Howard Watson Smith
Chartered Accountants

The Budget 2006

MAIN BUDGET PROPOSALS

- An attack on interest in possession and accumulation and maintenance trusts
- Bringing forward the personal tax return deadline to 30 September from 2008
- Childcare vouchers exemption increased
- Changes to the Enterprise Investment Scheme and Venture Capital Trusts
- Vehicle Excise Duty soars for high emission cars

PREVIOUS ANNOUNCEMENTS

Some of the changes detailed in this summary have been the subject of earlier announcements. Here is a reminder of some of the more important ones:

- New pensions regime and anti-avoidance measures
- Changes to the tax credits regime
- Changes to small company tax rates
- Relief for the tax effect of UITF 40
- Introduction of UK-REITs
- Significant increases in VAT annual and cash accounting scheme limits

Gordon Brown presented his tenth Budget on Wednesday 22 March 2006. Will it prove to be his last? Has he won public and parliamentary support for his bid to become Prime Minister?

He has had a tough job before him in this year's Budget. His public spending commitments meant choosing between increasing government borrowing or raising more tax revenue.

Tucked away in the vast amount of information which was published were some radical changes which result from Lord Carter's review of HMRC online services. Businesses and individuals will have to be ready for compulsory online filing of returns from as early as 2008.

Our summary focuses on the issues likely to affect you, your family and your business. To help you decipher what was said we have included our own comments.

If you have any questions please do not hesitate to contact us for advice.

The Budget proposals may be subject to amendment in the Finance Act. You are therefore advised to contact us before taking any action as a result of the contents of this summary.

CONTENTS

Tax rates

For the seventh consecutive tax year, income tax rates remain at 10%, 22% and 40%. The special rules for savings income and dividends continue to apply. Further details of tax rates and bands can be found on page 15.

Comment

Income tax rates stay put for a further year and the fears surrounding the prospect of national insurance increases have proved unfounded.

Allowances

The 2006/07 personal allowances were announced in last December's Pre-Budget Report. The personal allowance for the under 65s is increased in line with inflation to £5,035. Personal allowances for those aged 65 and over are increased in line with earnings. The allowances are summarised on page 15.

Tax credits

The childcare element of Working Tax Credit is currently limited to 70% of eligible childcare costs up to a maximum of £175 per week for one child or £300 per week for two or more children. From 6 April 2006 the percentage increases to 80%.

The government has announced a commitment to increase the child element of the Child Tax Credit at least in line with average earnings until the end of this parliament.

The problems caused by overpayments of Working Tax Credit and Child Tax Credit are well known. In many cases this is because claimants' income has risen compared to the income in the base year on which their tax credits award was initially calculated. On current rules, the first £2,500 of any increase in income is disregarded in recalculating the award. From 2006/07, this will increase to £25,000.

Comment

The change means that claimants' 2006/07 tax credits awards will not be recalculated simply because their income has gone up, unless their 2006/07 income is at least £25,000 more than their 2005/06 income. Clearly this will only apply in a very small percentage of cases.

Child Trust Fund (CTF)

Children born since 1 September 2002 receive at least £250 to invest in a tax free savings account. Children from lower income families receive £500. The Chancellor announced that at age seven children will receive a further payment of £250 or £500 for children from lower income families. The government will consult on making further payments to secondary school age children.

Children become entitled to the fund at age 18. Children, parents, family and friends are together able to contribute up to £1,200 a year to the account and there is no tax to pay on any interest or gains made on this money.

Comment

The further payment will be welcomed. Unfortunately this tax free account which is useful for tax free savings is not available to children born before 1 September 2002.

Pensions

The new taxation of pensions regime finally takes effect from 6 April 2006, referred to as 'A' day. There will be a single set of tax rules for all registered pension schemes.

Pensions - investments

From 'A' day the government will remove the tax advantages for investing in residential property or certain other assets such as fine wines, classic cars and art and antiques from pension schemes which are 'self-directed'. This will include Self Invested Personal Pension Schemes (SIPPs) and Small Self Administered Schemes. The effect will be to remove all tax advantages from holding prohibited assets directly or indirectly in such schemes. The broad result will be that it is at least no more advantageous to hold such assets in a pension scheme than it is to hold them personally.

The legislation will also apply to indirect investment in these assets. An example of this would be residential property owned by a company in which a SIPP held 100% of the shares. But not all indirect investment will be subject to these rules. Self directed pension schemes which invest in certain commercial vehicles that hold residential properties may be allowed. An example would be the proposed UK Real Estate Investment Trusts.

Pensions and the tax free lump sum

The new pensions regime allows a tax free lump sum of 25% of the fund up to the lifetime allowance to be withdrawn when a person is eligible to take pension benefits.

