Budget Statement 2016 – Initial Analysis

16 March 2016

The Conservative government presented its 2016 Budget today. The following summary provides an overview of the main points set out in the Budget and accompanying notes.

Contents

These comments are based on announcements made in the 16 March 2016 Budget, which may change before becoming law. We're not permitted to offer taxation and legal advice for regulatory reasons. We accept no responsibility for actions taken or refrained from on the basis of these comments.

1. Lifetime ISA

From 6 April 2017, the government will introduce a brand new option for savers who are under age 40. Branded as the Lifetime ISA, this will give eligible savers the opportunity to save flexibly over the long term for a home and for retirement in one account. It's also intended as a flexible alternative to pensions for the self-employed. Here's some of the proposed detail:

- A Lifetime ISA can be opened by anyone between the ages of 18 and 40.
- The maximum contribution a person can make is £4,000 per year to benefit from the government bonus.
- Savings made before a person's 50th birthday will receive an added 25% bonus from the government. So, if the maximum contribution of £4,000 is made in a tax year, the government will add in a further £1,000 at the end of the tax year. The ISA manager will claim the bonus and add it into the Lifetime ISA account.
- Any savings made into a Lifetime ISA are counted as part of the overall ISA limit (which is increasing from £15,240 to £20,000 from 6 April 2017).

Additionally, where savings are used for a first home:

- Any Lifetime ISA savings and the government bonus can be used towards a deposit on a first home worth up to £450,000 in the UK. This can be done at any time after 12 months of opening an account.
- Two first time buyers can benefit from the government bonus from their own Lifetime ISA if they are buying together.
- There will be rules to set out how 'Help to Buy' ISAs and Lifetime ISAs will interact in terms of the government bonus and transfers into a Lifetime ISA account.

Where savings are used for retirement:

- After a person reaches the age of 60, any withdrawals made from their Lifetime ISA will be tax-free. Any withdrawal made can be used for any purpose – it's not restricted to just providing retirement benefits.
- If savings are withdrawn before age 60 (other than to help buy a first home), the government bonus will be lost as will any interest or growth obtained on this. There will also be a 5% early withdrawal charge.

Funds can be withdrawn in full before age 60 if someone is in terminal ill-health. The government has also said they will consider whether Lifetime ISA funds plus the government bonus can be withdrawn in full for other specific life events in addition to buying a first home. They will also look at whether there should be flexibility to borrow funds without incurring a charge if the borrowed funds are fully repaid (they quote this as being possible in the USA with some 401K retirement plans).

Further information on Lifetime ISA's can be found in the following two government documents:

Lifetime ISA factsheet

Lifetime ISA technical document

Final details of the rules relating to Lifetime ISAs will be issued by the government later in 2016.

2. Pensions

Annual and lifetime allowances

No further changes have been announced to the annual and lifetime allowances for pensions despite prior rumour to the contrary. This means that the tapered annual allowance for high earners will be introduced from 6 April 2016 and that the lifetime allowance will reduce from £1.25m to £1m from the same date.

Pensions dashboard

To help people view and keep track of all of their pension savings in one place, the government will ensure the pensions industry develops and launches a new digital interface, referred to as the 'pensions dashboard', by 2019.

Salary sacrifice

The government has again re-iterated their concern about the growth of salary sacrifice schemes, quoting that requests to HMRC for approval of such arrangements have increased by more than 30% in the past six years. As a result, the government are considering limiting the range of benefits that attract tax and national insurance savings through salary sacrifice schemes. However, they have stated that pension saving, childcare and health-related benefits such as Cycle to Work should continue as is.

Pensions tax relief

The government has published a summary of responses to their consultation document titled 'Strengthening the incentive to save: a consultation on pensions tax relief'. The summary highlights the responses to the eight specific questions raised in the consultation and cites that 450 replies were received across various categories of respondent.

Technical pension tax rule changes

A number of technical changes will be made, via the Finance Bill 2016, to ensure the pensions flexibility rules introduced in April 2015 are working as intended –

- It will be possible to pay a serious ill-health lump sum to an individual who has already accessed some of their pension. This isn't allowed under current pension tax rules.
- A serious ill-health lump sum paid to an individual who has reached the age of 75 will be taxed at the individual's marginal rate rather than the existing flat rate of 45%.
- Dependants' drawdown funds and dependants' flexi-access drawdown funds payable to a child dependant under the age of 23 will convert to nominees' drawdown funds on reaching age 23. This will allow an individual to continue to receive drawdown income as authorised payments beyond age 23 and avoid the tax charges that currently apply.
- It will be possible to pay a trivial commutation lump sum from a defined contribution pension that is already in payment.
- The tax treatment of charity lump sum death benefits, paid after the death of a member under the age of 75, will be changed so that it is the same regardless of whether the lump sum is paid from drawdown or uncrystallised funds.
- It will no longer be necessary to pay either an uncrystallised funds lump sum death benefit or a drawdown/flexi-access drawdown fund lump sum death benefit within two years of the member's death where it's paid to a charity, in order to avoid a tax charge.

Employer-arranged pension advice

Implementing a recommendation made under the Financial Advice Market Review, the government will increase the existing £150 Income Tax and National Insurance relief for employer-arranged pension advice to £500.

