JOHN LAMB
FINANCIAL PLANNING

Insights

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INTRODUCTION

The backdrop to this year's Spring Budget was the better than expected economic growth to date but with measured concern for the future – given the uncertainty over what our post-Brexit world will look like.

Given the movement this year to an Autumn Budget followed by a Spring Statement (focused on responding to the forecast from the Office for Budget Responsibility) most commentators expected there to be little change to personal and corporate tax or pensions in this last Spring Budget and thought consideration of these sorts of changes would be deferred to the first Autumn Budget later this year.

And they were largely right – but there were some (notable) exceptions:-

- The reduction of the tax free dividend allowance from £5,000 to £2,000 from 6 April 2018
- Fundamental changes to QROPS
- Confirmation that the reduction in the Money Purchase Annual Allowance will be implemented from 6 April 2017
- More activity to combat aggressive tax avoidance
- Confirmation that the corporation tax rate will reduce to 17% from 1 April 2020

In what follows the income tax and NIC figures for 2017/18 have been included in full and are those announced in the 2016 Autumn Statement. In the remainder of the Bulletin we cover new changes announced in the Budget which are of relevance to financial services.

INCOME TAX

1. Rates of tax 2017/18

(i) The limit for the starting rate for savings income remains at £5,000 and the rate of tax on income in this band is held at zero.

(ii) The basic rate of income tax remains at 20%. The basic rate limit increases to £33,500 so that the higher rate tax threshold [ie. the basic rate limit (£33,500) plus the basic personal allowance (£11,500)] becomes £45,000. In Scotland, the higher rate tax threshold for earnings and rental income remains at £43,000.

(iii) The basic rate of tax will apply to taxable income in the band £1 to £33,500. Dividends in excess of the dividend allowance will be taxed at 7.5% for basic rate taxpayers. Taxable income in excess of £33,500 will be taxed at 40% or 32.5% (for dividends) up to the threshold of £150,000 when the additional rate of tax applies.

(iv) The additional rate of tax (which applies to taxable income in excess of £150,000) is 45% (38.1% for dividends).

(v) Trustees of discretionary trusts are subject to income tax at 45% (38.1% on dividend income) on income above their standard rate band (normally £1,000).

2. Personal allowances 2017/18

- The personal allowance increases from £11,000 to £11,500. Where an individual's adjusted net income exceeds £100,000, the level of the basic personal allowance will be reduced by £1 for each £2 over £100,000 until it reaches zero. This means that the basic personal allowance will reduce to zero where adjusted net income is £123,000 or more. The personal allowance of £11,500 is now the same for everyone regardless of their age.

- The married couple's allowance (MCA), which is only available provided at least one spouse was born before 6 April 1935, is increased to £8,445. There is a reduction in the MCA of £1 for every £2 additional income in excess of the total income threshold which is increased to £28,000. The MCA will not reduce below £3,260 (the "minimum amount") increased from £3,220.

- Relief in respect of the MCA and maintenance payments continues to be given as a tax reduction at the rate of 10%.

- Spouses and registered civil partners will be entitled to transfer £1,150 of their personal allowance (called the "marriage allowance") to their spouse or registered civil partner provided that after the transfer neither spouse pays tax at above the basic rate.

3. The Personal Savings Allowance

The personal savings allowance (PSA) began in 2016/17 and is unchanged for 2017/18. Broadly speaking, this means that if an individual is a:

- *basic rate taxpayer*, the first £1,000 of savings income will be untaxed;

- *higher rate taxpayer*, the first £500 of savings income will be untaxed;

- *additional rate taxpayer*, they will not receive any personal savings allowance.

'Savings income' in this instance is primarily interest, but also includes gains made on offshore investment bonds and UK investment bonds. Although called an allowance, the PSA is actually a nil rate tax band so it is not quite as generous as it seems. Since the introduction of the PSA, banks and building societies no longer deduct tax from interest and nor does National Savings & Investments. As previously announced, from 2017/18 the removal of the requirement to deduct tax on interest payments is extended to open-ended investment companies, authorised unit trusts, investment trust companies and peer-to-peer loan arrangements.

4. The Dividend Allowance

The £5,000 annual dividend allowance began in 2016/17 and is maintained at this level for 2017/18 (but see below). It was part of a reform of dividend taxation, ultimately designed to raise more revenue. The main target was private company shareholders who use dividends rather than salary to extract profits and thereby avoid National Insurance contributions.

