Budget 2018

October 2018

TAX IN A NUTSHELL

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HLB HAZLEWOODS
DRIVING LIFELONG PROSPERITY

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Introduction - Phil’s drive for UK prosperity

Before the Chancellor stood up, the thoughts were that, with the Brexit position still uncertain, surely there wouldn’t be much in it. Just over an hour later, all those thoughts had been dispelled.

The UK economy continues to grow, for an eighth consecutive year, whilst debt levels are falling, along with unemployment. As a result of this, Mr Hammond announced that the period of austerity is coming to an end and backed that up with a package of spending, the like of which we have not seen since the Conservatives came into power in 2010.

The NHS will receive an increased budget of £20.5 billion, after inflation, by 2023/24, with £2 billion per year being allocated to mental health. An extra £400 million is being given to schools this year, to help them buy the “little things”, £1 billion more on defence, £30 billion allocated to improve the roads (£420 million specifically for potholes), £1.7 billion to increase existing work allowances in Universal Credit, £650 million for social care and £1.5 billion to help the High Street.

With so much spending, you would think that taxes had to rise and valuable reliefs would be lost, but that doesn’t seem to have happened. In fact, the manifesto pledge of raising the personal allowance to £12,500 and the higher rate threshold to £50,000 is being delivered a year early from 6 April 2019. The annual investment allowance, whereby 100% relief is available on qualifying capital expenditure, is being increased from £200,000 to £1 million for the two years from 1 January 2019.

As always, the devil is in the detail and there were a few nasty surprises.

The period that qualifies for principal private residence relief after you move out is to be reduced again, from 18 months down to 9 months, whilst lettings relief will be reformed to only apply in shared occupancy situations. These measures are to be introduced from April 2020.

An immediate change applies to entrepreneurs’ relief where the individual must be beneficially entitled to 5% of the distributable profits as well as the capital, which has a significant impact on alphabet and growth shares. The qualifying holding period is to be extended from 12 months to 24 months for disposals after 5 April 2019. So, whilst not removing the relief completely, it is now harder to qualify.

Off payroll workers are still very much the target of this government, so the current rules that apply to the public sector (whereby they must decide whether or not to subject the payments made to the contractor to PAYE/NIC) will be extended to the private sector from April 2020, but only for larger companies.

These measures, along with the digital services tax, are expected to generate over £1 billion extra revenues each year, once fully introduced.

The Chancellor is clearly banking on a positive Brexit deal. Whether he ends up regretting his decision to hold the Budget before the conclusion of those negotiations, remains to be seen.

Personal Tax

INCOME TAX

The Chancellor continued his commitment to increase tax thresholds, particularly for the low or average paid worker. The tax free personal allowance will increase to £12,500 in 2019/20 and the basic rate tax band will become £37,500. This means that an individual will not pay higher rate tax (40%, or 32.5% on dividends) until their taxable income is greater than £50,000.

CAPITAL GAINS TAX

At present, where an individual sells their main home, principal private residence relief operates to ensure that the final 18 months of ownership is exempt from capital gains tax, even if the owner has moved out. From 6 April 2020, this period will be halved to 9 months, meaning that vendors will need to sell their previous homes more quickly if tax is to be avoided.

A further existing relief provides a capital gains tax exemption for up to £40,000 of gain (£80,000 for a couple) if the property was a residential let, provided for part of the time it was also the owner's principal private residence. From 6 April 2020, this relief will only apply in the case of shared occupancy, the most common example being where a room, or rooms are let to lodgers.

The announcement of an increase in the capital gains tax-free annual exemption for 2019/20 to £12,000 from £11,700 will be small compensation for the restriction to two valuable reliefs.

UNIVERSAL CREDIT

The amount an individual can receive as universal credits is restricted, depending on the claimant's earnings. The amount above which credits are tapered (the work allowance) will be increased by £1,000 meaning that a claimant can earn more without loss of support. This increase will commence from 6 April 2019.

Pensions and savings

The pre-Budget gloom of pension advisers that tax relief on pensions contributions would be withdrawn, was once again misplaced. A cynic might say it is a way of accelerating pension contributions perhaps.

Instead, all that happened on pensions was that the lifetime allowance for pension savings was increased in line with CPI for 2019-20, rising to £1,055,000.

Tax on savings was also mostly unchanged. The band of savings income that is subject to the 0% starting rate will be kept at its current level of £5,000 for 2019-20 and the adult ISA annual subscription limit for 2019-20 will remain unchanged at £20,000. The annual subscription limit for Junior ISAs and Child Trust Funds for 2019-20 will be increased in line with CPI to £4,368.

Entrepreneurs’ Relief

The fairly innocuous sounding announcement in relation to Entrepreneurs’ Relief (ER) in the Budget speech painted a far simpler picture than that contained in the draft legislation.

Mr Hammond announced that the qualifying ownership period was to be increased from one year to two years from 6 April 2019.

