - 120	£40	£50
C	121 - 150	£100	£110
D	151 - 165	£125	£135
E	166 - 185	£150	£160
F	186 - 225	£190	£195
G*	226 and above	£210	£215

\* Cars registered from 23 March 2006

## Capital Taxes

### Capital gains tax

The annual exempt amount has been increased in line with inflation for 2006/07 to £8,800 (2005/06 £8,500) for individuals.

### Trusts

The annual exempt amount is increased to £4,400 (2005/06 £4,250) for most trustees. Capital gains of trusts are taxed at the special trust rate of 40%.

### Bed and breakfasting

The Government is to introduce measures, applicable to acquisitions on or after 22 March 2006, which will prevent avoidance of CGT by schemes exploiting the 'bed and breakfast' identification rules.

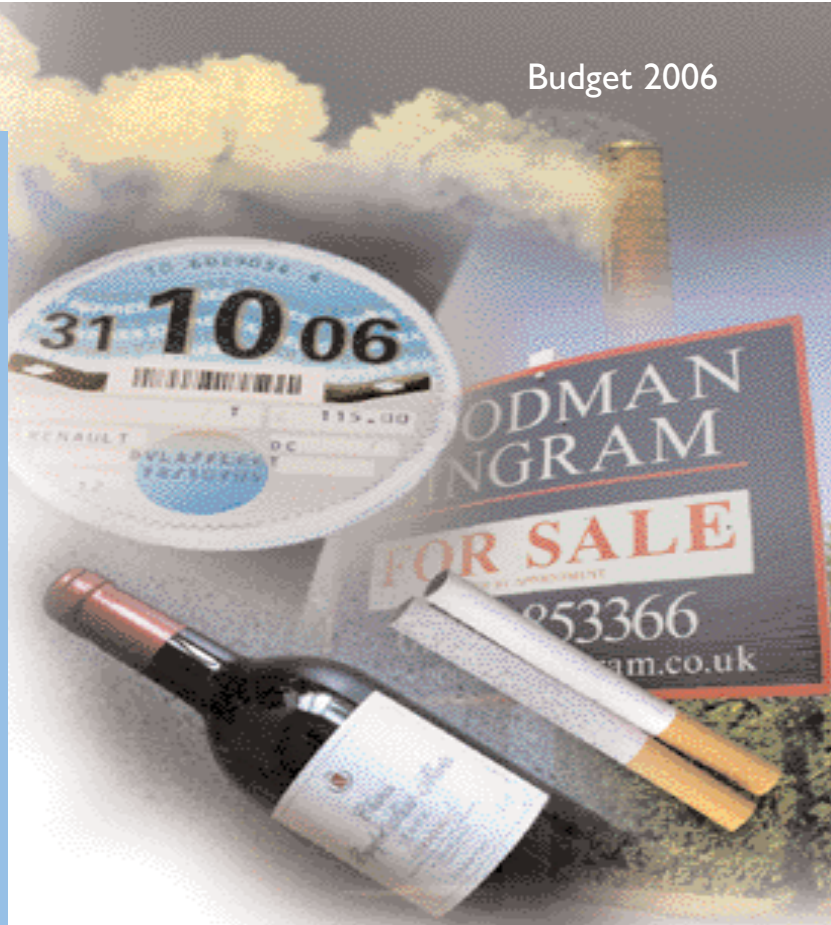
### Inheritance tax (IHT) Exemptions and rates of tax

It was confirmed that the IHT threshold would rise to £285,000 for 2006/07 and £300,000 for 2007/08. To continue to provide certainty for families, it was further announced that the threshold will be increased by more than the expected statutory indexation to £312,000 in 2008/09 and £325,000 in 2009/10.

The rate of IHT remains unchanged at 40%, with a reduced rate of 20% for chargeable lifetime transfers.

### Trust reforms

The IHT exemptions which presently apply to 'accumulation and maintenance' trusts (A&Ms) and/or 'interest in possession' trusts (IIPs) will be available only in certain prescribed circumstances. Otherwise IHT charges will apply in the same way as for all other trusts, preventing them from being used to shelter wealth from IHT. In effect all lifetime transfers into A&M or IIP trusts will be immediately chargeable to IHT and the usual regime of ten-yearly and exit charges will apply, unless the trust is set up for a disabled person. There will be transitional arrangements for existing trusts.



## Value Added Tax

### Reduced rate extension

From 1 July 2006 the sale of all contraceptive products, including sales by retailers, vending machines and the internet will be liable to the 5% reduced rate. Products supplied by medical practitioners or health professionals will be unaffected by this measure.

### Partial exemption

Businesses that operate special methods rather than the standard method, will be required to declare and demonstrate that the method proposed is fair and reasonable before it will be approved. In addition the rules for the recovery of VAT for partly exempt businesses making overseas supplies will be simplified. These measures will take effect from April 2007.

### Anti-avoidance measures

From Royal Assent to the Finance Bill 2006, HM Revenue & Customs will be able to direct that additional specified records be kept such as mobile phone IMEI numbers. The existing powers of HM Revenue & Customs to inspect and mark goods will also be clarified.