The allowance means that the first £5,000 of dividends received in a tax year are not subject to tax, regardless of the investor's marginal tax rate.
Like the personal savings allowance, the dividend allowance is in reality a nil rate band, so up to £5,000 of dividends will not disappear from tax calculations, even though they are taxed at 0%.

Budget announcements

- **Dividend allowance**

The dividend allowance will reduce by 60% to £2,000 from 2018/19. This was the big surprise – and the largest revenue-raiser announced in the Budget. While the cut will marginally reduce the advantages of incorporation, it will by no means eliminate them – most small business owners will be £225 worse off because the dividend allowance that they lose will fall into their basic rate band. However, the dividend allowance cut does not just hit small businesses; it will also hit some investors.

The arrival of the dividend allowance in April last year created winners and losers. The forthcoming reduction will only create losers – anyone with more than £2,000 of dividend income. For example, a portfolio of UK shares worth more than about £60,000 will provide over £2,000 of dividend income, based on the current UK stock market average dividend yield of about 3.45%.

The effects of the two changes are shown in the table below.

Taxpayer **(Dividend rate)**	**Worse off than in 2015/16 if dividends exceed**		**Maximum extra tax in 2018/19 compared to 2016/17**
	2016	**2017**	
Basic 7.5%	£5,000	£2,000	£225
Higher 32.5%	£21,667	£8,667	£975
Additional 38.1%	£25,250	£10,100	£1,143

- **Rent-a-room relief**

  The Government will consult on proposals to redesign rent-a-room relief to ensure it is better targeted to support long-term lodgings. Consultation will start in the Summer. The previously announced consultation on employer-provided accommodation, employee business expenses and the taxation of benefits in kind will begin on 20 March 2017.

- **Disguised remuneration**

  Consultation on tackling disguised remuneration avoidance schemes will start later in 2017.

NATIONAL INSURANCE CONTRIBUTIONS

The Upper Earnings and Upper Profits Limits (beyond which employee NICs are charged at 2%) for 2017/18 increase from £43,000 to £45,000, in line with the higher rate tax threshold.

The main rates for 2017/18 are as follows:-

- The Employee's Primary Class 1 National Insurance rate is 12% on earnings between the Primary Threshold (£157 per week - £8,164 pa) and Upper Earnings Limit (£866 per week - £45,000 pa).

- Employees, in addition, pay 2% Primary Class 1 National Insurance on all earnings above the Upper Earnings Limit (£45,000 pa).

- The Employer's Secondary Class 1 contribution rate on earnings above the Secondary Threshold (£157 per week - £8,164 pa) is 13.8%. This rate applies also to Class 1A and Class 1B contributions.

- The self-employed Class 4 rate on profits between the Lower Profits Limit (£8,164 pa) and Upper Profits Limit (£45,000 pa) is 9% and 2% above £45,000.

Budget announcements

- It was announced that the main rate of Class 4 National Insurance contributions paid by the self-employed would increase by 1% to 10% from April 2018, and by a further 1% to 11% from April 2019. This change would have reduced the gap in rates paid by the self-employed and employees, and would have recognised the fact that the self-employed will have the same access to the new State Pension as employed persons. However, in a swift U-turn this proposal was dropped and National Insurance contribution rates will not be changed for at least the duration of this Parliament.

- HMRC is monitoring National Insurance Employment Allowance compliance as some businesses are using avoidance schemes to avoid paying the correct amount of NICs.

CAPITAL GAINS TAX

Budget announcements

- For 2017/18 the annual exempt amount is increased to £11,300 for individuals and £5,650 for trustees (subject to dilution when the same settlor has created more than one trust).

- The lifetime limit on gains qualifying for capital gains tax (CGT) entrepreneurs' relief remains at £10 million as does the 10% rate of CGT for such gains.

- For individuals, the rate of CGT remains at 10% where total taxable gains and income are less than the basic rate limit (£33,500 or the extended basic rate limit). Gains above this will continue to be taxed at 20%. For trustees and personal representatives of deceased persons, the rate of CGT remains at 20%. A 28% (higher rate) and 18% (basic rate) rates will continue to apply to chargeable gains on residential property, for example buy-to-let properties, and carried interest (carried interest is a share of any investment fund profits that the general partners of private equity and hedge funds receive).

- In the 2016 Autumn Statement, the government announced that it would consult on the options for bringing non-UK resident companies, who are currently chargeable to income tax on their UK taxable income, and capital gains tax on certain gains, within the scope of corporation tax. This would broadly mean that these companies would then be subject to the rules which apply generally for the purposes of corporation tax, including the limitation to corporate interest expense deductibility and loss relief rules. This consultation began on 20 March 2017 as announced on 8 March.

