Budget 2017 analysis

March 2017

MAKING THE COMPLEX SIMPLE

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DRIVING LIFELONG PROSPERITY

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Introduction

HAMMOND EGGS ON THE ECONOMY

Philip Hammond's first, and last, Spring Budget was big on laughs (at Jeremy Corbyn's expense) but, as widely predicted, small on anything else. At a time of economic uncertainty with Brexit, now was perhaps not the time for anything radical, which was clearly the Chancellor's view.

The Office for Budget Responsibility (OBR) upgraded the growth forecast for 2016/17 from 1.4% to 2.0% and Mr Hammond took great satisfaction in pointing out the UK's growth is stronger than USA, Japan and France and is second only to Germany. The OBR also predicts a slowdown in growth for 2017/18 of 1.6%, rising steadily until it hits 2.0% again in 2021/22. A more conservative view on the economy's growth prospects is also not particularly surprising.

Annual borrowing is to be £51.7bn in 2016/17, £16.4bn lower than forecast, with forecasts of an increase to £58.3bn in 2017/18, £40.6bn in 2018/19, £21.4bn in 2019/20 and £20.6bn in 2020/21.

Public sector net borrowing forecast is to fall from 3.8% of GDP last year to 2.6% this year, then 2.9%, 1.9%, 1% and 0.9% in subsequent years, reaching 0.7% in 2020/21.

Social Care, which was much talked about in the lead up to the Budget, was given a boost with £2bn extra funding over the next three years, with £1bn available in 2017/18 to allow local authorities to create new care packages. With an extra two million over 75's in ten years' time, funding was necessary but the question is whether or not this amount is sufficient.

It is hoped that the funding for Social Care will reduce the pressure on the NHS, which received a further £325m investment for the local Sustainability and Transformation Plans and £100m to Accident and Emergency departments to reduce waiting times.

Investment was also announced for education and skills, with maintenance loans for those attending technical courses at National Colleges and Institutes of Technology, like those available for University students. It was also announced that 110 new free schools would be created, on top of the 500 already announced. Free transport will be available for children entitled to free school meals, to their closest selective school (between two and 15 miles away).

The question is how to pay for these measures? National insurance for self-employed individuals will increase by 1% to 10% in 2018 and to 11% in 2019, but there is to be no increase to the rate of 2% that applies above the basic rate band, which allowed many of the self-employed to breathe a sigh of relief

The dividend allowance of £5,000, only introduced in April 2016, is to be reduced to £2,000, to counter the supposed tax benefits of operating as a limited company, from 2018. This is predicted to raise over £800m per year once introduced. Despite this, there are still opportunities to structure remuneration efficiently.

The personal allowance is to increase to £11,500 and the higher rate band to £45,000, all part of the government's commitment to hit £12,500 and £50,000 respectively by the end of parliament.

There was some relief for smaller businesses, with a deferral in their Making Tax Digital requirements for a year, meaning those with turnover under the VAT threshold don't have to worry about it until 2019. It seems as though the exemption limit of £10,000 turnover will, however, remain in place.

Introduction continued

Businesses also were helped with £435m to support those affected by the business rates relief revaluation. Any business coming out of small business rates relief will pay no more than £600 extra in business rates than they did in 2016/17, with a further £300m provided to local authorities for discretionary relief.

So pretty much a “let’s not rock the boat” Budget, until some clarity is achieved on what Brexit will look like (we may have a couple more of these then!). With a second Budget due in November as we transition to Autumn Budget, it may be that Mr Hammond spends more time on his “Corbyn joke book” than he does on fiddling with the UK’s economy.

Tax free dividend allowance cut already

Budget 2015 brought in a £5,000 tax free dividend allowance with effect from 6 April 2016.

In an attempt to reduce the estimated loss to the Exchequer of £6 billion as a result of business incorporations, the tax free allowance will be cut to £2,000, just two years after its introduction, commencing 6 April 2018. Most affected will be owner managed businesses, where higher rate taxpayers can anticipate an increase in personal tax of £975 per annum.

