UK Budget 2007: Analysis

Budget 2007 economic forecasts – a positive outlook

GDP growth to remain robust, 3.25 per cent forecast for 2007 and then 3 per cent for 2008 & 2009.

Manufacturing growth expected to improve to above recent par rates, with up to 2 per cent forecast for 2007 and then up to 2.25 percent for 2008 & 2009. In recent years such optimistic growth forecasts have not been realised.

Targeted (CPI) inflation rate expected to be back to target at 2 per cent from 2007 to 2009, after a brief period in 2006/07 in the 2.5 to 3.0 per cent range.

Budget 2007 fiscal context – a neutral budget after PBR 2006 saw taxes rise
Fiscal rules continue to be met over years to 2012.

Asset sales, cost and efficiency savings will have a big role in sustaining current and capital spending from 2007 to 2012. Current receipts also expected to growth robustly at 5.7 per cent per annum over these five years.

Current spending grows at 4.9 per cent per annum and gross capital spending at 6.8 per cent per annum from 2007 to 2012.

Spending priorities continue to be Health and Education and Skills, taking a combined 46.1 per cent or £158.4bn of total spending planned for 2007/08. Total public spending on transport is expected to be £13.3bn for 2007/8 with another £1.1bn expected under private sector initiatives. More details on spending plans beyond 2007 are due in the summer and autumn Comprehensive Spending Review and Department allocations.

Despite the many changes to business, personal, environmental, transport and all other aspects of the tax and benefits system, overall impact of the many Budget 2007 changes is broadly neutral with a fiscal stimulus of £525mn being counter balanced by a revenue yield of £405 mn for 2008 & 2009. PBR 2006 resulted in a revenue yield of £2.5bn as a result of significant new revenue from anti-avoidance measures and increases to Air Passenger Duties.

Significant changes to business and personal taxation – but not in overall revenue
The range of reforms to business taxation included a cut in the corporation tax rate to 28 per cent from April 2008; changes to capital allowances, with a general plant and machinery pool and 20 per cent rate and also to the R&D tax credit regime and increased rates; increases in the small companies' tax rate from 19 to 22 per cent to 2009 and Annual Investment Allowances (AIA) to replace first year allowances as a different spur to investment.

For personal taxpayers there are several changes to the rates and structure of the income tax, NIC and savings regime. A key aspect is a cut in the basic rate to 20p

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from 22p at April 2008, removing the 10p entry rate and alignment of the higher rate thresholds for NICs. The revenue impacts of the actions largely offset each other.

Table 1: Motoring tax receipts £s bn

financial years	Fuel & VED Duties £bn	All current receipts £bn	Fuel & VED % share of all receipts
1997/98	23.9	315.7	7.6%
1998/99	26.3	335.9	7.8%
1999/2000	27.3	358.7	7.6%
2000/01	26.9	383	7.0%
2001/02	26.1	389.9	6.7%
2002/03	26.7	396.2	6.7%
2003/04	27.6	418.9	6.6%
2004/05	28.0	451.3	6.2%
2005/06	28.4	485.7	6.0%
2006/07	28.7	517.2	5.7%
2007/08	30.7	553.0	5.6%

Source: Budgets and PBRs:

Transport issues

Further reduction of carbon emissions from cars

Average new car emissions are today around 167 grams of carbon dioxide per kilometre. A medium term objective for the Government is 100 grams. The UK focus is to lead in developing the next generation of low and no carbon vehicles and fuels. The Transport Secretary and Chancellor have therefore invited Sir Nicholas Stern and the Vice Chancellor of Aston University, Professor Julia King, to report on the energy saving potential of innovation in this area.

Vehicle Excise Duty (VED)

Government has announced VED rates for this year and the next two years to sharpen the already-established environmental signals to motorists and to encourage the purchase of more fuel-efficient vehicles and continue to support the development of low-carbon market. The announcement is valid for three years, giving a level of certainty to the consumer.