The following sections highlight new changes announced in the Budget.

INHERITANCE TAX

There were no new announcements in the Spring Budget 2017.

A change taking place from 2017/18 sees the introduction of the dedicated residence nil rate band (RNRB). The RNRB starts at £100,000 and goes up by £25,000 each year until it reaches £175,000 by April 2020. It is available where the second death occurs on or after 6 April 2017.

Under another change, effective from 6 April 2017, UK residential property owned by a non-UK domiciled individual through an offshore company will be subject to inheritance tax.

SAVINGS AND INVESTMENTS

Changes to the ISA subscription limits were fixed in the 2016 Autumn Statement at £20,000 for the general ISA and £4,128 for the JISA and Child Trust Fund Account. No new announcements were made.

Some highly technical amendments will be made to the EIS, SEIS and VCT rules which clarify aspects of the rules and increase flexibility and certainty.

LIFE POLICY TAXATION

As announced at Autumn Statement 2016 and confirmed at Spring Budget 2017, the government will legislate in Finance Bill 2017 to change the current tax rules for part surrenders and part assignments of life assurance policies to allow policyholders who have generated a wholly disproportionate gain to apply to HMRC to have the gain recalculated on a just and reasonable basis.

Following consultation, the legislation has been revised to clarify who can apply and when; and how the recalculation is given effect. These changes will have effect from Royal Assent of Finance Bill 2017 and not 6 April 2017 as announced in the 2016 Autumn Statement.

PENSIONS

- **MPAA reduces to £4,000 from 6 April 2017**

The Chancellor confirmed that the government has seen no grounds to change its view on reducing the Money Purchase Annual Allowance (MPAA) from £10,000 to £4,000. A government response to the consultation was published on 20 March 2017 as announced in the Budget. The level of the MPAA will therefore be set at £4,000 with effect from 6 April 2017.

- **Overseas transfer charge**

Some significant changes to the Qualifying Recognised Overseas Pension Schemes (QROPS) regime were announced in the 2016 Autumn Statement so the Budget announcement came as a complete surprise. Although the changes announced do have wide reaching implications, it is fair to say that the government has actually changed the focus of QROPS transfers to that which was originally intended – individuals leaving the UK permanently and taking their pension savings with them.

The new overseas transfer charge of 25% will apply to transfers from a UK registered pension scheme to QROPS or QROPS to QROPS transfers requested (a substantive request to transfer to X not just a casual enquiry) on or after 9 March 2017.
The overseas transfer charge will not apply if:

- The QROPS and the individual are resident in the same country.
- The individual and the QROPS are both resident in the same country within the EEA plus Gibraltar.
- The QROPS is an occupational pension scheme and the individual is an employee of a sponsoring employer under the scheme.
- The QROPS is an overseas public service scheme and the individual is employed by an employer that participates in that scheme.
- The QROPS is a pension scheme of an international organisation and the individual is employed by that international organisation.

The overseas transfer charge works as follows:

The transfer payment made to a QROPS is still a Benefit Crystallisation Event No 8 (BCE8). This has the function of testing the transfer against the standard lifetime allowance or the individual's higher lifetime allowance if, for example, they have elected for transitional protection. The BCE8 will subject the excess over the lifetime allowance to a lifetime allowance excess charge of 25%.

The overseas transfer charge of 25% is then applied to the residual fund.

Example

- Fred successfully elected for Fixed Protection 2014 so has a lifetime allowance of £1.5m.
- He has a pension fund valued at £1.7m.
- He is UK resident but wants to transfer his fund to a QROPS in the Isle of Man which is not within the EEA plus Gibraltar.
- The BCE 8 means the £200,000 in excess of the lifetime allowance will be subject to a tax charge of £50,000.
- The overseas transfer charge will be made on £1.65m @25% = £412,500 leaving funds to transfer of £1,237,500.
- Total tax charge to transfer is £462,500

If the charge applies, the scheme administrator and individual are jointly and severally liable.

The transfer charge applies to all pension rights including pension credit rights, beneficiary's scheme pension/drawdown/flexi-access drawdown which will include nominees and successor's rights. Although these funds do not suffer a BCE8 test, if the overseas transfer charge applies a flat rate charge of 25% will be deducted from these funds on transfer.

There is also now a five year rule – this means that although the overseas transfer charge may not have been due on the original transfer, any change - for example change of residence - means that the charge becomes due for up to five full tax years (known as the relevant periods) after the date of transfer. In addition, should an exemption apply within the first five full tax years following the transfer a refund of the charge can be made.

