



# Budget 2006

## Overview: £200 council tax hike for pensioners, two months extra holiday for accountants

- Once again the tone of the chancellor's speech bears little relationship to the tone of the budget documentation
- The uncharitable might suggest that consolidating the £450m MRC and the NHS research spending (which in 1995 was targetted at 1.5% of its total budget) into a fund that will spend "over" £1bn on medical research might disguise a cut of £800m to fund extra expenditure on Iraq, but we won't.
- It might be suggested that this isn't the right time to be giving tax relief to encourage payments to volunteers for clinical trials of new drugs, but we won't.
- It might be suggested that trumpeting a increase of £40 in the road tax on Chelsea tractors while encouraging fuel consumption by failing to index duty immediately is less than green, but we won't.

## Income Tax

- From 2008 manually submitted tax returns will have to be with the Inland Revenue by 30 September and electronic returns by 30 November. This represents a reduction in the time allowed of four months if electronic submission is not used or two months if it is. This will enable the revenue to reduce data input staff and divert resources to other areas (tax credit call centres perhaps)
- The tax relief for investments in Venture Capital Trusts is reduced from 40% to 30% with effect from 6<sup>th</sup> April 2006.
- The majority of tax credits are increased in line with earnings rather than inflation and this will continue for the duration of the current parliament. Only the first threshold for those only entitled to child tax credit is increased (to £14,155) the other thresholds for withdrawal and the percentages remain unchanged. Quite how the resulting high effective tax rates motivate the British workforce is something of a mystery.
- Recipients of tax credits need not report increases of income of less than £25,000 and will continue to receive the credit at the previous rate. Note that this generosity is not extended to someone who is unemployed and gains work – their benefits cease instantly. No doubt there will

be some abuse of this provision which is primarily designed to reduce the public profile of the difficulties surrounding the tax credit system.

## Benefits in Kind

- Vouchers used to provide benefits that would be tax-free if provided directly (mobile phones for private use, eye tests and spectacles for VDU users) have been excluded from tax.
- The amount of child care vouchers that can be provided to employees free of tax has been increased from £50 pw to £55. It is important to remember that this is designed for employees who would not be better claiming the child care element of the child tax credit and employers should bear this in mind when designing schemes
- The ability to provide computers to employees for home use free of tax has been withdrawn from 6 April 2006, existing computers will not attract tax. The withdrawal is because the scheme was not achieving its objective of providing computers to workers rather than already highly paid employees.
- Retrospective changes have been made in respect of shares and options received as a result of employment.

### In figures - tax

	2006-07
<b>Income Tax</b>	
Personal allowance (age under 65)	£5,035
Personal allowance (age 65-74)	£7,280
Personal allowance (age 75+)	£7,420
Married couple's allowance* (aged less than 75, born before 6/4/1935)	£6,065
Married couple's allowance* (age 75 and over)	£6,135
Married couple's allowance* - minimum amount	£2,350
Income limit for age-related allowances	£20,100
Blind person's allowance	£1,660
<b>CGT exempt amount</b>	
Individuals etc	£8,800
Most trustees	£4,400
<b>Inheritance tax threshold</b>	£285,000
<b>Pensions</b>	
Lifetime allowance	£1,500,000
Contribution cap	£215,000
Tax free cash cap	£375,000
<b>VAT Thresholds</b>	
Registration	£61,000
Deregistration	£59,000

\* married allowance is at 10%

### Income tax: taxable bands

	Rate	2006-07
Starting rate:	10%	£0 - £2,150
Basic rate:	22%	£2,151 - £33,300
Higher rate:	40%	over £33,300

This has been necessary because a number of schemes have been disclosed where the rules are being exploited to convert income into capital gains by this means. So far as can be determined prior to the actual legislation where the shares or options genuinely generate a gain that is not predetermined at issue then that gain with escape being treated as employment income and subject to income tax and national insurance. The changes take effect from 2 December 2004 (sic)

## Pensions

- 6<sup>th</sup> April 2006 is A-day, the day on which huge changes in the pensions regime come into force, while these changes have been years in the making very few people believe that the rules will not continue to change.