The following changes were made:

- The rate for the most polluting cars (band G) has been increased to £300 in 2007-08 and £400 in 2008-09.
- The rate for low-carbon band B cars has been reduced to £35 in 2007-08, with that rate then frozen for the subsequent two years
- Rates in graduated bands C-E, cars registered before 2001 and all

light goods vehicles will increase by £5 in each of the next three years;

- Rates for graduated band F will increase by £10 in 2007-08, then £5 in each of the subsequent two years;

- In 2007-08 only, freezing the rates for motorbikes in the lower band with higher bands increasing by £1-£2; and freezing VED rates for Heavy Goods Vehicles (HGV), Special Types Vehicles, Combined Transport Vehicles and all vehicle categories that are linked to the basic goods rate;
- VED rates for petrol and diesel cars will be aligned as the differential in nitrogen oxides and particulate matter emissions for new cars is expected to fall to close to zero once Euro V and VI emission standards become mandatory.
- Changes to this year's VED rates take effect from 22 March 2007. All changes in subsequent years take effect from licenses commencing 1 April in the respective year.

New VED Bands – 22 March 2007

VED Band	CO_2	Change (2006-2007)	Petrol	Diesel	Alternative fuels
A	100g and under	0	£0	£0	£0
B	101-120	-£5 for petrol and -£15 for diesel and alternative fuels	£35	£35	£15
C	121 to 150	+£15 for petrol and +£5 for diesel and alternative fuels	£115	£115	£95
D	151 to 165	+£15 for petrol and +£5 for diesel and alternative fuels	£140	£140	£120
E	166 to 185	+£15 for petrol and +£5 for diesel and alternative fuels	£165	£165	£145
F	186-225	+£15 for petrol +£10 for diesel and alternative fuels	£205	£205	£190

G *	226+	+£90 for petrol and +£85 for diesel and alternative fuels	£300	£300	£285

*for cars registered after 22 March 2007

Summary: This was quite a significant increase, but gives certainty to the consumer. Government expect VED changes will bring in revenue of £125mn in 2007-8, £220mn in 2008-9 and £280mn in 2009-10. It is therefore likely that 95% of the new car market will see an increase in VED.

Fuel Duty Rates
In keeping with sustaining Government policy on fuel, fuel duty rises at 2p a litre, for 2008 at 2p, and for 2009 1.8p. The increase applies to all fuels. This year's annual fuel duty will be increased in October.

Company Car Tax/ECOS
CCT is frozen and ECOS is under further review because of the freeze on CCT.

Alternative fuels, biofuels and RTFO

Alternative Fuels Framework
The Government will explore areas where support for alternative fuels in aviation may be appropriate.

Biofuels
Transport fuel suppliers will be required to report on the carbon saving and sustainability of the biofuels they supply. The 20ppl biofuels duty incentive has been extended until 2009-10, offering further certainty to the industry. In addition, the Government has extended the 20ppl fuel duty differential to the use of biomass in conventional fuel production to encourage the development of this technology.

The Government has laid legislation to reduce the duty rate for biofuels mixed with rebated gas oil in approved pilot projects. It expects two such projects in the railway sector to begin shortly and will monitor the results closely. To further encourage the off-road use of biofuels, the Government intends to permanently reduce the current duty rate for biofuel/rebated gas oil mixtures with the new rate to be determined in the light of the outcome of the pilots and other factors.

Biodiesel: At Budget 2006 the Government announced that it would review the definition of biodiesel in the Hydrocarbon Oil Duties Act 1979 to ensure that environmentally friendly fuels continue to receive recognition through the duty system. The review concluded that the definition should be kept under active review as new fuels and approaches emerge. HM Revenue and Customs (HMRC) also issued at the 2006 Pre-Budget Report further guidance on testing biodiesel against the current definition. Following consultation, HMRC will relax requirements for small biofuels producers to register and submit returns and reduce the requirement for all but the largest producers from monthly to quarterly returns.

