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Summer Budget Newsletter – July 2015

This was the first Budget of a single party Conservative government for almost twenty years and, as such, it was a particularly political Budget.

One of the main themes in the Chancellor's speech involved a supposed move away from a high tax, high benefits system towards lower benefits and, hence, lower taxes. However, that is not necessarily borne out in the actual figures.

For example, increases in the dividend rate of tax and the insurance premium tax are estimated to bring in an additional £2.0 billion and £1.5 billion per annum respectively.

Overall, there is a planned tax increase in the order of £47 billion over the next five years. The general level of cuts is also not on the scale which was originally expected, being phased in more slowly and at a lower absolute level than previously suggested.

From a business perspective there was some good news, including a reduction in the main rate of corporation tax from the already low level of 20% to a new low of 19% in 2017 and then 18% in 2020. This is the lowest rate of corporation tax in the G20 and may well raise eyebrows abroad; increasing the attractiveness of the UK as a base for large international companies and having something of the appearance of a corporate tax haven.

On the flip side, the introduction of a compulsory living wage is not necessarily going to be popular with many businesses where staff costs are often the largest component of their cost base. The Chancellor said that "Britain deserves a pay rise" but this is not something which one would normally associate with a Conservative government. This will hit certain industries more harshly than others e.g. the care home sector, and may also form part of a wider policy to transfer the burden of supporting the low paid from welfare budgets to employers.

There were popularist changes to the taxation of non-domiciled individuals and a very modest increase in the point at which the 40% tax band kicks in. However, there was no reduction in the top rate of 45% income tax, an increase in dividend tax rates and a reduction in pensions relief for people with high earnings.

Whilst there was the well trailed proposal to introduce an inheritance tax ("IHT") allowance linked to family homes, this becomes less positive news when the fine detail is read. As will be seen in the more detailed notes below, this new relief will be phased in over four years and withdrawn for estates in excess of £2 million. In addition, the normal IHT nil rate band is now frozen until 2021 and will not have increased since 2009!

There is a sense, both in the broad analysis and also in some of the fine detail, that this was a Budget which was carefully calculated to reward, or appear to reward, many of the middle ground supporters of this newly elected Government whereas those who will benefit least are those who, for one reason or another, may not be inclined to complain too loudly.

In short, this was a complex and at times confusing Budget; designed to please many but difficult to unpick and work out who the real winners and losers might be. Maybe that was the point!

Some of the highlights of the proposals for private individuals are set out below.

- The personal allowance is to rise to £11,200 in 2017/18 (currently £10,600).
- The 40% tax rate threshold will rise very modestly to £43,600 in 2017 (currently £42,385).
- With effect from April 2016, individuals earning in excess of £150,000 will have a tapering off of their annual pensions allowance from £40,000 to £10,000.

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- There will be an additional IHT nil rate band where the family home is passed on death to the individual's children or grandchildren. This will be phased in, starting at £100,000 per individual (i.e. £200,000 per couple) in 2017 and increasing in stages to £175,000 in 2020. There will be measures to take into account "downsizing" of properties but there will be a tapered withdrawal of the relief for estates in excess of £2 million. It is unclear at this stage whether the additional nil rate band will be available where the property is left in trust rather than to children/grandchildren outright. The existing IHT nil rate band will remain at the level it has already been at for 6 years (i.e. £325,000 per individual) until 2021 (an increase was previously expected in 2019).

- The new dividend rates of tax will be 7.5%, 32.5% and 38.1% for basic, higher and top rate taxpayers respectively with effect from April 2016. Those at the bottom end may pay less tax (there will be a £5,000 exemption) whilst many of those with either large investment portfolios or receiving significant dividends from private companies will pay significantly more. Perhaps the measure is primarily targeted at those who choose to extract profits from private companies in the form of dividends rather than salaries/bonuses. The effective rate of tax for a top rate taxpayer will increase from circa 30% today to 38%.

- Mortgage interest on buy to let properties will only attract tax relief at the basic rate (20%). This is to be phased in from 2017. The annual wear and tear allowance is also to be replaced by a system whereby only actual costs incurred will be deductible.

- With effect from April 2017, non-UK domiciled individuals will be deemed to be UK domiciled for all tax purposes once they have been UK resident for 15 years. This radically changes the income tax and capital gains tax position of long term UK resident but non-domiciled individuals and will be a huge blow to some. It also brings forward the point at which an individual is deemed to be domiciled in the UK for IHT purposes (currently this only happens after 17 years of residence).

- A child born to a non-UK domiciled individual living in the UK will still acquire the legal non-domiciled status of their father at birth. However, whilst the child will not automatically be UK domiciled, after 2017 they will of course be deemed to be UK domiciled for tax purposes as soon as they have lived in the UK for 15 years.

- The current levels of the charge which a non-UK domiciled individual pays in order to be able to claim the remittance basis of taxation remain unchanged at £30,000, £60,000 and £90,000 after periods of residence of 7, 12 and 17 years respectively. However, after 2017 when a non-domiciled individual will be treated as UK domiciled after 15 years or residence, the £90,000 charge will naturally fall away.

- It appears that offshore trusts established by non-UK domiciled individuals before they become deemed domiciled at the 15 year mark will broadly retain their IHT, income tax and capital gains tax advantages.

- With effect from April 2017, if UK residential property is held through an offshore company, for IHT purposes the owner will be treated as holding a UK asset rather than an overseas asset (shares in the company). This will affect the IHT position of non-UK domiciled individuals (resident and non-resident) owning property through a corporate envelope. It will also affect the IHT position of trusts established by non-UK domiciled individuals which will often own UK property via an offshore company. This is the latest in a long line of attacks on UK residential property held through offshore companies and finally addresses the main reason why so many valuable UK properties are held by offshore companies.

If you would like to discuss any of these changes, please get in touch with your usual contact at Meridian.

Jon Croxford
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