However the government is introducing an anti-avoidance provision to prevent a device known as 'recycling'. The device works by taking a tax free lump sum from a scheme which is reinvested back into another scheme giving further tax relief on the amount invested. This in turn allows a further tax free lump sum to be paid out. The new rules will remove tax advantages in relation to lump sums which are artificially recycled in this way.

The legislation is not intended to affect cases where a person withdraws a tax free lump sum as part of the normal course of taking pension benefits.

Pensions - Alternatively Secured Pension (ASP)

The government has announced the inheritance tax (IHT) provisions which will apply to pension funds invested as an ASP. An IHT charge will apply to 'left over' ASP funds on the death of the scheme member.

Comment

The pensions tax rules require an individual to secure an income before they reach the age of 75. Most people will have an annuity or scheme pension, but ASP has been provided as an alternative. ASPs were designed for those who have a principled religious objection to annuitisation. The government is therefore trying to restrict the use of ASPs to their original limited purpose.

Unclaimed assets

The government proposes that unclaimed assets in the banking system should be reinvested in society while they remain unclaimed. Where the owners can be traced they can be reunited with their assets.

Unclaimed assets include accounts where there has been no customer activity for a period of 15 years. The money will be reinvested in the community, particularly in deprived communities, with a focus on youth services and financial education.

PERSONAL TAX

■ Venture Capital Trusts (VCTs)

In 2004 the government announced a temporary doubling of the rate of income tax relief for investments in VCTs to 40%. This will be reduced to 30% for shares issued on or after 6 April 2006.

Individuals currently must hold VCT shares for a period of three years to qualify for income tax relief. This period will rise to five years for shares issued on or after 6 April 2006.

The limit in the maximum size of companies able to raise money under VCTs is reduced to £7 million before investment and £8 million afterwards.

Comment

It had been anticipated that the VCT relief would be reduced to the previous level of 20% and so the 30% rate is to be welcomed.

■ Enterprise Investment Scheme (EIS)

Individuals who invest in qualifying EIS shares are entitled to income tax relief of up to 20% on their investment. For shares issued on or after 6 April 2006:

- the annual investment limit for income tax relief is doubled to £400,000
- the limit on the amount of shares subscribed for in the first six months of the tax year, which can be treated as if they had been issued in the previous tax year, will be doubled to £50,000
- the maximum size of companies able to raise money under EIS is reduced to £7 million before investment and £8 million afterwards.

EMPLOYMENT ISSUES

■ National Insurance Contributions (NICs)

There is no change in the rates of NIC. The detailed limits and rates are set out on page 16 of this booklet.

Action point

Although employees' NICs only become payable once earnings exceed £97 per week in 2006/07, it is still the case that earnings between £84 and £97 per week protect an entitlement to basic state retirement benefits without incurring a liability to NICs. Consider whether you are making full use of this rule. A PAYE scheme would be needed to establish the employees' entitlement to benefits.

■ Company car tax

Currently a company car is taxed according to the level of CO_2 emissions. The benefit on fuel provided for private use is also related to the same scale.

- The starting point for the scale was reduced to 140 grams per kilometre in 2005/06 and will remain unchanged until at least 5 April 2008. It will be reduced to 135 grams per kilometre for 2008/09.
- The government intends to introduce, from 2008/09, a new 10% rate for company cars with CO_2 emissions of 120 grams per kilometre or less.
- The fuel benefit calculation remains unchanged for 2006/07 at £14,400.
- The waiver of the 3% supplement for Euro IV diesel cars ceases from 6 April 2006 for cars registered on or after 1 January 2006.

Comment

Drivers who are provided with fuel for private use need to check if this really is a benefit.

■ Childcare costs

In April 2005 the government introduced a number of changes to provide up to £50 per week tax and NIC relief for employees who received certain types of childcare from their employers. This employer-supported childcare includes vouchers and other forms of approved childcare contracted for by the employer. The government intends to increase the limit to £55 per week from 6 April 2006.

The government has also announced capital grants, available to small and medium sized employers over the next two years, to help them establish workplace nurseries.

■ Exemptions for computers and mobile phones

Currently computers and mobile phones loaned to employees by their employer may be exempt from tax under certain circumstances, even if there is substantial private use of them.

The exemption for computers made available for private use will be withdrawn. Also the number of mobile phones that an employer can lend to an employee and their household tax free will be limited to one. Both of these changes take effect from 6 April 2006.

Comment

A number of tax and NIC-saving schemes have grown up over recent years which involved lending computers or mobile phones to employees. There was generally no tax or NIC charge year on year and subsequently the equipment would be sold to the employee for a much reduced value. Clearly the government wish to stop this tax planning opportunity.

