2012

AUTUMN STATEMENT

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This year, next year, sometime...

We were told to expect more bad news in the Chancellor's Autumn Statement: borrowing rising, deficits swelling, recession returning, austerity increasing. In the event, Mr Osborne read out long lists of numbers that had the pundits scratching their heads – he seemed to be claiming that things were not as bad as the worst predictions, but still so bad that he would have to extend his belt-tightening plans all the way to 2017/18. He claimed that the plans were working, but more slowly than hoped for because of economic problems in Europe and elsewhere; the Shadow Chancellor, Mr Balls, predictably responded that the plans were the problem and should be abandoned.

As well as Mr Osborne's baffling lists of national economic statistics, the Autumn Statement includes a number of much more detailed measures which make a practical difference to individual taxpayers and businesses. Because the Chancellor is making plans for the long term, some of these take effect immediately, some come in soon, and others are over the horizon. This summary explains the important changes that were announced in the speech or the reams of supporting documentation which were published on the internet when the Chancellor sat down. ●

Plant growth

The annual investment allowance (AIA) is a relief for businesses which invest in plant and machinery. Instead of claiming a tax deduction for accounting depreciation, businesses can claim writing down allowances at only 18% (or 8% for some assets). The AIA is an amount that can be spent in a year on which 100% of the cost can be claimed immediately, reducing current tax charges and providing a significant cash incentive to invest in new equipment.

When it was introduced in 2008, the AIA was set at expenditure of £50,000 a year, regardless of the size of business. The last Labour budget raised it to £100,000 in 2010, but it was cut to £25,000 from April 2012. Mr Osborne did not mention that cut when announcing a 'tenfold increase' which will take effect on 1 January 2013 – the 100% allowance will be available on expenditure of £250,000 a year for two years from that date. According to the Chancellor, this will cover the whole of the annual capital investment of 99% of small businesses.

There are usually complex rules around a change of rate which can produce surprising results – for example, a business with a year-end of 31 March 2013 will only be able to use 3/12 of the increased limit by that date. Businesses will be encouraged to invest, but it will be important to check the numbers first. ●

National Insurance

There were no changes to the percentage rates of National Insurance Contributions (NICs). As usual, the starting point for paying NICs went up slightly, and the upper earnings limit is adjusted downwards so that it continues to match the amount at which 40% tax starts (£41,450, equal to the personal allowance of £9,440 and basic rate band of £32,010). Although tax rates are complicated for someone who receives different types of income, someone with only salary will move from a total 'tax and NIC' rate of 32% at £41,450 to 42% at £41,451. ●

Small business rates

The Chancellor extended the temporary doubling of the Small Business Rate Relief scheme for a further 12 months from 1 April 2013. Over half a million small businesses are expected to benefit, with 350,000 paying no business rates at all until April 2014. ●

Cash basis

In the March 2012 Budget, the Chancellor announced that he was considering allowing small businesses to compute their profits using a 'cash basis' if they wanted to. This is considered simpler than the accruals basis that is currently required, and also means recognising profits later – and so delaying the payment of tax – if a business gives credit to its customers. This will be introduced on a voluntary basis from April 2013 for those businesses which trade below the VAT registration threshold (currently turnover of £77,000).

There is a 'cash accounting scheme' for VAT-registered traders with turnover of up to £1.6m, but this will be a completely different set of rules. Although it does potentially simplify accounting, changing to and getting used to a new system may present its own difficulties.

Unincorporated businesses will also be able to use flat rates to calculate some types of expenses rather than having to calculate actual amounts – or, presumably, keep records of that type of cost. ●

In the tank

It was widely predicted that the Chancellor would postpone or cancel the increase of 3p per litre (plus 0.6p in VAT) that was scheduled for January – and would remind everyone that it was proposed by Labour. The Conservative benches roared as if 'cancelling a tax increase' were the same as 'announcing a tax cut'. Still, it will help businesses and individuals, and will keep the Government's measure of inflation a little lower over the next year.

