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Summer Budget 2015: Implications for Education

The 2015 Summer Budget continued with the previous Budget's theme of delivering a truly national recovery, with specific focus on economic security.

The economic security agenda includes provisions to:

- Introduce legislation for a "tax lock" to rule out increases in the main rates of income tax, the standard and reduced rates of VAT and Class 1 National Insurance for the duration of this Parliament;
- Continue to target those who evade or avoid paying taxes to ensure all businesses and individuals make a fair contribution towards reducing the deficit;
- Address a number of imbalances identified in the tax system where support disproportionately benefits certain groups or types of business structure; and
- Establish the Office of Tax Simplification on a permanent basis with an expanded role and capacity.

A number of further specific provisions affecting the education sector were announced in the Summer Budget including:

- Funding to be raised to support 3 million apprenticeships starts this Parliament through a levy on large employers;
- Replacing maintenance grants with loans with the aim of putting higher education funding onto a more sustainable footing;
- Allowing Higher Education Institutions offering high teaching quality to increase their tuition fees in line with inflation from 2017-18;
- Committing to the establishment of a network of National Colleges;
- Supporting the UK's research base to deliver continued excellence, as well as driving the commercialisation of findings, by delivering on the Government's science capital commitment, investing in infrastructure, inviting universities to help map strengths and identify areas of strategic focus through a series of science and innovation audits.

There was one significant current issue in the education sector which was not mentioned in the Budget – Gift Aid.

Gift Aid

Final clarification continues to be sought from HMRC in relation to the corporation tax implications of the technical analysis of Gift Aid donations paid by wholly owned subsidiaries, as set out in the Technical release issued by the Institute of Chartered Accountants in England and Wales in October 2014. We understand that HMRC will conclude their thoughts in the near future.

We have summarised below the key taxation proposals which could affect education institutions arising from the Summer Budget Report delivered on 8 July 2015. Click here for KPMG's general commentary on the 2015 Summer Budget Report.

Corporation Tax

Research and Development Expenditure Credit (RDEC)

You will most likely already be aware that the legislation in respect of RDEC is to be changed so that universities and charities are unable to claim RDEC going forward. The Summer Budget Report states that this is to correct an anomaly in the legislation so that universities and charities cannot claim it, in line with the original intention of the policy. We do not currently know how the legislation will be changed, but will of course keep you updated.

The change is to apply to expenditure incurred from 1 August 2015, which means that claims can still be made for periods up to and including the year ended 31 July 2015.

It is common place for education institutions to own non-charitable subsidiary companies. The following announcements made in the Summer Budget will be applicable to such companies and may therefore be of interest to you.

Rate of corporation tax

The current rate of corporation tax is 20%. This is set to decrease to 19% from 1 April 2017 and to 18% from 1 April 2020.

Capital allowances

In the 2014 Budget there was an announcement that the Annual Investment Allowance limit would fall from £500,000 to £25,000 from 1 January 2016. The government has announced in this Budget that the allowance will be permanently set at £200,000 for expenditure on plant and machinery incurred from 1 January 2016.

Goodwill

Currently a tax deduction can be claimed for the acquisition cost of goodwill. This measure will apply to accounting periods beginning on or after 8 July 2015, but not in respect of acquisitions made before 8 July 2015.

A loss arising on a disposal of such goodwill (purchased on or after 8 July 2015) will be treated as a non-trade expense (currently it is part of the trading profits calculation). This means it cannot be offset against trading profits in a different period.

Tax payments

From 2017, corporation tax payments for groups with taxable profits over £20m will be payable in the 3rd, 6th, 9th and 12th month of the accounting period they relate to, a significant acceleration in their tax payment profile.

VAT and other indirect taxes

Introduction of Climate Change Levy (CCL) on energy from renewable sources

The exemption from CCL in respect of electricity generated from a renewable source will be removed from 1 August 2015. If you currently buy electricity from a renewable source you are not charged CCL by your supplier. From 1 August 2015 CCL will become payable, but only to the extent that the electricity is consumed for non-qualifying purposes.

