

The Pre-Budget Report was delivered to Parliament by Alistair Darling on 24 November. The headline measures in response to the current financial crises included a temporary reduction to the standard rate of VAT to 15% and an extension of the ability for businesses to carry back trading losses.

However, the *quid pro quo* is tax increases in the future including a higher rate of income tax at 45% and increases in National Insurance Contributions.

Tax rates and allowances

Individuals

The rate of income tax for taxpayers with savings income and earned income above £150,000 will increase from 40% to 45% from April 2011. A new dividend tax rate of 37.5% will apply to taxpayers with taxable income above £150,000, also from April 2011.

Changes to the personal income tax allowance will be as follows:

- For under 65s the personal income tax allowance will increase to £6,475 from April 2009
- The personal allowance for taxpayers with gross income between £100,000 and £140,000 will, from April 2010, be reduced by up to half (at the rate of £1 for every £2 gross income over £100,000) and will be further reduced for taxpayers with gross income in excess of £140,000 (at a rate of £1 per £2 of income above £140,000 up to a maximum of the full amount of the personal allowance).

From April 2011, employer's and employees' national insurance contributions (NICs) will be increased by 0.5%. From April 2009, the upper earnings limit will mirror the higher rate tax threshold (£43,875) and from April 2011, the primary threshold will mirror the income tax personal allowance.

Trusts

The dividend trust rate and the trust rate of tax will be increased to 37.5% and 45% respectively from 6 April 2011. These rates are not limited to income above £150,000. The increase in the dividend tax rate to 37.5% represents an effective tax rate of 24.75%

Pensions tax allowances to be frozen

The lifetime allowance and annual allowance will be frozen at 2010/11 levels for the following five years. The lifetime allowance is currently £1.6 million, and prospective increases have already been confirmed in secondary legislation, with the lifetime allowance due to increase to £1.8 million for the 2010/11 tax year. The annual allowance (currently £235,000) will increase to £255,000 for 2010/11 and will remain at this level up to and including the 2015/16 tax year.

Corporation tax: small companies' rates

The planned increase in the small companies' rates (SCR) of corporation tax from 21% to 22% from 1 April 2009 has been deferred until 1 April 2010. Profit limits will remain the same as at present.

The SCR for profits from oil extraction and oil rights in the UK and the UK Continental Shelf ("ring fence profits") will remain at 19%.

Trading loss: carry back for business

Businesses will be able (as a temporary measure) to carry back trading losses against the profits of the three preceding years and obtain a repayment of tax.

For corporation tax this will apply to losses for accounting periods ending in the period 24 November 2008 to 23 November 2009 and for unincorporated businesses it will apply to losses in the accounts forming the basis period for the 2008/2009 income tax liability. The amount that can be carried back against the profits or other income of the earlier two years will be limited to £50,000 in total. The relief is available in respect of losses on furnished holiday lettings as well as trading losses.

Tax refunds should be available that could otherwise be obtained only by ceasing to trade and claiming terminal loss relief.

Foreign business profits

Draft legislation will be published and included in the Finance Bill 2009. Overseas source dividends received by large and medium-sized groups on ordinary shares and most non-ordinary shares will be exempt from UK tax. However, there will be a worldwide cap on interest deductions.

There will also be an extension of the loan relationships unallowable purpose rules to include schemes or arrangements and consequential changes to the CFC rules.

The Treasury Consent rules and notification requirements will be repealed and replaced with a quarterly reporting requirement for transactions in excess of £100 million.

Changes to connected parties rules: debts

A creditor that releases a connected debtor from a trade debt may be denied a deduction for the loss on the debt. The debtor may be taxed on its corresponding profit. This charge will be removed.

A company that pays interest to a connected company more than 12 months after the end of the accounting period in which it was due does not obtain a deduction for that interest until it is paid. This will be changed but draft legislation has not yet been published.

