JULY 2015 BUDGET

SUMMARY IMPACT

The key announcements by The Chancellor of The Exchequer are outlined below.

PENSIONS

Annual allowance

- The standard annual allowance in 2016/2017 will be £40,000.
- The money purchase annual allowance in 2016/2017 will be £10,000. It applies to those who have accessed their pensions flexibly, including by 'flexi-access drawdown' or 'uncrystallised funds pension lump sums' and received any income.
- The annual allowance for high earners will be reduced to between £10,000 and £40,000 from April 2016.

Higher earners tapered annual allowance

- The reduced annual allowance will affect those with both 'adjusted income' of more than £150,000 and 'net income' of more than £110,000.
- ‘Adjusted income’ includes employer and employee pension contributions. ‘Net income’ excludes pension contributions, unless paid under a salary exchange (also known as salary sacrifice) agreement, set up on or after 9 July 2015. This is to prevent tax avoidance. Where adjusted income and net income exceed the respective thresholds, the taxpayer's annual allowance will be reduced by £1 for every £2 of adjusted income in excess of £150,000. The maximum reduction is £30,000, which would result in an annual allowance of £10,000. The level of adjusted income at which the maximum reduction in the annual allowance is reached is £210,000.
- All 'pension input periods' will be aligned with the tax year from 2016/2017, with no option to vary the period. The Government will consider at a later date if this can be simplified further by removing pension input periods altogether. Currently, the option to vary a pension input period is used in planning to maximise pension contributions.
- The alignment of pension input periods with the tax year will be achieved by ending all open periods on 8 July 2015. A further pension input period will then cover the period from 9 July 2015 to 5 April 2016. To ensure no tax charges arise against those who had fully funded their pensions in advance of the Budget, the total annual allowance for this tax year will be increased to £80,000, only £40,000 of which is available to cover pension input amounts paid after the Budget.
- ‘Carry forward‘ of unused annual allowances from the three previous tax years will be available as normal, but will be based on the tapered annual allowance rather than the standard annual allowance.
- The money purchase annual allowance of £10,000 will still be available, however, taxpayers who are affected by both the money purchase annual allowance and the tapered annual allowance will retain the £10,000 money purchase annual allowance but will suffer a reduced annual allowance for funding non-money purchase schemes.

Lifetime allowance (LTA)

- The LTA will reduce to £1 million for 2016/2017 and 2017/2018. There will be a new round of transitional protection to protect those with large pension pots, however, we still await the detail on this.
- The LTA will then be index-linked in line with the consumer prices index (CPI) from 2018/2019.
- As a reminder, those who want to apply for Individual Protection 2014 must do so online by 5 April 2017. This protection is available following the previous reduction in the LTA from £1.5 million to £1.25 million.

Tax relief

- Other than for higher earners as noted above, there's no change to the rate of tax relief for member contributions.

Pension tax relief reform

- The Chancellor said he was 'open to further radical change' in the pension industry. A Green Paper/Consultation has been announced which will look into possible new radical approaches such as ISA-style pensions where people would lose the tax relief when they pay in, but would be able to take their money out tax free. More subtle changes will also be considered, such as further adjustments to the annual or lifetime allowances. Responses are due by 30 September 2015.

Extension of Freedom and Choice agenda to existing annuitants

- The ability to sell annuities in payment is being deferred for a year, from April 2016 to 2017. This is in line with industry calls for it to be introduced over a more sensible timescale. The Government will set out its plans for the secondary annuities market in the autumn.

Lump sum death benefits

- The change in taxation of lump sum death benefits for members who die aged 75 or over was confirmed. Currently a temporary flat rate tax of 45% is applied. From 2016/2017 this rate will reduce to the beneficiary's rate of income tax.
- As expected, where payments are made to a discretionary trust the rate of tax will remain at 45%.

Pension transfers

- The Government plans to consult shortly on pension transfers. It wants to make the process quicker and smoother and to look at excessive penalties. The aim is to ensure people can access the new pension flexibilities easily and without excessive costs.

