AUTUMN STATEMENT 2013

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1. Introduction

We are all in this together, according to the Chancellor when he set out the painful measures he considered necessary to gain control of the country's deficit back in 2010. We might now say we are all in this forever. It is a sign of how bad things have been that the Chancellor was able to present his most optimistic and upbeat Autumn Statement so far, and still admit that the ratio of national debt to national income will continue to rise for another two years, and the government will only return to surplus in 2018/19. Of course, that is a long way away, in economics and in politics. The Chancellor must persuade the electorate in 2015 that he is the best person to still be in charge when that forecast is tested against the facts.

An even longer term measure announced is a plan to raise the state pension age earlier than previously planned. For women, it is being brought up to equality with men. Moving from 60 to 65 has already started. Then the 65 will become 66, 67 and 68. The Chancellor established a new principle: one third of the average adult life should be spent in retirement, and the other two thirds in work. With life expectancy increasing, the move to 66 will happen in 2020 and 67 in 2028. The Chancellor expects the age to rise to 68 in the mid 2030s and 69 in the late 2040s. People starting in the workforce now will have longer to save for their retirement and will have to worry more about the lifetime allowance for tax favoured pension funds.

This Autumn Statement did not contain any big surprises and that may be the best thing about it. However over 100 pages of notes were supplied on the internet after George Osborne sat down. They contained many details that will make a difference to the tax liabilities and reporting responsibilities of individuals and businesses with some now, some in April 2014, and some a year later.

Our summary covers the main tax changes announced yesterday and include:

- reintroduction of a transferable married couple's tax allowance from 2015,
- personal allowance to rise to £10,000 from 2014/15,
- halving of the final period CGT exemption for private residence relief from 2014,
- introduction of CGT on future gains made by non residents disposing of UK residential property from April 2015,
- bank levy to rise to 0.156% from January 2014,
- improvements to film tax relief for companies from April 2014,
- various anti avoidance measures to be introduced to cover total return swaps, world wide debt cap provisions, double tax relief, corporate debt and derivative contracts, CFCs, employment intermediaries, marketed avoidance schemes,
- abolition of Employers NICs for the under 21s.

2. Personal Taxes

Some of Mr Osborne's backbenchers are very keen to reintroduce a tax incentive for married couples. The married couple's allowance was restricted to those born before April 1935 from 2000 onwards; there are some CGT and IHT reliefs which are restricted to people who are married or in registered civil partnerships, but income tax rules generally apply in the same way to people living together whether they are married or not.

The Chancellor has confirmed that a measure of relief will be reintroduced from April 2015. A married or registered couple, where neither pays tax above the basic rate, will be able to transfer up to £1,000 of personal allowance between them. Because it is not available where either partner pays at 40%, the maximum benefit of this will be a tax reduction of £200 – where one has income at least £1,000 below the personal allowance, and the other pays tax at 20%. At the most, this is a recognition of married status, rather than a significant amount of money that might change people's behaviour.

Changes to personal allowances and tax rates used to be saved up for the very end of the Chancellor's March Budget speech. They were the dramatic punch line that everyone waited for. It is helpful that now we are told everything, or almost everything, four months earlier.

The Autumn Statement confirmed that the personal allowance will rise to £10,000 for 2014/15. This was one of the Liberal Democrats' main aims when entering the Coalition Agreement, and they will be pleased that it has been delivered a year ahead of schedule. It remains to be seen whether they will be able to take enough credit from it to benefit in the 2015 election.

The higher allowances for people born before 5 April 1948 remain frozen until the standard allowances catch up with them. Allowances are still withdrawn at £1 for every £2 by which income exceeds £100,000, which means that the benefit of the new higher personal allowance is completely lost by someone whose income is £120,000.

As expected, the rates of tax remain unchanged, and the level at which the 40% higher rate is payable will drop from £32,010 to £31,865. Combined with the personal allowance, someone with an income above £41,865 will pay at 40% 2014/15. For 2013/14 the figure is £41,450. In both cases, that figure is also the income level at which the rate of Class 1 NIC drops from 12% to 2%, and Class 4 drops from 9% to 2%. Although the higher rate threshold has gone up in monetary terms, it is only an increase of 1%. This means that more people will be liable for higher rate taxes in 2014/15, and more people will have to fill in self -assessment tax returns to settle their liabilities.

