Taxing small businesses: recent developments

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In the 2007 Budget the Government announced a series of reforms to the taxation of small companies "to deal with individuals artificially incorporating as small companies to avoid paying their due share of tax." These measures included, "a phased increase in the small companies' rate from 19 per cent to 20 per cent from April 2007, 21 per cent from April 2008 and 22 per cent from April 2009 to reduce the differential between incorporated and unincorporated businesses." In addition, a new Annual Investment Allowance (AIA) would be introduced from April 2008 "available to all businesses regardless of size and regardless of their legal form" enabling businesses to offset "100 per cent of expenditure up to £50,000 on general plant and machinery (other than cars) … against taxable profits".[1] This package of measures was confirmed in the 2008 Budget, along with further changes to the capital allowance regime in response to consultation.[2]

With the severe decline in the economy over the year, the Chancellor, Alistair Darling, announced a number of measures "to help businesses save tax" in his Pre-Budget statement on 24 November 2008. One of these was to *defer* the proposed increase in the small companies rate: the rate remains 21% for 2009-10.[3] This note discusses the reforms to taxing small businesses set out in the 2007 Budget, before looking at the recent change in the Government's approach.

The difficulty of providing tax incentives for small companies without encouraging 'tax-motivated incorporation' was illustrated by the four year history of the zero rate of corporation tax, introduced in April 2002. Many commentators argued the new zero rate would provide a substantial incentive for individuals to incorporate their businesses, and so it proved. The Government's attempt to deal with the problem with a new minimum rate of corporation tax on distributed profits in April 2004 was highly controversial, and both this new rate, and the zero starting rate, were abolished in April 2006. This history is discussed in detail in a second note.[4]

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1 HC Deb 21 March 2007 c 820; HC 342 March 2007 p 51

2 HC 388 March 2008 para 3.13

3 HC Deb 24 November 2008 c498. see also, HM Revenue & Customs Budget Note BN03, 22 April 2009

4 *Taxing small businesses: Budget 2000 to Budget 2006*, SN/BT/2904, 8 May 2009

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1 Budget 2007 – business tax reform

An outline of the way corporations are taxed is provided in HM Revenue & Customs' *National Statistics*:

> Corporation tax is charged on the profits made by companies, public corporations and unincorporated associations such as industrial and provident societies, clubs and trade associations. The tax is charged on the profits made in each accounting period, i.e. the period over which the company draws up its accounts. The rates of taxation are set for the financial year April to March; where an accounting period straddles 31 March the profits are apportioned between the two financial years on a time basis.
>
> Companies have been liable to corporation tax since 1965. Before that they were liable to income tax on their total income and also to profits tax. The system introduced in 1965 charged a uniform rate on all profits and an additional charge to income tax was made when profits were distributed.
>
> In 1973 a 'partial imputation system' was introduced to mitigate the double tax charge when profits are distributed. This was achieved by the twin mechanisms of advance corporation tax (ACT) and tax credits. In July 1997, the new Government began a series of reforms of tax credits and corporation tax payments. Payments of tax credits to pension schemes and UK companies were abolished on dividends paid on or after 2 July 1997 and the remaining payments of tax credits were cut from 6 April 1999. ACT was abolished for dividends paid on or after 6 April 1999 as were Foreign Income Dividends which allowed companies to pay dividends without tax credits. A system of quarterly instalment payments of corporation tax was introduced for large companies for accounting periods ending on or after 1 July 1999.
>
> **The partial imputation system**
> Until April 1999 a company paid ACT when it paid a dividend. This tax could be set off, within a limit, against the corporation tax liability of the accounting period. The remaining tax liability was called "mainstream" corporation tax. One purpose of ACT was to finance the tax credit which the Exchequer made available to the shareholder receiving the dividend. The tax credit could be set against the shareholder's income tax liability on the dividend or, until the payment of tax credit was abolished for non-taxpayers and exempt institutions, the credit would be paid to the shareholder.
>
> A company which could not set off the whole of the ACT paid against the tax charged on its profits had "surplus ACT". This could be carried back for up to 6 years (up to 2 years before 1984) to reduce tax liability in earlier accounting periods, or it could be carried forward without time limit. In any accounting period the amount of ACT set against tax on profits was limited to the amount which, with the distribution to which it related, absorbed the whole of the profits of the accounting period. For example, a

> company with profits of 100 would have had an ACT limit of 20 (assuming an ACT rate of a quarter), because a distribution of 80 and ACT of 20 would have absorbed all the profits of 100.

The note goes on to discuss recent trends in the rates of corporation tax, and the way a lower rate of tax applies to companies with small profits:

> **Tax rates**
> The rates of corporation tax … were substantially reduced from 1983 to 1986 as part of a range of measures which included the abolition of stock relief and major changes to capital allowances. The rate of ACT changed in line with the basic rate of income tax until 1992-93. From then until its abolition the rate was linked to the lower rate of income tax of 20 per cent with a transitional rate for ACT (equivalent to 22.5 per cent) in 1993-94.
>
> Since 1973, there has been a lower rate of corporation tax for companies with small profits. The rate applies when the profits are below a lower limit of profits … Between that limit and an upper limit, a higher marginal rate is applied to produce a smooth progression in the average tax rate from the lower rate to the main rate which applies above the upper limit. The profit limits are restricted for companies associated with one or more other companies according to the number of associated companies to prevent abuse by a company fragmenting into smaller ones. In April 2000 a new starter rate of 10 per cent was introduced on profits up to £10,000 but the benefit is withdrawn for more profitable companies by a higher marginal rate on profits in the band £10,000 to £50,000.
>
> In his April 2002 Budget the Chancellor reduced the starting to zero and the small companies' rate of corporation tax to 19%. In April 2004, the Chancellor introduced a 19 per cent minimum rate of corporation tax on distributed profits, commonly referred to as the Non Corporate Distributed Rate (NCDR). In the 2005 Pre-Budget Report, the NCDR and zero per cent rates were replaced with a single banding set at the small companies' rate of 19 per cent. This rate was raised to 20 per cent from 1 April 2007 and 21 per cent from 1 April 2008, and there is an intention to raise the rate further to 22 per cent from 1 April 2009. The main rate of CT was reduced from 30 per cent to 28 per cent from 1 April 2008.[5]

In his Budget speech on 21 March 2007 the Chancellor announced a package of reforms to business taxation, to "reflect the increasing importance in investment decisions of research and development, skills, intellectual property and environmental innovations"; this included changes to "deal with individuals artificially incorporating as small companies":

