

Budget 2010 – personal tax highlights

A welcome return to stability?

24 March 2010

Despite some speculation as to possible changes, particularly to capital gains tax rates, today's Budget was markedly lacking in any substantive change to the tax system and taxpayers should take heart from a welcome and long overdue bout of stability and consistency from this Government.

However, concerns will of course remain that the difficult decisions about funding the fiscal deficit have simply been postponed until after the election, rather than avoided and that there may be further changes later this year (the notes released today already envisage a second Finance Bill after the election). That notwithstanding, in any circumstances a budget that does not contain any significant upheaval must be considered as positive.

Perhaps the most significant long-term change announced today will be to extend charitable reliefs to certain European charities as well as British ones, bringing the UK into line with recent European Court rulings.

Income and capital gains tax

Income tax

The 50% top rate of income tax will be introduced with effect from 6 April 2010 as previously announced, but that remains the only change as the existing marginal rates are frozen. However, the Chancellor did adopt the 'stealth tax' method of raising revenue by not increasing the thresholds at which the rates apply.

Capital gains tax

Despite speculation that a 32% differential between the top rates of income and capital gains tax would make a rise in the capital gains tax rate inevitable, the Chancellor resisted the temptation to make any changes and it remains at 18% but, as with income tax, the annual exempt amount remains at 2009/10 levels. However, a sweetener was included, with the lifetime allowance for entrepreneurs' relief being doubled from £1 million to £2 million, for gains realised after 5 April 2010.

Charities

In line with the recent European Court rulings in the Stauffer and Hein Persche cases, the scope of all UK charitable tax reliefs has been extended to cover qualifying charitable organisations throughout the EU, not just the UK. This represents a dramatic change for philanthropists looking to fund projects and initiatives outside the UK and will be widely welcomed.

This will be particularly attractive for taxpayers on the remittance basis, who will be able to make donations from untaxed income outside the UK and then claim gift aid relief in the UK, to reduce their UK tax liability further.

Bank payroll tax

The bank payroll tax ('BPT') was announced in the Pre-Budget Report last December. This imposes a 50% tax charge on all bonuses awarded to 'relevant employees' to the extent the bonus exceeded £25,000. The BPT is imposed at the level of the entity paying the bonus, rather than being income tax payable by the employee.

The BPT applies to all bonuses awarded between 9 December 2009 and 5 April 2010 inclusive. There was speculation as to whether the initial period would be extended, but it has been confirmed that this will not be the case. It therefore appears that those banks which traditionally make bonus decisions and announcements after 5 April 2010 will not be subject to BPT.

This appears consistent with the statements made in today's Budget recognising the importance of the financial services industry to the UK economy, especially given that the BPT has raised more than was anticipated.

Stamp duty land tax

Two major announcements were made today with respect to stamp duty land tax ('SDLT').

For first time buyers, relief from SDLT on residential property up to £250,000 will apply for two years where the effective completion date is on or after 25 March 2010 and before 25 March 2012. It remains to be seen how 'first time buyers' will be defined.

Meanwhile, a new band of SDLT, set at 5% for residential properties over £1m, will come into force for purchases where the effective completion date is on or after 6 April 2011. This is a significant change from the current top rate of SDLT at 4% which applies to all properties over £500,000. It introduces a dichotomy between residential and commercial properties and will be very likely to trigger activity within the £1m plus bracket of the residential market during the next tax year, to ensure completion occurs before the new 5% rate comes into force.

Buyers of properties 'off-plan' should particularly beware as, depending on the pace of development, they may well find themselves with a higher bill on completion than they had anticipated.

Inheritance tax

While there were only limited tax increases announced in today's Budget, certain exempt amounts and allowances were frozen. Specifically, for inheritance tax ('IHT') the current nil rate band of £325,000 is to apply in the tax years 2011/12 to 2014/15.

This emphasises the need to put in place effective and timely lifetime planning arrangements to minimise exposure to IHT.

