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**NEWSLETTER JULY 2010**

**FEE PROTECTION INSURANCE**

Fee Protection Insurance is available to the firm's clients via Abbey Tax Protection.

The insurance arrangements cover the professional fees which arise in connection with income tax self assessment full enquiries, corporation tax self assessment full enquiries, corporation tax accounts investigations, employer compliance disputes and H M Revenue & Customs VAT disputes.

Cover is available at the following rates:

<b>Client Status</b>	<b>Fee per Annum</b>
Personal taxation clients	£30.00
Company directors	£30.00
Partners – in partnership	£30.00
Sole traders	£120.00
Partnerships – as distinct from the partners	£120.00
Companies – as distinct from the directors	£120.00

The fees are payable for scheme years commencing 1<sup>st</sup> September.

Clients may join the scheme at any time during a scheme year in which event a reduced premium will apply for that scheme year.

Clients at 1<sup>st</sup> July 2010 have received full details of the scheme. New clients from 1<sup>st</sup> July 2010 receive details of the scheme prior to the annual renewal on 1<sup>st</sup> September. Further information regarding the scheme is available to all clients upon request.

**NEW GOVERNMENT – FIRST BUDGET**

So we have a new government. Following the inconclusive results of the May 2010 general election and the first hung parliament since February 1974, we have a coalition government comprising the Conservatives and the Liberal Democrats.

Against a backdrop of the worst economic crisis for decades (and some would argue, in history) both in the United Kingdom and globally, the Chancellor of the Exchequer, George Osborne delivered the coalition government's emergency Budget on 22 June.

For the first time, the forecasts which supported the Budget measures were prepared by the newly constituted Office of Budget Responsibility (OBR) instead of the government. The OBR now forecasts economic growth of 1.2% in 2010, rising to 2.3% in 2011 due to the impact of the tax increases and spending cuts announced by the Chancellor in the emergency Budget.

The government's principal aim, both in this Budget and in its overall monetary policy, is to reduce the budget deficit. The deficit is now forecast to reduce from £149 billion to some £37 billion by 2014/15. The reduction in the budget deficit will be tackled in the main by proposed cuts in government spending as opposed to increases in taxation.

The government spending cuts announced in the emergency Budget include a £113 billion squeeze on public spending over a five year period (some £40 billion more than planned by the last government), with government departments being told to cut their budgets by some 25%.

For businesses, initial concerns proved, to a large degree, to be unfounded, except for the proposed increase in VAT from 17.5% to 20% from 4 January 2011 which will have a marked impact on businesses, especially in the retailing sector, as spending by the public declines.

The increase in the entrepreneurs' lifetime relief from £2 million to £5 million was especially welcome, as was the announcement that the rate of corporation tax will be reduced in future years.

The proposed banking levy, to be introduced in January 2011, has caused concern amongst the banks, but it is suggested that the banks' reaction will find little support from the public at large.

For individuals, the Budget contained a mixed bag, with a proposed increase in personal allowances in April next year and the much heralded increase in capital gains tax being less than was originally feared, remaining at 18% for basic rate taxpayers and rising to 28% for higher rate taxpayers. However, the higher rate income tax threshold will be reduced so that higher rate taxpayers do not benefit from the increase in the personal allowance.

However, the increase in VAT will cause concern to many, especially the lower paid, and the government's intention to cut welfare spending by £11 billion will impact many benefit claimants, including those claiming child benefit, housing benefit and tax credits.

The government and the nation will now have to hold its breath and wait to see if this historic emergency Budget will fulfill its objectives.

## THIS YEAR ... NEXT YEAR ... SOMETIME?

Many of our readers will remember the “good old days” of Budgets, before we had Pre-Budget Reports, when the contents of a Budget took effect almost immediately, in the tax year commencing immediately after the Budget.

But all this changed when Gordon Brown became Chancellor of the Exchequer. We now have a whole raft of measures announced in the autumn Pre-Budget Report, the majority of which are repeated in the Chancellor’s Budget speech in spring of the following year, many of which do not take effect until a year after the Budget, and in some cases several years after that.

All of this can lead to confusion and so in this article we summarise the main points included in the Chancellor’s emergency Budget of 22 June and indicate just when these measures will come into effect.

### **Business**

#### **Value added tax**

The standard rate of value added tax will increase from 17.5 per cent to 20 per cent **from 4 January 2011**.

#### **Corporation tax**

There will be no changes in the rates of corporation tax announced in the final Labour Budget of March this year. However the rate of corporation tax for large companies will be cut from 28 per cent to 27 per cent **for the year ending 31 March 2012** and will fall by a further 1 per cent **for the next three years**. For small companies the rate will decrease from 21 per cent to 20 per cent **for the year ending 31 March 2012**.

