

the bottom line

Welcome to the Winter edition of "the bottom line" our taxation and accountancy information newsletter. This edition deals with the 2005 Pre-Budget Report, Small Firms Loan Guarantee Scheme, Greenback Alan news and News in Brief.

2005 Pre Budget Report

On 5 December 2005 Gordon Brown delivered the Pre-Budget Report in order to provide a progress report on what has been achieved in the tax year to date, to provide an update of the state of public finances and the economy and to set out Government Policy in the run up to the Annual Budget in the spring. The main tax issues are summarised below but perhaps the most unexpected and controversial matter was the announcement that the relaxation of the rules which would have enabled Self Invested Personal Pension Schemes (SIPPs) and Small Self Administered Schemes (SSASs) to invest in residential and other personal chattels are to be reversed. This is a major change in the rules detailed in our Autumn 2005 newsletter.

Other tax issues include:

- Personal allowances for 2006/07 were announced. Most have been increased by inflation with the basic personal allowance for 2006/07 being increased to £5,035 (2005/06 £4,895).
- Income tax rates for 2006/07 will not be announced until next years Budget.
- Thresholds for National Insurance have broadly increased in line with inflation.
- UITF40 - legislation is to be introduced in the Finance Bill 2006 to spread the impact of the 'change in accounting practice' introduced by UITF40. This statement requires a different valuation for work in progress where an ongoing service is provided and in the main will impact on professional practices.

The increased profits arising following the implementation of UITF40 will be able to be spread over up to six years.

- The government will be taking steps to ensure that there is sufficient expertise within HMRC about research and development in particular in relation to small and medium-sized enterprises in relation to tax credits. They acknowledge that the tax credit regime has not always been managed as professionally as it could have been in the past.
- The Chancellor has announced that the zero starting rate band for corporation tax will be withdrawn and all small company profits will be taxed at 19%. The introduction of the new starting rate of corporation tax of 10% in April 2006 and its subsequent reduction to nil in April 2007 led to many more businesses incorporating, in order to take advantage of lower rates of corporation tax and the ability to extract funds from the company as NIC free dividends. In the 2004 Finance Act legislation was introduced to ensure that profits out of which non corporate distributions were made were taxed at a rate of 19%. This legislation is extremely complex and has resulted in an additional administrative burden on small businesses. It is not yet known when the withdrawal of the zero starting rate will be effective.
- From April 2006 the 50% rate of first year capital allowances for small businesses will be re-introduced.

- Consideration is being given to modernising the capital allowances system for business cars.
- The Disclosure of Tax Avoidance Scheme rules have been extended to cover all income tax, corporation tax and capital gains tax.
- From 5 December 2005 the rules relating to capital gains tax are being amended to prevent a deduction for CGT purposes for losses on disposals of certain insurance policies including capital redemption policies. Schemes have been in existence which purport to create allowable losses in circumstances where there is no matching economic loss. These have been disclosed and hence legislation is being introduced to prevent such schemes.
- The VAT Annual Accounting Scheme threshold will be increased from 1 April 2006 to £1.35 million from its present level of £660,000.
- From 1 January 2006 where an input tax claim is made in respect of road fuel purchased by employees for business mileage, the claim must be supported by a VAT invoice or invoices sufficient to cover the claim. This is regardless of whether the claim is based on mileage allowances or the actual cost of the fuel.
- Changes have been announced to the tax credits regime in order to deal with the well publicised overpayments problem. Under current rules the first £2,500 of any increase in income over a base year is disregarded in recalculating an award. This limit is to be increased to £25,000 such that in most cases, awards will be based on prior year income. This new limit applies for 2006/07 onwards. There have been a number of other changes to the scheme, mainly in respect of reporting.
- A new firm tax regime will come into effect from 1 April 2006 which will apply to production companies within the charge to corporation tax. If you would like advice on any of the proposed changes or have any other queries please do not hesitate to contact us.

NEWS IN BRIEF

EU Sales

HM Revenue and Customs have adopted a hard line approach to zero rating sales to other Member States. To qualify for zero rating the exporter needs to obtain and quote their customer's VAT registration number on their invoice and hold sufficient evidence of export to show the consignment left the EU. We recommend that all EU VAT numbers are checked with HMRC for validity prior to the sale. You should check with your hauliers and customers to ensure that original documentation is provided as evidence of export.

Gift Aid Donations

In recent years there has been a huge increase in the number of telephone donations to charity. As a result the Government has relaxed the rules relating to Gift Aid from 1 November 2005. Prior to this date a donor made a verbal declaration which was followed up by a written statement from the charity to the donor giving 30 days in which to cancel the declaration. This requirement has been removed although the charity will have to ensure that it maintains an adequate audit trail of the donor's name and address, together with a note that the operation of Gift Aid was explained to the donor. In addition to the charity being able to reclaim tax on the donation, the donor can also claim additional

higher rate tax relief on submission of their personal tax returns.

Christmas Party

It is worth providing a reminder of the tax exemption available in respect of an annual party or similar function provided for employees. The exemption applies provided the cost per head does not exceed £150. The cost is determined by dividing the total cost including VAT, transport and accommodation by the number of people attending (employees plus guests). This is an exemption, not an allowance and hence if the £150 limit is breached, the whole amount is assessable on the director or employee as a benefit. Where the limit is breached by say three functions, it is important to decide which one or ones are exempt.

Stop Press - Taxation of Husband and Wife Companies and Partnerships

Many of our readers will be delighted to hear the outcome of the 'Artic Systems' case which we covered in our Autumn newsletter was heard by the Court of Appeal at the end of November 2005. In summary the case focused on the Revenue's objections to the way some married couples who jointly own and run a company can use their salary and dividend payments to reduce their joint tax bill.

The decision of the Court of Appeal was a resounding victory for the taxpayers. In particular it means that in many circumstances where an individual and their spouse work together they will be outside the scope of the settlement legislation which the Revenue had tried to apply to ensure a higher tax take. The decision will not apply to all circumstances and if you want to discuss your position in detail please let us know. It remains to be seen if the Revenue will be able to take this case to the House of Lords or whether they intend to change the legislation.

Greenback Alan News

As last year, we did not send Christmas cards this year and instead we donated money to Theatre for a Change, a charity that uses interactive theatre to promote young people's rights to lead healthy lives free from abuse. For more information please go to their website at www.theatreforachange.com We wish you all a very happy and prosperous 2006.

Small Firms Loan Guarantee Scheme (SFLGS)

From 1 December 2005 there are changes to the SFLGS focusing on start ups and younger businesses. The main criteria will be:

- extending lending limits so that a simple £250,000 limit applies to all eligible small and medium-sized enterprises (SME's);
- lifting the turnover limit for eligible SME's to £5.6 million;
- evaluating each business on the quality of the business rather than on the borrowing history of individuals involved with the business;
- encouraging high street banks

and specialist lenders to make SFLG loans available for a period of between two and ten years;

- limiting the provision of SFLG to firms that have been in business for less than five years.

The SFLG will cover 75% of the lender's risk for which the business will have to pay an annual premium of 2% of the outstanding balance of the loan. SFLG loans may be of interest to SME's that have been unable to get normal loans because there is no security to guarantee it, if they operate in an approved sector and have a viable business plan.



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