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United Kingdom – Budget 2016 Contains a Few Surprises

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In This Issue:

On 16 March 2016, the Chancellor of the Exchequer presented the U.K.'s 2016 Budget Statement,[1] which, amongst other things, reiterated some previously-announced measures, tightened some reliefs for certain benefits and pensions, and lowered capital gains tax for disposals made on or after 6 April 2016. In addition, the Budget introduces a "Lifetime ISA" to help individuals save for buying a home and/or retirement.

Finance Bill 2016, which will include the specific detail on measures due to take effect from 6 April 2016, is expected to be published on 24 March 2016, and an update from KPMG LLP (U.K.) will follow shortly thereafter.

Why This Matters

The Budget measures, taken together with previously-announced changes, aim to tighten the conditions for some tax reliefs, but there are also some simplifications proposed. This could raise individuals' tax burdens and thus the costs to employers of international assignees.

However, the changes to the upper threshold for the basic-rate tax band and the rise in personal allowance could serve to slightly lower equalization costs for companies with inbound assignees; for those with larger populations, the cumulative savings may represent a significant saving on total costs. The savings and dividend exemptions, together with the reduction in capital gains tax, may limit the exposure to U.K. tax on the personal income and gains of most assignees.

For individuals on assignment to the United Kingdom where assignees are subject to U.K. taxation, and for assignees working outside the U.K. but still subject to U.K. taxation, international assignment cost projections and budgeting should reflect the changes described in this newsletter once they come into effect.

Generally, the Statement contained measures concerning the taxation of personal income, savings and capital gains, the application of National Insurance Contributions (U.K. social security, known also as "NICs"), and the treatment of termination payments, amongst other measures and plans. We describe the main measures impacting individuals and their employers below.

Termination Payments

Following a consultation last year, the government announced that, from April 2018:

- there will be a tightening of the conditions for income tax relief including, we understand, the withdrawal of Foreign Service Relief (FSR); and
- the introduction of employer NICs on payments over £30,000 which are subject to income tax.

Further details will be outlined in the forthcoming technical consultation over the summer.

KPMG Note

Any potential withdrawal of FSR would add to the tax complexity around termination of assignees or former assignees, making it necessary to give more consideration to the application of double taxation treaties. Any withdrawal of FSR might also naturally extend to the relief available to lump-sum payments from foreign pension plans.

Salary Sacrifice

There was considerable speculation prior to the Budget that the government would remove the use of salary sacrifice arrangements by employers wanting to provide benefits to employees in a tax efficient way. The government has now announced that it is considering limiting the range of benefits which can attract income tax and NIC relief in these circumstances.

The government confirmed, however, that salary sacrifice arrangements for pension saving, child-care, and cycle-to-work arrangements should continue to benefit from income tax and NICs relief, which is welcome news.

Deemed Domicile

In addition to the previously announced changes to the U.K. domicile rules (see GMS *Flash Alert* 2015-083 (9 July 2015)), Budget 2016 confirms that foreign domiciled individuals ("non-doms") who become deemed domiciled for all U.K. tax purposes on 6 April 2017 – because they have been U.K. resident for 15 of the past 20 tax years – can treat the cost base of their non-U.K. assets as being the market value on 6 April 2017. Therefore, only the increase in value accruing post 6 April 2017 will be taxed on the arising basis when assets are sold at a profit after this date.

KPMG Note

It is not clear whether this will be a one-off rebasing to market value at 6 April 2017 or whether the rebasing date will be linked to when an individual becomes deemed domiciled, if he or she is not deemed domiciled on 6 April 2017.

Income Tax

Thresholds

No changes were announced to the income tax rates and thresholds which were already planned to apply from 6 April 2016 (see *Flash Alert* 2015-083 (9 July 2015)).

The Chancellor announced in the Budget that the personal allowance will rise again to £11,500 in April 2017. The upper threshold for the basic-rate tax band will also increase further than previously announced (to £33,500 in April 2017). (See the table on the next page.)

	Rate	2015/16	2016/17	2017/18
Personal Allowance	0%	£10,600	£11,000	£11,500
Basic rate	20%	£0 - £31,785	£0 - £32,000	£0 - £33,500
Higher rate	40%	£31,786 - £150,000	£32,001 - £150,000	£33,501 - £150,000
Additional rate	45%	Over £150,000	Over £150,000	Over £150,000

KPMG Note

This will slightly lower equalization costs for inbound assignees; but for those companies with larger populations, the cumulative savings may represent a significant saving on total costs.