Biogas: The duty incentive for biogas of 40ppl at least at its current level until 2011-12, providing certainty to the industry. Future decisions on the biogas duty incentive will take account of the incentives offered for biogas through the Renewable Transport Fuel Obligation, alongside other issues.

Bioethanol: High-blend bioethanol E85 is awarded a 2 per cent company car tax discount from April 2008.

Road fuel gases, such as compressed natural gas (CNG) and liquefied petroleum gas (LPG), can deliver carbon and air quality benefits over conventional road fuels. In line with the Alternative Fuels Framework and previous practice, the Government today announces that it will maintain the CNG differential with main road fuels in 2009-10, and will decrease the LPG differential by a further 1ppl. Changes will be made to both rates before then in line with announcements at previous Budgets and Pre-Budget Reports.

Sulphur-free fuels offer local air quality benefits, while helping new engine technologies work more efficiently. Following consultation by the Department for Transport (DfT), regulations will be brought forward to ensure the widespread availability of sulphur-free diesel and sulphur-free 'super' grades of petrol. The regulations will enter into force in late 2007. In advance of that, HMRC will bring forward deregulatory changes to the definition of ultra-low sulphur diesel in the Hydrocarbon Oil Duties Act 1979, to assist the industry in delivering sulphur-free fuels at lower cost.

RTFO

Budget 2006 announced that the level of obligation would be set at 2.5 per cent in 2008-09 and 3.75 per cent in 2009- 10, before reaching 5 per cent in 2010-11. This will deliver net savings of around 1 MtC per year by 2010. The Government intends the level of the Obligation to rise above 5 per cent after 2010-11, provided that three critical factors are met: robust sustainability and carbon standards; a new fuel quality standard at EU level to ensure existing and new vehicles can run on biofuel blends higher than 5 per cent; and the costs being acceptable to the consumer and the wider economy.

RTFO Buy-Out

There has been little change on this area since last year's Budget. The RTFO buy-out price (the price paid by fuel suppliers who fail to meet their obligation for the first year of the RTFO) will be set at 15ppl in 2009-10. As set out in Budget 2006, the combination of duty incentive and buy-out price is guaranteed at 35 ppl in 2008-09 and 2009-10 but will reduce to 30 ppl in 2010-11. In line with the Alternative Fuels Framework, the Government will announce the level of the duty differential for 2010-11 in Budget 2008 but expects that the emphasis will move from the duty incentive towards the buy-out price as the principal support mechanism in future years. The Government's intention is that the level of the RTFO buy-out price should be sufficiently high to ensure that obliged suppliers do not routinely resort to using it, and so will keep the level of the buy-out price under review.

Emissions, climate change levy and EU ETS

Transport accounts for a quarter of emissions: the UK government's objective for Britain is the lowest carbon cars using the least polluting fuels.

Euro IV
The Euro IV emissions standards for small vans became mandatory from 1 January 2007, and therefore, newly registered vans are no longer eligible for the reduced rate of VED. However, the discount will remain for the lifetime of vans meeting the Euro IV requirements registered before 1 January 2007.

Reduced Pollution Certificates
A renewed scheme of Reduced Pollution Certificates for lorries and buses that meet the Euro V standards before they become mandatory in 2009 will come into force from October 2007. The nature of the scheme will be similar to the one that existed prior to October 2006 for Euro IV vehicles. This is good news and something that we have asked for. It has the potential to cut about £500 off the VED for a 44-tonne truck and smaller amounts of the VED bills for lighter trucks.

EU ETS
The UK government re-confirms its commitment to EU ETS. It believes that the tougher stance by the EC on phase II national allocation plans (NAPs) will ensure greater scarcity and thus make the scheme more credible. The UK's NAP they note was not toughened up by the EC and will deliver savings of 8MtC per annum below business as usual.

The 2007 Budget makes no new announcements on EU ETS, other than the UK will host an international conference later this year on the developing global carbon market, focusing on how to link schemes in different countries and enhance trading with developing nations.

The government re-iterates desire to add aviation to the scheme, to improve the liquidity of the market and ensure aviation plays its part in delivering real carbon reductions across Europe.