Pensions advice allowance

A further recommendation made under the Financial Advice Market Review will be consulted upon before its introduction. A new Pensions Advice Allowance will allow people under the age of 55 to withdraw up to £500 tax free from their defined contribution pension savings and use this towards the cost of financial advice. The age at which this allowance becomes accessible will be decided as part of the consultation.

Statutory financial guidance providers

The government is to restructure the Money Advice Service, The Pensions Advisory Service and Pension Wise. A new pensions guidance body will be created to ensure that consumers are able to get all of their pension questions answered in one place at all stages of their lives. In addition, there will be a new money guidance body which will identify gaps in the financial guidance market and arrange for providers to fill these gaps.

Unfunded employer financed retirement benefit schemes

The government is going to continue to monitor the use of EFRBS in relation to remuneration, following on from the informal consultation that was announced in the Autumn Statement 2015.

Undrawn pension fund in drawdown pensions

As announced in the Autumn Statement 2015, legislation will be introduced through the Finance Bill 2016 to ensure that an inheritance tax charge won't arise when a pension scheme member designates funds into drawdown, then dies before drawing the full fund. This change will be backdated to apply to deaths on or after 6 April 2011. It is designed to fix an anomaly in the current legislation which means that undrawn crystallised funds could potentially be considered for an inheritance tax charge.

Bridging pensions

As announced in the Autumn Statement 2015, legislation will be included in the Finance Bill 2016 to align the pension tax rules for bridging pensions with Department for Work and Pensions legislation, effective from 6 April 2016. This change is the result of the introduction of the new single-tier State Pension.

Dependants' scheme pensions

As announced in the Autumn Statement 2015, the tests that are carried out when a dependants' scheme pension becomes payable will be simplified. These changes will be effective from 6 April 2016 and will be introduced through the Finance Bill 2016.

3. Other

Maintaining the tax advantages of a deceased's ISA during the estate administration period

The government is proposing to consult with ISA providers and there will be further details emerging in 2016 about how these measures are going to be introduced together with legislation.

Help to save scheme

This is to be launched for people on low incomes. To be eligible, individuals have to be in receipt of universal tax credit with minimum weekly household earnings equivalent of 16 hours at the National Living Wage, or those in receipt of working tax credit. Where an individual saves £50 per month, they'll benefit from a 50% bonus (£600) from the government after 2 years. They can then continue to save for another two years and receive a similar bonus. There are no restrictions on what the cash can be used for.

Insurance premium tax

The rate will increase from 9.5% to 10% with effect from 1st October 2016.

Investment bond taxation

The government will consult on alternatives to the current tax rules on part surrenders and part assignments of life policies, later in the year. The aim is for legislation preventing excessive tax charges from arising to be included in the Finance Bill 2017. There will also be a further consultation later in the year on the categories of assets that bondholders can choose to hold within their bond wrapper without an annual tax charge arising under the personal portfolio bond rules.

Automatic deduction of income tax on savings income

The tax rules will be changed so that interest from OEICs, authorised unit trusts and investment trust companies can be paid without deduction of tax from April 2017.

Corporation tax

The main rate of corporation tax is reducing to 17% for the financial year beginning 1 April 2020.

Corporation tax loss relief

There will be a consultation on the reform of corporation tax loss relief published in 2016, with legislation following in 2017. From 1 April 2017:

- The government will limit the amount of profit that can be offset against losses carried forward to 50%. This will only apply where profits are greater than £5,000,000, also
- Businesses will be able to use carried forward losses against profits from other sources of income or from other group companies.

Close companies – participators' loans

Following the dividend tax changes being introduced from 6 April 2016, the rate of tax chargeable on directors loans will increase from 25% to 32.5%. This will prevent shareholder directors from gaining a tax advantage by taking loans from their close company rather than dividends.

Income tax

The personal allowance is increasing to £11,500 for 2017/18. The higher rate threshold will be £45,000 in 2017/18.

Capital gains tax

Basic rate taxpayers will suffer capital gains tax at 10% (currently 18%) and higher rate/additional rate taxpayers at 20% (currently 28%) from 6 April 2016. There is an exception though in relation to properties that don't qualify for principal private residence relief, where the rates of applicable CGT will continue to be 18% and 28% respectively. The intention behind this is to encourage savers to choose to invest in stocks and shares rather than property.

Entrepreneur's relief will be extended to external investors who invest in unlisted trading companies. The individual investor will benefit from a CGT rate of 10% on gains accruing on the disposal of ordinary shares in an unlisted trading company. The shares have to have been newly issued to the claimant and acquired for new consideration after 16 March 2016. They also have to have been owned for a period of at least three years starting from 6 April 2016 to qualify for this relief. There will be a lifetime cap of £10 million of qualifying gains. The investment must be made for a genuine commercial purpose and not for tax avoidance if this relief is to apply.

Modernising tax collection

From 2018 businesses, the self-employed and landlords who are keeping their records digitally and providing regular updates to HMRC can choose to pay tax as they go. There will be a consultation on these measures in 2016.

Stamp duty land tax on additional properties

From 1 April 2016, an additional 3% SDLT will be payable on the purchase of second homes and buy to let properties valued over £40,000. Purchasers will have 36 months rather than 18 months to claim a refund, if due to the move there is a period where they own two residences or they don't own a main residence. The higher rates will apply equally to individuals and corporate investors and there is no exemption for significant investors.

National insurance

From April 2018, class 2 national insurance contributions will be abolished for the self-employed. Class 4 NICs will be reformed.

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