Budget review

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Bill Dodwell sifts through the detail of last month's Budget

The Chancellor presented his eight Budget on 16 March, with a whirlwind of new measures for businesses and individuals alike. Unlike the first two Budgets of this parliament – which put up taxes and cut spending – this one was fiscally neutral, leaving aside unspecified public spending cuts in 2019/20 and beyond. This article looks at some of the interesting areas.

Property taxes

This Chancellor clearly wishes to increase the burden of property taxation. Economists argue this is less economically damaging than taxes on income. Non-residential and mixed use property gets the same SDLT treatment as residential, with a move to the ‘slice’ basis of taxation, accompanied by an increase in the top rate from 4% to 5%. The break point is just over £1m, meaning lower charges for over 80% of properties but a £500m boost to the Exchequer. More details of the 3% surcharge on second residential properties have come out, with a three year period to replace a main residence (up from 18 months in the original plan). Buyers will still have to fund the extra levy and claim a refund, making it more expensive to bridge. Separating couples will be treated as individuals once it is clear that the separation is likely to be permanent, which may help some buy new properties. There’s no relief at all for joint purchases, though, with 3% being levied on the whole price even where the property is the main residence of one of the buyers. Treasury Ministers obviously haven’t got grown up children who need a parental hand onto the property ladder.

Finally, the UK has worked closely with the Crown Dependencies to shut down a property development structure which allowed an offshore company to claim that UK property development income was exempt from UK corporation tax. The islands have agreed protocols to their tax treaties to allocate taxing rights to the UK.

BEPS

The UK is one of the leading supporters of the G20/OECD Base Erosion and Profit Shifting project – and this Budget produces the first public recognition of the increased corporation tax likely to result. Estimates signed off by the Office of Budget Responsibility suggest the UK will gain £1.3bn annually from outlawing hybrid mismatches, introducing limits on interest deductions and widening royalty definitions and adding a treaty abuse provision. This isn’t the full yield expected from BEPS, as there will be extra corporation tax from the new approach to transfer pricing (where most of the changes are already being applied by tax authorities, including the UK) and the forthcoming changes to permanent establishment (taxable presence) expected from 2017.

Few details of the interest restrictions were released, beyond confirming that the measures will start from 1 April 2017 and that interest payments below £2m will not be affected. The measure follows closely the G20/OECD specification in Action 4, rather than the more restrictive approach put forward to by the European Commission.

The broadening of the definition of royalties subject to withholding tax will take effect from Royal Assent and will bring in payments for the use of trademarks and brands. The UK does have a wide range of double tax treaties, most of which reduce royalty withholding tax to zero. It will be necessary to read the treaty definition, though, to make sure that it covers the actual payment being considered. There’s also a new treaty abuse clause which takes immediate effect, which may apply where payments are made to a treaty country which in turns makes payments to a non-treaty country.

Corporate losses

For losses incurred from 1 April 2017, companies will be able to use carried forward losses against profits from other income streams or from other group companies. However, for profits over £5m, only 50% of profits can be offset by carried forward losses (including those arising before 2017). Whether the overall impact is helpful or not will presumably in part depend on accounting – and whether it will become easier for a group to reflect deferred tax assets for its losses. Large companies engaged in long-term projects may well be the most affected as corporation tax payments are accelerated.

LISA

It is surely likely that one of the longer-lasting announcements of Budget 2016 will be the new Lifetime ISA. This does look remarkably like a re-badged Pensions ISA, since it is aimed at those saving for retirement. The LISA will be available from April 2017 and may only be opened by those aged 18 to 40. Savers may save up to £4,000 annually until age 50 and will receive a bonus of 25%, i.e. to a maximum of £1,000. Funds may be withdrawn without loss of the bonus from 60, or to buy a first home costing up to £450,000. The bonus means that the LISA is remarkably like a registered pension for a basic rate taxpayer, but there are some important differences too. It will be possible to take funds out early from a LISA, subject to a 5% penalty and the loss of bonuses. Further, funds taken at 60 from a LISA will be completely tax-free, unlike a pension, where the funds are taxable, other than the 25% lump sum. The government will also consider allowing investors to withdraw and subsequently replace funds, without charge. A LISA could thus be a useful alternative to a pension for a self-employed person, where government figures suggest that only a third are currently saving for a pension. It could also be a good investment for someone with capital but low income, e.g. a non-working spouse. For employees, it is likely that the employer matching under auto-enrolment or other schemes means that a LISA could be a top-up once employer matching has been exhausted. The final difference is that a LISA will form part of an individual's estate, in contrast to a pension fund. Help-to-Buy ISAs will remain open until 2019 but funds may be transferred to the LISA, which looks like the long-term replacement.

The Chancellor also announced that £20,000 may be invested in a general ISA from April 2017, although amounts invested in the LISA will count towards this limit.

Other investments

Surprisingly, the capital gains tax rates will be cut to 20% and 10% from April 2016. The move will benefit about 180,000 people, at an apparent annual cost of over £500m and looks unusual given that the Chancellor told us in 2010 that 28% was the revenue-maximising rate. However, the rates will remain at 28% and 18% for those realising gains from residential property and for fund managers receiving carried interest. More information will be needed on how losses should be used. Yet more complexity!

There will also be a new entrepreneurs' relief, confusingly also to be called entrepreneurs' relief, but entirely separate from the existing one and not aimed at entrepreneurs. Anyone who subscribes for new shares in an unlisted trading company from 17 March and then holds them for 3 years from 6 April 2016 may realise gains of up to £10m taxed at 10%. There will be some useful changes to the real entrepreneurs' relief, including allowing some joint ventures to resume qualifying for the relief from March 2015.

Employment taxes

A number of announcements are designed to raise substantial amounts in income tax and national insurance from a variety of employment arrangements. HMRC are aware that there are substantial amounts of loans made by arrangements now countered by the disguised remuneration law – but which were made before it took effect. If these loans are not repaid by 2019, a new income tax charge will be levied, which is expected to raise £2.5bn.

Termination payments from April 2018 above £30,000 will become liable to employers’ national insurance contributions. All payments in lieu of notice and certain damages payments will be taxable as earnings and foreign-service relief removed.

Finally, public bodies will be made responsible from April 2017 for assessing the employed/self-employed status of contractors. HMRC believe that many users of personal service companies are not operating PAYE and NIC properly and so will make the engagers responsible for withholding. It remains to be seen whether this is simply a first step and responsibility for withholding will also be extended to the private sector.

Online (and offline) trading

New allowances for the first £1,000 of trading income and the first £1,000 of property income will be introduced from April 2017. Individuals will no longer need to include details on tax returns and those with receipts above £1,000 can benefit by simply deducting the allowance instead of calculating their exact expenses. This sits alongside a package of measures aimed at tackling rapidly growing online VAT evasion. HMRC is strengthening existing VAT legislation for directing overseas businesses that should be registered for VAT in the UK to appoint a UK-established VAT representative and giving HMRC greater flexibility in relation to when it can require some form of security to cover the VAT likely to be payable. HMRC will also be given new powers to make online marketplaces jointly and severally liable for the unpaid VAT of overseas businesses who are non-compliant with UK VAT rules.