It is important for universities to ensure that they are maximising their qualifying use entitlement to ensure that not only do they receive the correct amount of energy at the reduced rated of VAT, but they can still benefit from a CCL exemption on energy used for qualifying purposes.

There were no significant VAT changes introduced that should impact universities.

Insurance Premium Tax

From 1 November the standard rate of Insurance Premium Tax will be increased from 6% to 9.5%.

Income and employment tax

<u>Simplification</u>

Making tax easier

The government is to commission the Office of Tax Simplification to review the closer alignment of income tax and National Insurance Contributions.

<u>Rates and thresholds</u>

Personal Tax

The income tax personal allowance will increase from £10,600 in 2015-16 to £11,000 in 2016-17. It will increase to £11,200 from 2017-18.

The government will increase the higher rate threshold from £42,385 in 2015-16 to £43,000 in 2016-17 and to £43,600 in 2017-18.

The government will also have a legal duty to consider the impact of the level of the personal allowance on an individual working 30 hours a week on the National Minimum Wage (NMW) and to report on this at each fiscal event. To underpin this, the government has also announced a review of the NMW timetable to align it with the tax year.

National Insurance

The NICs Upper Earnings Limit will increase to remain aligned with the higher rate income tax threshold.

<u>*National Living Wage & National Minimum Wage*</u>

A premium for those aged 25 and over, starting at 50 pence, will be introduced leading to a new National Living Wage (NLW) of £7.20 from April 2016.

An additional £1 million in 2015-16 to be invested in NMW enforcement to tackle non-compliant employers.

<u>*Employee expenses and benefits*</u>

Consultations on terminations and travel & subsistence

Following recommendations by the OTS, the government will consult on simplifying the tax and NICs treatment of termination payments and the tax treatment of travel and subsistence. We anticipate that the consultation papers will be published in the coming weeks.

Voluntary payrolling of benefits

Draft regulations have been published to underpin the introduction of voluntary payrolling of benefits in kind with effect from April 2016. The new regime has been extended to cover almost all benefits in kind, with the following exceptions: accommodation; beneficial loans; credit tokens and vouchers. Additional reporting requirements where employers payroll company cars will be introduced from April 2017.

Business expenses exemption and scale rate payments

Draft regulations have been published relating to scale rate payments under the forthcoming business expenses exemption, which will take effect from April 2016. Under the new regulations, the following "standard meal allowance" day rates will be available:

(a) £5 where qualifying travel is 5 hours or more; or

(b) £10 where qualifying travel is 10 hours or more; or

(c) £25 where qualifying travel is 15 hours or more and is ongoing at 8pm on that day.

And this will be supplemented by an additional meal allowance not exceeding £10, in cases where either the £5 or £10 meal allowance is paid and the qualifying travel remains continues beyond 8pm on that day.

Trivial Benefits Exemption

As announced at Autumn Statement 2014, from April 2016 the government will simplify the tax system by introducing a statutory exemption for trivial benefits in kind costing less than £50.

Company car tax rates for 2019-20

The appropriate percentage of list price subject to tax will increase by 3 percentage points for cars emitting more than 75 grams of carbon dioxide per kilometre (gCO2 /km), to a maximum of 37%, in 2019-20.

No announcement has been made regarding whether a benefit in kind will arise on the provision of electric fuel, nor has there been any indication of a published Approved Mileage Allowance Payments or advisory fuel rate for electric vehicles.

Employment Allowance

The government will increase the annual Employment Allowance from £2,000 to £3,000. This will come into effect from April 2016. Companies where the director is the sole employee will no longer be able to claim the Employment Allowance from April 2016.

Tax-Free Childcare

As announced on Wednesday 1 July, the government reaffirms its commitment to introducing Tax-Free Childcare to support working parents with the costs of childcare. Due to a legal challenge, Tax-Free Childcare will now be launched from early 2017.

Short Term Business Visitor (STBV) Agreement

HMRC announced that they will be introducing a new procedure to simplify the administration of PAYE in respect of short term business visitors (STBVs) who do not qualify for exemption from UK taxation under the terms of a double tax treaty.

