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AUTUMN STATEMENT 2010

Chancellor George Osborne presented the Autumn Statement to the House of Commons on 29 November 2010. This newsletter summarises the key points, and rounds up some of the recent tax changes announced by the Coalition Government.

... and recent tax measures

Inside this newsletter

The Autumn Statement is the Coalition's replacement for the previous Government's Pre-Budget Report. Whereas Gordon Brown and Alistair Darling used the occasion to make announcements on draft tax changes and legislation that would appear in the spring Budget, George Osborne gave a more concise speech focusing on the economy.

However, the Autumn Statement represents a good opportunity to take stock of where we are generally, in this busy first year of Coalition Government.

In this newsletter, we round up some of the most important tax and business changes announced in the last five months or so, starting with the Emergency Budget in June, including:

- The forthcoming increase in the standard rate of VAT
- Changes to pensions tax relief
- Planned reforms to corporation tax.

We also summarise October's Comprehensive Spending Review, in which the Chancellor unveiled over £80 billion in public sector spending cuts.

If you would like to discuss any of the issues mentioned in this newsletter, do contact us.

Britain 'on the mend', Osborne insists

Presenting his first Autumn Statement as Chancellor of the Exchequer, Chancellor George Osborne has asserted that Britain is 'on track' to recover from the deepest recession of post-war times.

The Statement was largely a response to the first Autumn forecast from the independent Office for Budget Responsibility (OBR), created by the Coalition Government earlier this year.

Despite issuing a cautionary note on the reliability of forecasts, Mr Osborne went on to argue that the OBR report vindicated the Government's 'decisive action' on the economy.

As widely predicted by economists, the economic growth forecast for 2010 was increased, from 1.2% to 1.8%. However, the estimates for 2011 and 2012 were reduced from 2.3% to 2.1%, and from 2.8% to 2.6% respectively, with the forthcoming increase in VAT – coupled with over £80 billion of spending cuts – expected to slow the pace and result in a period of 'sluggish growth'. Meanwhile public borrowing forecasts for the current financial year have been revised downwards by £1 billion, and borrowing is expected to fall from £148.5 billion to £18 billion in 2015/16.

Mr Osborne was keen to emphasise the OBR's view that Britain will not experience a double-dip recession, and that there will instead be a 'gradual rebalancing' of the economy, with the Government set to reach its target of eliminating the current structural deficit a year early.

Turning to employment, the Chancellor highlighted the OBR's prediction that public sector job losses over the coming four years will be lower than previously expected, falling from 490,000 to 330,000. This was said to be a result of the Government's emphasis on making welfare cuts, rather than reductions in departmental spending.

The Chancellor also set out a number of measures intended to support UK economic growth, with the announcement of a programme of 'significant and far-reaching' reforms to corporation tax to improve competitiveness, including plans to introduce a lower 10% rate of corporation tax on profits from patents. A new Growth Review has also been launched, with priority being given to planning and employment law, support for exporters and inward investors, and reforms to the competition regime.

The 2010 Comprehensive Spending Review

In recent years, Government spending has consistently exceeded Government receipts, resulting in an annual deficit and a spiralling national debt. Tackling this deficit has become the Coalition's top priority, prompting the Government to conduct a detailed review of public spending.

Chancellor George Osborne presented the Comprehensive Spending Review to the House of Commons on 20 October 2010. He unveiled over £80 billion in public sector spending cuts, including £7 billion in welfare savings, as part of the Government's commitment to eliminate the deficit by 2015. With Government departmental budget cuts averaging 19% over four years, the Chancellor estimated that around 490,000 public sector jobs may be lost, now predicted at £330,000.

Some of the key points from the Spending Review are outlined below:

- The state retirement age for men and women is to be equalised at 65 by November 2018. It will rise to 66 for men and women by 2020 – four years ahead of the previous plan
- Proposals will be set out to replace all working-age benefits and tax credits with a single, simple Universal Credit over the course of the next two Parliaments
- The educational maintenance allowance for 16-19 year olds will be dropped
- The child element of the Child Tax Credit will be increased by £30 in 2011/12 and £50 in 2012/13 above indexation, meaning annual increases of £180 and then £110 above the level promised by the Labour Government
- The Chancellor confirmed that Child Benefit will be removed from families with a higher-rate taxpayer. Child Benefit will now continue to be paid until a child leaves full-time education at the age of 18 or even 19
- Universal benefits for pensioners will be retained exactly as budgeted for by the previous Government and the temporary increase in the Cold Weather Payment will be made permanent
- Apprenticeship funding will be increased by 50% over the next four years, covering 75,000 extra places
- The Train to Gain programme will be dropped and replaced with an SME-focused training scheme
- A permanent tax levy on banks is being introduced.