> I need to act to deal with individuals artificially incorporating as small companies to avoid paying their due share of tax—a practice that, if left unaddressed, would cost the rest of the tax-paying population billions of pounds. I will take action in a way that will not raise the tax burden on the self-employed and small businesses overall. To reduce the tax difference between self-employment and small company incorporation, I will raise the small companies rate in three stages from 20p this year to 22p. I will recycle all those revenues to legitimate small businesses investing for the future. Small firms will be able to claim the new 100 per cent. relief for new capital investment up to £50,000, a 175 per cent. tax credit for R and D, and the new tax credit for environmental investment. A small company with profits of £150,000 and investing

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5 HM Revenue & Customs, *Corporate tax: introductory note*, November 2008 pp1-2. This note accompanies statistics on tax rates and yields collated at: http://www.hmrc.gov.uk/stats/corporate_tax/menu.htm

£50,000 of that will effectively pay tax of just 15 per cent. A firm investing the same from profits of £100,000 will pay tax of 11 per cent.—lower than today.[6]

The Budget report set out all of these measures as follows:

Box 3.3: Detail of the Budget announcement

The following reforms are announced in Budget 2007:

Cutting the rate of corporation tax

- a reduction in the main rate of CT from 30 per cent to 28 per cent, effective from April 2008;

A simpler two-rate system of capital allowances

- a reduction in the rate of capital allowances on the general pool of plant and machinery from 25 per cent to 20 per cent, effective April 2008, bringing it closer into line with economic depreciation;
- an increase in the rate of capital allowances on the pool of long-life assets, which applies to assets with expected lives of more than 25 years, from 6 per cent to 10 per cent, effective April 2008;
- fixtures that are integral to a building will be separately classified and will be included in the 10 per cent capital allowances pool, effective April 2008;
- the phased removal of the Industrial Buildings Allowances (IBA) and Agricultural Building Allowance (ABA) with the effective rate of allowance falling to 3 per cent from April 2008, 2 per cent from April 2009, 1 per cent from April 2010 and full abolition taking effect from April 2011. As part of this phased withdrawal, balancing adjustments will be withdrawn from today (21 March);

Re-focusing the incentives for small companies

- a phased increase in the small companies' rate from 19 per cent to 20 per cent from April 2007, 21 per cent from April 2008 and 22 per cent from April 2009 to reduce the differential between incorporated and unincorporated businesses;
- the 50 per cent first year allowance for small enterprises will continue to April 2008;
- the introduction of an Annual Investment Allowance (AIA) available to all businesses regardless of size and regardless of their legal form. This new allowance will mean that 100 per cent of expenditure up to £50,000 on general plant and machinery (other than cars) can be offset against taxable profits. The AIA will be effective from April 2008 and will target support on all businesses that are investing for growth. It will be particularly beneficial to small and medium sized businesses;

Promoting innovation

- an increase in the large company R&D tax credit from 125 per cent to 130 per cent from April 2008; and
- an increase in the enhanced deduction element of the SME and mid-sized R&D tax credit from 150 per cent to 175 per cent from April 2008 subject to state aid clearance.

The Government will consult over the coming year on the detail of draft legislation to implement the AIA, changes to the treatment of integral fixtures and payable Enhanced Capital Allowances. Further details on payable ECAs are described in Chapter A.

[6] HC Deb 21 March 2007 cc 819-20

In the report the Government also gave more details as to its concerns about tax-motivated incorporation:

> Successive Governments have tried to encourage greater investment through low rates of tax for small companies with the Small Companies' Rate (SCR).
>
> However:
>
> - it has become apparent that the SCR can be taken advantage of by people incorporating with the main aim of reducing their personal tax and national insurance liability by extracting labour income as dividends. This results in an unfair difference between the overall tax and NICs paid by the incorporated and the unincorporated, even where they are engaged in the same economic activity. This tax-motivated incorporation, if left unaddressed, would pose a growing risk to the Exchequer; and
> - the SCR is not well targeted. As companies qualify according to their taxable profits, not their size, around one third of tax paying large companies benefit from the SCR …
>
> Budget 2007 announces the introduction of an Annual Investment Allowance that will provide a major cash-flow benefit to those small businesses that invest to grow their business. The Government will be increasing the Small Companies Rate to reduce the advantage of incorporation and extraction of labour income by way of dividends, providing a fairer outcome for all. The Government will continue to monitor the level and extent to which labour income is extracted in dividends.[7]

The SCR applies to companies with profits below the lower relevant maximum amount (LRMA), which is currently £300,000. Marginal relief applies for companies with profits between LRMA and the upper relevant maximum amount (URMA), which is currently £1,500,000. From 1 April 2007 both the SCR and the fraction underpinning marginal small companies relief would be changed, though for North Sea oil companies – whose profits would be 'ring fenced' – the rates are unchanged:

> The small companies' rate, for all profits apart from ring fence profits, will become 20% from 1 April 2007 and the fraction used in smoothing the differences between the main rate of corporation tax and the small companies' rate (marginal small companies' relief) will be 1/40. Profit limits will remain the same. The small companies' rate for ring fence profits will remain at 19% from 1 April 2007 and the marginal small companies' relief fraction will be 11/400.[8]

The Budget report explained why the North Sea fiscal regime was being left unchanged:

> The Government recognises that the North Sea presents unique challenges and opportunities for both industry and government. In recognition of these challenges, this Government has introduced a unique capital allowance regime that encourages investment by providing full relief on cashflow outflow as it arises. This minimises the impact of the fiscal regime on investment decisions. In light of this, and of the need for stability and certainty, and given continuing high levels of profitability and investment, the reforms to business tax announced in Budget 2007 will not therefore apply to activity within the North Sea fiscal regime, which will retain its existing capital allowances regime and rate of tax.[9]

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[7] HC 342 March 2007 paras 3.22, 5.113-4

[8] HM Revenue & Customs Budget Note BN04, 21 March 2007

[9] HC 342 March 2007 para 3.37

In addition, first year capital allowances for small companies would be set at 50% for a further twelve months:

> Capital allowances allow the cost of capital assets to be written off against a business's taxable profits. They take the place of commercial depreciation charged in commercial accounts. The main rate of capital allowances for general spending on plant or machinery is 25% a year on the reducing balance basis. First-year allowances (FYAs) bring forward the time that tax relief is available for capital spending and allow a greater proportion of the cost of an investment to qualify for tax relief against a business's profits of the period during which the investment is made.
>
> The amounts of FYAs are set out in section 52 of the Capital Allowances Act 2001. Small and medium-sized enterprises can normally claim 40% FYAs on their investments in most plant and machinery. There are some exceptions, including spending on long-life assets, cars and assets for leasing. Finance Act 2006 increased the rate of FYAs for small businesses only, from 40% to 50% for a period of one year. This extension for a further year provides an increased cash-flow benefit for small business's investments in plant and machinery. The rate of FYAs for medium-sized enterprises remains unchanged at 40%.
>
> There are various reforms to the capital allowances system proposed for 2008-09 including the replacement of FYAs for small and medium-sized businesses by an annual investment allowance of £50,000 a year. [10]

Finally, subject to state aids clearance, the tax credit for research and development (R&D) costs incurred by both small and medium sized companies would be extended:

> The Government intends to increase the support available under R&D tax credits. The rate of relief for large companies will increase to 130% of qualifying R&D expenditure. In the case of the SME R&D tax credit scheme, the rate of relief will increase to 175% for companies claiming enhanced deductions against profits. The value of the payable credit available will remain broadly at its current value (24% of qualifying expenditure). The Government intends to legislate these changes in Finance Bill 2008. Changes to the SME scheme will be subject to state aid approval from the European Commission. Legislation will be introduced in Finance Bill 2007 to extend the support available under the SME R&D relief scheme to companies with fewer than 500 employees.
>
> Schedule 20 to the *Finance Act 2000* provides for tax relief for small and medium companies undertaking qualifying R&D activities. A 50% enhancement of qualifying expenditure can be claimed under the scheme and in some circumstances this can lead to a payable credit. A company is small or medium if it has fewer than 250 employees and an annual turnover not exceeding €50 million and/or a balance sheet total not exceeding €43 million. Schedule 12 to FA 2002 provides for tax relief for large companies undertaking qualifying R&D activities. Large companies can claim a 25% enhancement of their qualifying expenditure under this scheme …
>
> The new rules, which will be included in Finance Bill 2007, will extend the more generous support available (the 50% enhancement and the payable credit for loss making companies) under the SME scheme to companies with fewer than 500

[10] HM Revenue & Customs Budget Note BN06, 21 March 2007

> employees which have an annual turnover not exceeding €100 million and/or who have an annual balance sheet total not exceeding €86 million.[11]

Estimates in the Budget report show these changes to be broadly revenue-neutral. In 2008-09 the phased increase in the SCR would raise £370 million. By contrast, the one year-extension of FYAs at 50%, combined with the first year of the AIA and the increase in the SME R&D tax credit, were estimated to cost £310 million.[12] In 2009-10 the phased increase in the SCR combined with the withdrawal of 50% first year allowances, was estimated to raise £900 million. The new AIA was estimated to cost £920 million in the same year; the cost of the SME R&D tax credit was estimated to rise to £60 million.[13]

Further to this, the impact on the incentives for self-employed persons to incorporate was the subject of a written answer at this time:

> **Mr. Gauke:** To ask the Chancellor of the Exchequer what estimate he has made of the potential reductions in (a) corporation and (b) income tax avoidance from the increase in the rate of corporation tax announced in the Budget 2007.
>
> **John Healey:** The increase in the small companies' rate of corporation tax will reduce the tax advantage for a self-employed person to incorporate and receive labour income as dividends. This impact increases corporation tax collected but reduces income tax and national insurance collected. The measure will increase the corporation tax paid by those who have incorporated for tax reasons and will reduce the incentive for others to engage in this behaviour. The reduction in overall tax advantage depends on income level. For a self-employed person earning £30,000, the incentive to incorporate and take labour income as dividends will reduced by around £1,000 by 2009-10. As the Chancellor noted in his Budget speech, if the tax-motivated incorporation is not tackled, it could cost the rest of the tax-paying population billions of pounds.[14]

As noted, the Government anticipated that much of this reform package would be implemented in 2008 and 2009; the *Finance Act 2007* simply made provision to set the SCR for 2007 at 20%, to extend FYAs for small enterprises, and extend SME R&D relief to companies with fewer than 500 employees (sections 3, 37 and 50 respectively). In revenue terms, the first two of these were relatively minor changes for the current financial year: the first raised £10 million, the second cost £35 million, in 2007-08.[15]

The increase in the SCR came up when the Chancellor gave evidence to the Treasury Committee on 29 March; Peter Viggers MP asked "why are you reducing the corporation tax for larger companies, but increasing the corporation tax for small companies?" As part of his answer Mr Brown said:

> There are 4.4 million businesses in total in Britain, 3.2 million of which are not incorporated businesses, in other words, they do not come under these measures, so the vast majority of businesses are paying income tax and national insurance like any other individual and they are completely unaffected by the proposals that we are putting forward, in fact they benefit from the lower rate of income tax that we have announced in the Budget and 3.2 million companies are, therefore, better off because

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[11] HM Revenue & Customs Budget Note BN05, 21 March 2007

[12] £250m, £30m and £30m respectively.

[13] The increase in the SCR alone was estimated to raise £820m in 2009-10.

[14] HC Deb 2 May 2007 c1741W

[15] All estimates given in *Budget 2007* (HC 342 March 2007 p 208).

> of the income tax changes; and only 1.3 million of all our businesses are incorporated as companies and a large number of them, perhaps over 400,000 of them, pay no tax, they do not pay any tax whatsoever, so again they are unaffected by these proposals. There is a group of people, as part of the rest, who are incorporating purely for tax purposes and, if they are not investing in the future, then they will of course, by purely using the mechanism of setting up a company for avoiding national insurance in particular, but, until now, using it to get a lower rate of basic taxation, be affected, and we will start to eliminate what is a tax-avoidance mechanism.
>
> For all other companies that are investing in the future, they will be better off by using the investment allowances that are available to them. For the first time, we have created a £50,000 investment allowance which is available to these companies and they can claim that at 100% and, therefore, most companies which are investing in the future will not only be as well off, but better off under the proposals we made. There is no gain to the Exchequer in terms of revenues and in the figures that we have shown and published in the Red Book there is no gain to the Exchequer from these measures. All the money that we have had to take from making this change in the small business tax rate purely to deal with tax avoidance is recycled back into the business community as a result of what we have done either for small businesses or for the self-employed.[16]

In April 2008 the Institute of Chartered Accountants hosted a workshop on small business taxation, and one of the questions participants discussed was whether small businesses should be subject to a lower rate of tax in the first place:

> A key issue is whether the UK should tax businesses the same regardless of their size. Should we have a common starting point and then provide reliefs and variations to accommodate different factors? Or should we have a different regime for the large and the small enterprise?
>
> The consensus was that there was a natural dividing line between owner managed businesses and larger concerns. There was also much discussion about what was a 'small' business and the distinction between the very small or 'micro' business of, say, less than ten employees and other enterprises that certainly were not large but perhaps needed slightly less support than the very smallest of businesses. The majority thought that the smallest enterprise needed most support and encouragement, but with an understanding that not all businesses want to grow. There was strong support for a distinct small business tax regime.[17]

2 Reactions to the proposals for small companies

The small business community reacted negatively to the Government's proposals. The *Financial Times* reported the initial reactions of both the Federation of Small Businesses, and the British Chambers of Commerce:

> Small business groups yesterday hit out at the Budget, complaining that tax cuts for larger companies were being achieved at their expense … Carol Undy, chairman of the Federation of Small Businesses, said the chancellor "gives with one hand and takes with the other. She welcomed the chancellor's decision to reduce the business rate

[16] Treasury Committee, *The 2007 Budget* 23 April 2007 HC 389-II 2006-07 Q 248 Ev 36

[17] "Is there a better way?", *Taxation*, 22 May 2008

relief on empty commercial property, a measure proposed by the FSB. But she said that small businesses that use a van would be hit by the increase in road tax on larger engine vehicles and that other green measures may prove counter productive. "Small businesses employ 58 per cent of the private sector workforce - over 12m people - and the increase in their tax rate fails to acknowledge their contribution."

Karan Bilimoria, founder of Cobra Beer, said the tax increase could damage the chancellor's attempts to foster an entrepreneurial economy. "I understand the reasons behind the increase, but on the whole it sends the wrong signals." … The biggest concern about the tax increase is that it would hamper the growth of small businesses, according to David Frost, director general of the British Chambers of Commerce. "We have had a lot of start-ups, but we haven't got enough businesses in this country growing," he said. "What we don't want to do is to put processes in place which will further dissuade companies from growing. That would be a worry." … Andrew Hubbard, director of tax at Tenon, the accountancy firm, said smaller companies will probably look again at whether it is appropriate for them to continue to operate in corporate form. "The problem is that while it is relatively easy for a company to incorporate tax efficiently, there is currently no mechanism under which companies can disincorporate tax free."[18]

Helen Simpson at the Institute for Fiscal Studies observed that the measures "almost take us full circle":

The Chancellor announced a cut in the main rate of corporation tax from 30% to 28% in 2008–09. At the same time he announced a reduction in the generosity of capital allowances for investment. Taken together these imply a cut in the tax rate but a broadening of the tax base (the lower rate being applied to a larger fraction of profits). Companies investing heavily in buildings and in plant and machinery seem the least likely to benefit. The most profitable companies (where the value of tax allowances is small relative to income) are those most likely to gain, and the rate cut may make the UK a more attractive location for such firms.

The Chancellor also announced a gradual increase in the small companies' rate of corporation tax from 19% to 22%. This almost takes us full circle – in his first budget the Chancellor cut the rate from 23% to 21%; further cuts followed, plus the introduction and subsequent abolition of the 10% and 0% starting rates of corporation tax. The current increase is aimed at reducing incentives to incorporate (and take income in the form of dividends rather than wages) created by the tax system. These incentives were previously greatly enhanced by the ill-fated 0% starting rate. He also introduced a new Annual Investment Allowance (AIA) which allows all firms an immediate deduction of up to £50,000 for investment in plant and machinery. For some small companies this should lessen the effect on their tax bills of the increase in the small companies' rate. While the reforms for large firms lower the tax rate and broaden the tax base, for companies paying at the small companies' rate, the reforms increase the tax rate, but for those benefiting from the AIA, narrow the tax base.[19]

One practitioner writing in the *Tax Journal* argued that the phased increase in the SCR "will be a big burden for smaller companies, as they will find that their cost base increases considerably above the rate of inflation with what is effectively an increase of more than 15% in the corporation tax they will have to pay, assuming that they maintain steady profits over

[18] "Sweeteners fail to damp disappointment", *Financial Times*, 22 March 2007

[19] IFS press notice, *Analysis of Budget 2007*, 21 March 2007

the next three years."[20] A second writing in *Taxation* took issue with the Government's case for increasing the SCR: "[it] appears to target 'one man band' type companies [but] … this looks like a pretty feeble excuse, bearing in mind that this tax increase will affect a wide range of companies (with annual profits below £1.5 million), including many substantial businesses. Furthermore, most businesses operate through companies for many solid commercial reasons with tax often being of little relevance."[21] Writing on the *AccountingWeb* site, Simon Sweetman also commented on the Government's rationale for the change:

> The sufferers here will really be companies making between £50k and £300k in profits. This may include a large number of the growing businesses that the Chancellor wishes to encourage, which seems strange. In practice, though, a business of that size will probably be spending enough on plant to qualify for the £50,000 Annual Investment Allowance and will actually pay less tax rather than more. The Treasury's argument is that this has been done to reduce still further the tax incentive for small businesses to incorporate, though I would argue that the great days for that have gone already and that people are on the whole thinking more seriously before making the decision as to the legal form to adopt. It probably removes any tax incentive for incorporation, especially since the Treasury is clearly going to keep an eye on developments and will be prepared to turn the screw a bit further. We must remember, too, that the majority of small businesses are in fact unincorporated, and will not suffer from a change to the CT rates. The cut in the basic rate of income tax is a big headline for them, but the real differences will be very small because of the abolition of the lower 10% rate, and the changes to the NI thresholds at the same time, while a welcome simplification, will probably mop up any savings for most people. Families in the basic rate tax bracket are probably in tax credits, too. A 2% cut in the basic rate ought to be big news, but I don't think that it really is.
>
> But this is not all the story. The "small companies rate" is actually a "small profits rate" and many large companies are apparently able to take advantage of it. Most small companies in fact pay very little CT, since they are either investing or withdrawing the money. The Annual Investment Allowance will be significant for small businesses, both incorporated and unincorporated, when it comes in from April 2008. It should allow what is in effect free depreciation for small businesses on plant and machinery, and has the added benefit of being a simplification.[22]

In a follow-up article, the writer argued that "at a time when HMRC have been working very hard to restore some kind of relationship with small business, this announcement is a disaster in public relations terms."[23]

