A Guide to the emergency Budget 2010

Reducing the Budget deficit, rebalancing the British economy and designing a new model for economic growth

"The Chancellor of the Exchequer, George Osborne MP, delivered on 22 June what he described as a 'tough but fair' emergency Budget. In his speech, the Chancellor set out his five-year plan to reduce the Budget deficit, rebalance the British economy and design a new model for economic growth."

A 'tough but fair' emergency Budget

Rebalancing the British economy

The Chancellor of the Exchequer, George Osborne MP, delivered on 22 June what he described as a 'tough but fair' emergency Budget. In his speech, the Chancellor set out his five-year plan to reduce the Budget deficit, rebalance the British economy and design a new model for economic growth.

There will be a two-year pay freeze for public sector workers earning more than £21,000, although the 1.7 million lowest paid will get a flat £250 pay rise each year. Limits will be put on the salaries of the highest paid public sector workers.

Around 880,000 workers will no longer pay income tax after the Chancellor raised the personal allowance by £1,000 to £7,475 from £6,475. Basic-rate taxpayers will be £170 a year better off as a result. Those earning more than £40,000 will not benefit because they will be subject to the rise in National Insurance contributions, a Labour policy that Mr Osborne has decided to retain.

For investors, basic-rate taxpayers will continue to pay capital gains tax (CGT) at 18 per cent and the annual exemption of £10,100 remains. Higher-rate taxpayers will now pay 28 per cent.

Child tax credits will be withdrawn for families earning more than £40,000 a year, rather than £50,000, while child benefit will be frozen for the next three years.

For business, there were reductions in corporate tax rates and proposals to consult on corporation tax reform. However, the banking sector will have to bear the cost of a new bank levy.

To read the Chancellor of the Exchequer's emergency Budget speech in full, turn to page 20.

A full content listing appears on page 5.

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A platform for longer term recovery

Concrete measures to tackle debt

The Chancellor of the Exchequer, George Osborne MP, delivered his first Budget speech on 22 June and announced a £40bn austerity package which forms part of his five-year plan to reduce the Budget deficit, rebalance the British economy and design a new model for economic growth. The Chancellor said the Budget's twin aims were to deal with the deficit and provide a platform for longer term recovery.

Mr Osborne told MPs that unless the government took concrete measures to tackle debt, the consequences would be "higher interest rates, more business failures, sharper rises in unemployment and a potentially catastrophic loss of confidence and the end of the recovery".

He acknowledged that growth would initially be slower as a result of the Budget, but would pick up towards the end of the parliament and signalled that the government's "formal mandate" was to bring the structural current deficit into balance in the final year of the five-year forecast period, which is 2015/16.

A fixed target for debt will also be created, which in this parliament is to ensure debt falls as a share of GDP by 2015/16. But the Chancellor announced that the new Office for Budget Responsibility has suggested that the government's "cautious approach" meant it could achieve its aim a year earlier.

The Chancellor said he would protect the poorest from the impact of a coming New Year rise in VAT to 20 per cent, a two-year freeze on public sector pay, a three-year freeze on child benefit, and cuts of more than 25 per cent in spending by some Whitehall departments.

Mr Osborne said a £1,000 increase in the income tax personal allowance to £7,475 a year, restoring the link between the state pension and earnings, and a £2bn increase in child tax credits would help those on the lowest incomes and ensure that the well-off were hardest hit by the toughest package of measures since the early 1980s.

"This emergency Budget deals decisively with our country's record debt," Osborne said, as he revealed plans to raise an additional £32bn from spending cuts – including an £11bn reduction in the welfare bill and £8bn in tax increases.

"It pays for the past. And it plans for the future. It supports a strong, enterprise-led recovery. It rewards work. And it protects the vulnerable in our society. Yes it is tough – but it is also fair."

The Chancellor admitted that the impact of this emergency Budget would lead to lower growth and higher unemployment in the short term, but said "the need to avoid a Greek-style sovereign debt crisis left him with no alternative". The UK economy, Mr Osborne said would grow by 1.2 per cent this year and 2.3 per cent in 2011.

Full details of departmental spending cuts will be announced in the October spending review, but the Chancellor said welfare reforms would include less generous housing benefit and stricter rules for disability benefits.

Banks and building societies will have to pay a new £2bn levy following their pivotal role in causing the financial crisis that led to the longest and deepest recession in Britain since the Second World War. But the levy was smaller than the City had feared and there was also some relief that the Chancellor raised capital gains tax (CGT) from 18 per cent to 28 per cent on high earners rather than to the 40 per cent or 50 per cent that had been expected.

The VAT rise, due to come into force next January, will generate more than £13bn a year by the end of this parliament. Zero-rated items including food and children's clothes will remain exempt from VAT over the course of this parliament.

Although health and international aid would be ringfenced, the Chancellor said that reductions to other government departments totalling £17bn by 2014/15 equated to 25 per cent cuts over the next four years.

The Chancellor announced that from next year he will increase benefits, with the exception of pension and pension credits, in line with the lower CPI index of inflation, instead of the RPI index. This will save more than £6bn by the end of the parliament, he said. Pensioners will get a new "triple lock guarantee" of an annual increase in line with earnings, prices, or a 2.5 per cent increase, whichever is the greatest.

The Chancellor said the measures aimed to protect children and pensioners and ensure that the richest bore the largest share of the burden. "Sadly, with this unavoidable Budget we've had to increase taxes. We have to pay the bills of past irresponsibility and relearn the virtue of financial prudence. But in doing so we've ensured that the burden is fairly shared".

"Today we have paid the debts of a failed past and laid the foundations for a more prosperous future. The richest paying the most and the vulnerable protected: that is our approach".

The Chancellor's plans to raise personal allowances for basic-rate taxpayers by £1,000 to £7,475 from next April, will take 880,000 of the lowest paid out of income tax altogether and save 23 million lower-rate taxpayers up to £170 a year. He said the coalition aspired to increase this to £10,000 in the long term.

He said to cheers that the state pension would be linked to earnings, not inflation, from next April.

And, Mr Osborne announced the child element in the tax credit system would rise by £150 above inflation at a cost of £2bn. He said this would mean that there would be no increase in child poverty and tax credits would be targeted at "those who need the help most", meaning that payments to families earning more than £40,000 would be reduced from next year.

> "Mr Osborne told MPs that unless the government took concrete measures to tackle debt, the consequences would be "higher interest rates, more business failures, sharper rises in unemployment and a potentially catastrophic loss of confidence and the end of the recovery"

Those claiming the Disability Living Allowance (DLA) will face a new medical assessment from 2013. The Chancellor said the cost of the DLA had quadrupled in real terms to more than £11bn since its introduction 18 years ago, making it one of the largest items of government spending.

Mr Osborne also made a commitment that 1.7 million public servants who earn less than £21,000 would receive a pay rise of £250 in each of the next two years.

He confirmed that the operational allowance for soldiers serving in Afghanistan would double to £4,800.

The 10 per cent CGT rate for entrepreneurs which previously applied to the first £2m of qualifying gains has been extended to the first £5m.

Mr Osborne said that while everyone was being expected to contribute, the government would make sure that everyone would share in the rewards "when we succeed".

He added that the banking sector would be expected to make a greater contribution, with a banking levy introduced from next January. Once in place, the Chancellor has forecast this will generate more than £2bn a year. Smaller banks with liabilities below a certain level will be exempt from the levy.

The Chancellor announced the government was also exploring the costs of a financial activities tax on profits and remuneration, with international partners. He's offered a "deal" to local authorities, saying "if you can keep your cost increases low, then we will help you to freeze council tax for one year". He said this would save the average family £35 a year.

Citing the "dire need for reform" of housing benefit, the Chancellor outlined a package of measures that he said would reduce the bill by £1.8bn a year by the end of the parliament. They include a cap of £280 a week for a one-bedroom property and £400 a week for four or more bedrooms.

Mr Osborne said there would be no new increases in duties on alcohol, tobacco or fuel after the "substantial increases" announced in Labour's March budget. The additional 10 per cent levy on cider proposed in Alistair Darling's final budget in March is being scrapped.

The Chancellor told MPs: "It is a balanced package that will send the signal that Britain is open for business".

The key highlights

Emergency Budget 2010 at a glance

Take a look at our guide and see how your finances may have been affected by the emergency Budget.

EMERGENCY BUDGET 2010 HIGHLIGHTS

ECONOMY

- Growth is forecast to be 1.2 per cent this year, taking into account the emergency Budget measures. It is forecast to be 2.3 per cent next year, 2.8 per cent in 2012, 2.9 per cent in 2013 and 2.7 per cent in both 2014 and 2015.
- Debt will be falling and structural current deficit should be balanced by 2014.
- Consumer price inflation is expected to reach 2.7 per cent by the end of the year, returning to target in the medium term.
- Unemployment rate forecast to peak at 8.1 per cent this year and then fall for each of the next four years to reach 6.1 per cent in 2015.
- 77 per cent of total consolidation to be achieved through spending reductions and 23 per cent through tax increases.
- Public sector net borrowing will be £149bn this year, £116bn next year, £89bn in 2102/13, £60bn in 2013/14, £37bn in 2014/15, falling to £20bn in 2015/16.
- Public sector net debt as share of GDP will be 62 per cent this year and will peak at 70 per cent in 2013/14. It will then begin to fall, reaching 67 per cent in 2015/16.
- Additional current expenditure reductions of £30bn a year by 2014/15.
- No further reductions in capital spending totals.