IMPACT

- Those who had paid less than £80,000 between 6 April 2015 and 8 July 2015 can make further contributions without exceeding the annual allowance. The maximum contribution that can be made without an annual allowance tax charge arising, is the amount of the unused £80,000 annual allowance for the tax year, up to a maximum of £40,000 plus carry forward of unused annual allowance from the three previous tax years.
- A similar opportunity is available in this tax year for those who were already subject to the £10,000 money purchase annual allowance on 8 July 2015. Those individuals may now be able to contribute up to a further £10,000 to a defined contribution (also known as money purchase) scheme without triggering a money purchase annual allowance tax charge.
- Higher rate taxpayers with adjusted income below £150,000 or net income below £110,000 will still benefit from higher rate relief on contributions of up to £40,000 a year. With further potential restrictions to tax relief being considered, those with sufficient funds could consider funding sooner rather than later while full tax relief is still available.
- The reduction in the Lifetime Allowance to £1 million from 6 April 2016 will greatly widen the scope of those within the restrictions. While the introduction of index-linking from April 2018 is welcome, it's far short of a return to the £1.8 million LTA in place in 2011/2012 which itself was originally intended to rise in line with inflation.
- The delay in the implementation of the secondary annuity market to 2017 will be welcome as it gives more time for providers and advisers to ensure they are fully prepared for any changes.

CORPORATE NEWS

CORPORATION TAX

- The corporation tax rate will be cut from 20% to 19% in 2017 and then to 18% in 2020.
- For accounting periods starting on or after 1 April 2017, corporation tax payment dates will be brought forward for companies with annual taxable profits of £20 million or more. This threshold will be divided by the number of companies in a group. These companies will pay corporation tax in quarterly instalments in the third, sixth, ninth and twelfth months of their accounting period.
- The permanent level of the Annual Investment Allowance (AIA) will increase from £25,000 to £200,000 for all qualifying investment in plant and machinery made on or after 1 January 2016.

IMPACT

- Companies may consider making employer pension contributions before the lower rates of corporation tax reduce the effective rate of tax relief available.

DIVIDENDS

- From April 2016, the current 10% dividend tax credit will be abolished. It will be replaced with a new £5,000 a year dividend tax allowance.
- The new rates of tax on dividend income above the allowance will be:
    - 7.5% for basic rate taxpayers
    - 32.5% for higher rate taxpayers
    - 38.1% for additional rate taxpayers.

IMPACT

- The Government's stated intention is for these reforms to reduce the incentive to incorporate and remunerate through dividends. The tapered annual allowance for those with incomes including pension contributions of over £150,000 will also apply from April 2016. In addition, it won't be possible for companies where a single director is the sole employee to claim the National Insurance employment allowance. There will be considerably less scope to use dividends and employer pension contributions to maximise tax efficient director's remuneration in future. Companies with undistributed profits should consider taking advantage of the last chance to make the most of these strategies before the end of the current tax year.

NATIONAL INSURANCE

Employment allowance

- The £2,000 National Insurance employment allowance, which reduces the overall cost of employer National Insurance Contributions (NICs) for employers will increase from £2,000 to £3,000 from April 2016. From the same date, companies where the sole employee is the director will no longer be able to claim this allowance.

Salary exchange

- Salary exchange (also known as salary sacrifice) schemes are used to reduce the amount of employee and employer NICs. Whilst there were no changes to salary exchange the Government noted that these arrangements are becoming increasingly popular and so increasingly costly to the tax payer. The Government stated that it will actively monitor the growth of schemes and the impact on tax receipts.

IMPACT

- The removal of the employment allowance for companies where a single director is the sole employee, along with the changes to dividend taxation, significantly reduces the tax efficient remuneration planning advantages of incorporating.
- The increase in the employment allowance, along with the reduction in corporation tax, will provide some help for employers dealing with the cost of the increase in the national minimum wage for employees aged 25 and over from April 2016.
- As automatic enrolment continues to roll out, employers and employees are looking for ways to reduce the net cost of pension contributions. Salary exchange arrangements, where an employee opts to give up salary in exchange for a higher employer pension contribution, still offer NICs savings for both employees and employers.

NATIONAL MINIMUM WAGE

- From April 2016, those aged 25 and over will benefit from an increased rate of £7.20 an hour, branded as the National Living Wage.
- In the meantime, the current rates shown below will increase to the rates shown in brackets from 1st October 2015, as previously announced:
- £6.50 (£6.70) per hour - main rate for workers aged 21 and over.
- £5.13 (£5.30) per hour - workers aged 18 to 20.
- £3.79 (£3.87) per hour - workers aged under 18 and above school leaving age.
- £2.73 (£3.30) per hour - apprentice rate for apprentices under 19 or 19+ and in the first year.