Writing in *Taxation* some days after the Budget, Andrew Tenon, tax director at Tenon, was more cautious about the financial impact, but went on to make a much wider argument about tax-motivated incorporation, which is worth quoting at some length:

> We spent several hours on Budget day running numbers through spreadsheets trying to make sense of the various hints that we could pick up in the small print about what precisely the figures would be. It is a sign of just how complex this all is that, between us, with at least 100 years of combined tax experience, we could not agree on what the impact of the changes will actually be. The real lesson from this Budget is that the three-dimensional matrix between corporation tax, income tax and National Insurance

[20] "Budget 2007 – SMEs", *Tax Journal*, 2 April 2007
[21] "No tonic – owner manager businesses", *Taxation*, 22 March 2007
[22] Simon Sweetman, "Budget 2007: the Budget and small business", *AccountingWeb.co.uk*, 22 March 2007
[23] "Trying to understand small business policy", *AccountingWeb.co.uk*, 2 April 2007

makes it extremely difficult for the Government to make changes which have a consistent policy impact. It is like Rubik's cube: you twist and turn the cube until you have got one face all the same colour, only to find that the opposite face now resembles something Jackson Pollock would be proud of! … Now I am not one to be defeatist, but it does seem to me that in trying to solve the incorporation problem simply by adjusting rates, the Government is creating its own version of the cube problem. As one part of the Treasury works hard to make the 'stopping tax motivated-incorporation' side of the cube a consistent colour, other parts of the Treasury are making moves on their side of the cube which will shatter the pattern again!

So where does this leave us? To be fair to the Treasury, I think that the rate changes this year have probably reduced some of the differential between being self employed and operating through a personal company and taking dividends, but there is not a consistent pattern. In all of the calculations that I have seen to date, the corporate route still shows up as advantageous. It may be that some people will think a bit harder before they incorporate their business, which is to be welcomed because too many people incorporate without thinking through the wider consequences, but I think it unlikely that these measures will see the end of incorporation. Nothing I have seen so far suggests that people would now be best advised to move out of corporate structures. Besides, even if they wanted to, the lack of any disincorporation relief would be a big hurdle. Some businesses might be able to disincorporate without a tax cost, but many would not want to run the risk of HMRC arguing that there was a deemed transfer of goodwill out of the company back into the sole trader business. So if the Treasury really wants to encourage people to disincorporate, it should send out strong signals that it will consider introducing a disincorporation relief, so that people know that they will be able to unwind their corporate structure free of tax.

But there is a wider point … The decision to incorporate does not operate in a vacuum. There is no doubt that many people have incorporated to save tax, but there are a whole host of other factors here. Many businesses will simply not take on individual workers on an employed basis because of the employment law obligations which are imposed on them (to say nothing of the additional National Insurance burden) and will not run the risk of taking them on a self-employed basis in case there is a subsequent PAYE dispute. Therefore in many industries the only way of getting work is to operate through a limited company. If you operate through a limited company and pay yourself a salary, you are in a worse position than if you are an employee of the end user, because you have to fund the employer's National Insurance yourself. In theory the end user could pay a higher fee to your company because he is relieved of the obligation to pay employer's National Insurance, but how often does this happen in practice? So the dividend route becomes the only real option.

So we do not really have one Rubik cube here – we have several … It would, I think, be wrong to believe that no solution exists. Rather, we need to throw away the cube altogether and start playing a different game, say a jigsaw. There are lots of pieces in a jigsaw and it can take some time to put it together but there is a finite answer: you do not get into a position half way through where somebody says 'you thought that you were doing a jigsaw of the Rokeby Venus: we've now turned it into Michelangelo's David' (use your imagination!). In other words we have to ring fence the problem and work to find a coherent regime for the taxation of small businesses which is not going to be wrecked overnight by changes elsewhere in the tax system. Once we have found it, we should leave it alone. Making small adjustments to rates and allowances here and there may help in the short term, but in the end it can only be sticking plaster. If we

are serious about small business tax, and many of us are, then long-term structural reform is the only option.[24]

In their press notice in the Budget, the Institute for Chartered Accountants suggested that it was hard to assess the impact of all these changes on small business:

> There is to be a new annual investment allowance of £50,000 each year to be introduced from 2008-09 … with the scope of the allowance to be subject to consultation. As the details of the allowance have still to be spelled out, it is not clear how much of this allowance will go to small businesses. The sum of these measures suggests that the Government has begun to lose patience with the small business end of the market place and is clearly concerned that the small company rate of tax continues to be subject to manipulation and that generally small businesses are incorporating to save tax. This is probably a reasonable analysis, but the measures will also hit real small businesses that are seeking to grow.[25]

In their commentary on the Budget, the accountants Ernst & Young noted that "it is unclear exactly how this new annual investment allowance will work … It is likely that this new relief will provide less relief than the current FYA for small or medium-sized companies investing heavily in plan and machinery, since there is no current monetary limit on FYA, the definition of small and medium-sized companies being by reference to size etc, rather than the amount being spent on plant and machinery."[26] Other commentators argued that the AIA would do little to benefit the smaller business:

> Small professional services businesses and sole traders emerged as some of the biggest losers from this week's Budget [as] … they get little benefit from the chancellor's sweeteners, such as the expansion of the R&D tax credit scheme and capital allowances relief, which will help high-growth businesses that reinvest profits. "It is all geared to the Department of Trade and Industry's obsession with high-growth companies," Stephen Alambritis of the Federation of Small Businesses said. He said that only 7 per cent of the UK's 4m small businesses fitted this category.
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> The new annual investment allowance for £50,000 of plant and machinery was little use for a small consultancy that needs only a laptop and a phone to operate, according to Stephen Herring, senior tax partner at BDO Stoy Hayward: "There is a bit of a lack of joined-up government here." Reinvesting profits was a luxury most small businesses could not afford, according to Kevin Nicholson, head of entrepreneurs and private companies at PwC. "Most of them need to take the money out to have something to live on," he said. The chancellor's assertion that the effective small business tax rate had fallen to 15 per cent, given all the additional relief schemes assumed that company owners had the time and technical knowledge to apply for them, according to Mr Nicholson: "Hardly any small businesses change their behaviour because of these kinds of incentives and reliefs. It would have been better to simplify the system."[27]

3 Finance Bill 2007

[24] "Twists and turns", *Taxation*, 5/12 April 2007
[25] ICAEW press notice, *Budget 2007 – winners and losers*, 22 March 2007
[26] "Budget 2007 – he giveth and he taketh away", *Tax Journal*, 26 March 2007
[27] "Sole traders among worst off with tax blow of 22%", *Financial Times*, 23 March 2007

As mentioned above, although the Government proposed to increase the SCR from 19% up to 22% from April 2009, the *Finance Act 2007* made provision for just the first of these increases, setting the rate at 20% from April 2007.