■ Eye tests and glasses

From 6 April 2006 no tax charge will arise where an employer provides an eye test or corrective glasses for an employee. This applies whether the employer pays for this direct, reimburses the employee or provides a voucher to cover the cost.

Corporation tax rates

A starting rate of corporation tax of 0% was introduced in 2002 and applies to companies with taxable profits of £10,000 or less. Companies with profits between £10,000 and £50,000 enjoy a marginal relief from the small companies rate of 19%. The zero rate was introduced to encourage the creation of small businesses and to allow them to grow.

In 2004, the government thought the system was being 'abused' and introduced a 'non-corporate distribution rate' of 19% on profits that were distributed by companies.

The result has been a complex system and the government has concluded that many self-employed and employed people are still being advised to incorporate simply to reduce their tax and national insurance liabilities.

The government has therefore decided to replace the non-corporate distribution and zero rates with a new single banding. This is set at the current small companies rate of 19% on profits up to £300,000. The new rules take effect from 1 April 2006.

Tax relief for cars

A consultation document has been issued on tax relief for expenditure on cars. It concludes that the main problems with the current system are almost entirely associated with the special treatment for cars over £12,000. A range of options are suggested so that compliance costs associated with the current regime can be reduced for businesses.

A proposed regime also needs to be consistent with environmental objectives such as a reduction in CO_2 emissions.

The favoured proposal is for the introduction of a single new car pool with a reduced rate of capital allowances. There will be a range of first year allowances depending on the car's CO_2 emissions.

Leased plant and machinery

Currently a lease of plant and machinery is treated as the hire of an asset:

- the lessor brings in the rentals arising under the lease as income and can claim capital allowances in respect of its expenditure on the asset and

- the lessee deducts the amount of the rentals payable over the life of the lease.

Provisions are being introduced, effective from 1 April 2006, to align the tax treatment of leased plant and machinery with that of other forms of finance. Where leases function essentially as financing transactions the new regime will allow:

- the lessor to bring in only the finance element of the rentals as income
- the lessee a deduction only for the finance element of the rentals
- the lessee an entitlement to capital allowances.

The new rules will not apply to certain shorter leases (including all those where the term does not exceed five years) so the majority of leases will be unaffected by the changes.

Capital allowances

To ensure that small businesses are provided with incentives to invest for growth, the government will increase the first year capital allowances on plant and machinery from 40% to 50% in the year from April 2006.

Comment

A 50% rate of first year allowances was available to small businesses for expenditure incurred from April 2004 for one year. It has been reintroduced to mitigate the effect of the extension of the 19% corporation tax rate.

■ Research and development (R&D) credits

In 2000, an R&D tax credit was introduced for small and medium-sized enterprises (SMEs). This enables SMEs to claim tax relief on 150% of qualifying R&D costs. Companies without profits can take the relief up front as a payable R&D tax credit. They can surrender the loss attributable to the R&D and receive a cash payment of £24 for every £100 spent on qualifying R&D. The scheme was extended to large companies in 2002 enabling them to claim tax relief on 125% of qualifying R&D costs although the cash repayment option is not available to them.

The government intends to provide additional support to firms with between 250 and 500 employees through R&D tax credits. The support will be subject to the outcome of state aid discussions with the European Commission and further details will be published later this year.

Two changes are being made in the 2006 Finance Bill:

- an expansion of qualifying costs to include payments to clinical trial volunteers
- a harmonisation of time limits and claims procedures across both the payable tax credit and the enhanced relief.

■ Income recognition and accounting standards

UITF 40 ‘Revenue recognition and service contracts’ was issued in March 2005. It was intended to give guidance on income recognition for contracts for services such as those rendered by accountants and solicitors. In brief, it requires income to be recognised as a contract for services progresses and affects accounting periods ending on or after 22 June 2005.

This means that many businesses will recognise income before an invoice has been issued to a customer and therefore before payment has been received. This change may create a one-off uplift in profit, referred to as ‘adjustment income’.

The government will legislate in the Finance Bill 2006 to enable most businesses affected by the March 2005 changes in the income recognition rules to spread any extra tax charge over three years. Those businesses most severely affected will be able to spread the charge over six years.

The final details will not be available until the Finance Bill is published. However it is expected that businesses will need to calculate their ‘adjustment income’ and one-third of this will be taxed in the first year, ie for the first accounting period ending on or after 22 June 2005. A further one-third will be taxed in each of the next two years.