IMPACT

- The increase in the national minimum wage for employees aged 25 and over will lead to increased costs for many employers, which will be partially offset by the increased National Insurance employment allowance and the reduction in corporation tax.
- Remember the minimum wage when planning with salary / dividend / pension profit extraction and salary exchange / sacrifice.

TAX EFFICIENT INVESTMENTS

SEIS, EIS and VCTs

- The Government announced a range of essentially more restrictive technical changes to the rules governing investments eligible for Venture Capital Trusts (VCTs) and Enterprise Investment Schemes (EISs).

IMPACT

- The changes to the EIS and VCT rules may make it more difficult for mature businesses in particular to raise funds to support growth.

INDIVIDUAL NEWS

DIVIDENDS

- From April 2016, the current 10% dividend tax credit will be abolished. It will be replaced with a new £5,000 a year dividend tax allowance.
- The new rates of tax on dividend income above the allowance will be:
    - 7.5% for basic rate taxpayers
    - 32.5% for higher rate taxpayers
    - 38.1% for additional rate taxpayers.

IMPACT

- Higher rate and additional rate taxpayers with modest dividend income from share/OEIC portfolios will welcome the change, with a potential saving of up to £1,250 a year for a higher rate tax payer, compared to now.

INCOME TAX

Personal allowance and higher rate threshold

- In 2016/2017 the income tax personal allowance will see another substantial increase of £400 to £11,000. A further increase to £11,200 was announced for 2017/2018.
- The basic rate band increases to £32,000 for 2016/2017. Those entitled to the full standard personal allowance will pay 40% tax on income above £43,000. The threshold for higher rate income tax increases by £615 for 2016/2017.
- The basic rate limit will increase to £32,400 for 2017/2018. Together with the planned increases in the personal allowance, this means the higher rate threshold will be £43,600 for 2017/2018. These are the next steps in the Chancellor's stated aim of increasing the higher rate threshold to £50,000.

Property letting

- The tax relief on mortgage interest will be restricted to basic rate for mortgages on 'buy to let' residential properties. The restriction will be phased in over 4 years from April 2017.
- ‘Rent a room’ relief will be increased from £4,250 to £7,500 from April 2016. The relief had been frozen since 1997.

IMPACT

- Higher rate taxpayers will welcome the further increases in the higher rate threshold, however, the rates from 2016/2017 and 2017/2018 are still a long way off the Chancellor's stated aim of a £50,000 higher rate threshold. In the meantime pension contributions benefiting from higher rate relief remain an attractive savings option.
- A further substantial increase in the personal allowance means that higher earners can achieve even greater benefit

by using pension contributions to reduce adjusted net income above £100,000. For someone with gross income of £122,000 a pension contribution of £22,000 will cost just £8,800 in 2016/2017, attracting tax relief of 60%.

- Mixed news for property lettings. Those who rent out a room will welcome the increase in the tax free allowance to £7,500. However, the loss of higher rate relief on mortgage interest may impact the property market. High earners with mortgaged property portfolios will see a substantial increase in costs over time.

TAX EFFICIENT INVESTMENTS

ISAs

- The 'Help to Buy' ISA will be available from 1 December 2015. This new product will enable first time buyers to save up to £200 per month towards a first home, with an initial one-off deposit of £1,000. The Government will boost savings by 25% up to a maximum of £3,000, which will be paid when a property is purchased.
- The Government confirmed its commitment to introduce new flexible ISA rules from 6 April 2016. The rules will allow investors to pay withdrawals from a cash ISA back in to the account before the end of the tax year, without reducing their subscription limit further. The change will also cover cash held in stocks and shares ISAs.
- The Government will introduce the 'Innovative Finance' ISA, for loans arranged via a peer to peer platform, from 6 April 2016. It is also consulting on whether to extend the list of ISA eligible investments to include debt securities and equity offered via a crowd funding platform.

Personal savings allowance

- From 6 April 2016, a tax-free savings allowance of £1,000 will be available to those with taxable income of less than £43,000 i.e. basic-rate payers and below. Higher rate taxpayers benefit from a £500 tax-free allowance. Those earning over £150,000 are not entitled to an allowance.

IMPACT

- 'Help to Buy' ISAs are sure to boost the property market further alongside other initiatives such as the initial 'Help to Buy' scheme.
- The personal savings allowance provides more incentive for savers with even higher rate taxpayers benefiting from an allowance. However, it's most generous for low earners who will potentially pay no tax on their savings where total taxable income is less than £17,000 in 2016/2017. This has increased from £16,800 when originally announced, as a result of the further increase in the personal allowance to £11,000
- New flexible ISA rules allowing cash withdrawals to be returned to an ISA by the end of the tax year will help to maximise the benefits by removing an effective penalty on those who are forced to access their savings temporarily.

