DICKINSONS
CHARTERED ACCOUNTANTS

NEWSLETTER
PRE BUDGET REPORT OCTOBER 2007

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Tax Deadlines

2 November
Submit forms P46 (car) for quarter to 5 October.

19 November
PAYE & NIC to reach HMRC for month to 5 November.

22 November
Electronic payments of PAYE and NIC to reach HMRC for month to 5 Nov.

19 December
PAYE & NIC to reach HMRC for month to 5 Dec.

30 December
File personal tax return for 2006/07 by Internet to have tax due of up to £2,000 included in your 2008/09 PAYE code.

2008

1 January
Corporation tax due for companies with accounts to 31 March 2007. VAT at 5% on cost of renovating homes empty for two years or more.

18 January
PAYE & NIC due for month to 5 January, and 3rd quarter 2007/08.

31 January
Submit personal tax return for 2006/07, or automatic fine of £100. Final income tax and CGT due for 2006/07 year plus first 'on account' tax payment for 2007/08.

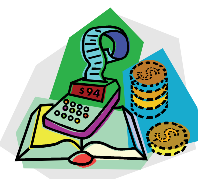
5 April
Taper relief and indexation allowance abolished for disposals after this date.

6 April
New tax rules for non-domicile UK residents. CGT at 18% applies to all capital gains made by individuals, PRs or trustees.

Stop press

If a company provides free fuel for a company car the employee's tax charge is based on a percentage of £14,400, according to the CO_2 emissions of the vehicle. From 6 April 2008 the tax will be based on £16,900, which will increase the fuel tax charge by about 17%.

Higher capital gains tax on your business



We need to calculate the tax loss or saving

The big surprise in Alistair Darling's Pre Budget Report on 9 October was the new flat 18% rate of capital gains tax, which will apply to all gains made by individuals from 6 April 2008. This replaces taper relief and indexation allowance which both work to reduce the total taxable gain.

If you are planning to sell your business, or an asset used by a business such as a commercial let property, you may save significant amounts of tax if you sell before 6 April 2008. This is because taper relief currently reduces the gain by up to 75% if the assets have been held for at least two years. This gives an effective tax rate of just 10% tax for a higher rate taxpayer, or 5% for a basic rate taxpayer. The new flat rate of 18% represents an 80% increase in the expected tax bill for a higher rate taxpayer, or a 260% increase for a basic rate taxpayer!

This increase in tax also applies where you are winding up the company after ceasing to trade. The exact calculation of the tax due on the sale or disposal will depend on how the business has been owned, or the property has been used over the last ten years, so ask us to check the potential capital gains tax bill for you.

Lower capital gains tax on other assets

The new 18% rate of capital gains tax may be good news for anyone selling non-business assets, such as residential property, but it does depend on how the property is held.

It may be better to wait until 2008

Property held in your own name can qualify for taper relief once it is owned for three years. The maximum discount under taper relief is 60% of the gain, which works out at 24% tax for higher rate taxpayers and 12% tax for basic rate taxpayers. If you are planning to sell a let property you may save tax if you wait until 6 April 2008. However, indexation allowance is also abolished from that date, which will penalise anyone who has owned a property, or any other asset for over 10 years, so the calculation is not straight forward.

If you hold your properties through your own company any gain on sale will be subject to corporation tax at 20%, to rise to 21% from April 2008, or at higher rates if it is a large company. However, indexation allowance will reduce the gain by the effect of inflation, and this continues to apply for companies. The snag is the proceeds are trapped within the company and winding up the company will mean at least tax of a further 18% in your hands, from 6 April 2008. If you wind up the company before 6 April 2008 the gain maybe reduced by taper relief giving a tax rate of only 10%.

On balance it now looks more tax efficient to hold properties in your own name rather than through a company. You may also save tax if the properties are held jointly, so the gain on disposal is spread over two annual exemptions.

Dickinsons Newsletter is written for the general interest of our clients and is not a substitute for professional advice. This edition was based on the documents released with the Pre Budget Report on 9 October 2007, more information will be available when the legislation is published. Please contact Dickinsons before taking any action.

