BUDGET BRIEFING

The Crisis Budget

March 2020

This will be remembered as the Budget when Boris Johnson's government overturned 40 years of orthodoxy in government finances to open the floodgates of public spending to deal with the urgent Coronavirus pandemic crisis, and to announce massive new infrastructure projects. There were however few significant tax changes to move the headlines away from these main themes.

To deal with the economic effects of the Coronavirus crisis, on the morning of the Budget the Bank of England had announced an emergency interest rate cut to 0.25%, the joint lowest rate since the creation of the Bank in 1694, together with substantial changes to stimulate lending, especially to small businesses. The new Chancellor, Rishi Sunak, followed this up with the announcement of a £12 billion "temporary, timely and targeted" plan to provide Coronavirus pandemic support to individuals and small businesses, with an additional £18 billion to be raised from wider policy measures, but with no support for large companies nor national chains. The government is therefore optimistically assuming that large companies will be able to cope with the effects of the pandemic. However, the nature of the support provided to smaller companies and individuals assumes that the retail, leisure, travel and hospitality sectors will effectively shut down for a period during the pandemic, and that 20% of all employees will be off work at its peak.

If the government's alarming assumptions are correct, then all businesses, both small and large, as well as individuals and society as a whole will face some very tough challenges ahead. So while the Chancellor's provision of financial support to individuals and small businesses during the pandemic is greatly welcomed, financial support may also be required for large businesses operating in the retail, leisure, travel and hospitality sectors, but potentially those in other sectors as well.

"Getting Things Done"

Apart from the Coronavirus measures, the other major theme of the Budget was "Getting Things Done", a slogan that was inspired by the popular Conservative Party election campaign slogan "Get Brexit Done" credited to Boris Johnson's chief adviser, Dominic Cummings. This more than hinted at the close involvement of Cummings in this Budget, a situation made possible by the abrupt resignation of the previous Chancellor, Sajid Javid, only four weeks ago.

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RAWLINSON & HUNTER

“Getting Things Done” denoted Johnson’s and Cummings’ determination to release the tight constraints imposed on government spending first introduced by Margaret Thatcher’s government in 1979, and adhered to by every government since. This shift was hinted at when the Chancellor announced that he had reconsidered the government’s fiscal framework “to allow us to make the right long-term decisions for our economic security and prosperity”. However, the extent of the policy change became clear with the announcement of a massive £175 billion increase in public expenditure on infrastructure projects over the next five years.

The most controversial tax measure in the Budget was not mentioned in the Chancellor’s speech, but was instead included in a single paragraph in the Budget Red Book. This was confirmation of the introduction, from 1 April 2020, of the 2% digital services tax on big tech multinationals like Facebook, Google, eBay and Apple. This new tax is controversial because it is the subject of an ongoing diplomatic row with the US government: in February, Steven Mnuchin, the US treasury secretary, said that the UK would “find themselves faced with President Trump’s tariffs” unless they shelved their digital tax. He said, “We think the digital tax is discriminatory...if people want to just arbitrarily put taxes on our digital companies we will consider arbitrarily putting taxes on their car companies… I’m sure the President and Boris will be speaking on it as well.”

Perhaps the biggest change to personal taxes in the Budget was to Entrepreneurs’ Relief, which reduces the capital gains tax liability on the disposal of certain businesses or shares in personal trading companies. With effect from Budget Day, the lifetime limit on gains was reduced from £10 million to £1 million. There are also new anti-avoidance provisions designed to negate planning which had looked to “bank” Entrepreneurs’ Relief before Budget Day for use at the time of a later disposal.

A 2% stamp duty surcharge on non-UK resident individuals and companies who purchase residential property in England and Northern Ireland was announced with effect from 1 April 2021, a policy that was originally announced by former Prime Minister Theresa May in 2018 at the rate of 1%. The top rate of stamp duty will now be 17% in certain circumstances, disappointing those who believed Mr Johnson’s pledge during his Conservative leadership campaign last summer to reduce stamp duty rates.

The Chancellor took the opportunity to correct potential weaknesses in his tax collection machinery as exposed by recent tax cases. In a move relevant to those with interests in LLPs, including taxpayers who have previously invested in film partnerships, HMRC are to protect their ability to issue tax assessments by providing that LLPs are treated as general partnerships under income tax rules. He also announced what has been dubbed a “Del-Boy” tax, by making the renewal of licences to drive taxis, drive minicabs and to deal in scrap metal conditional on applicants completing detailed checks to confirm that they are appropriately registered for tax. A cashless economy therefore moves ever closer.

In a victory for faceless bureaucracy, and also with retrospective effect, HMRC are to legislate to confirm that certain statutory notices issued by an HMRC computer have the same force as if signed by an individual inspector. Hector the Inspector, the original friendly face of HMRC who hung up his bowler hat in 2001, will be turning in his grave!