Looking forward, it was announced today that work will be undertaken during 2010 to consider how IHT can be brought within the scope of the Disclosure of Tax Avoidance Schemes ('DOTAS') rules, including a consideration of what 'hallmarks' should govern whether a particular piece of IHT planning would be subject to DOTAS.

In addition to the current freezing of the nil rate band, this suggests a new focus on IHT planning measures.

Pensions

Today's Budget confirmed the restriction of income tax relief for pension contributions for higher earners. For those with income of £150,000 or over (income to be calculated without taking into account deductions for pension and charitable contributions), but below £180,000, income tax relief will be restricted from 6 April 2011 so that the greater the earnings the lower the applicable rate of income tax relief, only basic rate relief will be available for those with income of £180,000 or more. Individuals could be in this bracket where their income is £130,000 or over but employer pensions contributions mean that their income is £150,000 or over. For those earning over £180,000 only basic rate income tax relief will be available for pension contributions with effect from 6 April 2011. Anti-forestalling provisions apply prior to 6 April 2011, in outline, for the current tax year relief may be restricted for those earning in excess of £130,000.

It is important to be aware of the anti-forestalling provisions and while the full restrictions do not come into effect until 6 April 2011, it would be prudent to investigate tax efficient pension alternatives in good time prior to that. It is important to remember that simply making higher pension contributions will not be a viable option for most higher earners as a means of mitigating the 50% income tax rate.

Detailed changes

Enterprise Management Incentives (EMI)

Technical changes will be introduced to the EMI rules so that companies using this tax efficient remuneration mechanism must have a permanent establishment in the UK.

Venture Capital Trusts (VCT) and the Enterprise Investment Scheme (EIS)

The rules relating to VCTs will be amended to increase the proportion of qualifying investments that must be held in eligible shares, but also to widen the definition of 'eligible shares'. Further changes are also introduced to both the VCT and EIS rules in accordance with an agreement with the European Commission.

The Remittance Basis

Non-domiciled taxpayers will have breathed a sigh of relief that they did not come in for a pre-election whipping, with the only a minor technical change to the remittance basis being announced. This amends the definition of 'relevant person' to include subsidiaries of 'close' non-resident companies.

Anti-avoidance measures

A series of specific anti-avoidance announcements were made. In relation to SDLT, measures to target avoidance that seek to avoid or reduce SDLT through the use of partnerships are to be introduced. SDLT partnership transactions entered into before today are likely to be unaffected.

Transactions in securities

With effect from today, the scope and operation of the legislation targeting income tax planning through transactions in securities is to be amended.

The transactions in securities legislation currently counters certain income tax advantages where a taxpayer receives an abnormally large dividend pursuant to one or a number of transactions in securities. New legislation will clarify precisely how to quantify the tax advantage, which may be helpful in terms of determining whether these widely drafted provisions do or do not apply to a particular transaction.

Employment Income and Trusts

Following what seems to be a very targeted announcement, there is to be a focus on preventing income tax and NICs avoidance through the use of employee benefit trusts and other entities, with specific legislation which will come into effect from 6 April 2011.

Although the scope and focus remains to be seen, this may represent a response to aggressive planning seeking to reduce the impact of the 50% income tax rate through the use of complex income payment arrangements.

HMRC's powers

As expected, there will be further measures to encourage the payment of the right amount of tax at the right time. The penalty regime for late filing of tax returns already applies to income, corporation, inheritance and other direct taxes and will be extended to VAT and a host of other levies and duties. The late payment of taxes and duties will be treated separately to late filing but both include an escalating series of penalties.

There will also be further deterrents for those who do not declare tax liabilities on offshore income and gains. This continues the theme of ensuring compliance by taxpayers who hold assets abroad. Of particular note is that penalties are higher for jurisdictions which do not automatically exchange information on savings income with the UK – here the penalty will be up to double the usual amount.

To find out more:

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