# Botting & Co Ltd News

Budget 2008

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## Delay for income shifting law

**Someone listened to small businesses**

Our January newsletter warned of the crackdown on small businesses that distribute profits to individuals who make unequal contributions to the business. The Government refers to this behaviour as 'income shifting'.

Draft proposals to counter income shifting where it saves tax overall were released for consultation in December 2007, and were criticised as being completely unworkable. Fortunately someone in the Treasury listened and the income shifting law will be delayed until at least 6 April 2009. Unfortunately we now have another year of uncertainty for small businesses while taxation policy is redrafted.

## Relief for Entrepreneurs

The Chancellor has confirmed a new capital tax relief will be available when you sell part or all of your business, or shares in your own company, after 5 April 2008. For deals made after that date taper relief and indexation allowance are lost, which increases the effective tax rate from 5% (for basic rate taxpayers) or 10% (for higher rate taxpayers) to a flat 18% for all.

The new entrepreneurs' relief restores the effective tax rate on the gain to 10%, before deduction of your annual exemption or any capital losses. However, the relief only applies to the first £1 million of gains made on and after 6 April 2008. Gains in excess of £1 million, or which do not qualify will be taxed at 18%.

The disposal must also meet some tight conditions to qualify for entrepreneurs' relief:

- The business must be 'trading' so property letting does not qualify, unless it is furnished holiday lettings.
- A single business asset, such as a building, must be disposed of at the same time as the associated business. Restrictions for ownership periods and non-business use will apply.
- You must have held the business assets or 5% of the voting shares of the company for at least one year before the disposal.
- Only shares in a company you have worked in, or been an officer of, for at least a year, will qualify.

If you are planning to sell your business the new entrepreneurs' relief may allow you to defer the sale until after 5 April 2008, and still pay the same amount of tax.

### Employee share schemes

Companies that use the Enterprise Management Incentive (EMI) share option scheme to help attract and retain employees, will be able to issue share options worth up to £120,000 to each employee from 6 April 2008. If the scheme is operated correctly the employees can acquire shares free of income tax and national insurance. However, when the employees sell their shares they are unlikely to qualify for entrepreneurs' relief, so they will pay capital gains tax at 18% on gains over their annual exemption.

## Tax Data 2008/09

**Income Tax**
Personal Allowance: £5,435
***Tax rates:***
Savings to £2,320 @ 10%
Earned to £36,000 @ 20%,
All above £36,000 @ 40%,
***Tax on UK dividends*:**
to £36,000@ 10%
above £36,000 @ 32.5%

**National Insurance**
***Class 1 employers:***
12.8% over £5,435
***Class 1 employees:***
11% on £5,435 to £40,040
plus 1% above £40,040
***Class 4:***
8% on £5,435 to £40,040 plus
1% on profits above £40,040
***Class 2:*** £2.30 per week
***Class 3:*** £8.10 per week

**Capital Gains Tax**
All gains taxed at 18%
Annual exemption: £9,600

**Inheritance Tax**
Nil rate band: £312,000
transferable to spouse on death
Excess taxed at 40% on death.

**Pension Contributions**
With no earnings: £3,600 gross
Otherwise: 100% of earnings.
Tax relief per year cap: £235,000
Pension fund cap: £1.65 million

**Corporation Tax**
Small co: 21% to £300,000
Marginal: 29.75% to £1.5 m
Large co: 28% over £1.5 m

**VAT turnover thresholds:**
Registration over: £67,000
Deregistration under: £65,000
VAT schemes max turnover
Flat rate small bus': £150,000
Cash Accounting: £1.35m
Annual accounting: £1.35m

**Tax free mileage rates**
***Own car:***
First 10,000 miles 40p
Over 10,000 miles 25p
***Company car (fuel only):***

| | Petrol | Diesel | LPG |
|---|---|---|---|
| To 1400 cc | 11p | 11p | 7p |
| To 2000 cc | 13p | 11p | 8p |
| 2000 cc + | 19p | 14p | 11p |

# Income tax changes

Tax is not that simple

We were told last March that basic rate of tax will drop from 22% to 20% on 6 April 2008 and the starting rate of 10% will go. But that is not strictly true.