The Chancellor also confirmed that the off-payroll working rules would apply to payments made for services provided to medium and large sector businesses on or after 6 April 2020. HMRC is however providing a variety of resources to assist in determining whether the off-payroll working rules apply to workers, including new interactive online guidance that will be made available this summer. However, this will provide scant comfort to many self-employed workers as the law surrounding their tax status continues to be complex and nuanced, with decisions often turning on points of fine detail. Given the Coronavirus pandemic and the challenges that this presents to self-employed workers in particular, 6 April 2020 appears to be the worst possible time to introduce these new rules.

As the Conservative Party had pledged not to increase rates in their election manifesto, it was a quiet Budget for changes to tax rates. The capital gains tax annual exempt amount is to rise to £12,300 for 2020/21, and the threshold at which employees pay NICs is to rise to £9,500 from April 2020. Pension changes were largely restricted to increases to income thresholds for calculating the tapered annual allowance. This was done to solve the issue with NHS GPs and consultants refusing to work extra shifts, or retiring early, due to unexpected tax bills arising on their pension contributions, a particularly unfortunate problem during a pandemic.

If the Budget had no real tax headlines, it had one great mystery: how would the Chancellor pay for the huge spending commitments he had outlined? According to the Office for Budget Responsibility the answer is higher borrowing. Taxpayers should however be very concerned that the longer term answer will inevitably lead to higher tax rates.

A. Coronavirus Pandemic Measures

The government's "coordinated, coherent and comprehensive" three-pronged attack against the Coronavirus pandemic will be through supporting public services, individuals and businesses.

From the public services perspective, aside from a £5 billion Coronavirus response fund for the NHS and local authorities, the government has committed hundreds of millions to finance domestic vaccine research and development efforts, as well as diagnostic testing and surveillance.

In an attempt to mitigate the impact of financial loss for those infected employees who will be unable to work, the government has committed to accelerating the payment of Statutory Sick Pay (SSP) – it will now become payable from Day 1 of sickness or self-isolation absence, with the ability for the employee to obtain a sick note over the telephone.

To mitigate the effect of financial disruption from the anticipated loss of productivity through employee sickness, reduced consumer demand and therefore restricted cash flow for businesses, the government has announced a number of measures including:

- Providing a refund of two weeks' of SSP paid per eligible employee to certain smaller businesses (with fewer than 250 employees);
- Abolishing business rates for the qualifying smaller businesses in the retail, leisure and hospitality sectors with an extra £5,000 afforded to pubs;
- Introducing the Coronavirus Business Interruption Loan Scheme to ensure lenders can still provide loans and overdrafts to those businesses in need; and
- Affording extra time to both businesses and individuals to settle their tax liabilities, and committing to waiving penalties and late payment interest.

B. Personal Taxation

Entrepreneurs' Relief - going, going…but not yet gone

Entrepreneurs' Relief was introduced on 6 April 2008 as a successor to Business Asset Taper Relief. It provided relief on chargeable gains up to a lifetime limit of £1 million on qualifying business assets. By 6 April 2011, this limit had been increased to a generous £10 million.

Following the announcement in the Budget, the lifetime limit has been reduced to the original £1 million for disposals made on or after 11 March 2020. This limit will take account of disposals made prior to 11 March 2020.

It had been thought that Entrepreneurs' Relief would be abolished completely, but it still survives, albeit at a much reduced level than that available before the Budget. HMRC noted that Entrepreneurs' Relief claimants tended to be "older, male, of above-average means" and included individuals who are retiring (and will not therefore go on to create new businesses). The lower limit of the relief is expected to encourage "genuine risk takers and entrepreneurs", but it remains to be seen whether the changes will impact on serial entrepreneurs who are likely to make gains significantly higher than the new £1 million lifetime limit.

Anti-forestalling measures have also been announced, which seek to prevent the use of unconditional contracts or a specific capital gains tax election relating to the exchange of shares and securities to "lock in" the £10 million lifetime limit available for disposals made prior to 11 March 2020.

Unconditional contracts

Under normal capital gains tax rules, the date of disposal under an unconditional contract is the date the contract is made, and not the date when it is completed (ie when the asset is actually transferred). However, under the anti-forestalling rules, the date of disposal for an unconditional contract entered into before 11 March 2020 will instead be the date the asset is transferred, when the lower Entrepreneurs' lifetime limit will apply.

This rule is subject to two exclusions:

I. Where the parties to the contract are not connected, and the seller can show that the contract was not entered into in order to take advantage of the normal rules relating to the date of disposal noted above.

II. Where the parties to the contract are connected, and the seller can show that the contract was entered into for wholly commercial reasons, and was not entered into in order to take advantage of the normal rules relating to the date of disposal noted above.

In each case, if the relevant requirements are met, the full £10 million lifetime limit will still be available. However, the claimant must submit a statement confirming this is the case together with the claim.

Exchange of securities

Generally, where there is an exchange of shares or securities as part of a company reorganisation, the CGT rules do not treat the "paper for paper" exchange as a disposal of the original shares or securities. Instead, the transaction is treated as taking place on a no gain no loss basis.