Surface transport in the context of EU ETS is not mentioned

CCL and CCA
Government says CCL has been a success. Independent analysis by Cambridge Econometrics estimates the levy will deliver cumulative savings of 16.5MtC to 2005 and by 2010 be saving 3.5MtC pa, well above initial estimates. The CCAs were forecast to deliver 2.5MtC pa, but by 2010 expect savings of 2.8MtC pa will be realised. Regular reviews of existing CCAs by Defra will energy efficiency and

emissions reductions are maximised (we are due to have a review later this year). The total package of CCL, CCA and Carbon Trust (funded by the CCL) is estimated to deliver annual emissions savings of over 7.5MtC by 2010.

From 1st April 2007 the CCL rates will increase for the first time since their introduction in 2001, as shown in the table below. From April 2008 a further rise, in line with inflation, was announced ***(although no actual figures given 2008 figure below is for illustrative purposes only)***.

	01/04/01	01/04/07	*01/04/08*
Electricity per kwh	0.43p	0.441p	*0.452p*
Gas per kwh	0.15p	0.154p	*0.158p*
LPG per kg	0.985p	0.985p	*1.011p*
Solid fuel per kg	1.201p	1.201p	*1.232p*

The government also announced a package of measures to simplify the operation of CCL. This includes simplifying how relief is applied to energy-intensive businesses that sign CCAs. More details on this package will be forthcoming.

Energy Performance Commitment: Was not included in this year's Budget.

Enhanced Capital Allowances (ECAs)
A review of the effectiveness of the ECS for energy-saving technology will be published later this year.

A payable ECA for companies not in taxable profit will be introduced, to ensure both profit and loss making firms have an incentive for energy-saving technology.

Carbon Trust: CT funding will be increased

Regional Development Agencies
The 9 English RDAs will pilot a streamlined business resource efficiency advice service, through Business Links in 2007-08 to support small and medium sized businesses. This will include on-site audits or resource efficiency.

Land fill tax
From 1 April 2008 the standard rate of the landfill tax will rise by £8/tonne pa until at least 2010-11. The lower rate will increase from £2/t to £2.50/t from 1 April 2008.

Carbon capture and storage (CCS)
CCS could reduce CO2 from fossil fuel power stations by up to 90 per cent. In an effort to make the UK a world leader in new technology the government is to launch a competition to develop the UK's first full-scale CCS demonstration. The results will be announced in 2008.

Other key environmental measures

- The Climate Change Bill aims to reduce CO2 in the UK by 60% by 2050 and 26%-30% by 2020.
- Energy Technical Institute: opening in 2008 and funded by industry (from the automotive side, Rolls Royce is involved).
- A competition to develop the UK's first full scale carbon capture and storage demonstration is to be announced next year.
- A cross-government taskforce on climate change: consultation to take place later this year.
- Climate Change Agreements: businesses that sign up to CCAs can benefit from an 80% reduction in CCL.
- Energy saving technology: payable enhanced capital allowance for companies not in taxable profit to ensure both profit and loss-making businesses have an incentive to use/invest in energy saving technology.
- Homes: Energy Production Certificates to be provided at the point of sale (giving a home an energy efficiency rating).
- Zero carbon homes with a value of under £500,000 will be exempt from stamp duty and those above £500,000 will qualify for a £15,000 reduction in stamp duty.
- By 2011, standard light bulbs will be phased out (making the UK the EU leader).
- Central government offices to be carbon neutral by 2012.
- Grants for pensioners of £300 to £4,000 installing insulation and central heating in their homes.
- £18 million microgeneration grants for householders.
- Representations to European Ministers for a European-wide decision to would reduce the rate of VAT from 17.5 per cent to 5 per cent on energy saving and environmentally friendly products in the home.
- The landfill tax will, from April next year to 2011; rise by 8 pounds each year.
- To reduce the environmental impact of quarrying, the aggregates levy - which has been frozen since its introduction - will rise in April 2008 from £1.60 to £1.95 per tonne.
- Proposal to establish an EU-US taskforce to facilitate the exchange of skills, knowledge and research and development on biofuels, including the development of 'second-generation' biofuels.