Business rates

There was a lot of pre-Budget speculation that the Chancellor would try to address some of the problems arising for small businesses due to the business rate rises due to come in from April this year. Three measures were announced as follows:

1. Businesses that lose their entitlement to some or all of their Small Business Rates Relief (which reduces or eliminates their rates) will be given transitional relief such that their rates increases will be capped at £50 per month.
2. Pubs with a rateable value below £100,000 will get a discount of £1,000 on their rates bill for 2017/18.
3. Local authorities will be given a fund of £300 million to give discretionary relief for individual hard hit businesses in their locality.

These measures are not particularly far reaching. They are unlikely to silence the voices criticising the disproportionate impact of the rates rises between both the north and the south of the country and the online versus high street businesses.

National insurance changes for the self-employed

The gap between the amount of national insurance paid by the self-employed and that paid by those who are employed is to be narrowed. The logic is that pensions rights have been aligned but it is acknowledged that the self-employed do not have access to other state benefits enjoyed by employees such as sick pay and maternity/paternity benefits.

Historically the self-employed paid Class 2 and Class 4 national insurance payments but it had already been announced that Class 2 national insurance would be abolished from April 2018. This alone would have increased the national insurance gap between the employed and self-employed. The Chancellor has now announced that Class 4 national insurance between the lower profits limit (£8,060 in 2016/17) and the upper profits limit (£43,000 in 2016/17) will increase from 9% to 10% from April 2018 and then from 10% to 11% from April 2019. This compares with 12% Class 1 national insurance paid by those who are employed.

An increase was anticipated prior to the Budget but with no change in national insurance above the higher rate threshold, the announcement was not as bad as it could have been.

The net financial impact of these measures is a cost of £215m per year for 2019/20 and 2020/21 falling to £145m from 2021/22 as announced by the Chancellor.

VAT Update

REGISTRATION AND DEREGISTRATION THRESHOLDS

From 1 April 2017 the VAT registration threshold will increase from £83,000 to £85,000 and the deregistration threshold from £81,000 to £83,000.

USE AND ENJOYMENT PROVISIONS FOR BUSINESS TO CONSUMER (B2C) MOBILE PHONE SERVICES

From 1 August 2017 the government will remove the VAT "use and enjoyment" provisions for business to consumer mobile phone services to individuals. This will resolve the inconsistency where UK VAT is applied to mobile phone use by UK residents when in the EU, but not when outside the EU (UK VAT will thus now be applied on all mobile phone use by UK residents). It will also ensure mobile phone companies cannot use the inconsistency to avoid UK VAT. This will bring UK VAT rules into line with the internationally agreed approach.

TACKLING VAT EVASION - FRAUD IN THE PROVISION OF LABOUR IN THE CONSTRUCTION SECTOR

Later this month, the government is to begin a consultation on options to combat missing trader VAT fraud in the provision of labour in the construction sector, in particular, the option of applying the reverse charge mechanism so that the recipient accounts for VAT. It will also consider other changes including to the qualifying criteria for gross payment status within the Construction Industry Scheme.

TACKLING VAT EVASION – "SPLIT PAYMENT" MODEL FOR ONLINE SALES

Building on the measures introduced in Budget 2016, the government will call for evidence later this month on the case for introducing a new VAT collection mechanism for online sales. This would allow VAT to be extracted directly by the Exchequer from online transactions at the point of purchase (thus the buyer pays the net element of the purchase price to the supplier and the VAT element to the government). This is often referred to as a "'split payment'" model. This is the next step in tackling non-payment of VAT by some overseas traders selling goods online to UK consumers.

TACKLING VAT EVASION - PENALTY CHARGES IN FRAUD CASES

As announced in the Autumn Statement 2016, the government will legislate in Finance Bill 2017 to introduce a penalty for participating in VAT fraud. Following consultation on the draft legislation, some minor changes have been made to improve the clarity of the measure and also to limit the naming of a company officer to instances where the amount of tax due exceeds £25,000. The new penalty will take effect once the Finance Bill receives Royal Assent.

'MAKING TAX DIGITAL' IMPLEMENTATION

The legislation to implement digital record keeping to be included in Finance Bill 2017 will include powers to make regulations, including on the form and content of periodic updates and 'end of period statements'. There are also powers to set out the scope and operation of certain exemptions. Following consultation, the legislation published in draft on 31 January 2017 has been revised and expanded to introduce a clause amending Schedule 11 to the Value Added Tax Act 1994, to enable equivalent regulations and exemptions for VAT purposes to those proposed for Income Tax.