However, there is a specific CGT election which can be made to disapply the normal rules. This election is usually made in cases where the original disposal would qualify for Entrepreneurs' Relief but a disposal of the new shares or securities would not.

The anti-forestalling rules will apply where there has been an exchange of shares or securities in Company A for those in Company B on or after 6 April 2019, but before 11 March 2020, and either;

I. The persons holding the shares or securities / controlling Company A immediately before the exchange are substantially the same as those holding the shares or securities / controlling Company B immediately after the exchange; or

II. Immediately after the exchange the relevant shareholders holding the shares or securities in Company B hold a greater percentage of the ordinary share capital in Company B than they did in Company A and the individual claiming Entrepreneurs' Relief meets certain conditions (broadly that they hold 5% of the share capital, voting rights, dividend entitlement and entitlement to assets on a winding up, and they are an employee or director of the company or a company in the same trading group).

In either case, if an election is made, the amount of Entrepreneurs' Relief will be calculated by reference to the lower £1 million limit.

Finally, HMRC have confirmed that in cases of uncertainty about the application of the new anti-forestalling rules, an application can be made for Non-Statutory Clearance.

Tax rates

There were minimal changes to the rates and thresholds for Income and Capital Gains Tax.

The Income Tax Personal Allowance for 2020/21 is unchanged at £12,500, and this will continue to be removed on a tapered basis for individuals with income in excess of £100,000. The 20% Basic Rate Income Tax Band remains unchanged at £37,500, as does the Savings Rate Band of £5,000. The 45% additional rate of income tax is also unaltered and will apply for individuals with income exceeding £150,000.

There has been an increase in the Capital Gains Tax annual exemption to £12,300 (an increase of £300 from the previous year). The rate of Capital Gains Tax is unchanged at 20% for higher/additional rate tax payers, with the continuing exception of gains relating to residential property or carried interest, which are taxed at 28%.

There have been increases to the thresholds for the payment of Class 1 National Insurance (by employees) Class 4 National Insurance (for partners and the self-employed). Respectively, these limits are known as the "Primary Threshold" and the "Lower Profits Limit", and both of these thresholds have increased to £9,500 per year. This is the government's first step in meeting its aim of eventually increasing these thresholds to the same level as the Income Tax Personal Allowance, at £12,500.

The adult ISA subscription limit is unchanged at £20,000 for 2019/20. However, the Junior ISA allowance has more than doubled from £4,368 to £9,000.

Tapered annual allowance for pensions

Although there is no limit placed on how much an individual can theoretically save or accrue in a registered pension scheme, there is an annual limit on the amount of an individual's tax-relieved annual pension savings or accrual (including employer contributions) in any one year, known as the Annual Allowance. The maximum Annual Allowance is £40,000, but any unused Annual Allowance from the three previous tax years can also be carried forward and added to the current Annual Allowance. Where an the individual's pension savings for the tax year exceed the total available allowance for the year, including any unused relief carried forward, the Annual Allowance tax charge will be applied to the excess.

For those on the highest incomes, the Annual Allowance is restricted, and tapers down from £40,000.

The tapered Annual Allowance is currently triggered when both the threshold income (i.e. income before tax, excluding pension savings) and the adjusted income (i.e. income before tax, including pension savings) exceed their designated limits. Where this applies, the £40,000 Annual Allowance is reduced by £1 for every £2 that the adjusted income exceeds £150,000, to a minimum Annual Allowance of £10,000.

The tapered Annual Allowance has given rise to some significant and, on occasion, unexpected tax charges which, by election, have generally been borne by pension fund trustees leading to a corresponding reduction in the pension benefits available to the individual on retirement. For example, as has been widely reported in the press, the Government has been concerned about the impact of the tapered Annual Allowance on the NHS and the retention of hospital consultants.

In a move designed to address this issue, particularly in the NHS, the two tapering Annual Allowance thresholds will each be raised by £90,000, so that from 6 April 2020 the threshold and adjusted income limits will be £200,000 and £240,000 respectively. This means that individuals with income below £200,000 will not be affected by the tapered annual allowance, and tapering of the allowance will only commence where the adjusted income exceeds £240,000.

However, for those on the very highest incomes, the minimum level to which the Annual Allowance can taper down will be reduced from £10,000 to £4,000. The full effect of this tapering will apply to individuals with total income (including pension accrual) in excess of £300,000.

Lifetime allowance for pensions

The Lifetime Allowance restricts the maximum amount an individual can accrue in a registered pension scheme in a tax-efficient manner over their lifetime without incurring additional pension tax charges when pension benefits are eventually drawn. The allowance will be increased for 2020/21 to £1,073,100 (currently £1,055,000), in line with the Consumer Prices Index.