The part that is causing the most concern is the inclusion of the amendments to the definition of ‘personal company’ in the legislation. Any disposals of shares on or after 29 October 2018 will only qualify for ER if the shareholder is beneficially entitled to at least 5% of the distributable profits of the company and at least 5% of the assets available on a winding up. This is in addition to the existing requirement to hold at least 5% of the share capital and 5% of the voting rights.

These changes could cause real problems for companies with different classes of shares with differing dividend rights. If you are affected, we will be in touch shortly.

Business tax changes

ANNUAL INVESTMENT ALLOWANCE

As expected, the Chancellor introduced some tax measures to stimulate investment in UK businesses. The Annual Investment Allowance (AIA), which provides 100% tax relief on capital expenditure, is being increased from £200,000 per annum to £1 million per annum for a two-year period from 1 January 2019. This is estimated to cost the government circa £1.2 billion in the two-year period but as apparently only 1% of businesses exceed the current AIA threshold, this suggests that businesses are expected to accelerate expenditure as a result.

STRUCTURES AND BUILDINGS ALLOWANCES

A new capital allowance (akin to the old industrial buildings allowance) is being introduced to give a 2% capital allowance for qualifying expenditure on structures and buildings incurred from today's date.

SPECIAL WRITING DOWN ALLOWANCE

To pay for the above new allowance, the writing down allowance rate for the special pool of capital allowances (typically long life assets such as property fixtures) will be reduced from 8% to 6%. This is apparently in line with the typical depreciation rate for this type of asset.

FIRST YEAR ALLOWANCES

The 100% first year allowances for energy and water-efficient equipment are being discontinued with effect from April 2020 whilst these allowances for electric charge-points will be extended until April 2023.

NEW INTANGIBLES RELIEF

HMRC has confirmed there will be a reintroduction of some form of tax relief on goodwill acquisition as well as extending the degrouping relief to assets in the intangible assets regime. The draft legislation has not yet been published but the changes are to be effective from 7 November 2018.

NEW CAPITAL LOSS RESTRICTION

Company capital losses will be restricted from April 2020 (in line with the recent restrictions to income losses) such that only 50% of annual capital gains can be sheltered by carried-forward capital losses. This is likely to have a significant impact on large property investment groups who don't qualify for the substantial shareholdings exemption. The £5 million annual allowance which exempts the first £5 million from this 50% restriction will now apply across income and capital losses.

Business tax changes continued

DIGITAL SERVICES TAX

Whilst not relevant to most businesses, as predicted, the Chancellor took action to introduce a new 2% tax on revenues relating to specific digital business activities involving UK users. A business will only be impacted if it has £500+ million global revenues and there are various other tests which will restrict the scope of this tax. On the basis that the government forecast that this will only raise circa £400m per annum this is unlikely to provoke a massive backlash from the Silicon Valley giants!

OTHER CORPORATION TAX CHANGES

Changes are being introduced to catch overseas groups who seek to abuse the ’permanent establishment’ rules in the UK to avoid creating a UK taxable presence. In a similar vein, new measures are to be introduced from April 2019 to charge UK income tax on royalties charged on offshore intellectual property structures (similar to the scheme for UK properties owned by non-resident landlords). There are also various technical changes on hybrid capital instruments and Diverted Profits Tax.

R&D tax credits

The Chancellor announced in his Budget speech that a reform to the 'SME' scheme of R&D tax credits will be made with effect from April 2020. Under the scheme as it currently works, a loss-making company can 'cash in' its R&D tax losses in exchange for a 'payable credit' from HM Revenue and Customs. However, from April 2020, the amount of 'payable credit' that a company can receive under this mechanism will be capped to three times the company's total PAYE and NICs liability for that year.

This restriction is being introduced to help prevent abuses of the scheme. HMRC has apparently identified and prevented attempted frauds on the scheme worth £300 million in total, which involved companies being set up to exploit the payable credit opportunity even though the companies concerned had no legitimate R&D activity and/or little, if any, employment or activity in the UK.

The government acknowledges that some genuine UK R&D companies could be adversely affected by this move. A consultation will therefore be published to consider how to apply the cap to minimise any impact on such businesses.

Businesses that could suffer from this move include, for example, relatively young companies which may outsource their R&D activities to subcontractors and specialists as they may have insufficient resource 'in house'. Such businesses often have limited staff, and the owner managers often take only a small salary (if any) until the business becomes established. In such circumstances, the company's PAYE and NICs liability would be relatively insignificant; even at three times that liability, the capped payable credit would mean that there would be little, if any, cash arising from an R&D tax credits claim.

Although it is proposed that the company could still carry forward unused R&D tax losses to set against future profits (as is already the case), this is unlikely to instil much interest in a young R&D-intensive business in need of immediate cash to survive and grow. It is to be hoped that the consultation will apply some relaxations or exemptions from the cap in such circumstances, such that it is more accurately targeted at abusive cases.

Business rates

The Chancellor announced cuts in business rates to try to help high street businesses.