Making Tax Digital for business

Plans to bring businesses into a modern online digital reporting environment have already been well publicised, although the short timeframe for small businesses has been widely criticised. Spring Budget 2017 has announced a deferral of registration for small businesses by one year. The revised timetable is as follows:

- April 2018 for businesses with turnover in excess of the VAT threshold (£85,000 from 1 April 2017) chargeable to income tax and Class 4 national insurance
- April 2019 for businesses that have turnover below the VAT threshold chargeable to income tax and Class 4 national insurance
- April 2019 for VAT reporting if registered and pay VAT
- April 2020 for entities chargeable to corporation tax

Although a deferral for small businesses is welcome, it falls short of a full exemption for micro-businesses. There is an exemption if turnover is less than £10,000 per year, although employed individuals with secondary income of greater than £10,000 per year will be required to register.

The proposals for Making Tax Digital for Business will bring in legislative changes so that businesses will have a prescribed method of keeping records digitally, filing quarterly data and an obligation to finalise the accounts within 10 months of the fourth quarter. For VAT, the quarterly reporting will effectively replace the traditional VAT return.

Parliament believes this will provide taxpayers with more up to date and relevant information regarding their tax liabilities and reduce errors by 10%.

Appropriations to trading stock

Today's Budget saw the introduction of a measure to alter the way in which companies are taxed when fixed assets are taken into trading stock. Until today the appropriation of a capital asset to trading stock was treated as taking place at market value meaning a chargeable gain or an allowable loss could arise. To counter the problem of tax becoming payable on an asset that might not have been sold, an election could be made which had the effect of reducing the chargeable gain or allowable loss to zero, and rebasing the asset for subsequent calculation of trading profits.

The changes introduced today will mean that the legislation will only permit this election to be made where the appropriation into trading stock gives rise to a chargeable gain and not where it gives rise to an allowable loss. Previously it was possible to effectively convert capital losses, that can only be used against chargeable gains, into more flexible trading losses. This measure, whilst in a less travelled area of corporation tax legislation, is indicative of the Treasury's continuing efforts to block what is perceived as tax avoidance.

Watch out for PILONs

Payments in Lieu of Notice (PILONs) have, in some cases, provided the opportunity for a leaving employee to receive substantial exemptions from tax and national insurance contributions (NIC). Reforms to be legislated in the 2017 Finance Bill will prevent all PILONs from avoiding taxation whether they are contractual or not, and also require that employees' basic pay be taxed if they do not work their notice period.

Parallel NIC legislation will align with income tax treatment for termination payments over £30,000, so that tax and employer's NIC will be due. Termination payments excluding PILONs under £30,000 will continue to be exempt from both tax and national insurance.

Cleansing of mixed funds for non-domiciles

It was announced in Budget 2015 that new rules to deem individuals domiciled for all UK tax purposes would be effective from 6 April 2017. To provide some transition for individuals caught by these provisions, a one year opportunity to 'cleanse' offshore mixed funds was provided.

A mixed fund arises where amounts are invested in offshore assets or accounts that derive from multiple sources of income or gains, and/or multiple tax years. Generally, where a non-domiciliary, who has used the remittance basis, sends money to the UK from a mixed fund, it is taxed at the highest rates first, leaving the non-taxable capital amounts as the last to be remitted.

'Cleansing' allows the individual to transfer amounts from the mixed fund to another account, and nominate what type and amount of income, gain or capital that transfer will comprise. Previously, the proposal would only give a one year window to make the transfer and election, but this has extended to two years, being 2016/17 and 2017/18. Parliament has gone further to allow the nomination to include any income, gains or capital arising prior to 2007/8, whereas previously it was anticipated that these old years would be blocked.

Stamp Duty Land Tax

After quite a few changes to the SDLT regime, this Budget, thankfully, only made one slight tweak. Previously, it was announced that the payment date was to be shortened from 30 days to 14 days after the tax point (completion or substantial performance), to take effect from April 2017. This has now been deferred until April 2018.

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