Those employees who receive the taxable benefit of fuel for company cars and vans, paid for by their employer, will see a tax increase next year. The taxable amount for cars is found by multiplying a fixed figure by the percentage rate used for company car benefits, derived from the carbon dioxide emissions rating of the car. The fixed figure rises for 2013/14 from £20,200 to £21,100, an increase of 4.46%. For the first time in several years, the percentage itself will not be going up – but there will be increases in April 2014, 2015 and 2016 for most cars.

The fuel benefit for company vans which can be used for more than business and home-to-work travel is a flat rate £550, which will rise to £564 in April 2013 – a 2.5% increase. ●

Ready or not!

Tax avoidance and evasion has been big news this year, with multinational companies such as Starbucks being the latest targets of public and political anger for using legal arrangements to minimise their tax liabilities. At least the Chancellor drew a careful distinction between evasion, which is illegal, and 'aggressive avoidance', which is not. HM Revenue & Customs are challenging many avoidance schemes through the courts, and many more by writing to those who have used the schemes, putting pressure on them to settle up rather than risk losing at law.

As usual, the Autumn Statement included measures against tax avoidance, but this year they were more general in nature – allocating more resources to HMRC's anti-avoidance drive, and confirming that a 'General Anti-Abuse Rule' will be introduced in 2013, rather than closing down a list of specific schemes. This is one area in which the Chancellor must feel confident that he will have the support of the public and the press, although what individual taxpayers consider 'acceptable' or 'aggressive' is a personal decision.

The detailed policy document sets out a list of areas in which the Chancellor believes HMRC can find more money that people are hiding or sheltering. An extra 2,500 inspectors will be devoted to looking for evaders. The department will be given more powers to collect information from businesses which process payment card transactions, to try to identify merchants who are not declaring all their income. More resources will be allocated to closing down some long-standing tax avoidance schemes by challenging them in the courts, where there is a long backlog of cases to work through. HMRC's attempts to persuade taxpayers to settle are often based on a lead case which has not yet gone to court – but they don't always win, so it would be wise to take advice before agreeing to anything.

The specific schemes that are being closed do not include the global business arrangements that have received so much attention in recent weeks – payments between connected companies for 'licensing rights' and other supplies which shift the profits out of the UK for tax purposes. If these companies don't decide that paying more tax will be good publicity, HMRC will have to challenge their profit-shifting using their existing rules and powers.

The Chancellor also commented on measures to clamp down on evasion, including a tax agreement with Switzerland under which Swiss banks will deduct money from UK residents' assets and pay it to the UK Exchequer – if the account-holder doesn't agree, their name and address will be given to HMRC, so their tax affairs will need to be in order. This is expected to bring in more than £3 billion in 2013/14, and nearly £6 billion over 6 years. That's more than three times as much as the total amount that they hope to raise from all the combined 'anti-avoidance' efforts over the same period. ●

We already knew…

The Autumn Statement makes no direct reference to many of the changes which were announced in March but which have not yet taken effect. For example, we know that the top rate of tax, for those earning above £150,000, will be cut from 50% to 45% in April 2013. Clearly responding to the accusations of unfairness that this produced, the Chancellor spelled out how the amount of tax paid by high earners fell when the 50% rate was introduced, and emphasised that they would pay more each year under his proposals – but the rate cut remains.

The clawback of child benefit for those earning over £50,000 will come into effect on 7 January 2013, complicating the tax affairs of many couples and creating a high marginal rate of tax where it applies. HMRC has written to all those thought to be affected. It will be common for the benefit to be paid to the mother, but clawed back from a higher earning partner who works full-time – the alternative is for the mother to stop receiving the payment, which will be simpler. ●

Rates and allowances

We were told earlier this year that the personal tax-free allowance would increase from £8,105 to £9,205 in April 2013. Surprisingly, the Chancellor announced that this will be increased instead to £9,440. This benefits everyone on incomes of up to £118,880 – the personal allowance is withdrawn at £1 for every £2 by which income exceeds £100,000, and disappears altogether by £118,880.