### > Tax Tip

*The cost of certain building conversions or renovations can be reduced. If the planned work results in a home, the VAT may be due at 5% rather than 17.5%.*

### > Value Added Tax rates and thresholds

From	1 April 2006	Currently
Standard rate	17.5%	17.5%
VAT fraction	$\frac{7}{47}$	$\frac{7}{47}$
Registration – last 12 mths or coming 30 days over	£61,000	£60,000
Deregistration – coming year under	£59,000	£58,000
Cash accounting scheme – up to	£660,000	£660,000
Annual accounting scheme – up to	£1,350,000	£660,000
Optional flat-rate scheme – up to	£150,000	£150,000

# Budget Round Up

Some of the other measures announced include:

## Online filing services

A report, published on Budget Day, endorses the Government's aim to achieve universal electronic delivery of returns for various taxes. Its main recommendations include bringing forward Self Assessment filing deadlines to 30 September for paper forms and 30 November for online returns from 2008. Starting from the same year, it also proposes phased introduction of online filing by businesses of VAT, company tax and PAYE returns.

## Employer supported childcare

New capital grants were announced in the Budget to help small and medium-sized employers to establish workplace nurseries. Additional encouragement is being offered from 6 April 2006 by increasing the tax and national insurance contributions exemption for employer-supported childcare from £50 to £55 per week.

## Child trust fund

Introduced in April 2005, the CTF is a long-term savings and investment account for children, born on or after 1 September 2002, into which the Government makes payments to help build up an useful asset for them at age 18. The Chancellor announced in the Budget that all children will receive a further Child Trust Fund payment at age seven of £250 with children from lower-income families receiving £500.

## Capital limits in benefits

Confirming previous announcements, the lower and upper capital limits are to be raised from April 2006 to £6,000 and £16,000 respectively for Income Support, Jobseeker's Allowance, Housing Benefit and Council Tax Benefit.

## Qualifying life assurance policies

An amendment to the legislation is intended to avoid unexpected tax consequences when certain policy returns are varied, such as when one insurance company takes over another.

## Tax relief on charity trading

New rules are proposed to legitimise HMRC's treatment of granting tax relief to charities which undertake a trade that is only partly carried out for charitable purposes.

## Tax Tip

If your child is under 3½ years old you should have received a Child Trust Fund voucher to open a savings account with. Don't put off deciding where to open this account, as the HM Revenue & Customs will make that choice for your child if the voucher is not used within 12 months of the issue date.

## Economic Overview

The Chancellor's Budget speech presented an optimistic outlook for the UK economy, with Brown's economic forecasts remaining unchanged from the revised predictions made in his 2005 Pre-Budget Report.

Public sector net borrowing is expected to reach £37bn this year, with the budget deficit standing at £11bn, while Government spending is set to reach £552bn.

The Chancellor asserted that Britain's economy is 'strong and strengthening', and insisted that the Government will continue to meet its fiscal rules, including the 'Golden Rule' on borrowing, which will be met with a surplus of £16bn.

This is despite the fact that the economy grew at just 1.8% in 2005, its slowest rate for over a decade.

## Tax and Travel

### Company cars

The threshold CO<sub>2</sub> emissions rate has been frozen at 140 g/km until 5 April 2008. The threshold for 2008/09 will be 135 g/km.

The rate of the taxable benefit ranges from 15% to 35% of list price (plus certain accessories) for most petrol or diesel-powered cars. Typical tax liabilities for an employee driving a £20,000 car in 2006/07:

Emissions CO <sub>2</sub> g/km	Fuel	Taxable %	Benefit £	Tax @ 22%	Tax @ 40%
158	Petrol	18	3,600	792	1,440
188	Diesel	27	5,400	1,188	2,160
188	Petrol	24	4,800	1,056	1,920
238	Petrol	34	6,800	1,496	2,720

### Employer providing fuel for private use

The tax charge for 2006/07 is calculated by establishing the emissions based percentage and multiplying the result by £14,400.

If the drivers of the first two cars in our example also received fuel for private use, their taxable benefit for 2006/07 will be:

Emissions CO <sub>2</sub> g/km	Fuel	Taxable %	Benefit £
158	Petrol	18	2,592
188	Diesel	27	3,888

### Company vans

From 6 April 2007, the taxable benefit for company vans with no restrictions on private use will increase to £3,000, with no reduction for older vans, and there will be an additional £500 taxable benefit for fuel for private mileage, if applicable.

Class 1A NICs are paid by employers on an amount equal to the employee's car, van and/or fuel benefit

### Mileage claims

The approved mileage rates for employees using their own transport for business travel are:

	First 10,000 miles	Each mile over 10,000 miles
Cars and vans	40p	25p
Motor cycles	24p	24p
Bicycles	20p	20p

HM Revenue and Customs has also sanctioned fuel only rates for those reimbursing their employers for private travel or claiming for business travel:

Engine capacity	Petrol	Diesel	LPG
Up to 1400cc	10p	9p	7p
1401 to 2000cc	12p	9p	8p
Over 2000cc	16p	13p	10p