- One further change announced on budget day relates to the treatment of alternatively secured pensions which were originally intended for followers of faiths that shun the payment of interest. Unfortunately a number of worshipers of Mammon (i.e. financial advisors) recognised these rules could be used to bypass the payment of inheritance tax. Changes remove this possibility.
- Basically the new rules allow a lifetime allowance "LTA" in respect of pension provision and pension funds over this value will attract tax at an effective rate of 55%. Each time retirement benefits in the form of a lump sum, annuity or pension drawdown is taken this uses up a percentage of the lifetime allowance (based on the then ruling rate). Annuities are assumed to have a capital cost of 20 times the annual amount for the purposes of these calculations. Thus if a lump sum of £200,000 and a pension of £20,000 were taken at a time when the LTA was £1,500,000 this would use up 40% of the LTA. Assuming the funds did not exceed the LTA on a day (in which case certain elections for primary or enhanced protection are necessary before 6 April 2009) then if all the balance of the funds were taken as annuity when the LTA was £2,000,000 then the maximum annuity which would not trigger the 55% tax rate would be £60,000.

## National Insurance

- Once again nothing has been done to align the upper limit for national insurance with the threshold for the higher rate of tax. This results in a band of £240 where the effective tax rate is 51% for employees and 48% for the self-employed. Consultation is promised on the issue.
- There are no changes in national insurance rates except for the Special Class 2 rate for volunteer development workers (up by 10p to £4.20 per week) and class three contributions.
- The threshold above which national insurance becomes payable is £97 per week for 2006/07 and the upper earnings limit for employees contributions is £645

## Business Taxation

- The starting rate of corporation tax has been abolished along with the non-corporate distribution rate. More than anything this perhaps reflects the inability of the revenue to make IR35 bite the way they intended and useful incentives to genuine businesses are swept away in consequence
- Group relief is extended to losses of subsidiaries or permanent establishments within the European Economic Area.
- Changes in relation to the sale of lessor companies and the use of tax motivated capital losses are introduced to combat disclosed tax avoidance schemes.

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## Capital Allowances

- First year allowances are increased from 40% to 50% from 1 April 2006.

## Stamp Duty

- The zero band of SDLT on residential property is extended from £120,000 to £125,000.

## Value Added Tax

- VAT on contraceptives will be reduced (subject to EU approval) to the lower rate (5%) from 1 July 2006.
- Subject to approval from the EU the grants available to reduce the effective rate of vat on the repair of listed faith buildings and memorials to 5% will continue.

## Other Taxes

- The threshold for inheritance tax increases announced last

year were reannounced, £285,000 (06/07) and £300,000 (07/08), and the threshold for 08/09 revealed to be £325,000

- For pensioners there is an effective increase of £200 in council tax over and above the increases imposed by local councils as the chancellor has not seen the need to bribe them again – perhaps connected with the fact there is no election this year.
- The lower rate of air passenger duty is extended to Croatia.
- Cigarette, wine and beer duties are increased, sparkling wines, cider and spirit duties are frozen

## Trusts

- Transfers into accumulation and maintenance trusts and interest in possession trusts during the lifetime of the settlor will now be subject to the relevant property entry (20%), periodic (6%) and exit charges, except where the trust is for a disabled person. In respect of trusts created on death the relevant property treatment is also avoided for trusts for a minor child who becomes absolutely entitled at the age of 18 or for the benefit of one life tenant in order of time who cannot be replaced.
- The standard rate band for trusts is doubled from £500 to £1,000.

### In figures – tax credits

	2006-07
<b>Working Tax credit elements</b>	
Basic	£1,665
Couple/parent	£1,640
30 Hour	£680
Disabled Worker	£2,225
Severe Disability	£945
50+ return to work (16-29 hours)	£1,140
50+ return to work (30+ hours)	£1,705
<b>Childcare element of WTC</b>	
Maximum one child (per week)	£175
Maximum two or more children (pw)	£300
Percentage of cost covered	80%
<b>Child Tax credit elements</b>	
Family	£545
Baby addition	£545
Child	£1,765
Disabled Child	£2,350
Severely disabled	£945
<b>Income thresholds and withdrawal rates</b>	
First income threshold	£5,220
Rate	37%
Second income threshold	£50,000
Rate	6.67%
First where CTC only	£14,155

*Ian J Fletcher FCA [ian@fgco.com](mailto:ian@fgco.com)*

*A David Simpson BA (Oxon) ACA [david@fgco.com](mailto:david@fgco.com)*

**11 Broad Street, Manor Row, Bradford BD1 4QT**  
**Telephone 01274 729178**

*Errors and omissions excepted.*

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