Charter Tax Consulting Ltd

Budget Announcements 3 December 2014: Client Summary Note

Introduction

On 3 December 2014, the Chancellor delivered his 2014 Autumn Statement. The Chancellor believes our economy to be in a recovery position, though very much the order of the day seems to be continuing to eliminate tax avoidance.

Probably the biggest unpleasant surprise for our resident but non-dom clients is the announcement that the remittance basis charge once one has been here for 12 years will increase to £60,000, with a higher still charge of £90,000 applying once one has been here for 17 years.

House buyers get some good news in relation to SDLT rates, though non-residents will start to be within the capital gains tax regime on UK residential properties from 6 April 2015. Clients with more than one home will also need to carefully review their position on principal private residence relief.

Set out below is an initial summary of the key proposals in today's announcements, that may affect our clients, though naturally bespoke advice will always be required and action should not be taken on the basis of these notes alone. As ever, we will be happy to assist our clients or contacts in relation to any of these issues, so please do contact us should you have any queries.

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Stamp Duty Land Tax (SDLT)

The long standing gripe with the SDLT system is that as soon as one of the SDLT thresholds is exceeded, the whole amount of the purchase price is then subject to a higher SDLT rate. This can have quite an effect on house prices, causing a plateaux at the place just before each SDLT threshold. For example, a property sold for £1,995,000 would attract an SDLT rate of 5% (£99,750). If the property is sold for £2m, the SDLT rate is at 7%, on the full amount (so £140,000).

At very long last, this system is to change! (albeit seemingly only for residential properties at the moment). From 4 December 2014, SDLT on residential properties will be payable at each rate on the portion of the purchase price which falls within each band, rather than at a single rate on the whole transaction value. The new rates of SDLT for residential properties being purchased by an individual will therefore be as follows:

Property value band	Rate
£0 - £125,000	0%
£125,001 - £250,000	2%
£250,001 - £925,000	5%
£925,001 - £1,500,000	10%
£1,500,001+	12%

Capital Gains Tax Extension for Non-Residents Owning UK Residential Property

Historically, non-residents have not paid UK capital gains tax on disposals of UK residential property. However, this will change from 6 April 2015, when non-residents owning UK residential property but not already within the charge to UK capital gains tax (such as through the ATED regime) will then come within the charge. Although no further information was given on these changes today, it is worth re-stating the recent announcements on this point.

The new charge will apply to disposals of UK residential property. Residential property will be defined as property suitable for use as a dwelling. There will be a time apportionment system to deal with property that has been residential, but not for the full duration of the period of ownership.

The charge will apply mainly to non-resident individuals/ non-resident trustees, personal representatives of a non-resident deceased person and some non-resident companies disposing of UK residential property. Partnerships will be regarded as tax transparent and as such the CGT charge will depend on the position of the underlying partners. There will be an exemption for certain large scale institutional investment, subject to passing a “narrowly controlled company test” which will work alongside a “genuine diversity of ownership” test.

This new charge will sit alongside – and be in addition to – the existing ATED regime (for offshore companies owning UK residential property in effect for own use/ use of connected parties). The existing ATED regime will not change and so this new charge will only apply to properties not already caught by ATED.

The extended CGT charge will not apply to the amount of the gain relating to periods prior to April 2015. This will be achieved by way of either a rebasing or a time-apportionment of the whole gain. Rebasing will be the default position, but taxpayers can elect for time-apportionment or even to use the actual gain (or loss). There will be a ring-fencing system for such losses, however.

The rate for non-resident individuals will be the same as the CGT rates for UK individuals (currently 18% or 28%, depending on the person’s total UK income & chargeable gains for the tax year, with an annual exemption also being available).

Similarly, the CGT rate for non-resident trustees will be 28%, with half the annual exemption that would normally be available to individuals (the same position as for UK resident trustees).

The rate for companies (not already within ATED) will mirror the UK corporation tax rate (currently 20%). The ATED rate stays at 28%, which is deliberately penal in comparison. There will be some ability to access indexation allowance and a limited form of group “pooling” (in effect group relief on disposals of UK residential property by different members of the same group). There will, though, be strict controls and information requirements over companies wishing to enter into such a pooling arrangement, that many non-resident clients may find off-putting.