#### **National Insurance**

The threshold at which employers start to pay national insurance will increase by £21 a week **from April 2011**.

The increase of 1 per cent in national insurance for employers which was announced by the last government will take effect **from April 2011**.

#### **Capital allowances**

The annual investment allowance will be reduced from £100,000 to £25,000 **from April 2012**.

### **Individuals**

#### **Personal allowances**

The personal allowance threshold will increase by £1,000 to £7,475 **from 6 April 2011**. The government’s long term objective is to increase this threshold to £10,000 but **no specific dates** have been announced for any further increases.

#### **Income tax rates**

**From 6 April 2011**, the higher rate income tax threshold will be reduced so that higher rate taxpayers do not benefit from the increase in the personal allowance (see above).

#### **National insurance**

The increase of 1 per cent in national insurance for employees which was announced by the last government will take effect **from April 2011**.

#### **Capital gains tax**

Capital gains tax remains at 18 per cent for basic rate taxpayers but increased **from 23 June this year** to 28 per cent for higher rate taxpayers.

#### **Entrepreneurs’ relief**

The lifetime relief for entrepreneurs increased from £2 million to £5 million **from 23 June this year**. From that date the net tax gain for standard rate taxpayers is 8 per cent and for higher rate taxpayers is 18 per cent, provided that the entrepreneur satisfies the conditions for the relief.

#### **Pensions**

The reinstatement of the link between the state pension and average earnings will take effect **from April 2011**.

#### **Tax Credits**

The annual increase in tax credits will be linked to the consumer prices index rather than the retail price index **from 2011**.

#### **Child benefit**

Child benefit is to be frozen **for the next three years**.

#### **Council tax**

Council tax is to be frozen for one year **from April 2011**.

#### **Insurance premium tax**

Insurance premium tax is to increase from 5 per cent to 6 per cent **from January 2011**.

#### **Fuel duty**

The Chancellor has not scrapped the last government’s proposals to increase the duty on fuel. There will therefore be a 1p per litre rise in fuel duty **in October** this year, followed by a 0.76 pence rise in **January 2011**.

#### **Stamp duty**

At present, first time buyers can claim relief from stamp duty land tax on residential transactions up to £250,000 until **24 March 2012**. This relief may be stopped after this date or, alternatively, the government may extend the relief period.

## THE CUTS BEGIN – GOODBYE TO THE CHILD TRUST FUND

In May of this year the new coalition government announced its intention to reduce and then stop government payments to Child Trust Fund (CTF) accounts. The demise of the CTF, once one of the flagship benefits of the outgoing government, is part of the many cuts in public spending announced, and to be announced, by this government.

Until the necessary changes are made to the legislation, the present rules relating to the CTF will continue to apply. Set out below are the present CTF rules, together with the proposed changes.

### **Initial payments**

#### *Present rules*

At present, parents receive a £250 voucher from the government which is paid into a CTF account when their child reaches age 7. If the child is from a lower income family the government pays an additional £250 at this time.

#### *Proposed changes*

Any child whose 7<sup>th</sup> birthday is after 31 July 2010 will no longer qualify for the above payments.

### **Disabled children**

#### *Present rules*

From April 2010, a child who was entitled to Disability Living Allowance (DLA) receives an annual payment of either £100 or £200, dependent on the care component of their DLA award.

#### *Proposed changes*

From the tax year 2011/12 onwards the government will make no payments into Child Trust Funds for DLA entitlement.

### **Children in local authority care**

#### *Present rules*

If a child in local authority care does not have a CTF, the Government will open an account for them into which it makes a payment of £500.

#### *Proposed changes*

For children who go into local authority care after 31 July 2010 the payment will be reduced from £500 to £100. Any child going into care from January 2011 onwards will no longer qualify for a CTF account.

### **Proposals for those with existing CTF accounts**

If you have a CTF voucher which you have not used before the new rules come into effect you are able to use the voucher to open an account, provided that it has not passed its expiry date. If you don't use the voucher before this date, HM Revenue & Customs will open an account for your child. The amount shown on the voucher will be paid into the account.

Any child born after December 2010 will not be eligible for a CTF. However, for any account that has been set up for eligible children, the child will continue to receive tax free investment growth and it will not be possible to withdraw money from the account until the child reaches age 18. Any friends or family of the child, together with the child, will be able to contribute to the account up to an overall total of £1,200 each year. It will still be possible to change the type of account and/or to move the account to another provider.