Bills will be cut by one-third for retail properties with a rateable value of less than £51,000 from April 2019 for a two-year period. The Chancellor estimates that this will benefit up to 90% of retail properties.

A review of the criteria for when self-catering and holiday lets are subject to business rates rather than council tax will also take place. This is to ensure the existing rules are not being exploited by falsely declaring the property is available for let.

Lastly, 100% business rates relief was announced for public lavatories, with the Chancellor joking that local authorities could at last relieve themselves, they shouldn't get bogged down in it and that it was about the only thing in his Budget speech that hadn't been leaked!

Employment taxes

EMPLOYMENT MEASURE – IR35

Off-payroll working rules, usually where individuals provide their services through a personal service company (PSC), are commonly known as the IR35 rules. If such individuals would be regarded as employees, if directly engaged, the amount of tax payable under the IR35 rules should be broadly the same as for those employed directly.

In 2017, reform was introduced to address non-compliance, by shifting responsibility for applying the rules from the individual's PSC to the public sector entity engaging them. This Budget extends this reform to medium-sized and large private sector businesses from April 2020. It is expected to raise £1 billion of extra revenue for the Treasury when it is introduced.

EMPLOYMENT ALLOWANCE

This allowance entitles employers to a reduction of up to £3,000 per annum in their National Insurance bills. This allowance is to be restricted to employers paying less than £100,000 employer's NICs from April 2020.

Charities

Measures to reduce the administrative burden on charities were announced as follows:

a) the upper limit for trading that charities can carry out without incurring a tax liability is to be increased from £5,000 to £8,000 (for charities with turnover of less than £20,000) and from £50,000 to £80,000 (where turnover exceeds £200,000);

b) charity shops using the Retail Gift Aid Scheme will only have to send letters to donors every three years (rather than every year) when their goods raise less than £20 a year; and

a) the individual donation limit under the Gift Aid Small Donations Scheme will be raised to £30. This applies to small collections where it is impractical to obtain a Gift Aid declaration.

Stamp Duty Land Tax (SDLT)

First the good news, Mr Hammond announced an extension to First-Time Buyers Relief to those purchasing properties through a qualifying shared ownership scheme. This will apply to property worth up to £500,000 to mirror the existing rules, but will also apply retrospectively to all purchases on or after 22 November 2017.

Another welcome, albeit minor change, is the extension of the time limit to claim a refund of the higher rate of SDLT where a previous residence is sold after the new one is purchased. Taxpayers will now be able to claim the refund by the later of 12 months from selling the old home and a year from the filing date for the SDLT return for the new home.

Obviously, there cannot be good news for everyone so he also announced a tweak to the rules relating to the definition of higher rate transactions where purchasers must pay the additional 3% SDLT. The rules will now also apply to 'undivided' shares in a major interest in a dwelling.

VAT

REGISTRATION AND DEREGISTRATION THRESHOLDS

Once the terms of the EU exit are clear, the government will continue to consider ways of removing the ’cliff edge’ impact of VAT registration, but in the meantime will maintain the registration threshold at the current level of £85,000 at least until April 2022.

Similarly, the deregistration threshold remains at £83,000.

VOUCHERS

Following consultation, the government will legislate in Finance Bill 2018-19 to implement EU legislation which ensures that the correct amount of VAT is charged on what the customer pays, irrespective of whether payment is with a voucher or other means of payment.

VAT GROUPING

The government will legislate in Finance Bill 2018-19 to extend the eligibility to join a VAT group to certain non-corporate entities with effect from 1 April 2019. In addition, revised VAT grouping guidance will be issued to:

- amend the definition of ‘bought in services’ to ensure that such services are subject to UK VAT; and
- provide clarity to businesses on HMRC’s protection of revenue powers and treatment of UK fixed establishments.

TACKLING VAT EVASION:

1. Fraud in the provision of labour in the construction sector

With effect from 1 October 2019, and as announced at the Autumn Budget 2017, the government will introduce a VAT domestic reverse charge to prevent VAT losses through so-called ‘Missing Trader’ fraud. This occurs when traders collect VAT on their sales but go missing before passing that VAT on to HMRC. This will shift responsibility for paying VAT along the supply chain to remove the opportunity for it to be stolen by those traders. The government is publishing secondary legislation alongside the Budget to implement this change.

2. Online sales – ’split payment’ model

Under a ’split payment’ model, the VAT element of the customer’s payment would be deposited directly with HMRC rather than being collected by the supplier. Following the consultation launched in the spring, the government is publishing its response, and will establish an Industry Working Group to address some of the main challenges associated with this policy through close cooperation with stakeholders.

And finally………………..

VAT continued

Making Tax Digital (MTD) implementation

As there were no announcements in the Budget, it must be presumed that MTD implementation is to proceed as planned from 1 April 2019 for those businesses with turnover above the VAT threshold, subject to a delay of six months to 1 October 2019 for certain “more complex” businesses.

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