BUDGET 2016 PREDICTIONS

March 2016
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Now that the Chancellor’s plans for raising revenue through the reform of pensions tax relief have reportedly been shelved, he will need to try and fill the Government’s coffers from other sources if he wants to achieve his aim of running a surplus from 2019–20. However, the pre-election commitment not to raise income tax rates, VAT or NICs, makes this job all the harder. Fuel duty may be one of the more obvious targets, but could we also see moves to accelerate tax collection, including from businesses and the self-employed? Read below for more of RSM’s considered predictions for Budget 2016.

What we are confident will be announced

Personal taxation
Proposed anti–avoidance measures affecting company distributions – Following consultation between 22 October 2015 and 14 January 2016, the Government is expected to confirm the proposed measures that will lead to many distributions, mainly at the end of a company’s life, being chargeable to tax at income tax rather than capital gains tax rates. Limited amendments may be made to reflect stakeholder feedback.

Corporate taxation
Interest deductibility – Following consultation between 22 October 2015 and 14 January 2016 on proposals to introduce a new restriction on the deductibility of interest costs incurred by companies including proposals for a ‘fixed ratio’ rule and possibly a ‘group ratio’ rule, in line with proposals in the OECD’s report on Base Erosion and Profit Shifting (BEPS), the Government will set out its response.

Patent box: substantial activities – Following consultation between 22 October 2015 and 4 December 2015 on proposals to reform the patent box tax regime, including a nexus ratio aimed at restricting access to companies undertaking activities in the UK and requiring profits to be streamed accordingly, the Government will set out its proposals to reform this regime in line with the OECD’s BEPS report.

Property taxation
Proposed higher rates of SDLT for purchases of second homes – Following consultation between 28 December 2015 and 1 February 2016 on technical aspects of the proposals such as how second homes are to be identified and when the proposed higher rates will apply, the Government is expected to confirm final details of policy design on how it intends to deal with these issues.

VAT and indirect taxation
The ‘tax lock’ clause in Finance (No 2) Act 2015 specifying that the rates of VAT will not rise, and that there would be no detrimental decrease in the scope of the VAT zero rate and reduced rate during the term of this Parliament, does not prevent a change to the scope of VAT being made, specifically where such a change may be applicable following a court or tribunal decision, or in response to infringement proceedings by the EU Commission. These would generally be a result of application of the EU Principal VAT Directive (PVD) and EU and UK case law.

VAT grouping eligibility provisions – Following recent EU court decisions, eligibility to be included in VAT groups may be extended to include, for example, partnerships.

VAT recovery by holding companies that are members of VAT groups – Following recent EU and UK court decisions policy changes are expected relating to VAT recovery by holding companies.

Services relating to immovable property – Under EU rules, the place of supply of services relating to immovable property will, from 1 January 2017, be where the property is situated. The Government will therefore need to adapt existing UK legislation where appropriate.

Pension fund management costs – Following EU court decisions, the policy of allowing recovery of input VAT on pension fund management costs will change, with new rules required to acknowledge the findings of the court and mitigate the direct tax consequences for the employer.

Strengthening the disclosure of tax avoidance schemes – Following recent proposed changes to the disclosure of tax avoidance scheme (DOTAS) rules for direct taxes, an announcement is expected to update and strengthen the related VAT disclosure regime (VADR) rules.

VAT reduced rate for energy saving materials – Following EU infraction proceedings against the UK, new legislation is expected to ensure the reduced rate of VAT on energy saving materials is maintained in line with EU law.

Union Customs Code – The Union Customs Code replaces the existing Community Customs Code that applies to all EU member states from 1 May 2016. Changes will be required to UK legislation to adopt the new code.

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What we might reasonably expect to be announced

**Personal taxation**

**Salary sacrifice** — The Government remains concerned about the growth of salary sacrifice arrangements so an attack on such arrangements might be considered.

**Pensions: secondary annuities market** — Legislation is to be introduced in Finance Bill 2017 to remove the current pensions tax restrictions on individuals seeking to sell their right to future annuity income. Announcements have already been made, but further changes might be announced.

**Reform to tax treatment of non–domiciled individuals** — The Government has published its partial response to the consultation which ended on 11 November 2015. Further details are expected.

**Business investment relief scheme changes** — The Government will consult on the details of how to change the rules for business investment relief (BIR) to make it easier for non–domiciled individuals (non–doms) who use the remittance basis of taxation to bring money into the UK to invest in UK businesses. Legislation will be introduced in a future Finance Bill to cover any proposed changes to BIR.