Where the taxable profits are low relative to the adjustment income the spreading period could extend to six years. Each year, one-third of the ‘adjustment income’ will be compared with one-sixth of the taxable income for that year. The extra taxable income for that year will be restricted to the lesser amount. There will be a sweep up of any amount not yet charged at the end of the six year period.

UK Real Estate Investment Trusts (UK-REITs)

The government will include legislation to establish UK-REITs in the 2006 Finance Bill. The proposals include the following key features:

- the regime will be open to UK resident companies, that are listed on a recognised stock exchange
- the majority of the UK-REIT's activity must relate to qualifying property letting business (at least 75% by reference to its income and assets)
- companies that meet the UK-REIT eligibility criteria will not pay corporation tax on qualifying property rental income or qualifying chargeable gains
- UK-REITs will be required to distribute at least 90% of the tax exempt profits each year
- dividends paid out of the tax exempt profits will be treated as property income in the hands of the shareholders.

It is expected that shares in UK-REITs will be eligible to be held in an Individual Savings Account, Personal Equity Plan or Child Trust Fund.

Comment

UK-REITs have been considered as a means to improve the efficiency of both the commercial and residential property investment markets by providing liquid and publicly available investment vehicles.

Companies can elect to join the regime with effect from 1 January 2007. They will pay an entry charge of 2% of the market value of their investment properties at the date they join the regime.

Comment

The intention of the conversion charge is to ensure no overall loss of revenue from the introduction of UK-REIT legislation.

Film Tax Relief

In the 2005 Budget the Chancellor announced an extension to the current tax reliefs for low budget films until 31 March 2006.

The government has now given details of the proposed new tax incentives for British films. The legislation will be published in the 2006 Finance Bill.

The regime will only apply to 'film production companies'. These are companies which have an active involvement in the process of film making.

Partnerships can no longer become involved in film production to shelter their members' income from tax.

Green Landlord Scheme

Landlords are to be encouraged to invest in the energy efficiency of their properties through a Green Landlord Scheme. The government will continue to explore reform of the existing wear and tear allowance, which was originally given to compensate landlords for the use made by tenants of the furnishings in the property. It is proposed that the allowance should be made conditional on the energy efficiency level of the property.

Group relief

A group company can claim to set the losses of another group company against its profits, thereby reducing the amount of corporation tax it pays. However this only applies if the two companies are UK resident or carrying on a trade in the UK through a 'permanent establishment'.

As a result of a tax case heard in the Court of Justice of the European Communities, legislation is being introduced to extend the group relief loss rules. The losses of foreign subsidiaries of UK parent companies, where the subsidiaries are either resident in the European Economic Area (EEA) or have relevant losses in a permanent establishment in the EEA, may be relieved against UK profits. However relief is only available where all possibilities of relief have been exhausted and future relief is unavailable in the country where the losses were incurred or in any other country.

The extension applies from 1 April 2006

Comment

The main scenario in which the extension will prove useful is where the foreign subsidiary goes into liquidation so the loss cannot be used against potential future profits.

Trading activities of a charity

Charities are exempt from tax on trading profits so long as the profits are applied solely to charitable purposes. The exemption applies either where:

- the trade is exercised in carrying out a primary purpose, such as the provision of residential care for the elderly, or
- the work of the trade is mainly carried out by the beneficiaries of the charity.

The exemption does not apply if part of the trade is not within the primary purpose or where the trade is partly (but not mainly) carried on by beneficiaries of the charity.

Measures will be introduced to provide relief on the profits that can reasonably be attributed to the part of the trade that is carried on for a primary purpose or that is carried out by the beneficiaries of the charity.

The new relief will apply for chargeable periods commencing on or after 22 March 2006.

Comment

Charities which have a small non primary purpose trade may already be exempt under legislation introduced in 2000.

Capital gains tax (CGT) annual exemption

The annual exemption for 2006/07 is £8,800. For most trusts the exempt limit is increased to £4,400.

CGT rates of tax

For individuals capital gains continue to be treated as the top slice of income. For 2006/07 rates continue to be aligned with those applying to savings income. Tapered gains are charged at 10% where gains plus total income do not exceed £2,150; 20% between £2,151 and £33,300; and 40% on any balance.

For trustees the rate of CGT is 40%.

Inheritance tax (IHT) threshold

The IHT nil rate band is increased to £285,000 with effect from 6 April 2006. The Chancellor has announced that the band will rise to £300,000 in 2007, £312,000 in 2008 and £325,000 in 2009.

Comment

It is disappointing that little attempt was made to increase the nil rate band to reflect recent rises in the housing market. The family home remains the main asset in many estates and some IHT planning should be considered if the value of the estate exceeds the nil rate band.