Emergency Budget highlights

Following a review, the newly appointed Chancellor George Osborne delivered an Emergency Budget on 22 June 2010.

Some of the key announcements are outlined below.

Value Added Tax (VAT)

As widely anticipated, an increase in the standard rate of VAT was confirmed, and will see the main rate rising from 17.5% to 20% on 4 January 2011. The move is expected to raise more than £13 billion a year by the end of the Parliament – see page 3 for more information.

Capital gains tax (CGT)

A new 28% top rate of CGT has come into effect for gains realised after 22 June 2010, where an individual has total taxable income and gains of more than the basic rate limit for income tax (£37,400 for 2010/11). The lifetime limit for Entrepreneurs' Relief, which reduces the effective CGT on qualifying gains to 10%, has been raised from £2 million to £5 million.

Personal allowance

With the aim of protecting lower earners from the squeeze, the income tax personal allowance will rise to £7,475 in April 2011, removing around 880,000 people from the requirement to pay any income tax. However, higher rate taxpayers will be prevented from reaping the benefits of the changes by means of a reduction in the basic rate limit for 2011/12.

National insurance contributions (NICs)

Employers will see an increase in the threshold at which they start to pay national insurance contributions, which will rise by £21 a week above indexation. In addition, qualifying new businesses in targeted areas of the UK can now enjoy a national insurance 'holiday' of up to £5,000 for each of the first 10 employees hired within the first year of business.

Corporation tax

Corporation tax will be reduced to 27% from April 2011, with a further series of 1% cuts taking place each year until the rate reaches 24% in 2014. The small profits rate will also be cut from 21% to 20% from April 2011.

Small business finance

In a bid to improve access to finance for small businesses, a new Enterprise Capital fund of £37.5 million has been introduced, and the Enterprise Finance Guarantee is providing £200 million of additional lending until 31 March 2011.

Other announcements included a series of proposed changes to capital allowances to take effect from April 2012, plans to replace Air Passenger Duty with a per-plane aviation duty, and the creation of the new Office of Tax Simplification.

Corporate tax reform – the 'five year plan'

Alongside the Chancellor's Autumn Statement on 29 November, the Treasury published the Government's plan to reform the corporate tax system over the next five years.

Key elements include:

- reiterating the Government's intention to reduce the main rate of corporation tax – intended to give the UK the lowest main rate in the G7 and the fifth lowest in the G20
- focusing more on profits from UK activity in determining the tax base rather than attributing the worldwide income of a group to the UK
- taking action to reform the Controlled Foreign Company (CFC) regime and the taxation of foreign branches by adopting a more territorial approach
- identifying where the tax system can be simplified to reduce compliance costs on business
- improving the effectiveness of research and development tax credits
- introducing a preferential regime for profits arising from patents, known as a Patent Box.

The Patent Box regime will be optional, but companies opting in can expect profits from patents first commercialised after 29 November 2010 to be taxed at a 10% rate from 1 April 2013.

Timetable

Following the publishing of papers and more details between now and Spring 2011, we will see legislation on capital allowances reductions, on CFC rules interim improvements and on foreign branch reform in Finance Act 2011, with the completion of the CFC changes and legislation on the Patent Box following in Finance Bill 2012. Some draft legislation will be published on 9 December 2010.

Alongside these changes, Spring 2011 sees the first planned reduction in the rates of corporation tax, with the main rate set to fall to 24% by Spring 2014.

Change in the standard rate of VAT

The standard rate of VAT is set to rise from 17.5% to 20% on 4 January 2011. It is hoped the additional revenue generated from the increase will help to reduce the UK deficit.

Applying the higher rate

The rate of VAT that businesses charge depends on the date that goods or services are supplied. For VAT purposes this is the date that goods physically change hands (or a service is completed); or payment is received; or an invoice is issued – whichever is the earliest. The rules are modified in certain situations, including when there is a change in the standard rate of VAT.

For any supplies of standard-rated goods or services that take place on or after 4 January 2011 businesses should charge VAT at the new rate of 20%. As a consequence, firms currently calculating their VAT using the VAT fraction of 7/47 should use the new fraction of 1/6 from 4 January 2011.

Zero-rated supplies, such as basic foodstuffs, children's clothing and books; exempt supplies, such as education and health; and supplies subject to VAT at the reduced 5% rate, such as domestic fuel and power, are not affected by the change.

Anti-forestalling legislation

Finance (No.2) Act 2010 included anti-forestalling legislation to prevent the 17.5% rate applying to supplies of goods or services that are provided on or after 4 January 2011.