All QROPS scheme managers as at 8 March 2017 must decide if they want their scheme to operate the overseas transfer charge and, if so, must submit a revised undertaking to HMRC by 13 April 2017. Any QROPS who fail to submit the undertaking will automatically cease being a QROPS from 14 April 2017. Therefore, from 14 April 2017 HMRC will suspend the ROPS notifications list and publish an updated list on 18 April 2017.

EMPLOYEE BENEFITS

The government is considering how the tax treatment of the various forms of employee remuneration could be made fairer and more coherent, including the taxation of benefits in kind and employee expenses. In addition to the measures previously announced and due to be introduced from this and next year the following consultations were announced in the Budget:

- **Taxation of benefits in kind**

The government will publish a call for evidence on exemptions and valuation methodology for the income tax and employer NICs treatment of benefits in kind, in order to better understand whether their use in the tax system can be made fairer and more consistent.

- **Accommodation benefits**

The government will publish a consultation with proposals to bring the tax treatment of employer-provided accommodation and board and lodgings up to date. This will include proposals for when accommodation should be exempt from tax and to support taxpayers during any transition.

- **Employee expenses**

The government will publish a call for evidence to better understand the use of the income tax relief for employees' expenses, including those that are not reimbursed by their employer.

CORPORATION AND BUSINESS TAX

- **Corporation tax will fall to 17% in 2020**

The government has confirmed that the corporation tax rate will reduce to 19% on 1 April 2017 and that it will reduce further to 17% for the Financial Year commencing 1 April 2020.

- **Research and development (R&D) tax review**

The Industrial Strategy green paper sets out the government's ambition to drive up the level of private investment in science, research and innovation across the economy. The review of the R&D tax regime has found that the UK's R&D tax credits regime is an effective and internationally competitive element of the government's support for innovation. To further support investment, the government will make administrative changes to the Research and Development Expenditure Credit to increase the certainty and simplicity around claims and will take action to improve awareness of R&D tax credits among SMEs. The government will continue to keep the competitiveness of the UK environment for R&D under review to ensure that the UK is profoundly pro-innovation.

- **Patient capital review**

This review aims to ensure that high growth businesses can access the long-term capital that they need to fund productivity enhancing investment. Alongside identifying barriers to institutional investment in long-term finance, the review will also consider existing tax reliefs aimed at encouraging investment and entrepreneurship to make sure that they are effective, well targeted and provide value for money.

- **Withholding tax on interest**

In order to encourage investment in the UK and make it easier for businesses to raise finance, the government will:

- renew and extend the administrative simplifications of the Double Taxation Treaty Passport scheme to assist foreign lenders and UK borrowers. This scheme simplifies access to reduced withholding tax rates on interest that are available within the UK's tax treaties with other countries

- introduce an exemption from withholding tax for interest on debt traded on a Multilateral Trading Facility, removing a barrier to the development of UK debt markets. The government will consult in Spring 2017 on implementation of the exemption

- **Tax treatment of appropriations of trading stock**

As announced at Spring Budget 2017, the government will legislate in Finance Bill 2017 to remove the ability of businesses with loss-making capital assets to obtain an unfair tax advantage by converting those losses into more flexible trading losses. The changes will take immediate effect from 8 March 2017.

PROPERTY TAX

- **Offshore property developers –** The government will amend legislation to ensure that all profits realised by offshore property developers developing land in the UK, including those on pre-existing contracts, are subject to tax, with effect from 8 March 2017.

- **Rent-a-room relief –** The government will consult on proposals to redesign rent-a-room relief to ensure it is better targeted to support longer-term lettings. The aim of the consultation is to align the relief more closely with its intended purpose which is to increase the supply of affordable long-term lodgings.

- **Stamp Duty Land Tax –** As a result of consultation, the government will delay the reduction in the Stamp Duty Land Tax filing and payment window (from 30 days to 14 days), until after April 2018.

- **Making Tax Digital** - The government has announced a one-year deferral (until April 2019) from the mandating of Making Tax Digital for Business (MTDfB) for unincorporated businesses and landlords with turnovers below the VAT threshold. This means that only those businesses, self-employed people and landlords with turnovers in excess of the VAT threshold with profits chargeable to income tax and that pay Class 4 NICs will be required to start using the new digital service from April 2018. Landlords with turnovers under £10,000 are exempt from these requirements.