PUBLIC SECTOR

- Two-year public sector pay freeze on staff earning more than £21,000.
- People earning less than £21,000 will each receive a flat pay rise worth £250 in each of the two years.
- Operational allowance for troops in Afghanistan doubled to £4,800.
- Will Hutton to draw up plans for fairer pay across the public sector, without increasing the overall pay bill, so that those at the top of organisations are paid no more than 20 times the salaries of those at the bottom.
- An independent commission chaired by John Hutton will review public sector pensions. There will also be consultation on scrapping the default retirement age.
- Rise in the state pension age to 66 will be accelerated.
- Government will seek private capital injection into the Royal Mail Group.

WELFARE

- Benefits, tax credits and public service pensions will increase in line with consumer prices rather than the Retail Price Index.
- Child benefit to be frozen for the next three years.
- Caps on housing benefit to be introduced from £280 a week for a one-bedroom property to £400 a week for a four-bedroom or larger. Together with other measures, this will reduce costs of housing benefit by £1.8bn a year by the end of the parliament.
- Sure Start Maternity Grant will go to the first child only.
- Eligibility for child tax credits to be reduced for families with a household income of more than £40,000 from April next year.
- The baby element of child tax credit will be abolished from April next year.
- Child element of the child tax credit to increase by £150 above indexation next year.

TAXES

- VAT to increase to 20 per cent on 4 January next year.
- Government to work with local authorities to freeze council tax for one year from April next year.
- Capital gains tax, increased for higher earners from 18 per cent to 28 per cent from midnight on 23 June. Low- and middle-income savers will continue to pay 18 per cent.
- Personal income tax allowance to be raised by £1,000 from April to £7,475.
- Higher-rate income tax threshold frozen until 2013.
- The standard rate of insurance premium tax to rise from 5 per cent to 6 per cent and the higher-rate to increase from 17.5 per cent to 20 per cent.
- 50p-a-month levy on phone lines to pay for the rollout of superfast broadband scrapped.

BANKING AND SAVINGS

- Bank levy to be introduced in January next year, to apply to the balance sheets of UK banks and building societies and to the UK operations of banks from abroad.

PENSIONS

- From April next year the basic state pension will be re-linked with earnings.
- Basic state pension will increase every year by highest of earnings, inflation or 2.5 per cent.

DOWNING STREET SW1
CITY OF WESTMINSTER

Capital gains tax

'One of the most chaotic areas of tax'

During his first emergency Budget speech, the Chancellor of the Exchequer, George Osborne MP, announced that higher-rate taxpayers would see the rate of capital gains tax (CGT) increase to 28 per cent from the previous 18 per cent, while the annual exemption of £10,100 would remain in place. He also said basic-rate taxpayers will continue to pay CGT at a rate of 18 per cent.

The rate of CGT will be held at 18 per cent if your combined taxable gains and income are below the upper limit of the basic rate of income tax, currently £37,400.

The Chancellor said the CGT regime was 'one of the most chaotic areas of tax' inherited from the Labour government and that he endeavoured to 'balance the competing demands of fairness, simplicity and competitiveness' in the reforms. He said the existing system had encouraged people to avoid paying tax by exploiting 'the wider gap between the rate of CGT and the top rates of income tax'.

He also announced that the 10 per cent CGT rate for entrepreneurs, which previously applied to the first £2m of qualifying gains made over a lifetime, would be extended to the first £5m of lifetime gains.

The Chancellor said that by leaving the rate at 18 per cent for low- and middle-income earners, he was excluding half the payers of CGT from the tax increase. The annual exempt amount for CGT remains at £10,100 this year and will continue to rise with inflation in future years. He said the government had considered introducing tapers or indexation allowances instead of the flat rates, but had concluded that the complexity and administration involved would have been 'self-defeating'.

Emergency Budget - taxation and allowances

What do the numbers mean to you?

The following information is based on proposals set out by the Chancellor in his emergency Budget of 22 June 2010 but is subject to amendment in the Finance Bill. Items marked "TBA" are to be announced at a later date.

Income Tax

Rates	%	2010/11
Basic	20	Up to £37,400
Higher	40	£37,401 to £150,000
Additional	50	Above £150,000

Non-savings income is taxed as the first slice of income, followed by savings income and then dividends.

Dividends falling into the basic rate band are taxed at 10%. The higher rate of tax for dividends is 42.5%. This is reduced by the dividend tax credit.

Savings income falling into the first £2,440 of taxable income will be taxed at 10%.

Reliefs

	2010/11
Payment on loss of office	£30,000
Enterprise Investment Scheme*	£500,000
Venture Capital Trust**	£200,000

* Relief restricted to 20% ** Relief available up to 30%

Allowances

	2010/11	2011/12
Personal allowance:		
Aged up to 64*	£6,475	£7,475
Aged 65 to 74*	£9,490	TBA
Aged 75 or over*	£9,640	TBA
Income limit for higher levels of personal allowance	£22,900	TBA

*Progressively withdrawn from 2010/11 for income over £100,000

Non-UK domiciled individuals

A £30,000 levy applies to certain non-UK domiciled individuals wishing to use the remittance basis of taxation.

National Insurance Contributions

Rates	2010/11	2011/12
Class 1 (earnings related)		
Lower earnings limit (LEL) (per week)	£97	TBA
Upper earnings limit (UEL) (per week – employees only)	£844	TBA
Upper accruals point (UAP)	£770	TBA
Earnings threshold (per week) for employees and employers *	£110	TBA
Employee rate:		
– between earnings threshold and UEL	11%	12%
– earnings above UEL Employer rate	1%	2%
– above earnings threshold	12.8%	13.8%
Class 2 (self-employed flat rate)		
Per week	£2.40	TBA
Small earnings exception (per year)	£5,075	TBA
Class 3 (voluntary): per week	£12.05	TBA
Class 4 (self-employed)		
Lower profits limit LPL (per year)	£5,715	TBA
Upper profits limit UPL (per year)	£43,875	TBA
Rate:		
– between LPL and UPL	8%	9%
– above UPL	1%	2%

* Increased by £21 per week above inflation from 6 April 2011. Exemption for new businesses in certain areas to be introduced.

Reliefs - Contracted out Class 1

	2010/11	2011/12
Employee (Between LEL and UAP)		
– Salary related / money purchase scheme	1.6%	TBA
Employer (Between LEL and UAP)		
– Salary related scheme	3.7%	TBA
– Money purchase scheme	1.4%	TBA

Individual Savings Accounts (ISA)

Rates	2010/11
Annual investment limit	£10,200
Maximum cash investment	£5,100

Income and gains on ISA investments are tax-free.

Inheritance Tax

Rates	2010/11	2011/12
Nil	Up to £325,000	Up to £325,000
40%	Above £325,000	Above £325,000

Any unused nil-rate band may be transferred to the deceased's spouse or civil partner. On death, any gifts made within the previous seven years will become taxable, but the tax payable will be reduced by tapering relief if the donor has survived at least three years.

Where tax is payable on a lifetime gift (other than those taxable only because they are made within seven years of death), tax is charged at 20%.

Various reliefs and exemptions are available.

Car and Car Fuel Benefits

Cars

The taxable benefit in respect of a petrol car provided by an employer is calculated by reference to the car's carbon dioxide emission rating, with the scale charge normally varying between 10% and 35% of the list price. There is a supplementary charge of 3% for diesel cars but not so as to take the total percentage beyond the maximum of 35% mentioned above. The rate for zero-emission vehicles is 0%

Car fuel

The taxable benefit in respect of fuel provided by an employer is the 'appropriate percentage' of £18,000 where the appropriate percentage is the figure (from 10% to 35%) used to determine the taxable benefit in respect of the provision of the car.

Approved Mileage Allowance Payments

Own cars and vans	2010/11
Up to 10,000 miles (per mile)	40p
Over 10,000 miles (per mile)	25p

Air Passenger Duty

	Lowest Class **		Standard Rate	
	To 31 Oct 2010	From 1 Nov 2010	To 31 Oct 2010	From 1 Nov 2010
Destination Bands* **				
Band A (0-2000 miles*)	£11	£12	£22	£24
Band B (2001-4000 miles*)	£45	£60	£90	£120
Band C (4001-6000 miles*)	£50	£75	£100	£150
Band D (over 6000 miles*)	£55	£85	£110	£170

* Distance from London to capital city of destination country.
** The lowest class rate does not apply where there is only one class of travel and the seat pitch exceeds 40.
*** This band system was introduced on 1 November 2009.

Insurance Premium Tax

	From 1 April 2010	From 4 Jan 2011
General rate	5%	6%
Higher rate (certain policies)	17.5%	20%

Capital Gains Tax

Rates

Companies pay corporation tax on capital gains after indexation allowance at their normal rate. Gains and losses on sales of shareholdings of 10% or more in trading companies or trading groups are exempt, subject to certain exclusions.

Gains realised by individuals are taxed as follows. Various reliefs and exemptions are available.

Capital Gains Tax

	From 6 April 2010	From 23 June 2010
Standard rate	18%	18%
Higher rate*	n/a	28%
Entrepreneurs' relief rate	10%	10% Annual
Exempt Amount	£10,100	£10,100
Entrepreneurs' relief** (cumulative lifetime allowance)	£2,000,000	£5,000,000

* To the extent that total taxable income / gains exceed income tax basic rate limit.
** Subject to conditions.

Pensions

	2010/11
Annual contribution allowance 100% of salary up to	£255,000
Permitted pension contribution (irrespective of salary)	£3,600
Lifetime benefit allowance	£1,800,000

Where income exceeds £130,000 individuals may be subject to a clawback of higher rate tax relief on a part of the pension contributions.

