

## ***17 APRIL 2002 - BUDGET 2002 BRIEFING FOR GARBETTS CLIENTS***

This is a brief summary of today's budget proposals as they impact upon typical clients of Garbetts clients – as such it is not intended to be a full exposition of all budget proposals.

As always, the comments are general in their nature and professional advice should be obtained before entering into or refraining from entering into any particular course of action.

### **Spin City**

This budget increase the alarming trend of the Chancellor treating the budget speech as a set piece performance, with separate press releases containing the substance of the budget proposals – proposals often completely ignored in the budget speech itself. One of the most controversial tax measures of the last decade – the notorious IR35 – was “announced” in such a way. In contrast several measures “announced” today have been pre-announced once or twice before, sometimes formally, sometimes by leak. Welcome to Spin City.

Crucially in this year's speech Mr Brown was “economical” with his announcement on NI increases – see the NI section below.

### **Income Tax**

- Rates unchanged. Allowances mostly indexed.

	2001-02	2002-03	
Personal allowance (under 65)	£4,535	£4,615	Frozen for 03/04
Personal allowance (65-74)	£5,990	£6,100	
Personal allowance (74 and over)	£6,260	£6,370	
Married couples allowance (born pre 6/4/35)	£5,365	£5,465	
Married couples allowance (over 75)	£5,435	£5,535	
Childrens Tax Credit	£5,200	£5,290	
Childrens Tax Credit – new baby bonus	-	£1,490	
Tax bands:			
0%	£1,880	£1,920	
22%	£1,881 to £29,400	£1,921 to £29,900	
40%	over £29,400	over £29,900	

- New fuel scale charge for company car users – linked to CO<sup>2</sup> emissions – from April 2003. This follows on from the car benefit changes from April 2002 which have been well documented.

- 100% capital allowances for businesses buying low emission cars for staff – emission ratings 120gm or less. Applies from today till 31 March 2008.

- Ability to carry charity donations back a year for immediate tax relief against last year's tax bill. Also a provision allowing tax payers to nominate a charity to receive any tax repayment arising from their annual tax returns, and enhanced tax relief for gifting land or buildings to charity.

**17 APRIL 2002 - BUDGET 2002**  
**BRIEFING FOR GARBETTS CLIENTS – Page 2**

**National Insurance**

- Announcement in the budget speech of a 1% rise in the employers, employees and self employed NI rates – deferred till April 2003 - but not in the speech was the extension of this 1% beyond current bands:

<u>Employees</u>	2002-03	2003-04
Employers and Employees primary threshold	£89 week	£89 week
Employees upper earnings limit (currently £575 a week, no change announced)	?	?
Employees rate on earnings between primary threshold and upper earnings limit (i.e. £87-£575 a week)	10%	11%
Employees rate on earnings over the upper earnings limit (i.e. on earnings over £575 a week)	-	1%
Employers rate on earnings over primary threshold	11.8%	12.8%
<u>Self employed</u>		
Lower profits limit for self employed	£4,615 pa	£4,615 pa
Upper profits limit for self employed (no change announced, currently £29,900 pa)	?	?
Class IV (self Employed) rate on profits between Upper and lower limits (i.e. £4,615 to £29,900 pa)	7%	8%
Class IV (Self Employed) on profits over upper limit	-	1%
No changes announced to Class II contribution	£2 week	£2 week

- I.E. What was announced as a 1% rise in fact was a 1% rise and an extension of the earnings scope to which NI applies. For the first time NI (at 1%) is payable on all earnings and self employed profits. These measures will impact upon businesses, employers and the self employed in equal measure, and will be noticeable – the equivalent of 1% on basic rate tax. The extension of the scope of NI on to all earnings / profits clearly signals the way ahead for NI – more rises in future budgets. These measures will hit Personal Service Companies caught by IR35 particularly hard.

**Corporation Tax**

-Reduction of the small companies rate to 19% from 1 April 2002, and reduction of the 10% starting rate to 0%. This means Corporation Tax rates will be:

Profits	% new From 1/4/02	% old
Up to £10k	nil	10%
£10k to £50k	23.75%	22.5%
£50k to £300k	19%	20%
£300k to £1,500k	32.75%	32.5%
£1,500k and over	30%	30%

- Reform of rules for Intellectual Property under Corporation Tax – depreciation can now be claimed on the purchase of goodwill and similar assets (a welcome change), and their sale will be taxed as income rather than capital gain (not so welcome – the benefit of indexation is lost).