PPR regime change

An obvious step for non-residents owning UK residential property might have been for them to elect that their UK property should be treated as their PPR and thus exempt from CGT. HMRC made it clear from the outset that this is a situation they will want to avoid and as such the PPR regime must also be amended. Again, no further details were released on this change today, though for completeness it is worth mentioning the changes.

From April 2015, a person's residence will not be eligible for PPR for a tax year unless:

- Either the person making the disposal was tax resident in the same country as the property for that year (i.e. so for a UK property, the individual would need to be UK resident), or
- The person spent at least 90 midnights in that property (or across all of the persons' properties where they have multiple properties in a country in which they are not tax resident) in that year – referred to as the "90-day rule".

For married couples and civil partnerships, occupation of a residence by one spouse or partner will be regarded as occupation by the other.

Remember, that for years in which the property is not one's PPR, in effect there is then a pro-rating of the gain as between what is and is not covered by the PPR exemption.

For non-residents, nominations to treat a residence as their only or main residence are to be made at the time of disposal.

Access to PPR will be available for trusts if the beneficiary is non-UK resident, on the same basis (i.e. if the property is one in which the beneficiary spends at least 90 midnights and they elect for it to be their PPR).

Annual Tax on Enveloped Dwellings (ATED)

The Government appear to wish to continue with the ATED regime, and pleas from the professional community to not have a regime for capital gains tax for non-residents generally and then another for those within the ATED regime have fallen on deaf ears. Remember that the ATED regime applies, broadly, to non-resident companies owning UK residential property which is/ can be used by in effect the owner of the company/ associates of his, rather than being let out to third parties.

As such, the higher ATED capital gains tax rate will apply on disposals of residential property within that regime (28%). The annual ATED charges will also continue and indeed will increase by 50% above inflation for residential properties worth more than £2million for the chargeable period 1 April 2015 to 31 March 2016.

Non Doms – Remittance Basis Charge Increase

Individuals resident in the UK but domiciled abroad are able to pay tax on the “remittance basis” meaning, broadly, that they do not pay tax on their foreign income/ gains, provided that this is not brought to the UK (directly or indirectly). For some well planned individuals with significant pre-residence capital, potentially this could mean that they do not pay any income or capital gains tax in the UK at all for a good number of years.

However, under the banner of ensuring that non-doms pay a “fair” share of tax, in recent years the rules have changed such that individuals who have been UK resident for 7 out of the last 9 years pay a £30,000 tax charge (known as the “remittance basis charge” – basically more akin to a fee for having the ability to use the remittance basis) and individuals who have been UK resident for 12 out of the last 14 years pay a charge of £50,000. The £30,000 charge is to remain the same but the charge for someone who has been UK resident for the 12 year period will increase from £50,000 to £60,000. A higher charge of £90,000 will also be introduced for individuals who have been UK resident for 17 of the last 20 years. The Government will also consult on making the election apply for a minimum of 3 years.

CGT Entrepreneur’s Relief and Purchased “Internal” Goodwill

Although the Government have reconfirmed their ongoing commitment to support entrepreneur’s through the availability of the 10% capital gains tax rate available for entrepreneur’s making disposals of their businesses, with effect from today [3 December 2014] a previously very useful tax planning mechanism is being closed down.

It used to be possible for, say, an individual with an unincorporated business to then incorporate and “sell” their assets & goodwill into the newly incorporated company. The sale would attract entrepreneur’s relief, and thus an effective 10% capital gains tax rate on sale. A loan account would be set up with the company, which the individual then draws down from over time. The company then shows this goodwill purchase as an asset, which it writes down over time and, depending on the date the goodwill was created, the company may get a corporation tax deduction for the goodwill write down.

Going forward, the tax position giving this beneficial arrangement is stopped and such goodwill sales to related close companies will not attract the 10% capital gains tax rate and likewise the company will not get a corporation tax deduction for such goodwill purchase write downs.