The Autumn Statement also includes other announcements of rate changes, including inflation linked uprating of some of the Child Tax Credit and Working Tax Credit figures, the first increase in child benefit for four years (20p for the first child and 15p for other children, less than 1%), and small increases in the taxable benefits for employer provided fuel for company cars..

As usual, the amounts that can be invested in tax-favoured ISAs, junior ISAs and Child Trust Funds will increase from April 2014 in line with inflation. The main ISA limit goes up from £11,520 to £11,880. As announced last year, the annual limit for contributions to tax-favoured pension schemes will fall from £50,000 in 2013/14 to £40,00 in 2014/15. Unused limits of the last 3 years may justify extra contributions.

No further changes have been announced to the other schemes [EIS, SEIS, or VCTs] apart from an anti avoidance measure to stop an investor selling VCT shares and soon after subscribing for more of the same share and claiming relief again.

From April 2014, the government will also introduce a new tax relief for equity and certain debt investments in social enterprises. The government will publish a 'roadmap', explaining what qualifies and how investors will benefit, in January 2014.

Individuals who are not resident in the UK are not liable to UK tax on gains, even on UK situs assets such as UK land and buildings or shares in UK companies. Any change to this rule is argued as very risky as it could drive away foreign investors. However, the Chancellor has announced one specific and important change. From April 2015, non UK resident individuals selling UK residential property will be subject to CGT on 'future gains'. Presumably this means that the charge will apply to gains accruing after April 2015. There will have to be an apportionment between exempt and taxable, where a property has been owned for some years before that date.

3. <u>Tax Avoidance</u>

In every Budget and Autumn Statement, and at regular intervals between, the Chancellor and his ministers make announcements about preventing tax avoidance. This time, he lumped together 'avoidance, evasion, fraud and error' as four related problems that would be tackled by 'the largest package of measures so far this Parliament', with the intention of bringing in £9 billion over the next five years.

Evasion and fraud are illegal, and error is unintentional, so the main area for honest taxpayers to be concerned about is what HMRC will do about avoidance. The schemes used by some very large companies to reduce their liabilities, perfectly legally but possibly artificially, have attracted a bad press. However ordinary taxpayers and tax inspectors tend to disagree over what is a 'scheme' and what is merely sensible behaviour.

One of the main points in this package is a proposal that taxpayers who use tax avoidance schemes, and then have to defend them in the Tax Tribunal, should have to pay the tax upfront if someone else has lost a case in relation to a similar scheme. At present, the Tax Tribunal does not set a binding legal precedent, so an appellant can demand their own day in court and probably learn from the earlier case how to present the argument better.

The circumstances in which taxpayers will have to pay upfront have not been detailed yet, but the rule already applies to most VAT appeals. A VAT assessment has to be paid before the Tribunal can hear an appeal, unless the trader can show that payment would cause financial hardship for the business.

The government also intends to take action against what it regards as ‘high risk promoters’ those advisers who, according to HMRC, encourage clients to enter into aggressive avoidance plans. During 2014, rules will be introduced to define who is a ‘high risk promoter’, and to impose extra conditions for disclosure of their activities by both the promoter and their clients. HMRC clearly hope that this will discourage many people from using such aggressive schemes.

4. Pre Announced Changes

Some changes were announced in the March 2013 Budget to take effect in April 2014. These include a rebate of up to £2,000 in employers’ NIC for all businesses and charities. At over a billion pounds, this is a larger measure than anything announced for the first time in the Autumn Statement. It will have a comparatively larger effect on smaller businesses.

We also knew that the lifetime allowance for tax-favoured pension schemes will be cut from a ‘pension pot’ of £1.5m at retirement to £1.25m for those taking benefits from 6 April 2014. Those whose funds are over or near £1.25m should take urgent advice on the different types of ‘protection’ that they can apply for, before and after April, to avoid charges on amounts above those limits.

5. Main Residence Exemption

The sale of your only or main residence is usually exempt from CGT. This is so even if you cannot sell your old house immediately, so for a time you are living somewhere else. In recent years, the last three years of ownership have remained exempt after you have moved out, even if you moved out years ago and the house has been rented to tenants. From April 2014, this three year period will be cut to 18 months. This should not affect most normal house moves, but will increase the tax charge on some former houses which are now investment properties.