Value Added Tax

	From 1 April 2010	From 4 Jan 2011
Standard rate	17.5%	20%
Lower rate	5%	5%
Registration limit – annual turnover above	£70,000	£70,000
Simplified arrangements – annual turnover below	£1,350,000	£1,350,000

Corporation Tax

Year to 31 March	2011	2012
Main rate*	28%	27%
Small companies' rate**/***	21%	20%
Where profits**	£0-£300k	£0-£300k
Marginal relief where profits**	£300k-£1,500k	£300k-£1,500k
Marginal relief fraction***	7/400	7/80
Profits threshold for quarterly instalment payments**	£1,500k	£1,500k

* Ring fence profits are taxed at 30%.
** Reduced by reference to number of associated companies.
*** Ring fence profits from UK oil extraction and rights are taxed at 19% with a marginal relief fraction of 11/400.

Intangible Assets

Companies receive a deduction for expenditure on an accounts basis. Allowances at 4% p.a. are available by election.

Research and Development

Qualifying revenue expenditure on research and development attracts an additional deduction where it is incurred at a rate of not less than £10,000 p.a.

	Additional deduction 2010/11
SMEs	75%
Non-SMEs	30%

SMEs which make losses can surrender the deduction in exchange for a payment of up to 24.5% of the qualifying expenditure.

Capital Allowances

	2010/2011
Plant and machinery	
– general writing down allowance rate*	20%
– special rate pool*	
Long life assets and integral features within a building	10%
– energy saving / environmentally beneficial assets	100% – 100% Annual
Investment Allowance on expenditure up to**	£100,000
Motor cars	
– low emission, 110g/km	100%
– emissions less than or equal to 160g/km*	20%
– emissions greater than 160g/km*	10%
Industrial buildings, hotels, agricultural buildings***	1%
Commercial or industrial building in an enterprise zone	100%
Research and Development	100%
Business Premises Renovation Allowance	100%

* Reducing balance General writing down allowance rate and special rate pool rate to be reduced from April 2012 to 18% and 8% respectively.
** Subject to conditions To be reduced to £25,000 from April 2012.
*** Allowances being phased out over the period to March 2011.

Finance matters

Introducing greater efficiencies

The key issues delivered on 22 June by the Chancellor of the Exchequer, George Osborne MP, centred on the UK economy, how to pay down the deficit and how to introduce greater efficiencies and better value for money from the public sector.

THE MAIN PROPOSALS

The Chancellor's rule of thumb is that deficit reduction will need to be achieved based on the 80:20 rule. With 80 per cent achieved through spending cuts and 20 percent from tax rises. The bulk of the tax rises will come through the increase in VAT to 20 per cent from 4 January next year from which the Chancellor hopes to raise about £12 billion per year.

In addition, the capital gains tax rate has increased from 18 per cent to 28 per cent for higher-rate taxpayers and entrepreneurs will benefit from the increase in the lifetime limit to £5 million.

Against this, the UK's tax competitiveness for companies will improve with the phased reduction in the main rate of corporation tax from 28 per cent to 24 per cent by one per cent for each of the next four years. Small companies will also benefit from a reduction in their rate to 20 per cent from next April. These reductions are partly funded by reductions to capital allowances with reductions in writing down allowances and the annual investment allowance.

A number of measures were introduced as part of rebalancing the economy from over-dependence on London, the South of England and the financial services sector;

- A regional growth fund will be introduced to support business employment outside the south of England where new businesses will get a substantial reduction in their employer National Insurance Contributions.
- A bank levy based on balance sheets will be introduced from January next year. The intention is for the levy to encourage banks to move to less risky funding profiles, and further measures to address the high profile issue of bank bonuses will be consulted upon.

The Chancellor has clearly picked up on the requirements for predictability, stability and simplicity in the UK tax system. Its full programme for reform will be set out in early autumn. It intends to move towards a more territorial basis for the taxation of foreign profits of companies, and to continue to counter tax avoidance. Consultation will take place in relation to the taxation of intellectual property and the support R&D tax credits can play in increasing innovation.

Existing annuity rules to end

Making more flexible use of pension savings

The rule that requires all pension savers to purchase an annuity by age 75 will end next year, the government announced on 22 June.

Retired workers will no longer be required to use their pension pot to purchase an annuity once they reach 75. Initially at least, the age will be revised up to 77, with a consultation process on whether the rule should be scrapped altogether.

According to the emergency Budget document released: 'The government will end the existing rules that create an effective obligation to purchase an annuity by age 75 from April 2011 to enable individuals to make more flexible use of their pension savings'.

'The government will shortly launch a consultation on the detail of this change and will introduce transitional measures for those yet to secure a retirement income who will reach 75 in the meantime', it said.

“Retired workers will no longer be required to use their pension pot to purchase an annuity once they reach 75. Initially at least, the age will be revised up to 77, with a consultation process on whether the rule should be scrapped altogether.”

Business matters

Tax facts

Mainstream corporation tax rate to fall to 27 per cent in 2011, 26 per cent in 2012, 25 per cent in 2013 and 24 per cent in 2014.

Small companies' rate of corporation tax to be cut to 20 per cent in 2011.

CAPITAL ALLOWANCES

The rate for general plant and machinery is to fall from 20 per cent to 18 per cent, and the rate for longer life assets from 10 per cent to 8 per cent from April 2012;

The Annual Investment Allowance is to fall to £25,000 per annum, also from April 2012.

The government is to agree the long-term approach to the taxation of foreign profits, intellectual property, and research and development for business.

BANKS

The government is exploring the possibility of a 'Financial Activities Tax' on profits and remuneration;

A bank levy is to be introduced from April 2011, which will apply to the balance sheet of UK banks and building societies, and the UK operations of overseas banks.

The furnished holiday lettings rules are to be reintroduced.

Protecting pensioners

Link with average earnings reinstated

The Chancellor of the Exchequer, George Osborne MP, on 22 June announced his intention to reinstate the link between the state pension and earnings from next April.

The decision to increase the state pension in line with average earnings rather than inflation is expected to lead to a considerable improvement in the real value of the state pension in the coming years.

The Chancellor said in the future pensioners would be protected by a "triple lock" guarantee that the state pension, currently up to £97.50 a week for a single person, would rise by the greater of either average earnings, inflation measures by the retail price index or 2.5 per cent.

The link between the state pension and prices was originally broken in 1980, leading to a fall in the value of the state pension in real terms. It has meant that the state pension has failed to keep pace with the cost of living in Britain.

Mr Osborne said: 'There will be no more 75p increases to the state pension. We will provide dignity in retirement.'

Mr Osborne also announced that compulsory annuitisation would be scrapped from April next year, ending the existing rules that require pensioners to buy an annuity with their pension pot by the age of 75.

'Open for Business'

Corporate taxes given some respite

The Chancellor of the Exchequer, George Osborne MP, said in his emergency Budget speech that he wants a sign to go up over the British economy saying 'Open for Business'.

Commenting, Richard Lambert, Confederation of British Industry (CBI) Director-General, said there was clear recognition in the Budget of the role that business needs to play in getting the economy back into shape and generating the jobs and wealth needed to sustain economic recovery.

BUSINESS HIGHLIGHTS

- Regional Growth Fund to provide finance for regional capital projects over the next two years.
- The 10 per cent capital gains tax rate for entrepreneurs, which applied to the first £2m of qualifying gains made over a lifetime, will be extended to the first £5m of lifetime gains.
- Capital allowances for the majority of plant and machinery assets to fall from 20 per cent to 18 per cent, while the allowance for longer-lived assets will fall from 10 per cent to 8 per cent from April 2012.
- Mainstream corporation tax rate to fall to 27 per cent in 2011, 26 per cent in 2012, 25 per cent in 2013 and 24 percent in 2014.
- Annual Investment Allowance to fall to £25,000 a year to April 2012.
- Small companies' rate of corporation tax to be cut to 20 per cent in 2011.
- The government is to agree the long-term approach to the taxation of foreign profits, intellectual property, and research and development for business.
- Banks: the government is exploring the possibility of a 'Financial Activities Tax' on profits and remuneration; a bank levy is to be introduced from April 2011, which will apply to the balance sheet of UK banks and building societies and the UK operations of overseas banks.
- The furnished holiday lettings rules are to be reintroduced.
- New firms outside the South-East/East to be let off employer National Insurance contributions, up to £5,000, for each of first ten employees recruited.
- Planned tax relief for video games industry to be scrapped.

Small businesses

A considered approach to implementing tax reforms

The Chancellor of the Exchequer, George Osborne MP, announced a number of measures that will affect small businesses around the UK in the new coalition government's first Budget.

Mr Osborne said the Lib-Con coalition would not be making any cuts to capital expenditure during this parliament and announced the introduction of a new tax scheme for small businesses. Under the new initiative, small businesses will be exempt from up to £5,000 of employer National Insurance payments for the first ten employees that are hired. This means new companies could save up to £50,000.

However, the scheme will not be offered to companies starting up in London or the South-East, the Chancellor said.

Mr Osborne explained, "The government will shortly announce details of a scheme to help new businesses in targeted areas of the UK that need it most. During a three-year qualifying period, new businesses which start up in these areas will receive a substantial reduction in their employer National Insurance contributions", Mr Osborne explained.

He added: "The countries and regions which will benefit will be Scotland, Wales, Northern Ireland, the North-East, Yorkshire and the Humber, the North-West, the East Midlands, the West Midlands and the South-West".

Mr Osborne commented: "The government understands the importance of the whole corporate tax system to business and will set out a more detailed programme for reform in the autumn. This will allow it to take a considered approach to implementing tax reforms and to listen to the needs of business through greater consultation.

The government will provide greater certainty for business by committing to principles for corporate tax reforms. In particular, it intends to develop its view that in general a broad tax base, a low rate and a more territorial approach will improve competitiveness".

Small businesses stand to see a more immediate reduction in the tax after the government announced that small companies corporation tax will be cut to 20 per cent in 2011.