Income Tax on Dividend and Savings Income

As previously announced, a Personal Savings Allowance (PSA) will be introduced from 6 April 2016, which exempts basic-rate taxpayers from income tax on the first £1,000 of savings income. Higher-rate taxpayers will be exempt from income tax on the first £500 of savings income. There will be no exemption for additional-rate taxpayers. In conjunction with this, the automatic withholding at source of 20-percent tax on savings income will cease from this date.

From 6 April 2016, a new Dividend Allowance of £5,000 per year will be introduced as previously announced. Dividend income above the allowance will be subject to tax at 7.5 percent for basic-rate taxpayers, 32.5 percent for higher-rate taxpayers, and 38.1 percent for additional-rate taxpayers.

National Insurance Contributions (NIC)

Rates and Thresholds

The previously announced NIC rates for 2016/17 are unchanged (see GMS *Flash Alert* 2015-144 (2 December 2015)).

Abolition of Class 2 NICs

As previously announced, Class 2 NIC will be abolished from April 2018. Whilst primarily a cost borne by self-employed individuals in the U.K., many U.K.-outbound assignees choose to voluntarily pay Class 2 NIC while away from the U.K. in order to maintain their eligibility for U.K. state benefits, principally a U.K. state pension.

KPMG Note

A full year of Class 2 contributions would currently cost £145.60 in tax year 2015/16. If no carve out is introduced from April 2018, individuals working and living outside the U.K. who wish to maintain their U.K. social security contribution record would instead have to opt to pay Class 3 NIC. A full year of Class 3 contributions in 2015/16 will cost significantly more at £733.20 a year based on current rates.

Capital Gains Tax (CGT)

Rates

The surprise announcement in the Budget speech was a reduction in CGT rates for disposals made on or after 6 April 2016. The highest rate will decline from 28 percent to 20 percent, and for basic-rate taxpayers the rate is reduced from 18 percent to 10 percent.

The existing 28-percent and 18-percent rates will continue to apply to carried interest and, of particular importance for assignees, to disposals of residential property. The rules on relief for principal private residences remain unchanged.

Annual Exempt Amount

The capital gains tax annual exempt amount for individuals, personal representatives, and trusts for individuals with a disability will remain unchanged at £11,100 from 6 April 2016. The exempt amount for all other trusts will rise to £5,550.

Pensions and Savings

Allowances

In the 2015 Summer Budget, the Chancellor announced several measures aimed at restricting tax relief for pensions (see GMS *Flash Alert* 2015-083 (9 July 2015)). There were no further changes to those measures, including the Annual Allowance (£40,000) and Lifetime Allowance (reducing from £1.25 million to £1 million) or the level of income at which the Annual Allowance would be tapered to £10,000 (£1 for every £2 between income of £150,000 and £210,000).

Unfunded Employment Retirement Benefit Schemes

The government has not announced any changes to the treatment of these arrangements, although such plans will continue to be "kept under review."

Individual Savings Account (ISA)

The total ISA allowance is increasing to £20,000 a year from April 2017. Income and gains arising on an ISA are exempt from U.K. tax and the allowance has increased significantly over recent years to encourage saving.

Lifetime ISA

The government has not chosen to go ahead with further radical reform of the U.K. pensions system. However, the Chancellor has announced the introduction, from April 2017, of a Lifetime ISA for those between the ages of 18 and 40. The aim of this is to both support the purchase of a home and retirement. Individuals will be able to invest up to £4,000 per year, with a government top-up of 25 percent. The Lifetime ISA might be seen as a transitory measure that will ultimately lead to the introduction of a "taxed-exempt-exempt" (ISA-style) pensions system.

The money saved can be used to buy a home costing up to £450,000 or can be withdrawn from the age of 60. The money can be withdrawn earlier for other reasons, but in these situations the government top-up plus interest on it must be returned with an additional 5-percent charge. A consultation on the detail will follow.

Other Measures

Disguised Remuneration

The government will tighten the existing anti-avoidance provisions applicable to "disguised remuneration" delivered via third parties such as Employee Benefit Trusts (EBTs).

Legislation will be included in Finance Bill 2016 and Finance Bill 2017 dealing with legacy loan arrangements, transitional relief provided further to the EBT Settlement Opportunity, and other specific avoidance that has been identified. The government has reiterated its determination that employees and employers "should pay their fair share of tax."

Footnote:

1 See: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/508193/HMT_Budget_2016_Web_Accessible.pdf and https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/508441/Overview_of_Tax_Legislation_and_Rates_2016.pdf .

For the 16 March 2016 government press release "Budget 2016: Some of the Things We've Announced," see: https://www.gov.uk/government/news/budget-2016-some-of-the-things-weve-announced .

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