Top slicing relief

Top slicing relief is a valuable relief for individuals who make profits (known as chargeable event gains) on life insurance policies or investments. Such gains are chargeable to Income Tax not Capital Gains Tax. The relief is designed to mitigate the impact of the individual being charged to tax at a higher rate due to the inclusion of a life insurance policy gain or gains in their income for the year of disposal. The relief only benefits individuals where the total gain(s) exceed the basic rate threshold so that some of the gain is chargeable to higher or additional rate Income Tax, i.e. at a rate of up to 45%.

However, the calculation of the relief is complex and can adversely affect taxpayers whose total life insurance policy gains in a tax year result in a restriction of their personal allowances.

Following a recent tax tribunal decision, the Chancellor announced that he will legislate in Finance Bill 2020 to put beyond doubt how top slicing relief is calculated with reference to allowances and reliefs. The measure will apply to all life insurance policy gains with effect from 11 March 2020.

The proposed change will ensure that taxpayers who make life insurance policy gains may still benefit from the appropriate part of the personal allowance in calculating the relief they are due.

The Government has stated that the measure is in line with the original policy intent, but it is notable that it took a taxpayer to successfully challenge HMRC in the courts to result in a change in the legislation.

C. Business Taxation

Employment Allowance

The National Insurance Contributions (NIC) Employment Allowance was introduced in April 2014, with the intention of supporting growth for businesses and charities by reducing the cost to them of taking on employees.

The Chancellor announced that the Employment Allowance would increase by £1,000 from £3,000 to £4,000 per annum from 6 April 2020, in a bid to ease the economic impact of Coronavirus on small businesses.

It was previously announced in the October 2018 Budget that the Employment Allowance would only be available to employers whose employers NIC bill was less than £100,000 pa from April 2020. This restriction is still to come into force, as the relief continues to be targeted at smaller businesses.

Business rates

The Chancellor announced a series of targeted one year business rates relief initiatives. These have the specifically stated aim of easing the economic impact of reduced consumer spending due to Coronavirus on the retail, leisure, hospitality and pub sectors.

Business rates on retail premises with a rateable value of less than £51,000 were previously to enjoy a discount of 50% in 2020/21. However, this discount has now been increased to 100% and also extended to the leisure and hospitality sectors.

Pubs with a rateable value of less than £100,000 were previously to enjoy a £1,000 discount on their business rates and this has now been increased to a £5,000 discount.

Whilst these initiatives are targeted short term measures, a more fundamental review of business rates was also announced, with a report due in the Autumn.

R&D Expenditure Credit Scheme (“RDEC”)

The RDEC rate will increase from 12% to 13% for expenditure incurred on or after 1 April 2020. The RDEC is available to both large companies and SMEs carrying out research & development.

This means that the value of a claim under the scheme will increase from up to 9.72p for every £1 spent to 10.53p for every £1 spent on qualifying R&D expenditure.

R&D SME tax credit restriction

The Government announced, in October 2018, that a cap on tax credits claimable under the SME R&D scheme would be introduced from April 2020, designed to restrict R&D tax credits payable to companies with limited UK activity or employment. The cap was set at three times a company’s total PAYE and National Insurance liability.

Following consultations, the introduction of this restriction has been delayed until April 2021 and further consultations will be held on the design of the cap, to ensure that it targets abusive behaviour without unduly restricting access to the relief.

This is a welcome response following industry concerns that this cap could affect companies who are undertaking genuine R&D activity in the UK.

Qualifying R&D expenditure

Claims under either the SME scheme or RDEC scheme can only be made if expenditure falls into a qualifying category.

In recognition of the changing nature of costs, as technology and working practices evolve, which companies may incur

in the course of R&D, the Government has announced that it will consult on whether expenditure on data and cloud computing should also be considered qualifying expenditure for R&D purposes.

This could increase the proportion of a company's expenditure which qualifies for enhanced relief under the R&D tax incentive schemes.

Structures and buildings allowances

Since its introduction in the October 2018 Budget, the Government considers that the Structures and Buildings allowance has enhanced the international competiveness of the UK's tax system, and has therefore moved to increase the annual rate of capital allowances to 3% per annum from April 2020.

Enhanced capital allowances – electric cars

Enhanced capital allowances allow for a 100% first year allowance and tax credits for loss making companies in respect of expenditure on certain environmentally friendly plant.

At present low emissions cars (CO2 emissions of 50g/km or less) qualify for first year allowances. Cars with CO2 emissions of 50g/km to 110g/km qualify for writing down allowances at the main pool rate of 18% pa, and all other cars receive writing down allowances at the special rate pool rate of 6% pa.

From April 2021, for four years, whilst zero emissions cars will continue to qualify for 100% first year allowances, cars with CO2 emissions of 50g/km or less will qualify for writing down allowances at the main pool rate of 18% pa, and all other cars will only receive writing down allowances at the special rate pool rate of 6% pa.

This results in a significant tax incentive for businesses to purchase zero or low emission cars. Combined with the availability of first year allowances on electric vehicle charging points, the Government hopes that this will enhance the UK's electric car infrastructure and also encourage the uptake of electric cars.