6. National Insurance Contributions

From April 2015, no employer’s NIC will be payable on the salary of a worker under the age of 21, up to the Upper Earnings Limit (in 2015/16, £813 per week). This will cut the cost of employing such a person on £12,000 pa by £550, and on £16,000pa by £1,100. The Chancellor claimed that this would remove the ‘jobs tax’ on a million and a half jobs for young people. The Autumn Statement promises that pension entitlements will not be affected by not paying employer’s NIC – employee’s NIC will still be payable in the normal way.

7. Value Added Tax

After his attempts in the 2012 Budget to make numerous changes to VAT proved extremely unpopular (the ‘pasty tax’ among others), George Osborne now seems wary of meddling with it. The only announcements relevant to VAT concerned some improvements to the retail export scheme [VAT rebates for tourists] and a consultation on the requirement to file VAT returns electronically.

A recent Tax Tribunal held that the requirement for everyone to file online was unreasonable: it did not make appropriate allowances for people with disabilities, a lack of access to or understanding of computers, or religious objections to their use. HMRC are proposing to amend the law, but the circumstances in which alternative filing options will be allowed are still described as 'exceptional'.

8. Employee Shares

From April 2014, the limits for awards of shares to employees in share incentive plans will be increased from £3,000 to £3,600 per year for free shares, and from £1,500 to £1,800 for partnership shares. The maximum amount that an employee can contribute to a 'Save As You Earn' savings arrangement will also increase from £250 to £500 per month.

A SAYE scheme is now only available if linked to a share option scheme, but it is not necessary to use the resulting cash saved to buy shares. If the return on the savings scheme appears attractive compared with other vehicles, it is a useful benefit even if the shares are never bought.

9. Employee Medical Expenses

For many years, medical checkups have been a benefit that an employer could provide to an employee without creating a tax charge, but paying for treatment or for medical insurance would be taxable. From April 2014, a new relief will apply to up to £500 of 'employer-funded occupational health treatment' – this is aimed at employees returning to work after a period of sickness, but could be a useful exemption.

10. Employee Partners

In his speech, the Chancellor commented that John Lewis' employee ownership arrangements contribute to its success, so he will introduce measures to encourage more businesses to follow that model.

From April 2014, transfers of shares that result in a controlling interest in a company being held by an employee ownership trust will be relieved from CGT. Transfers of shares and other assets to employee ownership trusts will also be exempt from IHT, providing certain conditions are met.

From October 2014, in time for Christmas, bonus payments of up to £3,600 made to employees of companies which are controlled by an employee ownership trust will be exempt from income tax. These are generous measures, but they will require business owners to be willing to hand over control of their companies to the workers

11. Corporate Tax

For many years, it has been important to count the number of 'associated companies' in a group. The profit limits of £300,000 and £1.5m for eligibility for the lower 20% small companies rate of corporation tax were divided between the associates.

From April 2015, the main rate of tax becomes 20%, so the rate will no longer be affected by the number of associates. However, liability to pay CT by quarterly instalments will still depend on whether a company's profits are above its own share of the group's £1.5m, so it will still be necessary to count associated companies.

The government will, however, replace the current definition of an associated company with something simpler, based on '51% group membership'. It seems likely that the reduced importance of the definition will enable the simplification of the rule.

The full rate of the Bank Levy is to increase to 0.156% from 1 January 2014.

Following a 2013 review into the operational efficiency of the Bank Levy, the government will introduce legislation to limit the protected deposit exclusion to amounts insured under a deposit protection scheme, treat all derivative contracts as short-term, restrict relief for a bank's High Quality Liquid Assets to the rate applicable to long term liabilities, align the Bank Levy definition of Tier One capital with the new Capital Requirements Directive from January 2014, exclude liabilities in respect of collateral that has been passed on to a central counterparty from January 2014, and widen legislation making powers within the Bank Levy from Royal Assent to ensure it can be kept in line with regulation.

These changes will take effect from January 2015, unless stated otherwise. A response to the consultation will be published alongside draft legislation on 10 December 2013.

Amendments to the existing corporation tax provisions are proposed to ease the rules restricting the availability of relief for corporation tax trading losses when companies change ownership. It will do that in two ways: by allowing a holding company to be inserted at the top of a group of companies and by amending the definition of 'a significant increase in capital' when a change of ownership occurs in a company with investment business, where it will be amended to the capital in the company after the change of ownership exceeding the amount of capital before the change of ownership by both £1 million and 25%.

The government will close down a tax avoidance scheme using total return swaps, with immediate effect, which has enabled companies to pay their profits to a company in the same group located overseas, thus escaping a corporation tax liability.