Inheritance Tax savings for couples

Inheritance tax (IHT) worries a lot of people because the IHT threshold, known as the nil-rate band, has not been increased in line with house prices over recent years. When you die all your wealth, including the value of your house, is taxed at 40% on all amounts above the nil-rate band, which is currently set at £300,000.

If your house is jointly owned the actual wealth in your hands alone may be less than the £300,000 threshold. When you or your spouse die and leave everything to the survivor there is no IHT to pay, as wealth inherited by a UK domiciled spouse is exempt from inheritance tax. However, when the surviving spouse dies there is usually a large IHT bill as all the wealth previously owned by the couple is now in the hands of one person, with only one nil-rate band to use.

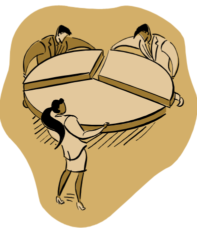
The Chancellor has tried to solve this problem by allowing any unused nil-rate band, following the death of the first spouse, to be transferred to the widow or widower who dies after 8 October 2007. That gives a total inheritance tax exemption for a married couple (or civil partners) of £600,000 (for 2007/08) rising to £700,000 for the tax year 2010/11.

IHT worries may be eased

Say Fred died on 1 October 2007 with an estate worth £500,000. His executors will be required pay IHT at 40% on £200,0000 (£500,000 – £300,000) amounting to £80,000. If Fred dies on 1 November 2007, and his wife did not use her nil rate band when she died previously, he has the benefit of two nil rate bands totalling £600,000. Now Fred's executors will pay no IHT at all on his estate of £500,000.

This inheritance tax change does not help couples who are not married, or in a registered civil partnership, so if you are in that position please talk to us about IHT planning as soon as possible.

Sharing profits in the family business



Who gets what slice of the profits?

Family businesses have been waiting anxiously for the full Government response to the triumphant win by Mr Jones in the Arctic Systems case. The Treasury are opposed to couples sharing income generated from a business to save Income Tax or National Insurance, but the rules have now been changed to allow the same couples to share their IHT nil rate bands to protect the value of their home from Inheritance Tax (see above).

The Treasury now refers to *income shifting*, defined as where one person diverts their income to a second person who is subject to tax at a lower rate, to obtain a tax advantage. The Pre Budget Report indicates that tax legislation to tackle *income shifting* will take effect from April 2008, but it will only apply to income paid in the form of company dividends or partnership profits. Thus paying your spouse a fair salary for work done will not be attacked.

The exact details of how the income shifting rules will apply are still being decided, but the factors that may be taken into account include:

- the work done by each person in the business;
- the amount of capital each person contributes to the business; and
- the business risks each person takes.

We believe it is going to be very difficult for HMRC to look inside small businesses and decide who does what work for the business, but the law may force you to keep records to prove your innocence. Let's talk about what evidence you could keep.

Non-domiciled UK residents

The main political parties are now competing to impose tax on non-domiciled or 'non-dom' UK residents. These are individuals who were either born abroad, or have a strong connection with another country, but who live in the UK. Currently they need only pay UK tax on income and gains they bring into the UK. Residents who do not have non-dom status pay UK tax on all their worldwide income and gains wherever it arises.

The choice in 2008 may not be clear

Those who choose B) will also be taxed in the UK on any overseas income or gains they bring into the UK. There is an exception for non-dom individuals who have overseas income amounting to less than £1,000 per year. They will be able to carry on claiming UK personal allowances and not pay the £30,000 charge, while at the same time ignoring any foreign income that is not brought into the UK.

From 6 April 2008 non-doms who have been tax resident in the UK for at least seven years will have a choice:

A) pay UK tax on all their worldwide income and have the use of their UK personal allowances against UK income; or

B) pay tax on their UK income without deduction of personal allowances, and pay an annual £30,000 tax charge.

From April 2008 the days that count as being present in the UK for the test of UK tax residence will include the days of arrival and departure. So if you spend a lot of time abroad we need to look at whether you will be considered to be tax resident in the UK from April 2008.