Intangible fixed assets (IFA) reform

Finance Bill 2020 will introduce an amendment to the IFA regime to allow the ability for companies to bring assets created or acquired before 1 April 2002 into the IFA regime with effect from 1 July 2020. Anti-avoidance legislation will prevent contrived arrangements where companies seek to benefit from this change (e.g. assets cannot be "refreshed"/"uplifted" on an intercompany transfer). However, this amendment should allow greater certainty and simplicity for UK companies disposing of or acquiring older intangible fixed assets from 1 July 2020. More detail will follow when the Finance Bill is published later this month.

Digital Services Tax (DST)

Despite the ongoing resistance from US headquartered technology businesses, the Government confirmed that it would be going ahead with the introduction of the DST from 1 April 2020. DST will apply to online businesses at a rate of 2% to the UK turnover in excess of £25m of multinationals with global revenue in excess of £500m. DST will be repealed once a global taxing solution for the digital economy has been implemented.

Corporate capital loss restriction

As announced in the 2018 Budget, with effect from 1 April 2020, the use of brought forward corporate capital losses will be aligned with other corporate tax loss regimes. The first £5 million of brought forward losses will remain unrestricted with a restriction of 50% to the remaining gain. This will potentially accelerate tax payment for some larger businesses making capital disposals after 1 April 2020.

Hybrid mismatch rules

Further consultation will take place to ensure that the UK's anti hybrid legislation works as intended. This is aimed at situations where businesses exploit differences in the treatment of financing instruments or entities between the UK and other jurisdictions.

Asset holding companies (AHCs) in alternative fund structures

A Treasury consultation has been announced:-

I. To review VAT recoverability on fund management fees; and

II. To consider the attractiveness of the UK as a location for AHCs used by alternative funds.

The second consultation is aimed at alternative funds - typically limited partnerships which invest in real estate, credit and private equity through a UK AHC, where the investors in the fund (limited partners) are sophisticated investors, pension funds, insurance companies and sovereign wealth funds. It will therefore be mainly of interest to private equity investors.

The consultation aims to remove Corporation Tax barriers faced by AHCs in the UK. It is part of wider measures aimed at maintaining the competitiveness of the UK's asset management sector post-Brexit.

The main measures to be considered in relation to private equity funds include:-

- Retaining the character of capital gains in target companies flowing up to investors;
- Withholding tax on corporate interest payable to non-residents; and
- Hybrid mismatch rules where interest paid is not taxed as such overseas.

The Treasury notes that the UK already has a competitive tax regime, but is aware that other jurisdictions offer a tax-free environment which could drive UK asset management functions overseas. We will be monitoring the progress of this consultation and any reforms that might result from it. We hope that any relaxation to the tax regime is not tempered with uncertainty in the form of anti-avoidance provisions.

Anti-avoidance rules aimed at businesses

The government has announced further funding for HMRC to expand tax compliance reviews and enforce debt collection.

From April 2021 a new large business notification requirement will be introduced, which will require large businesses to notify HMRC where they have adopted tax positions which HMRC is expected to challenge. This is expected to be modelled on IFRIC 23 – (Uncertainty Over Income Tax Treatments).

D. Inheritance Taxes

Excluded property and transfers between settlements

Draft legislation published last summer is included in the Finance Bill published with the Budget without amendment, and the consultation which had been anticipated has not taken place.

The new legislation was prompted by a 2017 Court of Appeal decision (Barclays Wealth Trustees (Jersey) Limited and Dreelan v HMRC); which HMRC lost. The case concerned a transfer of assets between settlements and the new legislation will reverse the effect of the Court of Appeal decision. The legislation changes some of the circumstances in which trust property is 'excluded property' for Inheritance Tax.

Additions to settlements

Generally, non-UK assets owned by individuals who are domiciled outside the UK, or settlements created by them, are outside the scope of Inheritance Tax as excluded property.

The existing legislation is clear that the Inheritance Tax status of trust property depends only on the domicile of the settlor at the time the settlement was made. HMRC have for a long time taken the view that if the settlor becomes UK domiciled, and then adds property to a settlement he created when he had a foreign domicile, this results in a second settlement which does not have excluded property status. Whilst generally accepted in practice, the leading commentaries say this position is difficult to support on the basis of the wording of the current legislation.

From the date of Royal Assent, the legislation will be changed to definitively reflect the HMRC view. The settlor's status when property becomes comprised in the settlement will become the relevant factor. This new rule will be deemed to have always been in place in relation to chargeable events, such as ten year anniversary and exit charges, which take place after Royal Assent. As noted above, most professional advisers have historically taken a cautious approach and followed the HMRC view, so on the face of it this change will not have a widespread impact.

The new legislation could have a substantial effect where assets have moved between two settlements (and so become comprised in the recipient settlement) and the settlor was UK domiciled at the time of the transfer. In particular, there could be an issue if the settlor retains an interest for the purpose of the Inheritance Tax Gift with Reservation of Benefit (GROB) provisions.