In their report on the Budget published on 23 April the Treasury Committee suggested that it was not clear changes to R&D tax credits, and the new investment allowance, "would have the desired beneficial impact on investment levels by small companies." The Committee quoted evidence from John Whiting at PriceWaterhouseCoopers, and Dr Martin Weale, at the National Institute for Economic & Social Research:

> Mr Whiting pointed out that "even if a smaller business does invest for a couple of years, at some stage … proprietors need to take some money out to live on". Furthermore, he told us that a PricewaterhouseCoopers survey carried out in 2006 had shown that the R&D tax credit was often given to companies who were already undertaking the R&D, and in many cases the R&D tax credit was not always claimed because it was too difficult to establish that the company qualified.[28] He argued that the changes to the taxation system in the 2007 Budget were unlikely to be behaviour-changing and that businesses tended to prefer a lower tax rate and simpler taxation system to incentives to invest. Dr Weale also stated that he was "in favour of tax simplicity rather than having lots of tax allowances" because "a major disadvantage of a complicated system is that people devote resources trying to exploit the boundaries and to put themselves on the favourable side of the boundary".[29]

In written evidence to the Committee Mr Whiting discussed the impact of these changes in more detail:

> It is understood that the reforms to smaller business taxation are driven by the objectives of increasing investment by this sector and reducing the incentive for tax-motivated incorporations. The impact will be uneven and governed by the type of business as much as the decision whether or not to invest: the service sector is essentially faced with a straight increase in their tax bills—or are they supposed to buy all employees a company car? It would be interesting to understand why the Treasury feel that the new investment allowance will work better than previous high capital allowances aimed at encouraging plant investment. Proprietors do need to take money out of their business to live on; they cannot invest all the time. Although an interesting idea, there should be a commitment to review its effectiveness after a period, with the option of reverting to lower tax rates. It is notable that the increase in the small companies' rate of corporation tax starts immediately (unlike the investment allowance).[30]

The Committee went on to recommend that, "prior to the 2009 Budget, the Treasury review the impact of these measures on business investment in order to ensure that the measures are having a positive impact on investment and business growth, including the impact on small businesses that do not qualify for R&D tax credit or the Annual Investment Allowance."[31] In response the Government acknowledged "the importance of evaluating the impact of both the increase in the R&D tax credit and the introduction of the Annual Investment Allowance", but that "evaluation restrictions apply to the Annual Investment Allowance (and indeed any tax measure)":

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[28] [see, "Companies unaware of enterprise tax breaks", *Financial Times*, 24 July 2006.]
[29] Treasury Committee, *The 2007 Budget* 23 April 2007 HC 389-I 2006-07 para 57
[30] HC 389-II 2006-07 Ev 56
[31] HC 389-I 2006-07 para 57

> The lags in data mean that, by April 2009, less than one year of tax data will be held by HMRC following the introduction of the Annual Investment Allowance. HM Treasury is unlikely, therefore, to achieve any quantitative analysis of the impact of the introduction of the Annual Investment Allowance by the Committee's recommended target of Budget 2009.[32]

The *Finance Bill 2007* received its second reading on 23 April 2007, and the reforms to small business taxation were discussed more than any other measure by Members. Speaking for the Conservatives, Theresa Villiers, argued the proposals "will not help small business", partly because they would lead to a "more complicated tax system", and partly because "reinvesting profits is a luxury that many small businesses cannot afford at the moment."[33] James Brokenshire raised the issue of businesses which had incorporated, but might now consider disincorporation: "Many small companies that have legitimately incorporated, for whatever reason, will be in the difficult situation of having to decide whether to accept higher taxes or higher professional costs to change from an incorporated to an unincorporated structure—possibly their former status."[34] In his evidence to the Treasury Committee John Whiting had suggested, "given the number of changes to this area of the tax code in recent years, surely it is time for a coherent look at the whole incorporated/unincorporated divide and how the tax system impacts on it, including perhaps reliefs for disincorporation."[35] The theme was also discussed by David Gauke at a later stage of the debate:

> In most cases, it is still better to be incorporated because there is just corporation tax, whereas with employment there are income tax and national insurance contributions. However, if the intention is to be tax neutral, will the Government do anything to encourage those companies that have moved into the incorporated sector to move out again? If so, many small businesses will be concerned that a decision to disincorporate will be treated as a deemed transfer of goodwill, and they will want disincorporation relief to secure their financial position … it is not entirely clear what the Government want to do.[36]

In his speech, Mr Brokenshire also referred to the comments made by Andrew Tenon, tax director at Tenon, quoted at length in the previous section of this note, on the difficulties of calculating the financial impact of these reforms: "If even learned tax advisers find it difficult to assess the effect on smaller companies of the changes in the Bill, it will be tricky, to say the least, for the companies themselves to work out what the impact will be and how to take advantage of the investment regime to ensure that the benefits are effectively applied."[37]

On a wider point David Gauke acknowledged that tax-motivation incorporation was a 'difficult problem', but argued that the Government's approach was "incoherent":

> In an attempt to solve the perceived problem with incorporation, the Government have increased the rate of corporation tax, but they have also raised the application of national insurance contributions, as announced in the Budget, while also increasing the threshold for higher rate income tax, which means that it would be possible to receive a higher amount of dividends without paying any tax. The two approaches do not entirely

[32] *Fifth special report*, 25 June 2007 HC 696 2006-07 p10
[33] HC Deb 23 April 2007 c 664
[34] HC Deb 23 April 2007 c 707
[35] HC 389-II 2006-07 Ev 56
[36] HC Deb 23 April 2007 c 738
[37] HC Deb 23 April 2007 c 708

fit together … On the one hand, one part of the Treasury is attempting to address the difference between the two structures, while on the other it is raising the higher rate threshold, which I support, and encouraging more sole traders to incorporate. The problem remains much the same … If the Government are not prepared to reduce the tax burden on small businesses as a whole, which is what will happen if they do not address the issue of incorporation, a more fundamental and careful review of our taxation system will be necessary.[38]

In response to the debate the then Financial Secretary John Healey argued that the AIA would be attractive to small businesses as a simplification measure; he went on to set out the Government's rationale for these reforms as follows:

The UK has 4.3 million small businesses. Of those, more than three quarters are self-employed. They do not pay corporation tax and are not affected by the changes in the Budget. Of those that remain, around a quarter do not pay any corporation tax because they do not declare profits. Of those that remain, we estimate that the majority have incorporated with the purpose of reducing their tax and national insurance liabilities.