**Inheritance tax on UK residential property held by non–domiciled individuals** — Proposals were outlined on 8 July 2015 for new IHT rules on UK residential property held indirectly by non–UK domiciled individuals or by excluded property trusts. A technical note was published alongside the separate technical briefing note on broader changes to the taxation of non–doms. Draft legislation is expected to be published in December 2016 as part of the DFB 2017. There might be a 2016 Budget announcement on this in conjunction with general non–dom tax changes.

**Employer provided living accommodation: call for evidence** — A call for evidence ran from 9 December 2015 to 3 February 2016 on the tax treatment of employer–provided living accommodation. The Government will use the information collected to consider whether there is a case for making changes to deliver simplification in this area.

**Abolition of class 2 national insurance contributions (NICs) and introduction of a contributory benefit test for class 4 NICs for the self–employed** — A consultation ran from 9 December to 24 February 2016 on these proposals. It is possible that the outcome will be published simultaneously with a Budget announcement.

**Making tax digital** — Most businesses, self–employed people and landlords will be required to keep track of their tax affairs digitally and update HMRC at least quarterly via their digital tax account. Further announcements might be made following concern about the proposals for quarterly reports — although HMRC has subsequently published a document designed to reassure taxpayers that this measure will not be particularly onerous. The Government has so far said that no decision has been made on whether the digitalisation of tax services will lead to businesses and the self–employed having to pay tax more quickly. However, there are obvious advantages for the Government in doing this, so this is a key area to watch in Budget 2016.

**Gift Aid small donations scheme** — A call for evidence ran from 9 December to 2 March 2016. The Government is expected to announce its response.

**Further anti–avoidance measures to tackle tax avoidance schemes relating to earned income falling outside the disguised remuneration rules** — The Government may announce measures intended to counteract tax avoidance schemes identified through the disclosure of tax avoidance schemes (DOTAS) rules and other means, including schemes involving arrangements such as contracts for differences (although it should be noted that HMRC believes contracts for differences schemes do not work under current legislation).

**Changes to entrepreneurs’ relief to relax the provisions introduced in FA 2015 relating to joint venture and partnership arrangements** — Following subsequent representations, changes are expected that will ensure these previous measures apply to target tax avoidance situations and do not adversely impact other commercial arrangements.

**IR35 reform** — The Government consulted with stakeholders in summer 2015 on ways to improve the intermediaries’ legislation (IR35) that counters disguised employment. The CIOT submitted a proposed new approach to IR35 to HMRC at that time. The outcome of the consultation and a response to the CIOT might form the basis of a Budget announcement.

**Simplification of the treatment of termination payments** — The Government consulted in summer 2015 on the income tax and NICs treatment of termination payments. The outcome of the consultation might form the basis of a Budget announcement.

**Corporate taxation**

**A progress report on the Government’s proposed business tax roadmap** — Further details may be announced in connection with the Government’s business tax roadmap for business taxes over the remainder of the current Parliament, due to be published by April 2016.
Review of the UK’s international tax rules to ensure they are compliant with BEPS requirements — The Government may announce a review and possible early changes to further UK tax rules, such as the controlled foreign company (CFC) rules, potentially affected by the proposals in the OECD’s report on BEPS.

‘Moneyboxing’ — Some proposed measures (or at least a specific consultation) on ‘moneyboxing’ as it was referred to in the recent company distributions consultation — perhaps something akin to the old close company apportionment provisions, possibly some form of tax transparency for certain close investment companies.

VAT and indirect taxation
Changes to the existing VAT zero-rating can be applied to the construction and/or conversion of buildings — The Government may announce changes to the extent that VAT zero-rating can be applied to the construction and/or conversion of buildings, resulting from UK case law. This may include: conversions carried out under permitted development rights; construction of buildings that retain or utilise parts of previously existing buildings; the VAT liability treatment of a dwelling formed from more than one building; and a change to the VAT treatment of the construction of annexes.

Charities in receipt of subsidies and grants — Formal consultation may be announced on the right to input VAT recovery by charities in receipt of subsidies and grants.

Investment management and related services — Resulting from EU case law, the Government may wish to establish clear criteria for determining whether there are separate VATable and exempt supplies of investment management and related services, particularly with regard to discretionary investment management and portfolio management arrangements.