Planning Gain Supplement (PGS)

The government has issued a consultation paper on the introduction of a PGS. Legislation may be introduced to tax some of the windfall gain accruing to landowners from the sale of their land for residential development to capture some of the uplift in value arising when full planning permission is granted.

The following are some of the principles that may be considered:

- a system for gathering information as to the value of land proposed for development
- the government would then set a tax rate on these values, to be paid by the developer
- the granting of residential planning permission would be contingent on the payment of the PGS
- there may be a lower rate for development on brownfield sites
- consideration may be given to allowing developers to pay their contributions in instalments over a period of time.

The government recognises that the introduction of a PGS would need to be accompanied by transitional measures. These would help developers already engaged in land sales contracts that were drawn up before this charge was introduced or those who hold large amounts of land where planning permission has yet to be secured.

Trusts

A package of measures to modernise the tax system for trusts will be included in the Finance Bill 2006. The rationale of the measures is to make the taxation of trusts more consistent across the income tax and CGT regimes.

Examples of the changes include:

- common meanings of 'settled property' and 'settlor' to apply for most income tax and CGT purposes
- rules to allow for the income of settlor-interested trusts to be treated as though it had arisen directly to the settlor
- a measure to legislate the existing practice of not taxing beneficiaries who receive discretionary income payments from the trustees of settlor-interested trusts
- an increase in the standard rate band for trusts from £500 to £1,000 from 6 April 2006.

Work is continuing on other measures in particular:

- provisions to allow income to 'stream' through a discretionary trust so that the beneficiary would meet any higher rate tax bill directly
- abolition of the 'tax pool' (this proposal is dependent on changes to an income streaming approach).

Comment

The measures are part of an ongoing process of reform which should help to reduce the administrative burdens on trustees, especially the trustees of smaller trusts. However the common meanings of settled property will not apply to inheritance tax and the more significant changes such as income streaming have been deferred.

■ Aligning the IHT treatment of trusts

Lifetime transfers into accumulation and maintenance trusts or interest in possession trusts are generally exempt from IHT if the settlor lives for the next seven years. Also these trusts are not subject to the periodic or exit charges suffered by other trusts.

Legislation will be introduced in the Finance Bill 2006 which will limit these special rules to trusts that are created:

- either on death or in the settlor's lifetime for a disabled person; or
- by a parent on death for a minor child who will be fully entitled to the assets in the trust at age 18; or
- on death for the benefit of one life tenant in order of time whose interest cannot be replaced (more than one such trust may be created on death as long as the trust capital vests absolutely when the life interest comes to an end).

These rules will apply to trusts created on or after 22 March 2006 and, from the same date, to additions of new assets to existing trusts. Subject to transitional provisions the rules may apply to other IHT-relevant events in relation to existing trusts.

Comment

These are significant changes. For new trusts lifetime transfers into a trust are no longer eligible for special treatment unless they are set up for a disabled person. All other transfers are immediately chargeable.

VAT thresholds

The VAT registration limits increase with effect from 1 April 2006 as follows:

- the threshold for compulsory registration is £61,000
- the threshold for voluntary deregistration is £59,000.

Annual accounting scheme

The annual taxable turnover limit for joining the scheme is to increase from £660,000 to £1,350,000 with effect from 1 April 2006.

Cash accounting scheme

The government intends to increase the turnover limit for joining the cash accounting scheme from £660,000 to £1,350,000.

Comment

This is an increase of more than 100% and may benefit up to one million small businesses.

Car fuel scale charges

The Chancellor announced in Budget 2005 the government's intention to align the VAT car fuel scale charges with the income tax benefit in kind provisions. This new system is to come into force on 1 May 2007.

VAT and property

Following on from the government's announcement that it intends to modernise, simplify and provide greater certainty for businesses dealing with some VAT and land and property matters, the legislation dealing with the option to tax provisions is to be rewritten. This will put it in clearer and easier to understand language and introduce appeal rights as well as improve practical administration.

Stamp duty

The rules are to be relaxed in respect of company reconstruction reliefs:

- the requirement that the acquiring company be registered in the UK will be removed
- strict rules relating to the proportion of shares held by any shareholder will be changed so that relief will be given provided there is no change in overall ownership of the reconstructed business.

The changes are to take effect from the date of Royal Assent.

Stamp duty land tax (SDLT)

A significant relief which has been available to unit trusts which acquire a property is being withdrawn. A number of measures are to be introduced to simplify and clarify the law generally. In addition Treasury regulations have been made to take a number of transactions outside the scope of SDLT including changes in the rules that deal with transfers of partnership interests.

Reliefs for alternative financing for the purchase of land and buildings by individuals are to be extended from the date of Royal Assent to include companies, clubs and trusts. The reliefs ensure that the SDLT due is no more than it would be under more traditional loan financing.