The Chancellor also announced that the enterprise finance guarantee scheme will be extended, ensuring that finance for businesses remains accessible.

One of the announcements made that will affect individual taxpayers was the confirmation of an increase in the personal tax allowance. The Chancellor announced a £1,000 increase, meaning income tax will now only be paid on earnings above £7,475 from April next year.

Mr Osborne also confirmed that Value Added Tax (VAT) will rise to 20 per cent from 4 January next year.

Anti-avoidance measures

Plans to 'engage informally'

The government announced that it plans to 'engage informally' with interested parties to explore whether a General Anti-Avoidance Rule (GAAR) should be developed.

There is to be consultation on bringing Inheritance Tax on trusts within the scope of the Disclosure of Tax Avoidance Schemes rules.

There will be targeted anti-avoidance measures in the following areas:

- Avoidance of corporation tax using the accounting "derecognition" rules in relation to loan relationships and derivative contracts;
- Life insurance business;
- Tax avoidance involving the creation for corporate investors in Alternative Investment; and
- Funds of a credit for UK tax where no UK tax has been paid.

The government is to examine whether changes should be made to the Stamp Duty Land Tax rules on high value property transactions to prevent avoidance.

Support for mortgage interest scheme

Chancellor reflects on mortgage costs

The Chancellor of the Exchequer, George Osborne MP, announced during his emergency Budget speech on 22 June that he was cutting one of the schemes designed to help households avoid repossession.

The government-funded scheme helps homeowners that are experiencing financial difficulties by paying the mortgage interest on a loan of up to £200,000 for those who claim income support, jobseeker's allowance or pension credit. The standard interest rate used to calculate SMI has been frozen at 6.08 per cent, a level which was set in the 2008 Pre-Budget report.

The Chancellor said that in order to "put SMI on a more sustainable footing and to better reflect mortgage costs" it will be paid at the level of the Bank of England's average mortgage rate from October this year. The Bank said it was not yet clear which average mortgage rate the Chancellor was referring to, but it looked likely to be the average effective rate, which is currently 3.67 per cent.

The winners and losers

How did your finances fare?

THE EMERGENCY BUDGET WINNERS

INCOME TAX PAYERS

Around 880,000 workers will no longer pay income tax after the Chancellor raised the personal allowance by £1,000 to £7,475 from £6,475. Basic-rate taxpayers will be £170 a year better off as a result. Those earning more than £40,000 will not benefit because they will be subject to a rise in National Insurance contributions, a Labour policy that Mr Osborne has decided to retain.

INVESTORS

Basic-rate taxpayers will continue to pay capital gains tax (CGT) at 18 per cent and the annual CGT exemption of £10,100 will remain.

DRIVERS

Fuel duty is to be frozen.

ENTREPRENEURS

New business set up outside London, the South-East and the East of England will be exempt from £5,000 of National Insurance contributions for each of the first 10 employees they hire.

PENSIONERS

Increases to the basic state pension will be in line with earnings from April 2011. Pensions will rise by at least 2.5 per cent every year.

THE EMERGENCY BUDGET LOSERS

PUBLIC SECTOR WORKERS

There will be a two-year pay freeze for public sector workers earning more than £21,000, although the 1.7 million lowest paid will get a flat £250 pay rise each year. Limits will be put on the salaries of the highest paid public sector workers.

A new government commission, led by John Hutton, the former Labour defence secretary, will examine the cost of public sector pensions and will publish an interim review in September. One solution to ease the burden of public sector pensions on the state is to increase workers' contributions.

FAMILIES

Child tax credits will be withdrawn for families earning more than £40,000 a year, rather than £50,000, while child benefit will be frozen for the next three years.
The baby element of the tax credit known as Sure Start, which is a one-off payment to help towards the costs of a new baby will be abolished.

The health in pregnancy grant of £150 will cease from April 2011. The government said it expected lone parents to look for work when their first child goes to school.

VAT

The main rate of VAT will rise from 17.5 per cent to 20 per cent from 4 January 2011. This will generate more than £13bn of extra revenues. Food and children's clothing will remain exempt.

INVESTORS

Capital gains tax (CGT) rise to 28 per cent from 18 per cent for higher-rate taxpayers, while the annual CGT exemption of £10,100 will remain in place.

HOUSING BENEFITS

The housing benefit is to be cut by £1.8bn by the end of this parliament. The measures include benefit being limited to a maximum of £400 per week for a four-bedroom or larger house.

DISABILITY LIVING ALLOWANCE

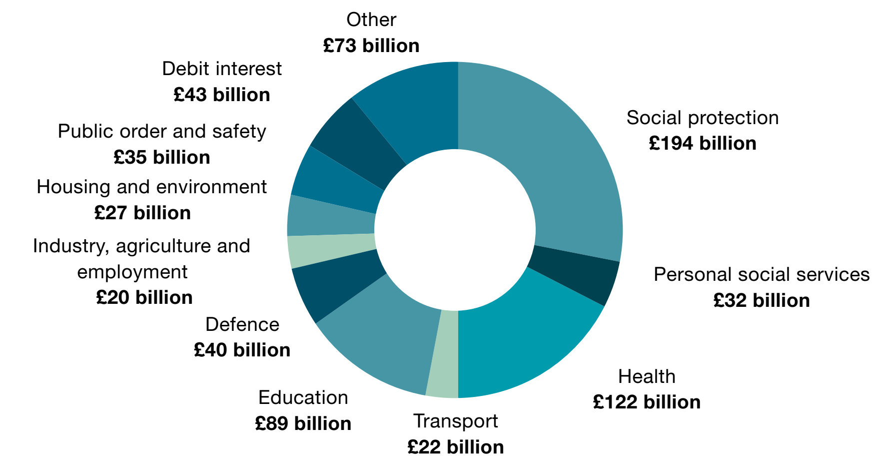
A medical assessment for new and existing claimants will be introduced to ensure that only those who need it can claim it. Three times as many claim as when the benefit was introduced 18 years ago. It costs £11bn a year.

The UK's fiscal landscape

A new model for economic growth

GOVERNMENT SPENDING 2010/11

Total spending - **£696 billion**

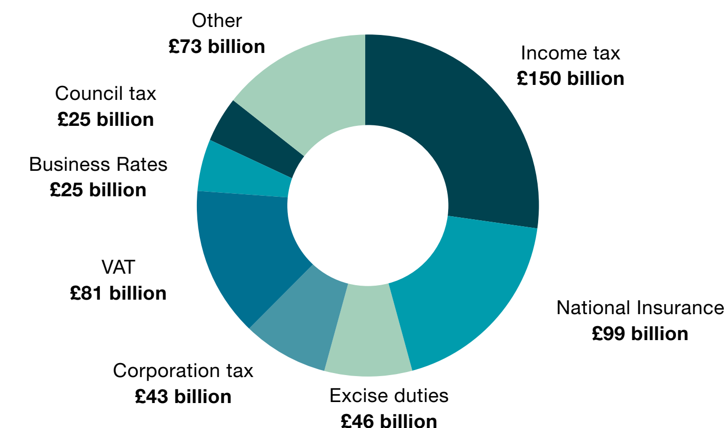


This graph shows the difference between the government's income and the government's spending over the last ten financial years. The source for this graph is data from the Office for National Statistics.

Source: Source: HM Treasury 2010/11 near cash projections. The allocation of spending to function is largely based on United Nations' Classification of the Functions of Government (COFOG). Other expenditure include general public services (including international services); recreation, culture and religion; public service pensions; plus spending yet to be allocated and some accounting adjustments. Social protection includes tax credit payments in excess of an individuals tax liability, which are now counted in AME, in line with OECD guidelines. Figures may not sum due to rounding.

GOVERNMENT RECEIPTS

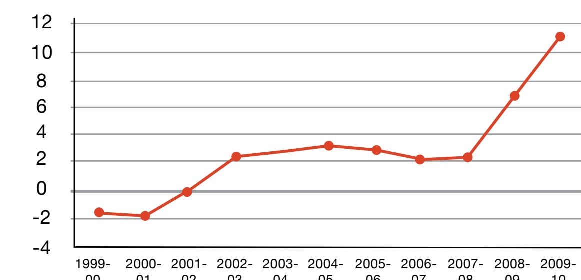
Total receipts - **£548 billion**



This chart presents public spending by main function. Total Managed Expenditure (TME) in 2010/11 is expected to be around £697 billion. TME is divided into Departmental Expenditure Limits (DEL) and Annually Managed Expenditure (AME). The source for this graph is data from HM Treasury.

Source: Office for Budget Responsibility 2010/11 estimates. Other receipts include capital taxes, stamp duties, vehicle excise duties and some other taxes and non-tax receipts - for example, interest and dividends figures may not sum to total due to rounding.

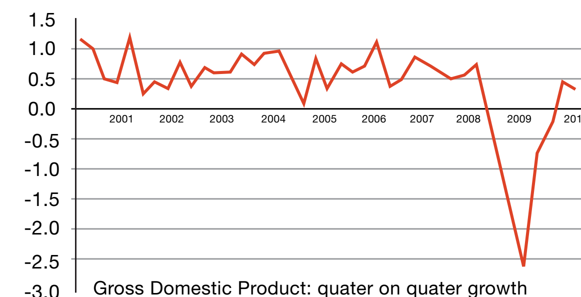
PUBLIC SECTOR NET BORROWING OVER THE LAST TEN YEARS



This graph shows the level of public sector net borrowing as a percentage of GDP in each financial year of the last parliament. The source for this graph is data from the Office for National Statistics.

Source: ONS, Public Sector Finances statistics bulletin, 18 June 2010 release, Borrowing excludes the temporary effects of financial interventions.