Narrowing the extent of VAT exempt insurance intermediary services — On the basis that current UK legislation is too broad an interpretation of EU law and that the EU court has stated the defining features of being an insurance broker or agent for VAT exemption purposes, UK legislation may be brought into line with these principles.

Health and social care integration — Guidance may be announced on where a local authority is the ‘host partner’, i.e. holds all the money, and commissions the provision of all goods and services in connection with Better Care Fund activities, with particular clarification sought on the timing of output tax accounting requirements.

Attribution and allocation of Scottish VAT receipts — Guidance may be announced on how Scottish VAT receipts will be identified and accounted for following implementation of the Scotland Bill.

What is possible but less likely

Personal taxation
ISAs: crowdfunding — Following consultation, the Government will legislate in autumn 2016 to allow certain debt securities issued by companies and offered via a crowdfunding platform to be held in the new Innovative Finance ISA, which will be available for certain peer-to-peer loans from 6 April 2016. Further details might be announced, especially if Pensions ISAs are on the Budget 2016 agenda, but this is more likely to be part of the Autumn Statement.

Capital gains tax: payment on account — A payment on account of any capital gains tax (CGT) due on the disposal of residential property will be required to be made within 30 days of completion of the disposal. Taxpayers will be able to reconcile their payment on account with their total CGT liability for the year, after the year end. Legislation will be introduced in Finance Bill 2017 and the Government will publish draft legislation for consultation in 2016. This is more likely to be part of the Autumn Statement.

Disguised remuneration schemes — The Government will consider legislating in a future Finance Bill to close down any further disguised remuneration schemes intended to avoid tax on earned income, where necessary, with retrospective effect from 25 November 2015. This is an ongoing process.

Taxation of income from sporting testimonials and benefit matches — Legislation will be introduced before 6 April 2017 for the NICs treatment of testimonial income for employed sportspersons to follow the income tax treatment. This is more likely to be part of the Autumn Statement.

Exclusion of energy generation from social investment tax relief (SITR) — Any company with a trade consisting substantially of energy generation activities (including the production of gas or other fuel) will be unable to use SITR when the scheme is enlarged at a later date (6–12 months from 9 December 2015), so something could be mentioned in the Budget but it is more likely to be in the Autumn Statement.

Increased CGT rates to align more closely with dividend tax rates — It seems unlikely given other developments to prevent taxpayers converting income to capital for tax purposes, but it is possible that the Government may, nevertheless, look at increasing CGT rates, partly with the aim of making it less attractive for taxpayers to receive value in capital form. The rate of CGT is not included in the ‘tax locks’ in Finance (No 2) Act 2015.

Restrictions on entrepreneurs’ relief (ER) — Statistics show that from 2009/10 to 2013/14 the amount of ER claimed approximately tripled. While recent changes have had the effect of restricting access to ER in a number of situations,
Further measures may be considered to restrict ER such as extending the required ownership period of shares or business/partnership interests or even reducing the lifetime limit from £10m to say £5m.

**Venture capital scheme replacement capital** — Legislation will be introduced at a future date to provide increased flexibility for companies to use money invested under the enterprise investment scheme (EIS) and by venture capital trusts (VCTs) for replacement capital, subject to EU state aid approval. Recent changes have severely restricted and essentially changed the business model of much of the VCT community. Funds previously dedicated to funding small buyouts in the UK have essentially had the rug pulled out from under them and are having to refocus on growth capital and earlier stage businesses. This essentially has restricted the funding available for small businesses to effect a change of control – sometimes a change of control and passing ownership to a new management team is the way to reinvigorate and drive new growth. There has been much lobbying by the VCT community so it is possible that this could lead to some relaxation.

**VAT and indirect taxation**

**Tour operators margin scheme (TOMS)** — to include ‘wholesale’ supplies (services supplied by an intermediary to another business for onward sale) within TOMS; current practice is at odds with EU VAT law and has been criticised by the tribunals.

**VAT reduced rates** — EU VAT legislation allows member states to apply a reduced rate of VAT to, among others, repairs and renovations of social and private housing; restaurant and catering services; hotel accommodation; and admission to fairs, amusement parks, theatres, shows and other cultural events — the UK doesn’t as yet, despite intense lobbying.

**Possible reduction in air passenger duty** — If such a measure is adopted, this will apply to UK airports other than Scottish airports, following the proposed transfer of such powers for Scottish airports to the Scottish Government under the Scotland Bill.