In all the changes that we have made to small business tax rates and policy, we have done so with a view to having a tax system that ensures that we get greater levels of investment and innovation and a fairness in the system. That was the purpose also of our consultation in 2004. However, the lower rates of tax have resulted in a significant number of people incorporating to take advantage of them, not to invest in business, but simply to extract the company profits in a way that reduces their personal tax and national insurance liabilities. They are doing that while still carrying out the same economic activity that they carried out before they incorporated. The tax break is clearly being subsidised by those companies that are following the rules and by ordinary taxpayers.

We are therefore refocusing the provision of investment incentives on small businesses. The increase in the small companies rate will reduce the differential in tax paid between the incorporated and the self-employed. The annual investment allowance will target assistance directly on those firms, incorporated and unincorporated, that invested their profits. The Budget is good for business, with the lowest corporation tax rate in the major economies, a small companies rate that will still be lower than the rate when we came to office in 1997, tax incentives focused on businesses that invest and innovate, and a fair deal for the self-employed.[39]

The business tax reform package was one of the issues considered by the House of Lords Economic Affairs Finance Bill Sub-Committee, which published its report on the Finance Bill in June 2007. The Committee suggested that the Government might consider a wider review of how small businesses are taxed:

We share the common view that small businesses need certainty and stability as much as large ones. There was general agreement that they too ought to be able to take commercial decisions—for example whether or not to incorporate—without regard to the tax implications. Too many decisions have been taken with tax in mind and this must be seen as a weakness in the tax system. In this context the frequent changes in the small companies rate of corporation tax have been unhelpful. However the change in the rate being made this year and the further changes which have been foreshadowed will, in conjunction with the proposed simplification of personal taxation,

[38] HC Deb 23 April 2007 cc 738-9
[39] HC Deb 23 April 2007 c758- 759

> be helpful by reducing the difference between the tax burden on incorporated and unincorporated businesses.
>
> This should however be only the start of the process. One approach towards reducing complexity and the distortions which tax considerations may bring to business decisions would be to stand back and review the issue as a whole in conjunction with the sector. It would certainly not be possible to remove all the complications, but the outcome might well be greater clarity and consistency.[40]

In July 2007 the Government consulted on the new regime for capital allowance, including the precise scope of the AIA."[41] Notably in their report on the Finance Bill, the Lords Economic Affairs Committee noted that witnesses did have concerns about the Government's proposed reforms to capital allowances, but the AIA "was not a matter to which our attention was very much drawn."[42] The Treasury published a note in December including draft legislation and a discussion of the responses they had received to these proposals;[43] on the AIA "all respondents [had] welcomed the proposal and agreed on the intentions of the incentive and identified in particular the benefit of the AIA to smaller businesses."[44] *Budget 2008* confirmed that the new allowance would be introduced with effect from April 2008 – though it does not appear to have generated very much comment.[45]

4 Recent developments

In January 2008 the IFS published their Green Budget, which discussed, among other issues, the incentives provided by the tax system for incorporation. The authors noted that it might require more action on the Government's part – such as abolition of the small companies' rate – to stem "the continued tide of incorporations":

> The [increase in the small companies rate from 19% to 22%, and the cut in the basic rate of income tax to 20%] will have the effect of increasing the effective tax rate paid on dividends (or capital gains) and, for many working-age individuals, decreasing the effective tax rate paid on salaries, thereby reducing the incentive to re-label income through incorporation … Compared with the impact of the starting rate on the incentive to incorporate, the combined effect of these changes is very small. Nevertheless, they are certainly a step in the right direction. But there is a danger that the government's doomed experiment with the 0% starting rate has highlighted the tax advantages available through incorporation to such an extent that the number of individuals switching legal form will remain higher than it was in 1996–97, despite the fact that the tax incentive is no longer significantly larger than it was at that time.
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> With this in mind, it may not be enough simply to return to the 1996–97 position to stem the additional flow of tax-motivated incorporation that occurred in the intervening period: it may be necessary for the government to go further towards alignment of the effective rates across the corporate and personal sectors. This would be considerably aided by further increases in – and perhaps the eventual removal of – the small

40 Lords Select Committee on Economic Affairs*, Fourth report: the Finance Bill*, 20 June 2007 HL 121 2006-07 paras 46-48
41 HM Treasury press notice 87/07, 26 July 2007
42 HL 121 2006-07 para 53
43 HC Deb 17 December 2007 c71WS
44 *Business tax reform: capital allowance changes - technical note*, December 2007 pp8-9.
45 HM Revenue & Customs Budget Note BN12, 12 March 2008

> companies' rate of corporation tax, which may be no bad thing (albeit unpopular with small-business lobby groups) as its economic rationale is unclear.[46]

Nevertheless, the 2008 Budget did not see any major changes in the Government's approach: the reforms to business taxation announced the previous year were confirmed, along with further changes to the capital allowance regime in response to consultation.[47] On the question of the small companies rate, it was also confirmed that the rate would rise to 21% from 1 April 2008 – apart from ring fence profits – and that profit limits would remain unchanged.[48] One important related development was the Government's announcement that it would consult further on proposals to prevent 'income shifting' – the use of the corporate form, usually by couples, to mitigate their joint tax liability. The proposals were controversial for, just as with the debate over incorporation, many in the accountancy profession took the view that the tax authorities were seeking to brand ordinary commercial decisions by small businesses as artificial tax avoidance.

By the time of the 2008 Pre-Budget Report, the prospects for the UK economy had changed dramatically. In his statement on 24 November, the Chancellor, Alistair Darling, announced a number of measures to support small businesses, including the decision to *defer* the proposed increase in the small companies rate. (Notably the Government also decided to shelve its plans for legislation to tackle income shifting.[49]) In his speech, Mr Darling announced new arrangements for late payment of tax by businesses:

> At this time of real difficulties for many small businesses, they need time to pay when meeting their tax bills, and I intend to meet that need. From today, Her Majesty's Revenue and Customs will enable firms facing difficulties to spread their tax on a timetable that they can afford. This will cover not just VAT, as some have suggested, but all business taxes—VAT, corporation tax, income tax and national insurance; and not for six months, but for as long as they need.