Tax schemes

In 2004 new disclosure rules were introduced in relation to certain tax schemes. Broadly the rules require ‘promoters’ to provide details of their schemes to HMRC shortly after the scheme is sold. The government now intends to:

- extend the regime to income tax, capital gains tax and corporation tax
- replace the ‘filters’ for direct tax with ‘hallmarks’ in line with the system for VAT
- require businesses (other than SMEs) to provide information on direct tax schemes and arrangements devised ‘in-house’ within 30 days, bringing them more in line with the rules for scheme promoters.

The changes will be effective from 1 July 2006.

Sale of lessor companies

Groups of companies have benefited from capital allowances in the early years of a lease, before selling lessor companies to loss-making groups, thereby avoiding paying tax on the subsequent profits.

Small changes will be made to the measure introduced from 5 December 2005 which imposes a charge on the lessor company to recover the tax benefits that have been taken but grants an equal relief on the day after the sale.

VAT measures

There are a variety of measures to be introduced in respect of VAT including:

- powers to allow HMRC to direct that an individual business be required to keep specified additional records in respect of goods such as mobile phones and computer chips
- measures affecting businesses which seek to avoid VAT on phone cards and other face value vouchers
- stepping up activities in an attempt to tackle Missing Trader Intra-Community VAT fraud
- clarification of powers relating to inspection of goods
- informal consultation on a proposed change to the partial exemption rules where approval is sought for a special method.

Other measures

A number of further measures will be introduced including some changes to those announced in the Pre-Budget Report:

- minor amendments are to be made to the legislation and guidance in respect of corporate capital losses. The rules were introduced with effect from 5 December 2005 to ensure that such losses can only be created and used as a result of genuine commercial transactions rather than to gain a tax advantage
- legislation will ensure that rewards obtained from avoidance schemes using options over employment-related securities will be subject to PAYE and NIC. This measure will apply with effect from 2 December 2004 when the government made the original statement regarding such schemes

ANTI-AVOIDANCE MEASURES

- a measure to ensure that individuals and trustees cannot exploit the 'bed and breakfasting' rules in respect of capital gains
- legislation will be introduced to block a variety of arrangements entered into by companies which involve financial products that are designed to avoid tax
- a measure to ensure that some companies which became non-resident in the UK as the result of a double taxation treaty before 1 April 2002 are brought within the controlled foreign companies legislation. This will have effect from 22 March 2006
- further details are available on the government's strategy to tackle tobacco smuggling
- as part of their review of tax and NICs the government will consult on action to tackle disguised employment through managed service company schemes
- three provisions will be introduced to prevent the exploitation of tax relief on certain donations to charitable bodies.

MISCELLANEOUS

■ Online filing

Lord Carter's review of HMRC online filing services has been published. HMRC have confirmed that in line with the report's recommendations they will only implement the new measures when the IT systems that will allow efficient online filing are in place and are fully tested.

Lord Carter's other key recommendations are to:

- require businesses to file their VAT returns, company tax returns and PAYE in-year forms online in phases from April 2008
- introduce new filing deadlines for income tax self assessment returns of 30 September for paper forms and 30 November for online returns from 2008
- promote online filing by tax agents and better quality data by withdrawing computer generated paper 'substitute' self assessment returns from 2007/08
- link the period that HMRC have to query a return to the date it is filed.

HMRC intend to work closely with businesses, taxpayers, agents and software developers on the implementation of the new measures.

Comment

The proposals are a clear indication of HMRC's intention to encourage online filing. The new requirements are expected to be introduced in phases and will apply first to large and medium sized VAT traders and employers although new VAT traders will also be required to file their VAT returns online from the outset.

PROPOSED RATES AND ALLOWANCES 2006/07

INCOME TAX RATES

2006/07 Band £	Rate %	2005/06 Band £	Rate %
0 - 2,150	10	0 - 2,090	10
2,151 - 33,300	22*	2,091 - 32,400	22*
Over 33,300	40**	Over 32,400	40**

* Except dividends (10%) and savings income (20%).
** Except dividends (32.5%).
Other income taxed first, then savings income and finally dividends.