VAT

Temporary reduction to the standard rate of VAT

The standard-rate of VAT will be reduced from 17.5% to 15% for a 13 month period which starts on 1 December 2008. The 15% rate will apply until 31 December 2009. Therefore, from 1 January 2010 the standard rate of VAT will revert to 17.5%.

Only standard-rate supplies (including imports and acquisitions from other member states) made between 1 December 2008 and 31 December 2009 are affected by the measure. The measure does not affect supplies that are exemption zero-rated or reduced-rated for VAT.

The measure causes two consequential changes which are also effective from 1 December 2008:

- An amendment to the percentages used in the flat-rate VAT scheme
- The timing of credit notes issued following the cut will be affected

There will be "anti-forestalling" provisions in Finance Bill 2009 to prevent business from using artificial arrangements, entered into on or after 25 November 2008, where there is no current economic activity, to reduce VAT on goods or services to be provided on or after 1 January 2010, when the rate reverts to 17.5%.

VAT on property

From early 2009 it will be easier for VAT to apply to supplies of land and property which would otherwise be VAT exempt supplies. While there are no specifics on how this will be achieved, the announcement may indicate a simplification of the VAT option to tax rules.

Simplification: flat rate scheme

Businesses with a turnover of up to £150,000 may, under the VAT flat rate scheme, pay VAT as a flat percentage of turnover. Rates are set according to business sector and are intended to reflect effective rates of VAT across that sector.

HMRC has made two announcements aimed at simplifying the flat rate scheme. Currently, a business must check that both its taxable turnover is less than £150,000, and that its total income is less than £187,500. The latter requirement will be lifted, so that entry to the scheme and depends solely on taxable turnover. Secondly, a business must currently check whether its annual income exceeds £225,000, and if it does it must have leave the scheme. This test is to be amended so that income is calculated in accordance with the method used by the business to calculate its VAT liability while it is in the scheme. These changes are to have effect from 1 April 2009.

An application has been made to the European Commission to renew the 2007 reverse charge mechanism introduced for supplies of CPUs and mobile phones.

VAT retail schemes: threshold increases

Retailers with an annual turnover beneath a certain threshold are subject to one of five special VAT accounting schemes. The current threshold is £100 million and is now set to increase to £130 million. This change is to take effect from 1 April 2009, although retailers with an annual turnover between £100 million and £130 million will continue to operate their bespoke schemes until they end.

Enterprise Investment Scheme

Changes to the EIS regime to be included in the Finance Bill 2009:

- The expenditure requirements will be simplified such that 100% of the money subscribed must be employed within two years
- Relief for 10% of the investment can be carried back against income of the preceding tax year (subject to the annual investment limit)
- An anomaly between the EIS and capital gains tax rules will be rectified, namely, when there is a share-for-share exchange and a gain arises on a deferred gain and on the disposal of the shares.

Land remediation relief

Draft legislation has been published which will extend land remediation relief to the remediation of long term derelict land and to Japanese knotweed. Comments have been invited on the draft, and the provisions will be included in the Finance Bill 2009.

The proposed relief will be available for specified expenditure on

derelict land, which must have been derelict since 1 April 1998 when acquired.

Instead of extending the scope of existing land remediation legislation to include expenditure incurred on the clearing of Japanese knotweed, as previously proposed, the government will introduce powers to make secondary legislation in the Finance Bill 2009 to allow relief for a specified list of naturally occurring contaminants.

North Sea tax regime

Changes to the North Sea tax regime are to be included in the Finance Bill 2009.

The proposals aim to maximise economic recovery of oil and gas from the UK's continental shelf. They include:

- Encouraging investment in the UK's continental shelf by the introduction of a "value allowance" resulting in adjusted corporation tax ring fence profits being taxed at a lower or zero rate of supplementary charge
- Clarification of the tax treatment of transactions involving the change in use of North Sea ring fence assets to other uses (such as gas storage)
- Introduction of a tax roll-over regime for "swaps" of North Sea licences and a exemption where a licence interest is sold and the proceeds reinvested in ring fence licence interests
- Ensuring that companies have the potential for full PRT relief for decommissioning costs when licences are terminated prior to completion of decommissioning.