CAPITAL GAINS TAX (CGT)

- No changes were announced with individuals continuing to be entitled to an annual exempt amount of £11,100 for 2015/2016 and trustees to a maximum of £5,550.
- The 18% and 28% rates of capital gains tax remain, as does the interaction with the amount of the taxpayer's unused basic rate income tax band (if any) to determine at which rate tax will be paid. The potential exists to reduce the rate at which a gain is charged to CGT by extending the basic rate income tax band by making a pension contribution.
- Since 6 April 2015, non-residents disposing of UK residential property will face a CGT charge on gains realised on or after that date. Only the amount of the overall gain relating to the period from 6 April 2015 is chargeable to tax. HMRC needs to be informed within 30 days of the sale being completed.

INHERITANCE TAX (IHT) AND TRUSTS

- The Government aims to reduce the number of estates paying IHT by introducing an additional nil-rate band from April 2017. This will apply where the main residence passes on death to direct descendants such as children and grandchildren. This will be worth up to £100,000 in 2017/2018, £125,000 in 2018/2019, £150,000 in 2019/2020 and £175,000 in 2020/2021 with CPI indexation applying thereafter. As with the existing nil-rate band, any unused nil-rate band will be able to be claimed on the death of their surviving spouse or civil partner. Those with net estates worth more than £2 million will see the additional nil-rate band scaled back by £1 for every £2 over this threshold. Consultation will be published in September 2015 with details of how the additional nil-rate band will apply to those who have downsized or ceased to own a home on or after 8 July 2015.
- The IHT nil-rate band is currently frozen at £325,000 until 5 April 2018 and this will continue to apply until April 2021.
- The Summer Finance Bill will include new legislation targeting IHT avoidance through the use of multiple trust arrangements and to simplify the calculation of trust charges.

IMPACT

- As widely expected, the headline measure removes the family home from the IHT net for all but the wealthiest homeowners although the maximum benefit of £1m won't be available until tax year 2020/2021 due to phasing of the allowance.
- Those with larger estates will still need advice on steps they can take to mitigate IHT.
- The specific measure affecting trusts restricts the ability to gain an advantage of multiple nil-rate bands through setting up a series of trusts. It will still be possible to place property in trust up to the nil-rate band every seven years.

NON-DOMICILES

- From April 2017 foreign domiciles who have been long term resident in the UK - more than 15 of the past 20 tax years will be deemed to be UK domiciled for taxation purposes. This will mean they will no longer be able to use the remittance basis of taxation and will be subject to tax on a worldwide basis on their income and gains. They will also be deemed domiciled for IHT purposes – bringing forward the point at which IHT applies to their worldwide assets from the current period of 17 out of the past 20 years ending in the year of transfer.
- It will no longer be possible for individuals born in the UK to UK domiciled parents to leave the UK, claim non-domicile status then return to the UK and continue to claim non-domicile status for tax purposes.
- The Government also intends to introduce new rules from April 2017 to ensure IHT is payable on all UK residential property owned by non-domiciles regardless of their residence status.
- Consultation documents on the above measures will be published later in the year.

WELFARE REFORMS

- Working-age benefits, including tax credits and Local Housing Allowance, will be frozen for 4 years from 2016/2017.
- The freeze doesn’t include Maternity Allowance, statutory maternity pay, statutory paternity pay and statutory sick pay.
- The household benefit cap will be reduced to £20,000 (£23,000 in London).
- Support through Child Tax Credit will be limited to 2 children for children born from April 2017.

- Those aged 18 to 21 who are on Universal Credit will have to apply for an apprenticeship or traineeship, gain work-based skills, or go on a work placement 6 months after the start of their claim.
- Rents for social housing will be reduced by 1% a year for 4 years, and tenants on higher incomes (over £40,000 in London and over £30,000 outside London) will be required to pay market rate, or near market rate, rents.

Every care has been taken to ensure that this information is correct and in accordance with our understanding of the law and HM Revenue & Customs practice, which may change. However, independent confirmation should be obtained before acting or refraining from acting in reliance upon the information given. This information is based on announcements made in the July 2015 Budget which may change before becoming law.

SCOTTISH WIDOWS

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