Summer Budget 2015 – Initial Analysis

8 July 2015

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

Contents

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1. Pensions

Lifetime allowance

The lifetime allowance reduction announced in the March 2015 Budget will go ahead. So, there will be a drop from £1.25m to £1m from 6 April 2016. The Summer Budget Statement confirms that there will be new fund protection options introduced to allow those with funds in excess of this limit to protect the greater amount held. There is also confirmation that the Finance Act 2016 will include indexation of the lifetime allowance in line with CPI from 6 April 2018.

Annual allowance

To pay for the reforms to inheritance tax (covered below), there will be a reduced annual allowance from 6 April 2016 for those with 'adjusted annual incomes' including pension contributions of over £150,000. Adjusted annual income includes taxable earnings and all pension contributions, but doesn't include charitable contributions. The reduction will work by tapering with a £1 reduction in the annual allowance for every £2 of adjusted income above £150,000. So, someone with adjusted income of £180,000 will have an annual allowance of £25,000 and anyone with adjusted income above £210,000 would have an annual allowance of £10,000. If an individual's net income (excluding pension contributions) is no more than £110,000 then they will not normally be subject to the tapered annual allowance.

Pension input periods

In an unexpected move, that has immediate effect, the government is aligning all pension input periods with the tax year. All pension input periods already open will end today, 8 July 2015. The next pension input period, the end date of which can't be changed by a pension scheme member or provider, will then start on 9 July 2015 and end on 5 April 2016. All subsequent pension input periods will then run in line with tax years and can't be varied. Complex transitional arrangements will be introduced to ensure that individuals who made pension savings before the Summer Budget will not be disadvantaged. The government's longer term goal appears to abolish pension input periods altogether.

Pensions tax relief

The government has today launched a Green Paper – Strengthening the incentive to save: a consultation on pensions tax relief – consulting on whether there is a case for reforming pensions tax relief to strengthen incentives to save. Possible outcomes could range from radical reforms, such as bringing pensions taxation into line with ISA taxation (the 'taxed, exempt, exempt' structure) to keeping the status quo.

Taxation of death benefits

From 6 April 2016 taxable lump sum death benefits payable to a beneficiary who is an individual will be subject to tax at the recipient's marginal rate of income tax (currently taxed at 45% if paid in tax year 2015/16). Where the recipient of the lump sum is not an individual, for example a trust or a company, the 45% charge will continue to apply.

Transfers and early exit penalties

The government also wants to ensure that people can access the new pension flexibility options easily and at a reasonable cost. They intend to consult during the summer on options to make the process of transferring pensions from one scheme to another quicker and smoother. This will include reference to excessive early exit penalties with the government stating that if there is evidence of such penalties, they will consider imposing a legislative cap on these charges for those aged 55 and above. We may also see a relaxation on transfer rules relating to protected tax-free lump sums and protected pension ages.

Salary sacrifice

Although rumoured beforehand, there are no changes being made to the operation of salary sacrifice arrangements. The government have noted, though, that such arrangements are becoming more popular and the cost to the taxpayer is rising. As a result, they intend to actively monitor the growth of salary sacrifice schemes that reduce employment taxes and their effect on tax receipts.

Pension Wise
According to government figures, 85,000 people have taken advantage of the new pension flexibility options that were introduced from 6 April 2015. To coincide with the new flexibility options, Pension Wise was launched to allow consumers to access free, high quality guidance on their choices. The government is intending to extend access to the service to those aged 50 and above and will launch a nationwide marketing campaign for help further raise awareness of the service.

Secondary annuity market
Having already consulted on the issue, the government will set out its plans for a secondary annuities market in the autumn. Implementation will be delayed until 2017. This will ensure there's a robust package in place to support the decision making process.

EFRBS
The government have announced that they will launch a consultation on tackling the use of unfunded employer financed retirement schemes (EFRBS) in relation to remuneration.

State pension triple lock
The triple lock for increases to the State Pension will be maintained. The triple lock works by increasing the State Pension each year by the highest of the rate of increase in prices, the increase in earnings and 2.5%.

2. Other

Inheritance tax main residence nil rate band

An additional main residence nil rate band is to be introduced with effect from April 2017, for each parent passing their main residential property to their children or grandchildren. The additional allowance is going to be phased in over four years, as follows:-

- £100,000 in 2017/18
- £125,000 in 2018/19
- £150,000 in 2019/20
- £175,000 from 2020/21

Thereafter it will rise in line with the Consumer Prices Index.

As with the current nil rate band, any unused allowance can be transferred to the surviving spouse for use on their subsequent death. This will mean that where couples own a main residential property, they will potentially be able to benefit from a combined nil rate band of £1,000,000 from 2020/21.

Where someone downsizes or sells their home from 8 July 2015, this additional allowance will also be available where they leave assets of an equivalent value to their direct descendants. The nil rate band will be frozen at the current level of £325,000 until the end of 2020/21.

There will be a tapered withdrawal of the additional allowance where the net value of the IHT estate is greater than £2,000,000. This will be on the basis of a £1 reduction in the additional allowance for every £2 that the estate exceeds the £2,000,000 threshold.

Non-domiciled individuals

From April 2017, anyone who has been resident in the UK for more than 15 out of the past 20 tax years will be deemed UK domiciled for tax purposes.

This will bring more people into the IHT net on their worldwide assets, as the period of qualifying UK residency has been shortened from 17 tax years out of 20 to 15 years tax years out of 20.

These deemed domicile rules will also impact on other taxes, such as income tax and capital gains, meaning that if an individual has been resident in the UK for 15 out of 20 tax years, they will be subject to UK income tax and capital gains tax on their worldwide income and capital gains.

Insurance premium tax

Insurance premium tax is to be increased from 6% to 9.5% from 1 November 2015.

Corporation Tax Rates

Corporation tax rates will reduce from 20% to 19% in 2017 and then to 18% in 2020.

Addressing complexity in the tax system

The Office of Tax Simplification (OTS) is to be established on a permanent basis. The terms of reference for the next reviews will be published shortly and these will include a review of a possible closer alignment of income tax and national insurance, together with a review of small company taxation.

Buy to lets
Mortgage interest relief for landlords is to be cut to basic rate. This restriction will be introduced on a phased basis over four years starting from April 2017. Also, the 10% wear and tear allowance is to be abolished and tax relief will only be available for costs that landlords actually incur.

These measures may make investments in buy to let properties slightly less attractive.

Savings
The personal allowance will increase to £11,000 and the higher rate threshold to £43,000 for 2016/17. The Government's objective is to raise the personal allowance to £12,500 and the higher rate threshold to £50,000 by the end of the parliament.

The 10% notional tax credits for dividends is to be abolished from April 2016. This will be replaced by a new yearly £5,000 tax-free dividend allowance, which will be available to all tax payers.

From April 2016, where their dividend income is greater than £5,000, a basic rate taxpayer will pay tax at 7.5%, a higher rate taxpayer will pay tax at 32.5%, and an additional rate taxpayer at 38.1% on their dividend income. Pensions and ISAs won't be impacted by these measures.

Where an individual receives dividends from a close company they will pay additional tax, meaning that there will be less incentive to be paid by dividend rather than salary.