However, the point at which 40% tax will start falls to taxable income of £32,010 (with the tax-free allowance, a total of £41,450) compared to £34,370 in 2012/13 (total income of £42,475). This means that more people will have to pay at the higher rate, and the full benefit of the increase in personal allowances is partially clawed back from them. Someone with a salary of exactly £42,475 in each year will pay income tax on it of £6,874 in 2012/13 and £6,812 in 2013/14.

The March Budget also included the announcement that the age allowances for those over 65 will be frozen from 2013/14. Not surprisingly, he did not return to this piece of 'bad news'. The age limit will also be changed so that only people born before 6 April 1948 will qualify – in 2013/14, that means that only those who are already 65 at the beginning of the year will enjoy age allowance, and only those who are over 75 will receive the higher rate. ●

Pensions capped?

It was widely predicted that the Chancellor would further restrict relief for pension contributions. His decision was to cap the annual pension contributions that an individual can make at £40,000 – down from £50,000 – but only from April 2014, not next year.

Although the great majority of people do not use their full allowances at present, this can adversely affect those fortunate enough to be in final salary pension schemes when they are awarded a pay rise. The value of their pension fund is calculated by multiplying up their entitlement at the beginning and end of the year by 16 – so a pay rise of a few thousand pounds converts into a large capital sum which might breach the limit and trigger a tax charge. However, someone who has not used their full £50,000 in the last three years can set the spare capacity against a large contribution. This rule may become more important when the limit has been cut to £40,000. The unused limit brought forward from 2013/14 and earlier years will still be based on £50,000.

The lifetime limit on amounts saved in pension funds will be cut from £1.5m to £1.25m, also in April 2014. Those who are adversely affected will be able to keep the benefit of the higher limit by making a tax election and not putting any more money into their funds afterwards. The number of people who have funds of that size is very small, and it will become harder to reach that level with the current lower annual contribution limits. ●

Unlimited reliefs

In the March Budget, the Chancellor announced that there would be a restriction on 'unlimited' income tax reliefs such as the offset of losses against taxable income, to apply from 2013/14. The maximum would be set at the higher of £50,000 or 25% of the taxpayer's income in any year. The Autumn Statement confirms that this will be introduced, but charitable reliefs will be exempted from the change. The main restriction will therefore be on the offset of 'sideways loss relief' from a lossmaking business against other income. ●

They won't be doing…

The Autumn Statement also included comments on some of the ideas that were put out for consultation earlier in the year, but which they have decided not to proceed with. The 'IR35' law, which attacks the use of personal service companies to avoid PAYE and employee NICs, was under review – there was a proposal to collect the tax from the person paying for a worker's services, rather than from the personal service company. They have decided not to go ahead – mainly, they say, because HMRC have been policing the existing rules more vigorously and clamping down on avoidance. ●

Fair shares?

In October 2012, the Chancellor announced the introduction of a new employee share scheme, under which employees would receive shares in their employer in exchange for some of their existing legal rights as employees. The relative benefits of share ownership and employment protection are still not clear, and the tax advantages of the new arrangements are still under development. The Autumn Statement included an announcement of proposals to exempt awards of up to £2,000 of shares from income tax and NICs, and gains of up to £50,000 on these shares from CGT. ●

Mr One Per Cent

The Chancellor announced that many tax and benefit numbers will be restricted to 1% annual rate increases, which also applies to public sector pay. He emphasised the need for fairness between those who work and those who claim benefits – as several commentators pointed out, this is no longer a clear distinction, as many benefits are paid to supplement low pay.

The nil rate band below which Inheritance Tax is not charged has been frozen at £325,000 since 6 April 2009. It will remain at this level until 6 April 2015, when it will start to increase again – but at only 1% each year (to £329,000 in 2015/16).