THE UK'S ECONOMIC PERFORMANCE OVER THE LAST TEN YEARS



This is a graph of the UK's quarterly percentage growth in GDP over the last ten years. The source for this graph is data from the Office for National Statistics.

Source: ONS, UK output, income and expenditure statistical bulletin, 1st quarter 2010. GDP is the chained volume measure.

Emergency Budget 2010

Chancellor of the Exchequer's Budget speech in full

Mr Deputy Speaker,

This emergency Budget deals decisively with our country's record debts. It pays for the past. And it plans for the future. It supports a strong enterprise-led recovery. It rewards work. And it protects the most vulnerable in our society. Yes it is tough; but it is also fair.

This is an emergency Budget, so let me speak plainly about the emergency that we face.

The coalition government has inherited from its predecessor the largest budget deficit of any economy in Europe with the single exception of Ireland.

One pound in every four we spend is being borrowed. What we have not inherited from our predecessor is a credible plan to reduce their record deficit. This at the very moment when fear about the sustainability of sovereign debt is the greatest risks to the recovery of European economies.

Questions that were asked about the liquidity and solvency of banking systems are now being asked of the liquidity and solvency of some of the governments that stand behind those banks.

I do not want those questions ever to be asked of this country. That is why we have set a brisk pace since taking office. In the last seven weeks: We have announced, conducted and completed a review of this current year's spending and identified six billion pounds of savings.

We have announced, established and received the report of the independent Office for Budget Responsibility.

The power the Chancellor has enjoyed for centuries to determine the growth and fiscal forecasts now resides with an independent body immune to the temptations of the political cycle. And we have examined, decided on and in some cases halted the mass of unfunded commitments, IOUs and overcommitted reserves that greeted us on entering office.

This early, determined action has earned us credibility in international markets. It has meant that our promise to deal decisively with the deficit has been listened to. Market interest rates for Britain have fallen over the last seven weeks, while those of many of our European neighbours have risen. Those lower market interest rates are already supporting our recovery. But unless we now deliver on that promise of action with concrete measures, that credibility – so hard won in recent weeks – will be lost. The consequence for Britain would be severe.

Higher interest rates, more business failures, sharper rises in unemployment, and potentially even a catastrophic loss of confidence and the end of the recovery. We cannot let that happen. This Budget is needed to deal with our country's debts. This Budget is needed to give confidence to our economy. This is the unavoidable Budget.

I am not going to hide hard choices from the British people or bury them in the small print of the Budget documents.

You're going to hear them straight from me, here in this speech.

Our policy is to raise from the ruins of an economy built on debt a new, balanced economy where we save, invest and export. An economy where the state does not take almost half of all our national income, crowding out private endeavour. An economy not overly reliant on the success of one industry, financial services – important as they are – but where all industries grow. An economy where prosperity is shared among all sections of society and all parts of the country.

In this Budget everyone will be asked to contribute. But in return we make this commitment.

Everyone will share in the rewards when we succeed. When we say that we are all in this together, we mean it.

Mr Deputy Speaker, the first challenge for this Budget is to set the fiscal mandate – or in other words, our overall objective for the public finances. The previous government had two fiscal rules, one for debt and one for the current budget. They were supposed to force Chancellors to set aside money in the good years so they could borrow sustainably when the economy turned down. They completely failed in that task.

And as this is the last budget in which this golden rule will appear, I would like to be the last Chancellor to report on it. We are set to miss the golden rule in this cycle by 485 billion pounds.

We now know the intrinsic weakness in backward-looking fiscal rules. Past prudence was an excuse for future irresponsibility. And the judge of the rules was the very same Chancellor they were supposed to be restraining.

We propose a more credible approach. Our fiscal mandate will be forward-looking, and the judge of whether we are on course to meet it will be not the Chancellor but the independent Office for Budget Responsibility.

On behalf of the House, I want to thank Sir Alan Budd and his fellow Committee members, Geoffrey Dicks and Graham Parker, for their highly professional effort. In the space of just seven weeks I believe we have established the Office for Budget Responsibility as a permanent improvement to economic policy making and the transparency of government.

The legislation to put the Office on a statutory footing will now be drawn up and I hope it will command all party support. I now turn to what that fiscal mandate will be.

The view of the international community was clearly expressed at the latest G20 meeting, and we will be taking the same message to the G20 summit in Toronto this weekend. Surplus countries should do more to support global demand. So we welcome China's announcement to come off the dollar peg.

At the same time the international community believes countries with high fiscal deficits need to accelerate the pace of fiscal consolidation. That is precisely what we now propose to do.

The formal mandate we set is that the structural current deficit should be in balance in the final year of the five-year forecast period, which is 2015/16 in this Budget. This mandate is: Structural – to give us flexibility to respond to external shocks; Current – to protect the most productive public investment; and credible – because the Office for Budget Responsibility, not the Chancellor, will decide on the output gap.

In order to place our fiscal credibility beyond doubt, this mandate will be supplemented by a fixed target for debt, which in this parliament is to ensure that debt is falling as a share of GDP by 2015/16. I can confirm that, on the basis of the measures to be announced in this Budget, the judgement of the Office for Budget Responsibility published today, is that we are on track to meet these goals.

Indeed, I can tell the House that because we have taken a cautious approach, we are set to meet them one year earlier – in 2014/15. Or to put it another way, we are on track to have debt falling and a balanced structural current budget by the end of this Parliament.

Mr Deputy Speaker, at this point in the Budget speech, the Chancellor would normally read out their own set of economic and fiscal forecasts.

They normally tell you more about the political cycle than the economic one. Those days have gone for good.

Instead I will give the House the latest forecasts from the independent Office for Budget Responsibility, taking into account the measures in the Budget.

Growth in the UK economy for the coming five years is estimated to be: 1.2 per cent this year and 2.3 per cent next year; Then 2.8 per cent in 2012 followed by 2.9 per cent in 2013; Then 2.7 per cent in both 2014 and in 2015.

Consumer price inflation is expected to reach 2.7 per cent by the end of the year before returning to target in the medium term. And let me take this opportunity to confirm that the inflation target remains at 2 per cent as measured by the Consumer Prices Index.

The unemployment rate is forecast by the Office for Budget Responsibility to peak this year at 8.1 per cent and then fall for each of the next four years, to reach 6.1 per cent in 2015.

Some have suggested that there is a choice between dealing with our debts and going for growth. That is a false choice. The crisis in the Eurozone shows that unless we deal with our debts there will be no growth.

And these forecasts demonstrate that a credible plan to cut our budget deficit goes hand in hand with a steady and sustained economic recovery, with low inflation and falling unemployment.

What is more the forecast shows a gradual rebalancing of the economy, with business investment and exports playing a greater role and government spending and debt-fuelled consumption a smaller role.

A sustainable private sector recovery built on a new model of economic growth, instead of pumping the debt bubble back up. Part of the reason, as we have always argued, is that tighter fiscal policy can enable interest rates to stay lower for longer.

And as the Governor of the Bank of England confirmed this last week at the Mansion House, "if prospects for growth were to weaken, the outlook for inflation would probably be lower and monetary policy could then respond."

The subject of interest rates brings me to say this about attempts to directly compare last week's forecasts with this one.

As the Office for Budget Responsibility notes in today's Budget document, any such comparison would be "misleading", because last week's forecast included the lower interest rates that expectations of this week's Budget have already brought about.

So as Sir Alan Budd and his colleagues have written, to actually follow the fiscal path set out by the previous government "would lead to higher interest rates and so lower economic activity" than his forecast showed.

Mr Deputy Speaker, let me now turn to the measures in the Budget designed to deliver this accelerated reduction in the structural deficit.

The coalition government believes that the bulk of the reduction must come from lower spending rather than higher taxes.

The country has overspent; it has not been under-taxed.

Our approach is supported by the international evidence, compiled by the Organisation for Economic Cooperation and Development, the International Monetary Fund and others, which found that consolidations delivered through lower spending are more effective at correcting deficits and boosting growth than consolidations delivered through tax increases.

This is the origin of our 80:20 rule of thumb – roughly 80 per cent through lower spending and 20 per cent through higher taxes.

This evidence has been available in the Treasury for some time, but was only published in a redacted form by the previous government.

We intend to follow international best practice and the Treasury's own analysis.

My measures today mean that 77 per cent of the total consolidation will be achieved through spending reductions and 23 per cent through tax increases. I believe this gets the balance right.

Mr Deputy Speaker, I now turn to the Office for Budget Responsibility's fiscal forecasts.

But as a result of the measures I will announce today, public sector net borrowing will be: * £149 billion this year, * falling to £116 billion next year, * then £89 billion in 2012/13, * and then £60 billion in 2013/14.

By 2014/15 borrowing reaches £37 billion, exactly half the amount forecast in the March Budget.

In 2015/16, borrowing falls further to £20 billion.

As a share of the economy, borrowing will fall from 10.1 per cent of GDP this year to just 1.1 per cent in 2015/16.

We now know, thanks to last week's Office for Budget Responsibility forecast, that the structural current deficit is significantly larger than we were told – 0.8 per cent of GDP or £12 billion next year.

Thanks to my action today, the structural current balance will be minus 4.8 per cent of GDP this year.

That deficit will then be eliminated to plus 0.3 per cent in 2014/15 and plus 0.8 per cent in 2015/16.

In other words, it will be in surplus.

Public sector net debt as a share of GDP will be 62 per cent this year, before peaking at 70 per cent in 2013/14.

Because of our action today, it then begins to fall, to 69 per cent in 2014/15

and then 67 per cent in 2015/16.

While under the plans we inherited, debt would have increased every full year of this parliament.