- Extension of Research and Development Tax Credit to large companies.

- Reform (penalisation) of the taxation of foreign companies running branches in the UK.

**17 APRIL 2002 - BUDGET 2002**

**BRIEFING FOR GARBETTS CLIENTS – Page 3**

### **Capital Taxes**

- No rate changes. Increase in CGT annual exemption to £7,700 pa. IHT exemption increased in £250,000.
- Package of technical changes for CGT in respect of taper relief and similar anomalies
- Acceleration of Business Asset Taper Relief so that it applies in full after two years rather than four – this cements BATR as one of the most significant tax exemptions for business.
- Stamp duty exemption for transfers of goodwill – a welcome relief for anyone selling a business or incorporating a sole trade/partnership to into a limited company.
- Stamp duty anti avoidance rules for large property deals (£10m and over).
- Stamp duty exemption on commercial property deals in disadvantaged areas.

### **Value Added Tax**

- Increase in registration threshold to £55k, no change in vat rate or scope.
- Much heralded introduction of flat rate vat system for businesses turning over up to £100k, and a promise to extend this to businesses turning over up to £150k – do not be misled into thinking this will save you vat – the flat rates are not generous and most business will be better off not applying the scheme. A quick check on Garbetts own vat for the last 12 months (although we are considerably in excess of the turnover thresholds so would not qualify) shows that our VAT costs would have risen by around £1,500 over the period if the proposed flat rate had applied.
- Simplification of vat bad debt relief, including removing the requirement to notify debtors that you are claiming relief (the so called “I’m giving in” letter).
- Extension of the 5% VAT rate for certain residential property conversions (not previously lived in for three years or more).

### **Excise duties**

- Sprints, wine and beer frozen. Cuts on duties for small brewers. Increase in tobacco duties.
- Freeze on fuel duties (the memories of the fuel protests in 2000 are still fresh) and road fund licence.

### **Other business measures**

- EU provisions on mutual assistance in recovery of debts to be legislated – the UK will collect other EU member countries tax debts from UK residents, removing the age old tradition of tax liabilities not being enforceable across national boundaries.
- New package of tax reliefs for amateur sports clubs, although to some extent this only formalises current practice. Aligns reliefs for such clubs more closely with those given to registered charities (most sports clubs do not currently qualify as charities)
- Distance based road user charge for the haulage industry, with promised compensating tax cuts elsewhere for the haulage industry – intended to be neutral for UK operators, and to tax increase the tax burden on overseas hauliers operating in the UK.
- Compulsory filing of employers PAYE returns by internet by 2008-09 with incentives for starting earlier.

**17 APRIL 2002 - BUDGET 2002**

**BRIEFING FOR GARBETTS CLIENTS – Page 4**

- Improvements to CIS scheme (Construction Industry) to allow CIS deductions suffered by a business to be offset against the PAYE and CIS deductions due from the business – a useful cash flow advantage to businesses without CIS exemption.

- Community Investment Tax Credit for business and individual investment in disadvantaged areas.

### **Other personal measures**

- New Child Tax Credit from April 2002 – means tested, but still applicable in family incomes up to £50k pa.

- New Working Tax Credit from April 2002 – applies regardless of having children or a disability – income support under another name.

- Review of annuity arrangements linked to pension schemes – a welcome step at addressing the problems arising from low annuity rates, so long as it follows through to action.

- Review of tax rules for residence and domicile – could be a helpful clarification of the law in this notorious tax minefield where much relies on practice and case law rather than legislation.

### **Public expenditure & economics**

- 7.4% pa real growth (i.e. after inflation) in Health spending over the next five years

- 2.5% pa real growth in non health public expenditure in 2004-05 and 2005-06 (3.3% including health)

- 2-2.5% overall economic growth predicted for 2002, 3-3.5% for 2003

### **Conclusions**

As before Mr Brown likes his tax credits, and tinkering with them.

NI is the major revenue increase for now and the foreseeable future.

For most small businesses there is now more incentive than ever to incorporate – why does Mr Brown like companies and not sole traders/partnerships – does he have shares in a formation agent?