## SOME GOOD NEWS FOR ENTREPRENEURS

In the coalition government's emergency Budget, the Chancellor of the Exchequer announced that the lifetime allowance for entrepreneurs' relief was to be increased from £2 million to £5 million pounds from 23 June this year. This article explains the significance of this increase and summarises the principal features of entrepreneurs' relief. This topic is complex and it is therefore important that those readers who feel that they are able to claim the relief, or are likely to do so at some time in the future, contact us before making any decisions so that we may provide timely advice.

Entrepreneurs' relief was first introduced in April 2008 by the Labour government in an effort to assist owners of small businesses when they came to dispose of business assets. The relief takes the form of a reduction in the rate of capital gains tax (CGT) which, at the time of the introduction of the relief, stood at 18% for all taxpayers. The net CGT payable after a disposal was reduced to 10% which represented a reduction of 8%. However, in the emergency Budget the rate of CGT for higher rate and additional rate taxpayers was increased from 18% to 28%, but the net CGT after entrepreneurs' relief remained at 10%. This saving of 18% in CGT has naturally been welcomed by those higher rate taxpayers disposing of or thinking of disposing of their business assets.

The maximum gain to which the disposal of business assets can apply is now £5 million. Remember that this is a lifetime limit so if a person makes disposals of a number of businesses the aggregate gains on all disposals will be subject to the overall £5 million lifetime limit. The maximum relief for a basic rate taxpayer is therefore the difference between the CGT rate of 18% and the rate for entrepreneurs which is 10%. Applying this reduction in tax to the lifetime limit results in a maximum saving of £400,000 whilst the saving for a higher rate taxpayer is now 18% x £5 million = £900,000.

Entrepreneurs' relief applies to three types of business – sole traders, partnerships and companies.

### **Sole traders**

In the case of sole traders, the relief is available if the sole trader disposes of the whole business or a distinct part of the business. It is not available if the owner sells some of the assets of the business. What is deemed to be a "distinct part" of the business will be judged according to the circumstances of each case and so it is not possible to lay down any specific rules.

It is interesting to note that the relief is available if the sole proprietor sells his business as a going concern to a company which is owned by him. In this case, any gain in value of the assets of the business when sold will benefit from the relief. However, any valuations made of these assets will be closely scrutinised by the taxation authorities.

Note that the relief also includes furnished holiday lettings but not other types of lettings,

### **Partnerships**

The conditions for claiming entrepreneurs' relief when an outgoing partner sells his or her share in a partnership are complex as the sale of a partner's share in a partnership is effectively the sale of part of the goodwill of the partnership, as the partnership itself will continue. Once again, each case will be considered on its own merits but the general rule is that provided that the partner sells his share in the partnership and the sale generates a capital gain, then the relief is available to that partner.

### **Companies**

Entrepreneurs' relief in relation to companies will relate to the sale of shares or other securities in the company. In order to qualify for the relief the company must be a trading company, the definition of which can be complex, but basically the company must carry on trading activities and there must be no substantial non-trading activities.

The company can be the holding company of a trading group but must have been so for at least 12 months prior to the disposal.

The most important condition attaching to the relief is that the person disposing of the shares must own at least 5% of the ordinary share capital of the company and his shares must have entitled him to at least 5% of the votes. So non-voting shares will not count. In addition, the person disposing of the shares must be an officer of the company or an employee. In relation to both the above conditions, they must have existed for at least 12 months prior to the disposal. It is important to note that provided the minimum holding of 5% of shares has been held for 12 months, the relief will apply to all shares that are subsequently disposed of. So, for example, if a director of the company has held 5% of shares for at least 12 months but in the last 12 months he had purchased a further 20% of the shares, the relief will apply to his total 25% holding.

Of course, not all disposals will be shares sold by a shareholder in a company which continues to trade after the disposal. In the case of a company which is wound up the relief can still apply, provided that the distribution of the assets on the winding up is deemed to be a capital distribution for tax purposes and not income. The relief will only apply if the distribution takes place within 3 years of the company ceasing to trade, provided that the required conditions have been met for a period of at least 12 months prior to the cessation of trade.

Care should be exercised if shares are disposed of and the consideration for these shares is shares in another company to whom the shares have been sold. There can be problems if the shares given in the new company are less than 5% of the shares of this company.

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<sup>i</sup> *The articles in this newsletter are of necessity summaries of the topics covered. The publisher has taken all due care in the preparation of this publication. No responsibility for loss occasioned to any person acting or refraining from action as a result of any material in this publication can be accepted by the authors or the publishers. The publisher accepts no responsibility for the content of any material provided by third parties or for the content of any hypertext site referred to in this publication. The Publisher accepts no responsibility for the content of any website of other document referred to in this publication.*