And the House will want to know that as a result of our measures debt interest payments will be £3 billion a year lower by the end of this parliament.

Mr Deputy Speaker, I have one further announcement to make regarding macroeconomic policy.

I can confirm that, as set out in the coalition agreement, this government will not be joining the euro in this parliament. Therefore, Mr Deputy Speaker, I have abolished the Treasury's Euro Preparations Unit.

Yes, one does exist. And the official concerned has been redeployed to more productive activities.

Let me now turn to my other decisions on public spending. Mr Deputy Speaker, the state today accounts for almost half of all national income. That is completely unsustainable.

All parties in this House now accept that spending needs to be cut. And we have made a start. But we need to go much further if we are to meet our fiscal mandate and see debt falling by the end of this parliament.

Today we are setting out the overall path of public spending that will achieve that. Let me begin with current spending. Current expenditure will rise from £637 billion in 2010/11 to £711 billion in 2015/16.

Although this is an increase, the House should remember that we inherit a rapidly rising bill for debt interest – a bill that won't start falling until the debt itself starts to fall.

Debt interest payments alone will cost the taxpayer a quarter of a trillion pounds over this period.

One of my predecessors used to call this spending the costs of social failure – I say it is the price of economic failure.

Compared to the plans set out by the previous government, I am announcing today additional current expenditure reductions of £30 billion a year by 2014/15.

The plans for public investment we inherit from our predecessors envisage a steep drop from £69 billion last year to £46 billion in 2014/15.

After the initial in-year reductions, the question we have faced is how much further to go.

Well-judged capital spending by government can help provide the new infrastructure our economy needs to compete in the modern world.

It supports the transport links we need to trade our goods, the equipment we need to defend our country, and the facilities we need to provide quality public services.

I think an error was made in the early 1990s when the then government cut capital spending too much – perhaps because it is easier to stop new things being built than to cut the budgets of existing programmes.

We have faced many tough choices about the areas in which we should make additional savings, but I have decided that capital spending should not be one of them.

There will be no further reductions in capital spending totals in this Budget.

But we will still make careful choices about how that capital is spent.

The absolute priority will be projects with a significant economic return to the country.

Assessing what those projects are will be an important part of the autumn spending review.

Mr Deputy Speaker, the government can also dispose of assets which should rightly be in private ownership.

Yesterday we launched the sale of High Speed 1.

We will look at how to dispose of our shareholding of NATS, the air traffic control services.

We will aim to sell the student loan book, and look at options around early repayment for individuals.

And we will resolve the future of the Tote – at last.

My Right Honourable Friend the Business Secretary will also facilitate a private capital injection into the Royal Mail Group, something that has been long overdue.

Before I turn now to discuss departmental budgets, I need to say something first about another area of spending – the Civil List.

The Civil List is the government's support for Her Majesty the Queen in Her duties as Head of State.

I am sure everyone in this House will want to join me in recognising The Queen's loyal service and immense contribution to public life.

The amount provided by the Civil List has remained unchanged over the last twenty years at £7.9 million.

This has required careful management.

Because of inflation, the annual payment is today worth only a quarter of what it was twenty years ago.

I can announce that, with the full agreement of The Queen, the Civil List will remain frozen at £7.9 million for the coming year.

I will propose a new means of consolidated support for Her Majesty for the future, at a later date.

In addition, the Royal Household have agreed that in future Civil List expenditure will be subject to the same audit scrutiny as other government expenditure, through the National Audit Office and the Public Accounts Committee.

I believe this will mean clear accountability in this House and it will strengthen public confidence.

Let me turn now to my decisions on departmental expenditure limits.

In recent years, Chancellors have been reluctant to explain what their total spending projections will mean for Whitehall departments.

This is entirely self-defeating.

It normally takes the Institute for Fiscal Studies less than 24 hours to work it out for themselves and let the public know the truth.

I will save them the effort.

We have inherited from the previous government spending plans to cut departmental budgets by £44 billion a year by 2014/15.

This implies an average real reduction for unprotected departments of 20 per cent.

Not that this was ever said. Nor was a single pound of cuts to programmes even identified.

Because the structural deficit is worse than we were told, my Budget today implies further reductions in departmental spending of £17 billion by 2014/15.

We have committed to providing the National Health Service with real increases throughout the parliament and we will honour our international aid obligations to the poorest in the world.

Once these are taken into account, the Budget figures imply that other departments will face an average real cut of around 25 per cent over four years.

Clearly, if we can find any additional savings to social security and welfare beyond those which I will shortly outline, then that will greatly relieve the pressure on these departments and that 25 per cent figure.

Of course, not all departments will receive the same settlement.

I recognise, for example, the particular pressures on our education system and on defence.

Final departmental settlements, and the final split between departmental expenditure and annually managed expenditure on welfare, will be set in the spending review.

Rather than follow the usual practice of keeping the date of that review a secret until a few weeks before it happens, let me tell the House that it will be presented on Wednesday 20th October.

A further way we can ease the pressure on public services is to agree that we need to restrain public sector pay in these difficult times.

And we need to do something about the spiralling costs of public sector pensions.

Many millions of people in the private sector have in the last couple of years seen their pay frozen, their hours reduced, and their pension benefits restricted.

They have accepted this because they knew that the alternative in many cases was further job losses.

The public sector was insulated from these pressures but now faces a similar trade off.

I know there are many dedicated public sector workers who work very hard and did not cause this recession – but they must share the burden as we pay to clean it up.

The truth is that the country was living beyond its means when the recession came. And if we don't tackle pay and pensions, more jobs will be lost.

That is why the government is asking the public sector to accept a two-year pay freeze.

But we will protect the lowest paid.

In the past I have said that we would be able to exclude the one million public sector workers earning less than £18,000 from a one year pay freeze.

Today, because we have had to ask for a two year freeze, I extend the protection to cover the 1.7 million public servants who earn less than £21,000.

Together they make up 28 per cent of the public sector workforce.

They will each receive a flat pay rise worth £250 in both these years, so that those on the very lowest salaries will get a proportionately larger rise.

In recognition of our armed services who are risking their lives for us all in Afghanistan, we have also doubled the operational allowance to £4,800.

And we have asked Will Hutton to draw up plans for fairer pay across the public sector, without increasing the overall pay bill, so that those at the top of organisations are paid no more than 20 times the salaries of those at the bottom.

The culture of excessive pay at the very top of the public sector simply has to end.

Mr Deputy Speaker, we also need to deal with the cost of public service pensions.

This is one of the greatest long term pressures facing our nation's finances.

The Office for Budget Responsibility today publishes figures showing that by 2015/16 we will be spending over £10 billion a year simply to meet the gap between pension contributions and payments to the unfunded pensions they support.

That is why I have asked John Hutton to carry out an investigation.

As the Work and Pensions Secretary in the previous government, he brings experience and an unbiased approach.

He will provide an interim report in September this year to help inform any decisions required for the spending review, and a full report in time for next year's Budget.

The government will also accelerate the increase in the State Pension Age to 66. A call for evidence will be launched later this week.

And we will consult on whether to phase out the Default Retirement Age.

Mr Deputy Speaker, let me now address the largest bill in government – the welfare bill.

It is simply not possible to deal with a budget deficit of this size without undertaking lasting reform of welfare.

It has been a key component of most successful fiscal consolidations elsewhere in the world.

And around Europe, countries are now tackling their benefits bill.

Germany has already announced 30 billion euros worth of cuts to welfare spending.

And others are taking similar steps.

Here in Britain, the explosion in welfare costs contributed to the growing structural budget deficit in the middle part of this decade.

Total welfare spending has increased from £132 billion ten years ago to £192 billion today.

That represents a real terms increase of a staggering 45 per cent.

It's one reason why there is no money left.

It has also left an increasing number of our fellow citizens trapped on out-of-work benefits for the whole of their lives.

A greater proportion of our children grow up in workless households than any other country in Europe.

We are wasting the talent of millions, and spending billions on it in the process.

So we will increase the incentives to work, and reduce the incentives to stay out of work.

We will focus our benefits more towards those in need.

And we will end some one-off payments that the country cannot afford anymore.

First, we need to put the whole welfare system on a more sustainable and affordable footing.

So from next year, with the exception of the state pension and pension credit, we will switch to a system where we up-rate benefits, tax credits and public service pensions in line with consumer prices rather than retail prices.

The consumer price index not only reflects everyday prices better, it is of course now the inflation measure targeted by the Bank of England.

This will save over £6 billion a year by the end of the parliament.

I believe this is a fairer approach than a benefits freeze.

In time for the next Budget we will also publish proposals to move the indexation in the tax system from RPI to CPI in a way that protects revenues.

Tackling spiralling welfare costs means also addressing the bill for tax credits.

Spending on tax credits has increased from £18 billion in 2003 to £30 billion this year.

This is unsustainable.

There are over 150,000 families with incomes over £50,000 receiving tax credits.

Taking into account the various disregards means that families earning up to £83,000 are eligible for this means tested benefit.

The country can simply not afford this.

We need to target tax credits on those who need the help most.

So we will: * Reduce payments to families earning over £40,000 next year and then align the thresholds for the child and family element; * Increase the taper rate at which awards are reduced; * Remove the baby element for new children from April 2011; * Remove the one-off payment to new workers over 50 from April 2012; * Reduce the income disregard from

£25,000 to £10,000, and then £5,000; * Introduce an income disregard for income falls; * Reduce back-dating from three months to one month; * And we will not introduce the pre-election promise of a new tax credit element for infants.

Sadly, there are further benefits which the country can no longer afford.

So we will abolish the poorly-targeted Health in Pregnancy Grant from April 2011.

At the same time we will restrict the sure start maternity grant to the first child only.

And we will expect lone parents to look for work when their youngest child goes to school.