INCOME TAX RELIEFS

		2006/07 £	2005/06 £
Personal allowance	- under 65	5,035	4,895
	- 65 - 74*	7,280	7,090
	- 75 and over*	7,420	7,220
Married couple's allowance (relief at 10%)	- aged less than 75 and born before 6.4.35*	6,065	5,905
	- 75 and over*	6,135	5,975
	- min. amount	2,350	2,280
*Age allowance income limit		20,100	19,500

(reduce age allowance by £1 for every £2 of excess income over £20,100)

Blind person's allowance		1,660	1,610

TAX CREDITS

	2006/07 £	2005/06 £
Working tax credit (WTC)		
Basic element - max.	1,665	1,620

Childcare element
80% (70%) of eligible costs up to £175 (£175) per week (£300 (£300) if two or more children)

	2006/07 £	2005/06 £
Child tax credit (CTC)		
Child element per child - max.	1,765	1,690
Family element	545	545
Baby addition	545	545

Reductions in maximum rates
37% of income above £5,220* p.a.

*If only CTC is claimed, the threshold is £14,155 p.a. (£13,910). The family element of CTC is not reduced unless income is more than £50,000 p.a. when it is reduced by £1 for every £15 of additional income.

PENSION PREMIUMS

2006/07

- Tax relief available for personal contributions: higher of £3,600 (gross) or 100% of relevant earnings.
- Employers will obtain tax relief on employer contributions if they are paid and made 'wholly and exclusively'. Tax relief for large contributions may be spread over several years.
- Any contributions in excess of £215,000, whether personal or by the employer, will be subject to income tax on the individual at 40%.
- No carry back of pension contributions.

INDIVIDUAL SAVINGS ACCOUNTS (ISAs)

2006/07 and 2005/06		£
Overall investment limit	- **maxi ISA**	7,000
	- **mini ISA** - stocks, shares and life insurance	4,000
	- cash	3,000

CAR AND FUEL BENEFITS

Company cars 2006/07 and 2005/06

CO_2 emissions (gm/km) (round down to nearest 5gm/km)	% of car's list price taxed	Fuel benefit (£14,400 x %) £
up to 140	15	2,160
145	16	2,304
150	17	2,448
155	18	2,592
160	19	2,736
165	20	2,880
170	21	3,024
175	22	3,168
180	23	3,312
185	24	3,456
190	25	3,600
195	26	3,744
200	27	3,888
205	28	4,032
210	29	4,176
215	30	4,320
220	31	4,464
225	32	4,608
230	33	4,752
235	34	4,896
240 and above	35	5,040

Company cars
- For diesel cars add a 3% supplement, but maximum still 35%. This is waived for Euro IV diesels. For 2006/07, no waiver for diesels registered on/after 1 January 2006.
- Discounts apply to certain environmentally friendly cars.
- For cars registered before 1.1.98 charge is based on engine size.
- The list price includes accessories and is subject to an upper limit of £80,000.
- List price is reduced for capital contributions made by the employee up to £5,000.

Fuel benefits
- The fuel benefit charge is proportionately reduced if provision of private fuel ceases part way through the year.
- The fuel benefit is reduced to nil only if the employee pays for all private fuel.

Van benefit per vehicle - 2006/07 and 2005/06

Vehicles under 4 years old	Vehicles at least 4 years old
£500	£350

Notes
1. The charge only applies if there is unrestricted private use of the van.
2. Van benefits include fuel for private use.

MILEAGE ALLOWANCE PAYMENTS

	2006/07 and 2005/06 Rate per mile
Cars and vans	
Up to 10,000 miles	40p
Over 10,000 miles	25p
Bicycles	20p
Motorcycles	24p

These rates represent the maximum tax-free mileage allowances for employees using their own vehicles for business. Any excess is taxable. If the employee receives less than the statutory rate, tax relief can be claimed on the difference.

CAPITAL ALLOWANCES

	Writing Down Allowance
Plant and Machinery*	25%#(reducing balance)
Motor Cars**	25% (reducing balance) - £3,000 max.
Industrial and Agricultural Buildings and Hotels	4% (straight line)

* **For small businesses:** first year allowances (FYAs) of 50% for 12 months from 6.4.06 (1.4.06 for companies). 40% otherwise.
For medium-sized businesses: FYAs of 40%.
For all businesses: 100% FYAs on expenditure on energy saving plant and machinery.
**100% FYAs on new cars with CO_2 emissions not exceeding 120 gm/km until 31.3.08.
#6% on certain long life assets.

PROPOSED RATES AND ALLOWANCES 2006/07

CORPORATION TAX

	Year to 31.3.07 Profits band £	Rate %	Year to 31.3.06 Profits band £	Rate %
Starting rate	N/A	N/A	0-10,000	0*
Marginal (starting) rate	N/A	N/A	10,001-50,000	23.75
Small companies rate	0-300,000	19	50,001-300,000	19
Marginal (small companies) rate	300,001-1,500,000	32.75	300,001-1,500,000	32.75
Full rate	Over 1,500,000	30	Over 1,500,000	30
Starting rate fraction		N/A		19/400
Small companies fraction		11/400		11/400

*Minimum rate of 19% applies when profits are distributed to non-company shareholders.