Transfers between settlements

In contrast to the position for additions to trust, the new rules do not generally take a retrospective approach for trust transfers. For the purposes of any 10 year anniversary charges, where there have been transfers of non-UK assets before Royal Assent, excluded property status will be retained provided the settlor of the transferor settlement was domiciled outside the UK when the property became comprised in the settlement, and the settlor of the transferee settlement was also non-UK domiciled when that settlement was created.

However, this “grandfathering” of historic transfers is not extended to the general excluded property provisions, and so if the settlor retains an interest in these circumstances then, in the event of a death after Royal Assent, the assets will be within the scope of the GROB provisions without the protection of excluded property status.

In respect of 10 year anniversary charges, for transfers on or after Royal Assent, which the legislation refers to as ‘new cases’, the position is more restrictive. When trustees transfer non-UK property to another settlement, that property will only retain excluded property status if the settlor of the transferor settlement was not UK domiciled at the time of transfer (or he had died before the transfer). Again, for these new cases, if the settlor is a beneficiary, loss of excluded property status would mean that assets subject to Inheritance Tax are then included in his taxable estate, by reason of the GROB provisions.

Initial Life Interest of Settlor or Spouse

Amendments are also made to the rule which applies where the settlor or spouse of the settlor has an initial interest in possession in settled property. At present, property is treated as becoming comprised in the settlement when the last of those interests comes to an end, and domicile is tested then. The new rules provide that there will also be a retest of the settlor’s domicile at that time.

This is a complex area of tax legislation, and specialist advice is essential. In particular, when a transfer between trusts is contemplated, the possibility of tainting a trust which has protected status should be considered.

Residence nil rate band

As previously announced, the residence nil rate band (RNRB), which was first available from 2017/18, will increase to £175,000 for 2020/21. After 2020/21 it has been confirmed that the RNRB will increase in line with inflation. The RNRB provides for relief from Inheritance Tax where an individual leaves their main residence to a “lineal descendant”. This means that for 2020/21 an individual who qualifies for the RNRB can leave up to £500,000 free from Inheritance Tax. The RNRB will continue to be tapered for estates worth more than £2 million.

E. Employment & Self-Employment Taxes

Reform of off-payroll working (‘IR35’) rules for private sector end users

In April 2017, following a review of the treatment of off-payroll working rules which deal with the taxation of the provision of services by individuals to end users via intermediary companies, new legislation was introduced for workers who provide services to public sector entities through intermediary companies.

This legislation was introduced to address significant non-compliance with rules that were introduced via IR35 in 2000, to deal with workers providing services via intermediaries who would otherwise have been treated as employees of the end user had they provided services to them directly.

The effect of the rules that were introduced in April 2017 was to move the responsibility for determining the worker’s employment status from the worker themselves to the end user, although the worker is required to provide information to assist the end user in this process. If the off-payroll working rules apply so that the worker would be treated as an employee of the end user but for the existence of the intermediary company, the end user who pays the intermediary

company is obliged to deduct tax and National Insurance (NI) from the payments for the worker's services, apply employer's NI, and report the deductions of tax and NI to HMRC via the Real Time Information (RTI) system.

Proposals were announced in the Autumn 2017 Budget to extend these new rules to medium and large sized entities outside the public sector, with consultations held prior to the publication of draft legislation in July 2019. A review of business readiness and implementation issues was undertaken in January 2020 with representatives of end users, contractors and the tax profession. The final legislation is to be introduced in Finance Bill 2020.

It has been confirmed that the off-payroll working rules will only apply to payments made for services provided to medium and large sector businesses on or after 6 April 2020, and that information obtained as a result of the changes to the rules will not be used to open an enquiry for years prior to 2020/21 as long as fraud or criminal conduct have not taken place. HMRC will operate a 'light touch' approach to penalties in the 12 months following the implementation of the reforms except in cases of deliberate non-compliance. HMRC's Employment manual has been updated to reflect the findings of the review.

HMRC is providing a variety of resources to assist in determining whether the off-payroll working rules apply to workers. In particular, an enhanced online Check for Employment Status Tool ('CEST') was introduced in November 2019 to assist end users and individuals in determining their employment status. The tool has been developed based on case law and settled cases. HMRC has also published guidance for businesses and intermediaries and has established a dedicated support team to assist further. New interactive online guidance will also be made available this summer.

However, the case law surrounding the employment status of workers is complex and nuanced, with decisions often turning on points of fine detail. This can be seen in the differing decisions reached by the Courts in the cases of TV personalities Christa Ackroyd, Lorraine Kelly, Kay Adams and Eamonn Holmes where each operated as daytime TV presenters on live programmes, providing their services through intermediary companies. The conclusions reached by the Courts were that Christa Ackroyd and Eamonn Holmes would have been treated as employees but that Lorraine Kelly and Kay Adams would not, despite the number of similarities in their respective arrangements. It remains to be seen how effective the resources being offered by HMRC will be in correctly applying the relevant principles more broadly to workers operating through intermediaries.