We have decided that we simply cannot afford to extend the Saving Gateway and we have also had to take a difficult decision about child benefit.

I have received many proposals about this.

Some have suggested we means test it; others that we tax it.

All these proposals involve issues of fairness. This benefit is usually claimed by the mother.

To tax it would mean the working mothers received less than the non-working partner of a millionaire.

Means test it and we would have to create a massively complex new system to assess household incomes.

I do not propose to do these things. I know many working people feel that their child benefit is the one thing they get without asking from the state.

So instead, to control costs, we have decided to freeze child benefit for the next three years.

This is a tough decision, but I believe it strikes the right balance between keeping intact this popular universal benefit while ensuring that everyone, across the income scale, makes a contribution to helping our country reduce its debts.

That brings me to another universal benefit, Disability Living Allowance.

Mr Deputy Speaker, it is right that people who are disabled are helped to lead a life of dignity.

We will continue to support them, and we will not reduce the rate at which this benefit is paid.

But three times as many people claim it today than when it was introduced eighteen years ago.

And the costs have quadrupled in real terms to over £11 billion, making it one of the largest items of government spending.

We will introduce a medical assessment for Disability Living Allowance from 2013, which will be applied to new and existing claimants.

This will be a simpler process than the complex forms they have to fill out at present.

That way we can continue to afford paying this important benefit to those with the greatest needs, while significantly improving incentives to work for others.

Mr Deputy Speaker, spending on housing benefit has risen from £14 billion ten years ago to £21 billion today.

That is close to a 50 per cent increase over and above inflation.

Costs are completely out of control.

We now spend more on housing benefit than we do on the police and on universities combined.

And among these enormous numbers for total spending there are some equally enormous individual awards.

Today there are some families receiving £104,000 a year in housing benefit.

The cost of that single award is equivalent to the total income tax and national insurance paid by 16 working people on median incomes.

It is clear that the system of housing benefit is in dire need for reform.

We will do that by: * Re-setting and restricting Local Housing Allowances; * Up-rating deductions; * Reducing certain awards; * Re-adjusting Support for Mortgage Interest payments; * Limiting social tenants' entitlement to appropriately sized homes; * And, lastly, we will for the first time introduce maximum limits on housing benefit – from £280 a week for a one-bedroom property to £400 a week for a four-bedroom or larger.

Our package today reduces the costs of Housing Benefit by £1.8 billion a year by the end of the parliament, or 7 per cent of the total budget.

It will also improve incentives to work.

But at the same time we will target more resources to those who need it most, by increasing the budget for Discretionary Housing Payments, to deal with hardship cases, by £40m.

And from now we will cover the cost of an additional room for those claimants with a disability who need a carer.

Mr Deputy Speaker, taken together, all these measures to control the costs of welfare will save the country £11 billion by 2014/15.

Governments in the past have said they were going to get to grips with welfare and reward work. We are delivering.

My Right Honourable Friend the Secretary of State for Work and Pensions will bring forward proposals to further reform the benefits system as a tool to support work and encourage aspiration in time for the autumn spending review.

But as I said right at the start of this speech, this Budget is not just about paying for the bills of the past.

It is also about planning for the future.

It is my deeply held belief that a genuine and long-lasting economic recovery must have its foundations in the private sector.

That is where the jobs will come from – and we will do absolutely everything to support their creation.

We argued that imposing a jobs tax was the last thing Britain needed in a recovery, and the businesses of the country agreed with us.

So we will adopt a different approach.

We will make it cheaper for companies to employ people.

From April 2011 the threshold at which employers start to pay National Insurance will rise by £21 per week above indexation.

The cost of hiring people on incomes lower than £20,000 will be less than it is today.

And in one move we will have lifted 650,000 employees out of this tax altogether.

But if we are to have a sustained, job-creating recovery, we need more than this.

We need to see growth not just in one corner of our country, nor in just one sector.

For we live in a world where the competition for business is growing ever more intense.

I want a sign to go up, over the British economy, that says "Open for Business".

And this is how I propose to do it.

Corporation tax rates are compared around the world, and low rates act as adverts for the countries that introduce them.

Our current rate of 28 pence is looking less and less competitive.

So we will do something about it.

Next year we will cut corporation tax by one per cent to 27 pence in the pound.

The year after we will cut it again by one per cent.

And again the year after, and again the year after that.

Four annual reductions in the rate of corporation tax that will take it down to just 24 per cent.

It will give us the lowest rate of any major Western economy, one of the lowest rates in the G20, and the lowest rate this country has ever know.

At the same time we will agree with business a long term approach to the taxation of foreign profits, the treatment of intellectual property and the proposals from James Dyson on research and development.

We will also reduce the small companies tax rate.

The previous government was planning to increase this tax rate next year to 22 per cent, at the very time we should be encouraging small businesses to grow.

We instead will cut it to 20 pence.

This will benefit some 850,000 companies.

And because small business are struggling to obtain credit at the moment, I will extend the Enterprise Finance Guarantee Scheme, which supports SME access to lending.

These changes will benefit at least 2,000 small businesses.

My Right Honourable Friend the Business Secretary will be coming forward in the summer with further proposals to expand the availability of credit, to make sure the economic recovery is properly financed.

There are many small businesses in the tourism industry today.

To help them, I am reinstating the favourable tax rules for furnished holiday lettings, which our predecessors had planned to repeal.

And I can also announce that there will be measures to cancel certain backdated business rates bills, including for many businesses in ports.

In the current climate, with the deficit the size it is, all these reductions in tax must be more than paid for by other changes to business taxation.

So, Mr Deputy Speaker, we will not go ahead with the poorly-targeted tax relief for the video games industry.

There will be a small reduction in the rates for capital allowances, which will remain broadly in line with economic depreciation.

For the majority of plant and machinery assets, the rate of allowance will fall from 20 to 18 per cent, while the allowance for longer-lived assets will fall from 10 to 8 per cent.

In other words businesses will still receive full tax relief on their qualifying expenditure, but over a longer timeframe.

I have also decided to reduce the Annual Investment Allowance to £25,000 a year, to ensure support is focused on investment by smaller firms.

Over 95 per cent of businesses will continue to have all of their qualifying plant and machinery expenditure fully covered by this relief.

Manufacturing as a whole will pay less tax.

And I have listened to the argument that changing these crucial allowances during the early stages of the economic recovery could be disruptive.

So I will delay the reductions in capital and investment allowances to April 2012.

This will give businesses the extra early advantage of the tax cuts, which start to come in from next year.

Mr Deputy Speaker, our reforms today will also mean a greater contribution from the banking sector, one that far outweighs any benefit they receive from the lower tax rates I have just announced.

In putting in order the nation's finances, we must remember that this was a crisis that started in the banking sector.

The failures of the banks imposed a huge cost on the rest of society.

So I believe it is fair and it is right that in future banks should make a more appropriate contribution, which reflects the many risks they generate.

Such an approach has already been recommended by the International Monetary Fund.

We are exploring the costs and benefits of a Financial Activities Tax, on profits and remuneration, and we will work with international partners to secure agreement.

But today the British government takes the initiative in this global debate about the appropriate risks and rewards in international banking.

From January 2011, we will introduce a bank levy.

It will apply to the balance sheets of UK banks and building societies, and to the UK operations of banks from abroad.

There will be deductions for Tier one capital and insured retail deposits, and a lower rate for longer maturity funding.

Smaller banks with liabilities below a certain level will not be liable for the levy.

Once fully in place, we expect the levy to generate over £2 billion of annual revenues.

There are those who have argued that we should wait until every country in the G20 introduces a bank levy.

I believe that is not reasonable or fair.

Indeed I can tell the House that the French and Germans have joined the UK today in committing to introduce a bank balance sheet levy.

In a joint statement, our three governments have pledged to ensure our banks make a fair contribution to reflect the risks they pose.

Mr Deputy Speaker, the message I hear from the business community is unequivocal.

They want certainty and stability from government so that they start the long process of rebuilding their businesses.

Today I am offering them just that.

A five-year plan to reform the corporation tax system, with lower rates, simpler rules and greater certainty.

The most fundamental and far-reaching reform of our corporate tax regime in generations.

It offers a stable and consistent platform for a private sector recovery.

It is a balanced package which will send a clear signal that Britain is open for business.

It will help companies invest, attract foreign investment, and boost growth.

Above all, it will help create jobs.

And by increasing the amount of business investment by an additional £13 billion between now and 2016, these reforms will help rebalance the economy away from household debt and government consumption.

Mr Deputy Speaker, we will also take forward our plans to create a Green Investment Bank, bringing forward private investment in clean energy and green technologies.

And we also need investment in our digital infrastructure.

But the previous government's landline duty is an archaic way of achieving this, hitting 30 million households who happen to have a fixed telephone line.

I am happy to be able to abolish this new duty before it is even introduced.

Instead, we will support private broadband investment, including to rural areas, in part with funding from the Digital Switchover under-spend within the TV Licence Fee.

Mr Deputy Speaker, over the past decade the British economy has become deeply unbalanced.

Nowhere are these disparities as marked as between the different regions of Britain.

Between 1998 and 2008, for every private sector job generated in the North and the Midlands, 10 were created in London and the South.

We need a new approach.

One that empowers local leadership, generates local economic growth, and promotes job creation in all parts of the country including Wales and Scotland.

We will publish a white paper on how we intend to deal with these issues later in the summer, followed by a consultation paper on rebalancing the economy of Northern Ireland.

And as a step towards rebalancing our economy, we are today announcing support for those regions more dependent on the public sector.

First, even when money is so short, we will commit to these important regional transport projects: The upgrade of the Tyne & Wear Metro; The extension of the Manchester Metrolink; The redevelopment of Birmingham New Street station; And improvements to the rail lines to Sheffield and between Liverpool and Leeds.