The profits limits are reduced for accounting periods of less than 12 months and for a company with associated companies.

VALUE ADDED TAX

Standard Rate	17.5%
Reduced Rate	5%
Annual Registration Limit - from 1 April 2006 (1.4.05 - 31.3.06 £60,000)	£61,000
Annual Deregistration Limit - from 1 April 2006 (1.4.05 - 31.3.06 £58,000)	£59,000

VAT on private fuel - scale charge due per quarter per car for accounting periods beginning on or after 1 May 2006.

	Petrol Charge	Petrol VAT	Diesel Charge	Diesel VAT
Up to 1400cc	£273	£40.66	£260	£38.72
1401 - 2000cc	£346	£51.53	£260	£38.72
Over 2000cc	£508	£75.66	£331	£49.30

CAPITAL GAINS TAX

	2006/07 £	2005/06 £
Individuals		
Exemption	8,800	8,500

Balance of gains (reduced by taper relief) charged as top slice of income (at savings rates - ie 10%, 20% or 40%)

	2006/07	2005/06
Trusts		
Exemption	4,400	4,250
Balance of gains (reduced by taper relief)	40%	40%

Taper relief 2006/07 and 2005/06 disposals

Percentage relief depends on number of complete years asset owned after 5.4.98.

Years of ownership	1	2	3	4	5	6	7	8	9	10
Business assets (% relief)	50	75	75	75	75	75	75	75	75	75
Non-business assets* (% relief)	0	0	5	10	15	20	25	30	35	40

*Add one extra year if asset owned before 17.3.98.

STAMP DUTY & STAMP DUTY LAND TAX

Land and buildings (On full consideration paid)

Rate	Residential property: Disadvantaged areas £	Residential property: Other £	Non-residential £
Nil	0 - 150,000	0 - 125,000*	0 - 150,000
1%	150,001 - 250,000	125,001 - 250,000	150,001 - 250,000
3%	250,001 - 500,000	250,001 - 500,000	250,001 - 500,000
4%	Over 500,000	Over 500,000	Over 500,000

*Limit raised to £125,000 (£120,000) from 23 March 2006.

Shares and securities - rate remains unchanged at 0.5%

INHERITANCE TAX

Death Rate %	Lifetime Rate %	Chargeable Transfers 2006/07 £'000	Chargeable Transfers 2005/06 £'000
Nil	Nil	0 - 285	0 - 275
40	20	Over 285	Over 275

Reliefs

Annual exemption	£3,000	Marriage	- parent	£5,000
Small gifts	£250		- grandparent	£2,500
			- bride/groom	£2,500
			- other	£1,000

Reduced charge on gifts within seven years of death

Years before death	0-3	3-4	4-5	5-6	6-7
% of death charge	100	80	60	40	20

NATIONAL INSURANCE

Class 1 (employed) Contracted in Weekly earnings	2006/07 Rates Employer	2006/07 Rates Employee
Up to £97	Nil*	Nil*
£97.01 - £645	12.8%**	11%**
Over £645	12.8%**	£60.28 + 1%♦

* Entitlement to contribution-based benefits retained for earnings between £84.01 and £97 per week.

**On earnings above £97.

♦ On earnings above £645.

Class 1A (employers)	12.8% on employee taxable benefits
Class 1B (employers)	12.8% on PAYE Settlement Agreements
Class 2 (self-employed)	flat rate per week £2.10 small earnings exception p.a. £4,465
Class 3 (voluntary)	flat rate per week £7.55
Class 4 (self-employed)	8% on profits between £5,035 and £33,540 plus 1% on profits over £33,540

MAIN SOCIAL SECURITY BENEFITS

Weekly Benefit	2006/07	2005/06
Basic Retirement Pension - single person	£84.25	£82.05
- married couple	£134.75	£131.20

Statutory pay rates - average weekly earnings £84 (£82) or over

	2006/07	2005/06
Statutory Sick Pay	£70.05	£68.20
Statutory Maternity Pay		
First six weeks	90% of weekly earnings	
Next 20 weeks	£108.85*	£106.00*
Statutory Paternity Pay - two weeks	£108.85*	£106.00*
Statutory Adoption Pay - 26 weeks	£108.85*	£106.00*

* Or 90% of weekly earnings if lower

First Floor, St Giles' House, 15/21 Victoria Road, Bletchley,
Milton Keynes MK2 2NG
Tel: 01908 376424 Fax: 01908 648730
Website: www.hwsmk.co.uk Email: info@hwsmk.co.uk