- **Tax simplification –** Following consultation, the government will increase the cash basis entry threshold to £150,000, and exit threshold to £300,000, and will extend the use of the cash basis to unincorporated landlords. The government will also simplify the rules on capital and revenue expenditure within the cash basis, to make it easier for businesses to work out whether their expenditure is deductible for tax – see also the tax simplification and administration section later.

TAX AVOIDANCE AND EVASION

Avoidance

- **Promoters of Tax Avoidance Schemes (POTAS): associated and successor entities rules**

Apparently some promoters of tax avoidance schemes have been seeking to circumvent the POTAS regime by re-organising their business by sharing control of a promoting business or putting a pension between them and the promoting business.

Changes to the POTAS legislation were introduced in Finance Act 2015 to ensure promoters cannot use associated and successor entities to circumvent the legislation. This measure will ensure these associated and successor entities rules function as intended.

Legislation will be introduced in Finance Bill 2017 to amend the control definitions in paragraph 13A of Schedule 34 to Finance Act 2014. These amendments introduce the term 'significant influence' to ensure promoters cannot reorganise their business so that they put a person or persons between themselves and the promoting business. The amendment also ensures that the control definitions apply where 2 or more persons together have control or significant influence over a business.

- **Strengthening tax avoidance sanctions and deterrents**

As announced at Autumn Statement 2016, the government will introduce a new penalty for a person who has enabled another person or business to use a tax avoidance arrangement that is later defeated by HMRC. This new regime reflects an extensive consultation and input from stakeholders. The government will also remove the defence of having relied on non-independent advice as taking 'reasonable care' when considering penalties for a person or business that uses such arrangements.

- **Tax treatment of appropriations to trading stock**

The government will remove the ability for businesses to convert capital losses into trading losses from 8 March 2017. This will eliminate an unfairness in the tax code which is being exploited by certain businesses.

- **VAT: Use and enjoyment provisions for business to consumer mobile phone services**

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. 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.

Evasion

- **VAT: Fraud in the provision of labour in the construction sector**

The government will consult on options to combat missing trader VAT fraud in the provision of labour in the construction sector, in particular, applying the reverse charge mechanism so the recipient accounts for VAT.

- **VAT: 'Split Payment' model**
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Some overseas traders avoid paying UK VAT, undercutting online and high street retailers and abusing the trust of UK consumers who purchase goods via online marketplaces. Building on the measures introduced in Budget 2016, the government will shortly publish a call for evidence on the case for a new VAT collection mechanism for online sales. This would harness technology to allow VAT to be extracted directly by the Exchequer from online transactions at the point of purchase. This is often referred to as a 'Split Payment' model.

This is the next step in tackling the non-payment of VAT by some overseas traders selling goods online to UK consumers.

TAX SIMPLIFICATION AND TAX ADMINISTRATION

Overview

The importance of the government's 'Making Tax Digital' initiative cannot be underestimated. There are some important objectives underpinning this initiative:

- simplifying the 'tax return' process will signal the end of the annual tax return process for millions

- making it easier for individuals and businesses to get their tax right and to keep on top of their affairs and, inevitably

- increasing compliance and cash flow for HMRC.

Digital administration

The government will provide an extra year, until April 2019, before Making Tax Digital is mandated for unincorporated businesses and landlords with turnover below the VAT threshold. This will give them more time to prepare for digital record keeping and quarterly updates. The government will also consult on the design aspects of the tax administration system, including interest and penalties, with the aim of adopting a consistent approach across taxes. This will simplify the system for taxpayers.

Tax simplification

Following consultation, the government will increase the cash basis entry threshold to £150,000, and exit threshold to £300,000, and will extend the use of the cash basis to unincorporated landlords. The government will also simplify the rules on capital and revenue expenditure within the cash basis, to make it easier for businesses to work out whether their expenditure is deductible for tax.

HMRC large business risk review

HMRC will work constructively with businesses and interested parties to consult over the Summer on its process for risk profiling large businesses and promoting stronger compliance.

DOMICILE AND RESIDENCE

Nothing new was announced presumably because major changes already come into effect from 6 April 2017. The main change is that non-UK domiciled individuals will be deemed UK domiciled for all tax purposes after they have been UK resident for 15 of the past 20 tax years.

INCOME WITHDRAWAL RATE FOR APRIL 2017

The appropriate gilt yield, used to determine the 'relevant annuity rate' from HMRC's tables for an adult member commencing income withdrawals (or reaching an income withdrawal review date), in April 2017 is 2.0%.

As usual, the contents of this Bulletin are based solely on the proposals put forward by the Chancellor in his March 2017 Budget and need to be approached with caution as details may change during the passage of the Finance Bill through Parliament