Better regulation, administrative burdens, and business support

Alongside Budget 2007, the Gibbons Review of employment dispute resolutions is published – aiming to promote the early resolution of disputes and reduce the number of tribunal claims.

The DfT will consult on reform of the MOT regime in late Spring 2007 (a Davidson Review recommendation – which examined the implementation of EU regulation in the UK). With regard to the consultation expected later this Spring, SMMT will present its concerns on the potential safety and market implications of reform of the MOT system.

On business support – a consultation will be published before July, seeking views on the proposals for the design of the new portfolio of government business support.

Better regulation remains on the Government's agenda – and the tax policy reforms outlined in Budget 2007 are, overall, deregulatory for business. SMMT supports the ongoing better regulation agenda (both UK and EU), however concerns remain regarding the efficiency and effectiveness of UK efforts on administrative burdens.

R&D and innovation

Government is committed that private and public sector R&D investment reach 2.5% of GDP. From April 2008: R&D tax credit increase to 130% from 125% for large companies; SME R&D tax credit increase to 175% from 150% (subject to state aids clearance).Legislation will be introduced in Finance Act 2007 to extend the SME R&D tax credit scheme to companies with between 250 and 500 employees (mentioned in Budget 2006).

In the next few months UKTI are working (with other government departments) on attracting high-tech R&D investment to the UK. There will be increased support for the Technology Strategy Board (TSB) and Board will allocate £100 million for Collaborative R&D. In addition to the current innovation platforms (which includes Intelligent Transport Systems), three new platforms will be developed by the TSB, one of which is environmentally friendly vehicles.

These announcements are positive for the UK automotive sector, and encourage continued investment in R&D, however concern remains for tax credit opportunities for larger businesses with low-profits, where for example, offsetting tax credits against NICs would be a more appropriate incentive for R&D investment.

Skills (incl. Leitch)

Skills and education are key issues threaded through the Budget (as part of a continued commitment to increasing the UK's position in an increasingly competitive global market). Following recommendations in the Leitch review of skills, a Commission for employment and skills will be established by the end of 2007. SMMT supports much of the Leitch report, and has (for a long-time) recognised the need for investment in the UK skills base. The automotive industry has concern over the impact of manufacturing skills shortages and the importance of a highly skilled workforce on the competitiveness of UK industry; whilst balancing the cost and time pressures of investing in staff training.

The Budget announces increased investment in education and skills in England by 2.5 per cent a year in real terms (5.3 per cent in nominal terms) on average between 2008-09 and 2010-11.

UKTI will be assisting firms with migration advice when high-skilled employees are not available locally in the UK.

On 22 March a Green Paper will propose raising compulsory participation in education from 16 to 18. Further proposals in the paper will include, further support of businesses using Train to Gain to identify training opportunities, accredited training paid for by Government, and for those employers who do not want to arrange training for staff to release employees from work to undertake training.

Transport Policy (incl. Eddington, Barker, Lyons)

In Spring 2007 the Government will publish a White Paper of proposals in response to Rod Eddington's infrastructure planning recommendations (and Kate Barker's land use planning recommendations). Government also agrees with the Lyons report's (into Local Government) recommendations that if national road pricing policy were to be rolled out in the future, central government would need to bring any existing (local) schemes into the wider context of national road pricing policy. There is no further insight into road pricing in this Budget, we still await the much needed clear remit and plan.

Haulage

The Government will triple the amount that is currently spent on the targeting non-compliant haulage vehicles, which affect the safety of road users and the competitiveness of the UK haulage industry (focused in South East). Conclusions on foreign driver databases will be announced in the Pre-Budget Report 2007.

Vehicle licensing fees

Following the series of consultations on the DVLA's vehicle licensing fees Budget 2007 does not include any further information (or mention at all) timings, costs and potential future changes – the focus is on VED.