He went on to announce another two measures to "help businesses save tax":

> First, I have decided to defer the increase in the small companies rate of corporation tax that firms pay on their profits. That will provide a boost to small companies, leaving their tax rate in 2009 unchanged. Secondly, I want to support viable small companies that are finding it harder to make a profit at the moment. We already have a system of tax repayments, which are available to help those businesses, previously profitable, but now making losses. Currently, companies are able to offset losses only against profits made in the last year, but it is important to offer more support to businesses at the moment. So I am today extending this repayment scheme so that losses of up to £50,000 can be offset against profits made for the last three years. An estimated 75,000 businesses will benefit from this change, by receiving tax repayments. And of these, 90 per cent. will have their full current losses wiped out.[50]

In the Pre-Budget Report, the Government noted that although the small companies rate would be frozen at 21% for 2009-10, it remained "committed to the aims of the business tax package announced in Budget 2007, to refocus incentives towards investment and growth, and to reduce the differential between incorporated and unincorporated businesses."[51] The

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46 *The IFS Green Budget*, January 2008 pp244-5

47 HC 388 March 2008 p44, 54

48 HM Revenue & Customs Budget Note BN03, 12 March 2008

49 For more details see, *Income shifting*, Library standard note SN/BT/4620, 2 February 2009

50 HC Deb 24 November 2008 c497-8

51 Cm 7484 November 2008 para 4.14

cost of this decision was estimated to be £460m in 2010-11, although it is an indication of the slump in corporate profits since then, that *Budget 2009* revised this estimate to £310m.[52] The change was mentioned by a couple of witnesses to the Treasury Committee in their report on the PBR; for example, John Whiting at PriceWaterhouseCoopers, when asked about the Chancellor's proposals to help small businesses, said:

> Let us be clear: the measures that were taken were welcome and particularly the possibility of negotiating with the Revenue when you can pay. That is arguably one of the most valuable measures. The deferment of a 1% increase in corporation tax is good news because that was feared. The virtual abandonment of income shifting, which was a big problem hanging over an awful lot of businesses, is good. The loss relief sounded good but it was a bit of a souffle´ because when you pricked it it collapsed. It is only a one-year thing; it is only for £50,000. Yes, it is helpful but it would have been so much better had they just looked at mechanisms whereby the business could agree its loss much quicker, get the loss carryback established much more quickly and either just negate a tax payment or generate a tax repayment much more quickly. It is a seven out of 10 package, I think.[53]

The general response from the small business sector appears to have been quite positive,[54] particularly to the new 'time to pay' arrangements.[55] At the time of the 2009 Budget the Government reported that the new service had, "helped over 100,000 businesses, who collectively employ over 600,000 people, spread tax payments worth almost £2 billion."[56] One change the department has made to the scheme is to take into account the fact that many businesses who had made profits in 2008 now expect to make a loss in 2009:

> Many businesses have told us that while they made a profit last year (and are due to pay CT or IT on that profit) the indications are that they will be making a loss in the current year. Normally if a business makes a loss they can ask for a repayment to be made to them of any CT or IT which they have paid on last year's profit. To do this though they need to wait until the end of their accounting year to be sure about the size of the loss they have made. Businesses have told us that if they could show they are likely to make a loss in the current year they would like us not to collect the tax due on last year's profits until they knew how big the loss is going to be. While we cannot agree not to collect the tax due on last year's profits, what we will now do is to take into account the fact that a business is likely to make a loss for the year when deciding how much time we can give a business to pay any IT or CT due on its profits from last year.[57]

More details on the Government's general approach to dealing with the economic crisis are given in another Library note.[58]

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52 Cm 7484 November 2008 p194; HC 407 April 2009 p154

53 *Second report: Pre-Budget Report 2008* 28 January 2009 HC 27 2008-09 Q95 Ev18

54 For example, "Warm welcome for capital reforms", *Financial Times*, 25 November 2008; "Early Xmas present", *Taxation*, 4 December 2008

55 "Season of goodwill reaches the tax office – for now", *Financial Times*, 3/4 January 2009.; "Cash-strapped thrown Revenue lifeline", *Financial Times*, 19 January 2009. Details of the service are provided on HMRC's site at: http://www.hmrc.gov.uk/pbr2008/business-payment.htm

56 HC 407 April 2009 p73

57 HM Revenue & Customs, *Business Payment Support Service: Further extending our support to businesses - HMRC Internet Guidance*, 22 April 2009 p2

58 *The economic crisis: policy responses and economic indicators*, SN/BT/4968, 28 April 2009

Although the small business sector welcomed the decision to defer the increase in the small companies rate, in their 2009 Green Budget, published in January 2009, the Institute for Fiscal Studies was critical, suggesting that it added "yet more certainty to the future of the small companies' tax rate … it is not clear that this will be an effective way to stimulate economic activity in 2009-10":

> Businesses make investment decisions based on the expected tax rates for the duration of an asset's productive life and not just based on the current corporate tax rate. A one-year deferral of the small companies' rate increase might therefore be expected to have little effect on investment. It is also not clear that the temporary deferral will help credit-constrained firms in the near future, since it will be some time before they feel the financial benefit. Small companies do not pay their corporation tax until nine months after the end of the financial year, so the tax savings for financial year 2009-10 will not be realised until the end of 2010. Indeed, the Treasury's own estimates suggest that of the cumulative £610m cost of this deferral over the three yeas from April 2009, only £20m will be given away in 2009-10.[59]

The authors went on to ask the much wider question why the Government had thought that a tax incentive for incorporation would effectively encourage entrepreneurship:

> The literature on entrepreneurship and the effect of taxes provides mixed evidence over whether lower taxes on corporations encourage entrepreneurship. At best, the positive effects found are very small … Stability and a lack of uncertainty are important features of a good tax system. Rather than regularly tweaking the tax system, it would be better for government to make a judgement about the small companies' rate and then stick to it. At the end of the day, we see no good economic rationale to have a different tax rate on small profits and large ones. One option, therefore, would be to align the small companies' rate with the main rate of corporation tax.[60]

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[59] *Green Budget 2009*, January 2009 p234. In *Budget 2009* these figures are now calculated to be: total cost of £410m over 2009-12, of which £10m given in 2009-10 (HC 407 April 2009 p154).

[60] *Green Budget 2009*, January 2009 p233-4