Second, we will create a large Regional Growth Fund to provide finance for regional capital projects over the next two years.

We will announce the details shortly but priority will be given to projects that have the greatest impact on innovation and jobs.

Third, we will shortly announce a new tax scheme to help create new businesses in those regions where the private sector is not nearly strong enough.

For the next three years anyone who sets up a new business outside London, the South East and the Eastern region will be exempt from up to £5,000 of employer national insurance payments, for each of their first 10 employees hired.

We aim to have the scheme up and running by September, but any qualifying new business set up from today will also receive help.

And the Treasury estimate that some 400,000 businesses will benefit – ensuring all parts of our country contribute to a more balanced and sustainable economic future.

Mr Deputy Speaker, let me turn now to some further decisions we have made on taxation.

I am someone who believes in the virtues of lower taxation; but the only sustainable route to lower taxes is by first achieving sound public finances.

The sovereign debt crisis means we need to the reduce the deficit even more quickly in order to protect our economy.

And the Office for Budget Responsibility has revealed the size of the structural deficit to be even larger than we feared, £12 billion larger next year.

As a result, this Budget announces a further fiscal tightening of £40 billion a year by the end of this parliament, including welfare and spending measures, over and above the previous government's plans.

To achieve that additional tightening while maintaining the right "four-to-one" balance between spending and taxation means that I have to announce further tax rises today.

On 4th January next year, the main rate of VAT will rise from 17.5 to 20 per cent.

The years of debt and spending make this unavoidable.

This single tax measure will by the end of this parliament generate over £13 billion a year of extra revenues.

That is £13 billion we don't have to find from extra spending cuts or income tax rises.

I can also give this House a commitment that we will keep everyday essentials such as food and children's clothing, as well as other zero-rated items like newspapers and printed books, exempt from VAT over the course of this parliament.

And, Mr Deputy Speaker, in line with the increase in the main rate of VAT, the higher rate of insurance premium will also rise from 17.5 to 20 per cent, while the standard rate will increase from 5 to 6 per cent.

Let me turn to my decisions on duties.

The March Budget included substantial increases in these.

I can tell the House that my Budget today includes no new increases in duties on alcohol, tobacco or fuel.

We will report back in the autumn on the scope for targeting alcohol duty at the products most associated with binge drinking and underage consumption.

We will explore changes to the aviation tax system, including switching from a per-passenger to a per-plane duty, and consult on major changes.

That will help reduce our carbon emissions.

We are examining the impact of sharp fluctuations in the price of oil on the public finances, to see if pump prices can be stabilised.

We will also look at whether a rebate for remote rural areas could work.

I have one final announcement on duties.

We have decided to reverse the previous government's plan to increase the duty on cider by 10 per cent above inflation and the reduction will come into effect at the end of this month – just in time to celebrate England's progress to the quarter finals, or else to drown our sorrows.

Mr Deputy Speaker, that brings me to Council Tax.

At times like this, when money is short, we think all parts of government should work hard to keep costs down.

And we want to give councils every incentive to do just that.

So we will offer a deal to local authorities in England.

If you can keep your cost increases low, then we will help you to freeze council tax for one year from next April.

That will mean that the average family will be some £35 better off next year and every year thereafter.

It will be one less rising bill for families to worry about – and it will drive value for money throughout all levels of government.

Mr Deputy Speaker, one of the most chaotic areas of tax that the new government inherited from its predecessor is the capital gains tax regime.

Some of the richest people in this country have been able to pay less tax than the people who clean for them.

That is not fair – and it stems from the avoidance activity that has exploited the wider gap between the rate of capital gains tax and the top rates of income tax.

These practices are costing other taxpayers over £1 billion every year.

It is therefore right, as set out in the coalition agreement, that capital gains tax should increase in order to help create a fairer tax system.

I have listened carefully to everyone's views and considered all the options.

My concern has been to balance the competing demands of fairness, simplicity and competitiveness – and I believe my decision gets that balance right.

Low and middle income savers who pay income tax at the basic rate make up over half of all capital gains taxpayers.

They will continue to pay tax on their capital gains at 18 per cent.

From midnight, taxpayers on higher rates will pay 28 per cent on their capital gains.

I have also decided that the Annual Exempt Amount for capital gains tax will remain at £10,100 this year and will continue to rise with inflation in future years.

I am acutely aware of how important it is to protect the incentives to succeed in business and to innovate.

So to promote enterprise, the 10 per cent capital gains tax rate for entrepreneurs, which currently applies to the first £2m of qualifying gains made over a lifetime, will be extended to the first £5m of lifetime gains.

I asked the Treasury to examine what would happen if we had increased the rate much further beyond 28 per cent, and their dynamic analysis showed that this would have resulted in smaller total revenues.

I also considered in great detail the options presented to me for introducing tapers or indexation allowances, and concluded that the complexity and administration involved would have been self-defeating.

The changes I have made mean that: * the capital gains of the majority of taxpayers are protected; * we have a top rate that is in line with our international competitors; * we keep the system simple and easy for any taxpayer to understand; * and we reduce the incentive to convert income to capital gains.

It is revealing that the great majority of the almost £1 billion of extra receipts we expect to see as a result of this change will come from additional income tax payments. I believe this is the right way to reform the taxation of capital gains. Let me say something here about the previous government's policy to reduce pension tax relief for people on high incomes, due to come in next year. Many businesses are alarmed at the complexity this will introduce.

I have listened to those concerns. However, I must also protect the £3.5 billion of revenues this policy was set to raise from high income people. I will therefore work with industry on alternatives ways of raising the same revenue, potentially by reducing the Annual Allowance.

Let me turn now to income tax. Mr Deputy Speaker, a responsible society is one that rewards the efforts of those who choose to work. The income tax system, and in particular the abolition of the 10 per cent rate of income tax, has meant that many people on lower incomes face higher average tax rates. I believe it is important to lift people out of the income tax system and allow them to keep more of their hard-earned money. It is especially important to make progress in this Budget where we are asking so much of so many. And it demonstrates that this coalition government puts fairness first.

In the current system, everyone under the age of 65 is eligible to a tax-free personal allowance of £6,475.

This means there are many thousands of people who have their income taken away from them in tax, only to have to apply to get it back in benefits.

This does not reward work.

So today I can announce that we will increase this personal allowance by £1,000 in April.

People will be able to earn £7,475 before they have to start paying income tax.

23 million people who are basic rate taxpayers will each gain by up to £170 a year.

880,000 of the lowest income taxpayers will be taken out of tax altogether.

Higher rate taxpayers will not benefit from this change, and the higher rate income tax threshold will have to remain frozen to 2013/14.

Our long-term objective remains to increase the personal allowance to £10,000, as set out in the coalition agreement, and we will make real steps towards achieving that objective through the rest of this parliament.

Mr Deputy Speaker, I do not disguise from this House that the combined impact of the tax and benefit changes we make today are tough for people.

That is unavoidable given the scale of the debts our country faces, and the catastrophe that would ensue if we failed to deal with them. My priority in putting together this Budget has been to make sure that the measures are fair.

That all sections of society contribute, but that the richest pay more than the poorest. Not just in terms of cash, but as a proportion of income as well. That is far from straightforward when the deficit is this high and when the burden of reduction must rightly fall on government spending. Too often when countries undertake major consolidations of this kind, it is the poorest – those who had least to do with the cause of the economic misfortunes – who are hit hardest. Perhaps that has been a mistake that our country has made in the past. This coalition government will be different.

We are a progressive alliance governing in the national interest. And that requires us to make two final decisions.

First, we will provide lasting help for pensioners. This earnings link was broken by the last Conservative government and never restored through 13 years of the Labour government. It meant that each year more and more pensioners were drawn into the means test, punishing those who had done the right thing and saved for their retirement.

I can today announce that from April next year we will re-link the basic state pension to earnings. Now pensioners can save with confidence.

They will also be protected by our new triple lock which will guarantee each and every year a rise in the basic state pension in line with earnings, prices or a 2.5 per cent increase – whichever is the greater. There will be no more 75p increases in the basic state pension. With this coalition government pensioners will have the income to live with dignity in retirement.

Second, we will provide additional support to families in poverty. These are among the most vulnerable people in our society and they need our help. I have decided to increase the child element of the child tax credit by £150 above indexation next year. This is a £2 billion a year commitment to low income families. And we make it even now, in these difficult times.

I can tell the House that the policies in this Budget, taken together, will not increase measured child poverty over the next two years. Overall, everyone will pay something, but the people at the bottom of the income scale will pay proportionally less than the people at the top. It is a progressive Budget.

Mr Deputy Speaker. Today we take decisive action to deal with the debts we inherited and confront the greatest economic risk facing our country. We've been tough but we've also been fair.

We have set the course for a balanced budget and falling national debt by the end of this parliament. We have insisted that four pounds of every five needed to reduce our deficit will be found from government spending. We have protected capital investment from additional cuts and got to grips with the soaring costs of welfare. We have provided the foundations for economic recovery in all parts of our nation and given our country some of the most competitive business taxes in the world. We have taken almost a million people out of income tax. Half a million people out of national insurance. And we have done all this without increasing child poverty.

Sadly, with this unavoidable budget we've had to increase taxes. We've had to pay the bills of past irresponsibility.

We've had to relearn the virtue of financial prudence. But in doing so we have ensured that the burden is fairly shared. Today we have paid the debts of a failed past. And laid the foundations for a more prosperous future.

The richest paying the most and the vulnerable protected. That is our approach.

Prosperity for all. That is our goal. And I commend this Budget to the House.

Emergency Budget

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