The 10% tax band has been abolished for all income except for **savings income**. Most people will pay 20% tax on all of their taxable income up to £36,000 in 2008/09, and 40% on income above that threshold. However, UK dividends are still taxed at 10% up to £36,000 and at 32.5% above £36,000. The 10% dividend tax credit means as a basic rate taxpayer you pay no additional income tax on dividends.

Savings income is basically interest paid by banks and building societies. It is taxed as a slice on top of your earned income but before your dividend income. The first £2,320 of savings income is taxed at 10%, if your other earned income hasn't already pushed you into the 20% rate.

**Example**

In 2008/09 you take a salary of £5,435 and gross dividends of £33,000 from your company. You also receive £2,000 in gross interest from a savings account. Your personal allowance of £5,435 covers your salary leaving nothing taxable. The gross interest is taxed as the next slice of your income, and falls within the savings income band of up to £2,320, so is taxed at 10%. Your total taxable income amounts to £35,000 (£33,000 + £2,000), which is within the £36,000 limit for higher rate tax, so all of your dividend income is taxed at 10%

**EIS relief**

The only income tax relief to be extended in the Budget is EIS relief, available when an individual subscribes for EIS shares. He can claim income tax relief of 20% of the amount subscribed, up to a limit of £400,000. This caps the income tax relief at £80,000 (20% x £400,000) for each tax year. This income tax relief is increased to £100,000 on an investment of up to £500,000 made from 6 April 2008.

# Capital allowances and cars

The new Annual Investment Allowance (AIA), which gives 100% deduction for the cost of new equipment up to a total of £50,000 per year, will come into effect from April. The cost of assets not covered by the AIA is given tax relief by an annual 20% writing down allowance (WDA), or at 10% for equipment that is an integral feature in a building.

Most small businesses won't have to worry about claiming the WDA on new equipment as the full cost will be covered by the £50,000 AIA. However, you will need to claim the WDA for equipment purchased before April 2008, which has not yet been given full tax relief. This could be a pain as the amounts of unrelieved costs get progressively smaller each year. Now for accounting periods starting on or after 1 or 6 April 2008 (depending on the structure of your business) you will be able to write off the full cost of old assets, where the total unrelieved cost is £1,000 or less.

More smog less tax relief

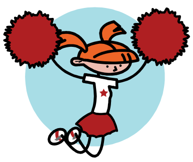
The capital allowances system for company cars is to be reformed from **April 2009**, not from April 2008 as we had been lead to believe. The new system will categorise all cars on the basis of their $CO_2$ emissions.

Low emissions cars will continue to qualify for a 100% first year allowance, but the definition of low emissions will be changed from $CO_2$ of 120g/km or less, to 110g/km or less from **1 April 2008** (note the earlier year). High emissions cars are those with $CO_2$ emissions of 160g/km or more and will only qualify for a 10% WDA. All other cars will qualify for a 20% WDA. This new system will lengthen the time taken to get full tax relief for the cost of cars, particularly for higher polluting vehicles.

# Three cheers for VAT changes

**Registration**

If your business is not VAT registered you now have more headroom for sales before you must register for VAT. The compulsory VAT threshold is increased from £64,000 to £67,000 from 1 April 2008. This covers vatable sales in the previous 12 months, or sales expected in the next month. You can register voluntarily for VAT when sales are below this threshold. If your sales drop below the deregistration threshold (£65,000 from 1 April 2008) you can ask to be deregistered for VAT.



**Small errors**

As a VAT registered business you may make small errors in your VAT calculations. If the total net error amounts to no more than £2,000 you can work the under or over payment into your next VAT return. If the VAT difference is more than £2,000 you should write to the VAT office and confess. Unfortunately this normally generates a demand for interest on the late paid VAT. This error reporting threshold will be raised to the greater of £10,000, or 1% of the reported turnover for the VAT quarter, subject to a cap of £50,000. This will apply for accounting periods beginning on and after 1 July 2008.

**VAT claims**

Where you have overpaid VAT, HMRC prevent you from reclaiming overpayments for periods ending over three years ago. The House of Lords has just ruled this three year cap is illegal. You now have until 31 March 2009 to reclaim overpaid VAT from periods before 4 December 1996 and claim VAT on purchases for periods prior to 1 May 2006. We can help you draft your claim.