Salary Sacrifice

The government will actively monitor the growth of salary sacrifice schemes that reduce employment taxes and their effect on tax receipts. No further announcement on pension or any other salary sacrifice has been made.

Remuneration Planning

Unfunded employer financed retirement benefit schemes (EFRBS) – The government will consult on tackling the use of unfunded EFRBS to obtain a tax advantage in relation to remuneration planning.

Intermediaries

Employment intermediaries and tax relief for travel and subsistence

As initially announced in March, the government intends to restrict tax relief for travel and subsistence for workers engaged through an employment intermediary, such as an umbrella company or a personal service company. A consultation on the detail of the measures has been published and following its conclusion the changes will take effect from 6 April 2016.

IR35 reform

The government will engage with stakeholders this year on how to improve the effectiveness of existing intermediaries' legislation ('IR35') which is designed to protect against disguised employment. Any organisation that engages individuals through the individual's personal service business (limited company or partnership) may be affected by any proposed changes.

Non-Domiciled Individuals

The government will legislate so that from April 2017 anybody who has been resident in the UK for more than 15 of the past 20 tax years will be deemed to be domiciled in the UK for tax purposes and any individual born in the UK to parents who are UK domiciled will not be able to claim non-domicile status whilst they are resident in the UK.

Pensions

Annual Allowance and Lifetime Allowance

The Chancellor has announced a reduction to the Annual Allowance to £10,000 a year for higher earners. This is in addition to the cut in Lifetime Allowance to £1 million from 2016 which has already been announced and will impact those earning around £75,000 or more. Those earning over £110,000 are very likely to be impacted by both the Lifetime and Annual Allowances, which means that they may not get value back for their own pension contributions and may leave their scheme. The new rules will be effective from 6 April 2016.

The Annual Allowance reduction will be tapered from the current £40,000 threshold down to £10,000 for those earning between £150,000 and £210,000. Earnings for this purposes is based on a new definition, "adjusted income", which includes income from investments and property for example. Crucially, it also includes the value of the employer's contributions (see below). The reduction is applied by removing £1 of Annual Allowance for every £2 of adjusted income.

The value of the employer's contributions is easy to assess for Defined Contribution schemes. Not so for Defined Benefit schemes. So the value will have to be calculated in the same way as for the Annual Allowance calculation, by applying a factor of 16 to the increase in the benefit. This "Pension Input Amount" will be adjusted to reflect employee contributions to determine a deemed employer contribution. Higher earning Teachers Pension Scheme and Local Government Pension Scheme (and Universities Superannuation Scheme (USS) Final Salary section) members with long service and a real pay rise can relatively easily accrue a Pension Input Amount which exceeds £40,000. Those in the USS Career Revaluated Benefits section may also be impacted and the current reform proposals will make a significant impact on pension growth calculations for those who move from the Final Salary section to any new CRB scheme.

The Chancellor's detailed notes include reference to another new earnings definition called "threshold income", which includes earnings sacrificed for pension provision and other income such as from investments and property. Those with threshold income of £110,000 or less will not be subject to any reduction in the Annual Allowance (it will remain at £40,000). For those with threshold income above £110,000 the adjusted income figure will apply, and the inclusion of the employer contribution amount will count towards the £150,000 and may then lead to a tapering in the Annual Allowance. This means members are very likely to see their Annual Allowance reduce. So they will incur an additional Annual Allowance charge (or a new charge if otherwise they would not have had one), as well as a Lifetime Allowance charge.

Our initial calculations show that employees earning above around £170,000 will see full tapering of the Annual Allowance down to £10,000. This means they may face an additional Annual Allowance tax charge of £13,500 a year – this is above the amount they may have paid anyway. At this earnings level, the Budget changes could be viewed as a 10% pay cut. When viewed alongside continued pay restraint we anticipate that affected members may be seeking to understand their options – without options they may leave the scheme and possibly their employment. With an inflexible pension such as the TPS and LGPS, options may seem limited, but must be explored. The USS has some options currently and as mentioned the proposed change to CRB for all future service will lessen the likelihood of breaching the Annual Allowance. But the risk remains for those with income above the new definitions that they will still be affected and could be facing higher tax charges.

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