The legislation prevents forestalling by introducing a supplementary charge to VAT of 2.5% on the supply of goods or services where the customer cannot recover all the VAT on the supply, and one or more of the following conditions are met:

- the supplier and customer are connected parties;
- the value of the supply (and any related supplies made under the same scheme) exceeds £100,000. But this does not apply if the prepayment or issuing of an advance VAT invoice is normal commercial practice;
- the supplier or someone connected to the supplier funds a prepayment for the goods or services; or
- an advance VAT invoice is issued where payment is not due in full within six months (except hire purchase invoices issued in accordance with normal commercial practice).

The supplementary charge to VAT is due on 4 January 2011 and must be accounted for on the supplier's VAT return covering that date.

Pensions tax relief – the latest changes

In the Emergency Budget, the Government made it clear that it intended to replace a series of complicated changes to the pensions regime, due to start next April. Draft replacement legislation has recently been issued, with rules which apply to everyone, rather than targeting high earners.

Annual allowance

The main change will be to reduce the annual allowance (AA) from its current level of £255,000 to £50,000 with effect from 6 April 2011. AA is the amount by which the total pension savings can grow each year; above this value the surplus gives rise to an annual allowance charge as the individual's top slice of income.

Pension savings

Members of defined contribution (DC) schemes, in particular personal pensions (PPs), will need to look at the total of the contributions (whether personal, employer or third party) during the pension input period (PIP) for all of their pension savings. The PIP is usually the scheme year to the anniversary date which falls within the relevant tax year.

Members of defined benefits (DB) schemes, such as occupational final salary schemes, will have to work out how much their accrued pension has increased during the PIP.

Example

Self employed personal pension with AA charge

Alison, who is self employed, has taxable income of £110,000 in 2011/12. She is a member of two different PP schemes. Scheme A has a PIP ending on 31 March; Scheme B's ends on 30 November. She contributes £2,000 per month (£2,500 before basic rate tax relief) to Scheme A and £2,800 per month (£3,500 before tax relief) to Scheme B. She has been contributing similar amounts to these schemes for the previous three tax years. During the tax year ending 5 April 2012, her total pension contributions are:

Scheme A (year to 31 March 2012)	£30,000
Scheme B (year to 30 November 2011)	£42,000
Total pension savings	£72,000
AA for 2011/12	£(50,000)
Excess subject to AA charge	£22,000

The AA charge will therefore be £8,800 (£22,000 @ 40%).

The three year carry forward rule

Unused AA for the previous three tax years can be carried forward and added to the current year's £50,000 AA. For the tax year 2011/12, the first of the new regime, carry-forward will be available against an assumed AA of £50,000 for each of the tax years 2008/09, 2009/10 and 2010/11. No carry forward is available from an earlier tax year unless the individual was a member of a registered pension scheme at some time during that tax year.

Lifetime limit

The lifetime limit, which sets the maximum figure for tax-relieved savings in the fund, currently stands at £1.8 million. However, this limit is to be reduced to £1.5 million, probably from April 2012.

For more information on the new rules, please contact us.

Looking ahead

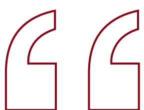
On 9 December the Government will publish draft clauses planned for inclusion in the Finance Bill 2011. This fulfils the Government's pledge to publish draft clauses for each Finance Bill at least three months in advance. The change forms part of the Coalition's new approach to tax policy making, which is supposedly based on 'predictability, stability and simplicity'.

At the same time, the Government will also report back on several key consultations including:

- Tax policy making: a new approach
- Simplification of Corporate Capital Gains for companies
- Pensions Annuitisation
- Furnished Holiday Lettings and
- The review of HM Revenue and Customs' powers.

The Chancellor has already announced that the 2011 Budget will take place on 23 March. While it is unclear exactly what new measures will be included, there are some changes that have already been announced for the 2011/12 tax year. These include an increase in the personal income tax allowance, a rise in national insurance contribution rates, and a reduction in the corporation tax rate. Please see page two for more information.

What they said...



'Employment is growing. The deficit is falling. Unemployment is set to fall. The plan is working.'

Chancellor of the Exchequer, George Osborne

'The Growth Review demonstrates a welcome focus by the Government on returning the UK economy to balanced, sustainable growth – something that will reassure businesses as they look towards making 2011 a Year for Growth.'

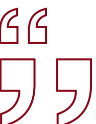
David Frost, British Chambers of Commerce

'This Autumn Statement does nothing to alleviate the effects of the summer recklessness that led the Chancellor to gamble with our future.'

Shadow Chancellor, Alan Johnson

'No politician should seize on these figures as some sort of good news story, least of all one that has just abandoned their plans to publish a jobs and growth strategy for the country.'

Brendan Barber, Trades Union Congress



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