The government will, with immediate effect from 5 December 2013, make two changes to improve the effectiveness of the world wide debt cap. The first change is to the grouping rules and the second change is to the regulation-making powers.

The government will, with immediate effect from 5 December 2013, close two loopholes to reinforce the UK's double taxation relief policy that relief for foreign tax should only be given where income has been doubly taxed, once in the UK and once in the foreign territory.

The government will introduce legislation to enhance existing anti-avoidance provisions to prevent abuse of the 'bond fund' rules, clarify and rationalise certain aspects of those rules, and permit corporate investors to make a claim in certain prescribed circumstances to disapply the bond fund rules.

Legislation will also be introduced to clarify and rationalise the taxation of corporate partners where loan relationships and derivative contracts are held by a partnership. These changes follow consultation on the review of the legislation governing the taxation of corporate debt and derivative contracts.

The government will, with immediate effect from 5 December 2013, make changes to the CFCs rules to address the transfer offshore of profits from existing UK intra-group lending, and also make a simple legislative fix to ensure the rules work as intended.

The government will cap the amount deductible for intra-group leasing payments for large offshore oil and gas assets, known as bareboat charters, and introduce a new ring fence to protect the resulting revenue. The government will consult with industry in early 2014.

The government has published a list of those banks that have unconditionally adopted the strengthened Code of Practice on Taxation for Banks. Finance Bill 2014 will provide for HMRC to publish an annual report from 2015, which will name those banks that have and have not adopted the Code, and may also name any bank that in HMRC's opinion is not complying with the Code.

12. Business Rates

The Chancellor announced a package of measures to reduce the impact of business rates. A temporary relief for small businesses was supposed to end in April 2014, but has been extended for a further year.

A 2% cap has been imposed on rate increases for the year from 1 April 2014, and a discount of £1,000 will be given to retail food and drink businesses with a rateable value of up to £50,000 for the same year.

There are also reliefs for second properties, longer payment periods, clearing the backlog of rating appeals, and longer term administrative reform.

13. Disguised Employment

HMRC have long had a preference for taxing individuals as employees rather than self employed traders as PAYE gets the money in quicker, and Class 1 NIC is higher than the Class 4 charge.

Where people have set up personal companies to provide their services, the 'IR35' rule has brought them back within PAYE, but HMRC's record in disputes about IR35 suggests it is not as powerful a weapon as they would like.

The Autumn Statement includes an announcement that the legislation on 'employment intermediaries', personal companies, managed service companies and some partnership structures will be strengthened with effect from April 2014, probably focussing on 'umbrella' companies base in offshore tax havens.

This was presented as a measure to stop abuses by the ultimate employer forcing their workers to use the intermediary structure so the employer does not have to apply employment rights such as the minimum wage, employment protection and holiday pay. However, according to the statistics, it is one of the larger revenue raising measures included in the statement.

The Chancellor expects an extra £500m in tax in 2014/15 as a result. Anyone who currently uses such a structure and believes that it avoids Class 1 NIC should be aware that they may come under scrutiny.

14. Qualifying Loan Interest

There are plenty of tax rules which have historically restricted a favourable treatment to UK residents or businesses. It is surprising how many of these linger on, years after it became obvious that European law requires us to be as generous to people and businesses from the EU in general as we are to our own.

One minor change announced in the Autumn Statement is the extension of relief for interest paid on loans to buy shares or make loans to invest in close companies. From April 2014, the borrower will be able to claim a tax deduction if the company is resident anywhere in the EEA. It is also arguable, as this is based on EU law, that anyone who has been denied the relief in the past would be entitled to it before that date.

15. Company Cars

When the tax charge on company cars was introduced, the taxable benefit was usually a lower amount than the annual cost of leasing the car. Now, it can be the other way around. So some employers have tried to reduce the tax by getting their employees to sign the papers, and paying the rentals for them. It seems reasonable that this should be taxed on the money paid rather than on the figure calculated on the basis of the car's list price and carbon dioxide emissions rating, but it appears that HMRC have decided that this is a form of avoidance that threatens tax revenues, so they are introducing rules from April 2014 to make sure that the CO_2 based figure will be used to charge the benefit in this situation.

They will also make sure that any payments made by an employee to the employer, in order to reduce the taxable amount of the benefit, are actually paid in the relevant tax year, rather than much later.

There are likely to be more announcements on 10 December with the publication of draft Finance Bill 2014 legislation and again in March next year.

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