Compliance and anti-avoidance measures

Real estate investment trusts: anti-avoidance

The Finance Bill 2009 will amend the conditions to be met by a company or group in the UK Real Estate Investment Trusts (REIT) regime to prevent the artificial creation of new group structures to avoid those conditions.

Following the changes the conditions and tests to qualify as a REIT will be applied more widely to the whole economic group. Such that all owner-occupied property will be excluded from the tax exempt business. The amendment conditions and test will apply to accounting periods beginning on and after 1 April 2009.

Amnesty: offshore disclosure

Offshore bank account holders will be provided with another opportunity to disclose, voluntarily, any unpaid tax and settle liabilities.

SDLT disclosure regime and residential property: identification of scheme users

It was announced in April 2008 that the stamp duty land tax (SDLT) disclosure rules will be extended to residential property

where the value of the property is greater than £1 million. It has now been announced that this will include a mechanism for identifying users of schemes which are disclosed. This change will align the SDLT disclosure rules with the direct tax disclosure rules in this respect.

Late payment of tax debts

HMRC has launched a Business Support Service for taxpayers who are anticipating problems paying their tax debts on time as a result of cash flow difficulties.

The new service is intended for new enquiries, and not those already being dealt with by local offices. Additional late payment surcharges will not apply to payments included in repayment arrangements made with the service. Late payment interest will still apply.

Aligning rules on interest/penalties for late filing of returns and payment of tax

Following publication of summary responses to a consultation in June 2008, HMRC is proposing that simple interest should be charged and paid across all taxes and that a higher rate for late payment than for repayment interest be implemented.

Anti-Avoidance rules for employee securities

The treatment of employment-related securities acquired at an under-value under Chapter 3C (notional loans) of Part 7 of the Income Tax (Earnings and Pensions) Act 2003 will be simplified in the Finance Bill 2009.

Tax disclosure regime: amending the scheme reference number

Draft regulations will be published to amend the way in which tax avoidance scheme reference numbers are reported to HMRC.

The report will need to be made in the tax return for the year in which the scheme is implemented rather than the year in which the reference number is received.

The circumstances in which the report must be made on form AAG4 rather than a tax return will be extended.

Offshore financial centres

There will be a review of the UK's Crown dependencies (Jersey, Guernsey, the Isle of Man) and overseas territories (for example, Anguilla, British Virgin Islands, Cayman Islands) as offshore financial centres. The review will cover, amongst other things, financial supervision and transparency, fiscal arrangements and international cooperation.

Income shifting: nothing in Finance Bill 2009

The government will not now be introducing income shifting legislation in the Finance Bill 2009 to counter arrangements which divert income from one individual to another who is subject to a lower tax rate, to obtain a tax advantage. The issue will, however, be kept under review for future budgets.

Asset management

The following measures were announced:

- Simplification of the rules for the Qualified Investor Scheme from 1 January 2009
- Changes to encourage take-up of Property Authorised Investment Funds
- Discussions with industry about the potential for increased legislative certainty on the distinction between trading and investment in relation to the tax treatment of transactions of Authorised Investment Funds (AIFs), such as authorised unit trusts and open ended investment companies (OEICs)
- Changes to the AIF rules to prevent the "corporate streaming" rules from applying at all to investors for whom a dividend from an AIF is a trading receipt. This change will block attempts to circumvent the current anti-avoidance provision.

Taxpayers' Charter

HMRC will produce the first draft of a Taxpayers' charter, which it will publish for consultation in early 2009. The charter will cover taxpayers rights and obligations and clearly signpost the complaints procedures at HMRC. There will be provisions in the Finance Bill 2009 giving the charter statutory authority.

Disclaimer: This briefing gives general information only and is not intended to be an exhaustive statement of the law. Although we have taken care over the information, you should not rely on it as legal advice. We do not accept any liability to anyone who does rely on its content.

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