This will also apply to the higher rate threshold for income tax, which will increase by 1% in 2014/15 to £41,865 and 1% in 2015/16 to £42,285. This will raise revenue and will bring another 400,000 people into higher rate tax.

The Capital Gains Tax annual exempt amount will also rise by 1% in those years to £11,000 and £11,100. Although it does not appear in the tables issued with the Autumn Statement, this suggests that the annual exempt amount for 2013/14 must be £10,900 (up from £10,600 in 2012/13). ●

Corporation tax drops

The Chancellor has already reduced the main rate of Corporation Tax, due from companies with profits of more than £1.5m a year, from 28% in 2010 to 24% in 2012, with a planned reduction to 22% in 2014. The rate will instead be 21% from 1 April 2014, giving the UK a much lower corporate tax rate than those which apply in many competitor countries.

The small profits rate, which is paid by companies with profits of up to £300,000 a year, will then hardly be different – it remains at 20%, unchanged since 1 April 2011. ●

Drawdown up?

Traditional pension plans required the purchase of an annuity – an income that was fixed for the rest of a person's life, or which increased by fixed amounts. An annuity is simply a contract between the pension provider and the pensioner – as long as the company doesn't go bust, it has to carry on paying in accordance with the agreement.

A more flexible alternative has been available in recent years – 'income drawdown', in which the pensioner's fund remains separately identifiable within the assets of the provider, and the income on that fund is paid out instead of a contractual annuity. The pensioner can choose to receive a smaller amount each year, allowing the fund to build up still within a tax shelter – or a larger amount, which is taxable income. To prevent people spending the whole of their savings too quickly, the law puts a maximum on the drawdown. It was set at 120% of the equivalent annuity that could be purchased with a fund of that size, regularly reviewed – but this was reduced to 100% in April 2011.

That seems sensible – anything more would appear to be likely to erode the capital value – but it took no account of how much income might be earned on the fund. If the managers were doing well, or the individual had control of the assets in a Self-Invested Pension Plan, there might be little risk in paying a higher amount. The Chancellor has listened to those campaigning for an increase in the limit, and has agreed to put it back up to 120% of the equivalent annuity. The date for this change is not given in the statement, but presumably it will be implemented by April 2013. ●

VAT backtracking

In March, the Chancellor stepped into a storm of protest when he tried to raise VAT on hot takeaways – the 'pasty tax' – as well as static caravans used for holidays, approved alterations to protected buildings, and self-storage facilities. All these measures were supposed to take effect on 1 October, raising money and helping to ease the deficit – but each of these measures was modified after consultation. Freshly cooked food that is cooling down will still be zero-rated, and caravans will be charged at 5% in April rather than 20% now. The Treasury's forecast revenues have had to be adjusted downwards by £400m over the six year review period.

Although there are many other VAT rules which might yield more money, the Chancellor has not mentioned any proposals to change them for the moment – perhaps he has realised that it is not as easy as it seemed to add 20% to the price of sausage rolls. At least there is no sign of another increase in the main rate of VAT – other European countries are having to put it up, and 20% is among the lowest standard rates in the EU. It is also easier to work out than 17.5% or 21%! ●

Simple!

Apart from the proposal to allow small businesses to use the cash basis for determining profits, the statement announced that the Office for Tax Simplification (OTS) has made recommendations for improving the rules for employee share schemes. These have grown in a haphazard way over many years, often arising from the enthusiasm of a particular Chancellor for one type of scheme or another, and could be made much more sensible. Details will follow later, but these changes are expected to take effect in 2013.

The OTS will now move on to examine the tax treatment of employee expenses, benefits and termination payments. It seems unlikely that this new organisation, created by this government, will run out of work any time soon. However, there was nothing new about an even bigger project that was mentioned in March – the possible unification of income tax and National Insurance Contributions. That is perhaps too complicated for simplification. ●

This newsletter is written for the benefit of our clients. Further advice should be obtained before any action is taken.