Review of the Enterprise Management Incentive scheme

The Enterprise Management Incentive ("EMI") scheme allows small companies to reward, retain and motivate employees in a way which provides generous tax advantages for both the employer and the employee.

In particular, provided various conditions are met, employees are able to acquire shares at the market value on the date the option is granted even if the shares have increased in value significantly by when the option is exercised, and the increase is only subject to capital gains tax, and not income tax.

In addition, provided certain conditions are met, it is usually possible for employees to qualify for Entrepreneurs' Relief on the sale of the shares, even if they do not have the minimum 5% holding usually required.

HMRC has announced that this valuable tax advantaged scheme is to be reviewed to ensure that it is providing support for the small high growth companies it is aimed at, and to consider whether more companies should be eligible to participate. However, no timetable has been announced for this review.

The EMI scheme is a valuable and tax efficient way in which eligible small businesses can reward, retain and motivate their employees. The review is therefore to be welcomed. It will be interesting to see whether the scheme is extended to allow more companies which are currently excluded from participation to take advantage of the tax reliefs available.

Limited liability partnerships

The Chancellor announced that legislation will be introduced in Finance Bill 2020 (with retrospective effect), which clarifies that LLPs should be treated as general partnerships under income tax rules.

This follows the recent First Tier Tribunal ("FTT") case of Inverclyde and another vs HMRC [2019], where a HMRC enquiry and subsequent closure notices issued under the TMA 1970 were found to be invalid. Under company law, LLPs are body corporates, but are treated as transparent partnerships for tax purposes under deeming provisions which do not extent to TMA 1970. Therefore, the FTT held that HMRC should have opened the enquires under Corporation Tax provisions into the tax returns of the partnership, not Income Tax provisions.

As a result of this ruling, all HMRC enquiries into partnership tax returns opened under TMA 1970 were potentially invalid, meaning that HMRC would not be able to raise additional tax following the enquiry. The time limits for HMRC to open enquiries under the correct provisions may also have passed, meaning HMRC's only potential recourse would be to consider whether there are grounds to raise discovery assessments.

In practice, this measure is unlikely to have a significant on-going effect, as it effectively legislates what had been considered accepted procedure until quite recently. However, for those LLPs with ongoing enquiries opened under TMA 1970, the precise operation of the legislation will need to be carefully considered, in particular its retrospective application.

F. Property Taxes

2% non-resident stamp duty surcharge…coming soon

Following consultation published in February 2019, HMRC has now confirmed that it will introduce the new non-resident Stamp Duty Land Tax ("SDLT") charge with effect from 1 April 2021, and that it will be set at 2%, rather than the 1% originally suggested. The effect will be a 17% top rate of SDLT- one of the highest property purchase taxes in the world.

No details have yet been published of exactly how the new SDLT surcharge will work, but assuming that it is broadly based on the consultation document it is likely to feature the following:

- The 2% surcharge will apply to purchases of residential property in England and Northern Ireland by non-resident persons (individuals and companies / other entities).
- The 2% surcharge will apply to the whole purchase price (in the same way as the 3% additional property surcharge).
- It will apply on top of the 3% surcharge (where applicable). It will also apply on top of the flat 15% rate which applies to certain purchases of residential property by companies.
- An individual will be treated as non-resident if they spend less than 183 days in the UK in the 12 months ending with the date the transaction occurs. Presence anywhere in the UK (not just England and Northern Ireland) at midnight on a given day will be treated as a day of residence.
- It will be possible to obtain a refund of the surcharge if an individual spends more than 183 days in the UK in the 12 months following the date of the transaction.
- There will be a separate corporate residence test for SDLT purposes.
- There will be anti-avoidance rules to prevent the use of UK resident companies by non-UK resident companies which are broadly under the control of five or fewer non-resident persons.
- The surcharge will not apply to non-residential and mixed (both residential and non-residential) transactions.
- Where there is more than one purchaser, the surcharge will apply to the whole transaction if one or more of the purchasers is non-resident.
- Where the transactions are linked (broadly part of a series of transactions between the same parties), the surcharge will be paid on the total amount for all the linked transactions.

The introduction of a non-resident surcharge was originally announced in the 2018 Budget, and is aimed at discouraging purchases by overseas buyers looking for a "safe" home for their money in UK property. However, given the low value of sterling currently, it will be interesting to see whether it has its desired effect. Given that calculating the correct amount of SDLT on a property transaction can already very complex, It will also be interesting to see whether the rules will be as simple as has been promised.

Corporation tax on UK property income for non-resident companies

As announced in July 2018, from 6 April 2020, non-UK resident companies will be liable to corporation tax on profits from UK property businesses, rather than income tax as currently.

HMRC announced some further changes which will apply from 6 April 2020 which are designed to "ensure a smooth transition" between the existing income tax regime and the new corporation tax regime for rental income. The intention is to ensure that non-UK resident company landlords are entitled to the same reliefs for pre-trading finance costs as UK companies.