Inheritance Tax

Although changes to the inheritance tax legislation were largely expected today, not least following a consultation on the inheritance tax regime for trusts, so far it seems there are no further such announcements., other than some welcome news for the armed forces & emergency services that there will (quite rightly in the authors view!) be an inheritance tax exemption for death in service. Humanitarian aid workers will also be able to benefit from the exemption. In addition, there will be an extension of the existing inheritance tax exemption for certain medals/ awards for service men and women.

Base Erosion and Profit Shifting

A brave new world for large international corporates has been on the horizon for a little while now as far as their corporation tax compliance function is concerned. Public opinion is very much against the likes of Starbucks who have their shops here but yet manage to take profit outside of the UK through intellectual property arrangements and other means. As a taxpayer, the author has some sympathy with this public opinion. As a tax advisor, one can't help but cry "but they were allowed to do that – if you don't want them to do that, change the law!". Well, the law is now to be changed.

A new tax to counter the use of aggressive tax planning techniques by multinational enterprises to divert profits from the UK will be introduced. The Diverted Profits Tax will be applied using a rate of 25% from 1 April 2015.

Legislation will also be introduced that gives the UK the power to implement the OECD model for country-by-country reporting. The new rules will require multinational enterprises to provide high level information to HMRC on their global allocation of profits and taxes paid, as well as indicators of economic activity in a country.

Furthermore, a consultation will be launched on the UK's plans for implementing agreed OECD rules for addressing hybrid mismatch arrangements. The new rules will prevent multinational enterprises avoiding tax through the use of certain cross-border business structures or finance transactions.

Other Anti-Avoidance Aspects

Anti-avoidance remains high on the agenda for Government, with further changes to be as follows:

- **Income tax - Miscellaneous loss relief -** Legislation will be introduced to counter avoidance of income tax involving losses from miscellaneous transactions. Legislation denying loss relief where a miscellaneous loss, or miscellaneous income, arises from relevant tax avoidance arrangements will have effect from 3 December 2014.
- **Bank loss-relief restriction - T**he Government will restrict the amount of a bank's annual profit that can be offset by carried-forward losses to 50% from 1 April 2015. The restriction will apply to losses accruing up to 1 April 2015 and will include an exemption for losses incurred in the first 5 years of a bank's authorisation.
- **Civil deterrents for offshore tax evasion -** Legislation will be introduced to enhance civil penalties for offshore tax evasion, including a new aggravated penalty of up to a further 50% for moving hidden funds to circumvent international tax transparency agreements. The changes will come into effect from April 2016, apart from the aggravated penalty which will come into effect following Royal Assent.
- **Promoters of tax avoidance schemes -** Legislation covering 'high-risk' promoters of tax avoidance schemes will be updated and enhanced.
- **Disclosure of Tax Avoidance Schemes (DOTAS) -** Legislation will be introduced to strengthen the DOTAS regime, including through updating existing scheme hallmarks, adding new hallmarks, and removing 'grandfathering' provisions for the future use of schemes that were excluded by those provisions.

New Reliefs

To end on a more cheery note, a number of tax reliefs are to be introduced/ enhanced, including:

- **Children's television tax relief -** to be introduced from 1 April 2015. The relief will be available at a rate of 25% on qualifying production expenditure.
- **Orchestra tax relief -** The Government will consult in early 2015 on the introduction of an orchestra corporation tax relief from 1 April 2016.
- **High-end television tax relief -** The Government will explore with industry whether to reduce the minimum UK expenditure for high-end TV relief from 25% to 10% and modernise the cultural test, to bring the relief in line with film tax relief.
- **R&D tax credit - Rates -** The rate of the above the line credit will increase from 10% to 11% and the rate of the small and medium (SME) scheme will increase from 225% to 230%. These will take effect from 1 April 2015.
- **R&D tax credits - Qualifying expenditure -** Legislation will be introduced to restrict qualifying expenditure for R&D tax credits so that the costs of materials incorporated in products that are sold are not eligible, with effect from 1 April 2015. An advance assurance scheme for small businesses making their first claim to R&D tax credits will also be introduced along with new guidance.