Currently, property businesses are able to obtain income tax relief for finance costs incurred prior to the business commencing. However, there is no equivalent corporation tax relief for the financing costs of a non-UK resident company carrying on a UK property business.

New rules will be introduced which will allow a non-resident company to bring into its first accounting period a net amount of financing costs relating to UK property held before it starts to carry on its UK property business. Relief will broadly be limited to costs incurred within the seven years prior to commencement of the property business, net of any credits arising in the same period.

There are also a number of other technical changes designed to facilitate the move from the income tax to corporate tax regime by ensuring that non-resident landlord companies have the same time limits for making certain elections as are available to UK resident companies.

G. Anti-Avoidance Provisions

The loan charge

Disguised remuneration schemes are typically used by employers and individuals to avoid Income Tax and National Insurance contributions. These schemes take various forms, but they commonly result in loans from a third party on such terms that are never repaid in practice. At Budget 2016, the government announced a package of changes to tackle disguised remuneration schemes. This included the "Loan Charge" on disguised remuneration loan balances outstanding at 5 April 2019. This gave scheme users three years to repay their disguised remuneration loans, reach a settlement with HMRC, or be subject to the charge (i.e. income tax on the entire loan based on their marginal rate of tax for 2018/19).

As a response to objections made by those affected and their professional representatives, the government commissioned Sir Amyas Morse to conduct an independent review of the loan change in September 2019. The review was published on 20 December 2019, and the government announced that it would accept all but one of the recommendations.

Although stressing the need to take further action to stamp out disguised remuneration schemes, the Budget confirms the government's response to the loan charge review, and confirms that changes will be legislated for in the forthcoming Finance Bill including:-

- The loan charge will only apply to outstanding loans made on, or after, 9 December 2010;
- The loan charge will not apply to outstanding loans made in any tax years before 6 April 2016 where the avoidance scheme use was disclosed to HMRC but they did not take any action (i.e. by opening an enquiry); and
- HMRC will refund voluntary tax payments already made following reaching a settlement agreement where the loan charge no longer applies (i.e. for loans made before 9 December 2010) or where loans were made before 6 April 2016 and disclosed to HMRC who did not take action. However, HMRC will not be able to process any refunds until changes to the loan charge legislation have been enacted by Parliament.

HMRC climb the insolvency league table

HMRC are to move up the creditor hierarchy for the distribution of assets in the event of insolvency. From 1 December 2020 HMRC will be secondary preferential creditors in respect of taxes paid by employees and customers that a company collects on behalf of HMRC (eg VAT, PAYE, employees' NIC, construction industry scheme deductions).

The present rules will remain unchanged for taxes owed by the company itself (such as corporation tax and employers' NICs) where HMRC will remain an unsecured creditor.

These changes were originally scheduled to take effect from 6 April 2020, but have now been delayed to 1 December, as well as being extended to include Northern Ireland.

HMRC note that the changes will impact secured creditors with floating charges and unsecured creditors. Prioritising the recovery of HMRC's tax debt could therefore mean that banks, in particular, are affected as they are the main holders of floating charges.

H. Value Added Tax

The Chancellor made two significant VAT announcements:

I. The anticipated abolition of VAT on women's sanitary products from 1 January 2021, which will enable these products to be zero rated for VAT purposes.

II. The unexpected abolition of VAT on digital publications from 1 December 2020, to bring these publications into line with printed publications which are currently zero rated for VAT purposes.

With the expected end to the Brexit transition period on 31 December 2020, the Chancellor also announced simplification measures for the movement of goods.

From 1 January 2021, postponed VAT accounting will be introduced for the import of goods into the UK, whereby import VAT is accounted for on the importer's VAT return rather than paying the import VAT at the time of importation of the goods.

For the intra-EU movement of call-off stock, legislation is to be introduced to allow businesses to delay the accounting for VAT until the goods are called-off.

The government will also engage with interested parties to conduct an informal consultation, over the Spring 2020, on the VAT treatment of goods crossing UK borders after the UK exits the EU. A similar consultation process will take place to gather views on the approach to passenger duty and tax free allowances after the UK departs from the EU.

The financial services sector will be consulted to ensure the UK remains an attractive place for business, with the government setting up an industry working group to review the VAT treatment of financial services. There will also be specific clarification on the VAT treatment of fund management services, which is currently a complex area of the VAT legislation.

The government is to continue to engage with stakeholders in relation to the simplification of the VAT rules on Partial Exemption and the Capital Goods Scheme, with the results being published in due course.

In an effort to combat VAT avoidance, the previously announced VAT domestic reverse charge for building and construction services will be introduced on 1 October 2020. The new rules will put the onus of accounting for VAT on sub-contractors' services on to the main contractor in an attempt to prevent VAT losses through "missing trader" fraud.

To avoid VAT losses within the agriculture sector, the government will introduce new entry and exit rules for the VAT Agricultural Flat Rate Scheme.

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This Briefing Note provides a commentary on those parts of the Budget which we think will be of specific interest to our clients and contacts.

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