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UK Summer Budget 2015

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On Wednesday, 8 July 2015, George Osborne delivered the UK Summer Budget. The first Budget of the new Conservative government (and the second Budget of 2015), the Summer Budget is wide-ranging in scope and potentially significant in effect. Set out below are some of the announcements that will be relevant to the financial services industry and a list of the key measures that took effect as of 8 July 2015.

Changes effective as of 8 July 2015

Carried interest: capital gains treatment

As of 8 July 2015, individual investment fund managers may be charged to UK capital gains tax (CGT) on the full amounts of their carried interest. The amount subject to UK CGT will be calculated after certain (limited) deductions, such as cash consideration in money given by the carried interest holder to acquire the carried interest or amounts that constitute taxable earnings of the carried interest holder. "Base cost shifting," which allowed the carried interest holder to reduce his/her chargeable gain in respect of the carried interest by claiming a deduction for acquisition costs of investment incurred by the other investors in the fund, has been stopped as of 8 July 2015.

Additionally, going forward, the new rules may mean that gains will be treated as UK-sourced to the extent that the individual performs his/her investment management services in the UK. This may mean that, to the extent of their UK activities, UK resident but non-UK domiciled individuals may be subject to CGT on carried interest whether or not this is remitted.

Anti-avoidance provisions will apply to counteract arrangements designed to secure that the new rules do not apply.

Corporation tax: no relief for business goodwill amortisation

For transactions taking place on or after 8 July 2015, corporation tax relief will not be available for the acquisition costs of goodwill and certain intangible assets from a third party seller. Debits arising on the disposal of goodwill and intangible assets that are subject to the new rules will be treated as non-trading debits.

The UK government considered that tax relief for purchasing goodwill was one of the main factors in determining whether to structure an M&A transaction as a business acquisition rather than an acquisition of the shares in the target. This type of structuring will now need to be revisited.

Controlled foreign company: loss restriction

As of 8 July 2015, companies subject to a controlled foreign company (CFC) charge will no longer be able to set off any losses or surplus expenses against such an amount.

Restricting tax relief for bank compensation payments

Legislation will be introduced to prevent banks and building societies from taking deductions for tax purposes in respect of compensation payments made to customers for misconduct and mismanagement issues. This measure applies to compensation payments made on or after 8 July 2015.

Other relevant announcements

Corporation tax: main rate to be reduced

One of the headline changes announced as part of the Summer Budget was the forthcoming reduction of the main rate of corporation tax, which will take effect as follows:

- 1 April 2017 – the main rate of corporation tax will be reduced to 19 percent
- 1 April 2020 – the main rate of corporation tax will be further reduced to 18 percent.

Financial intermediaries: requirement to notify customers of the impact of the Common Reporting Standard

As part of the UK government's continued commitment to the increasingly global efforts to combat tax evasion, legislation will be introduced to require financial intermediaries, tax advisors and other professionals to notify UK resident customers with UK or overseas accounts about the Common Reporting Standard, the civil and criminal penalties for tax evasion and to highlight opportunities to disclose their tax affairs to Her Majesty's Revenue & Customs (HMRC). Regulations implementing these changes will be made after the date of Royal Assent to the Summer Finance Bill 2015.

Consortium relief: removal of location of link company requirements

Historically, for corporation tax group relief to flow between a consortium and a company in the same group as that consortium (the link company), the link company was required to be located in the United Kingdom or the European Economic Area. This requirement has been lifted and, provided that the other conditions for group relief are satisfied, relief will now be available regardless of the location of the link company. This measure will have a retrospective effect for consortium claims to group relief for accounting periods beginning on and after 10 December 2014.

Corporate debt and derivatives rules

The Summer Budget confirmed that the UK government intends to proceed with the reform of the loan relationships and derivatives rules, details of which were announced in the 2014 Autumn Statement and in respect of which draft legislation was published on 10 December 2014. To recap, the main changes are:

- removal of the requirement that amounts brought into account for tax must "fairly represent" the profits, gains and losses arising
- new rules stating that, when calculating loan relationship credits and debits, regard is had to only the profit and loss account so that taxation will be based on only amounts recognised as items of

accounting profit or loss rather than on amounts recognised anywhere in accounts (e.g., in reserves or equity)

- introduction of new “corporate rescue” provisions that have the effect of (i) extending to corporate borrowers in financial distress the existing exemptions from taxation on debt releases and (ii) introducing a new tax exemption for such borrowers on refinancing (or “amend and extend”) transactions
- new regime-wide anti-avoidance rules to counter arrangements entered into with a main purpose of obtaining a tax advantage under the loan relationships or derivative contracts rules.

The changes set out above will be effective for accounting periods commencing on or after 1 January 2016, with two exceptions:

- the new corporate rescue exemptions will apply to releases and modifications of debt taking place on or after Royal Assent to the Summer Finance Bill 2015
- the new regime-wide anti-avoidance rules will apply to arrangements entered into on or after the same date.

Peer-to-peer lending: withholding and bad debt relief

Another measure originally introduced in the 2014 Autumn Statement that has made its way through to the Summer Budget is new legislation providing relief for individuals lending through peer-to-peer platforms. Individual lenders will be allowed to offset any losses from such loans against interest income received from similar peer-to-peer loans. Draft legislation is due to be published later in 2015, with the measure expected to be included in the Finance Bill 2016.

The UK government has also pledged to consult on proposals regarding the introduction of a withholding regime for income tax applicable to all peer-to-peer lending platforms, with legislation expected to be introduced in the Finance Bill 2016.

Non-UK domiciled individuals

The UK government is proposing to limit the availability and benefit of non-UK domiciliary status, with effect from 6 April 2017.

Under the proposals:

- individuals resident in the United Kingdom for more than 15 out of the past 20 tax years will be deemed UK-domiciled for UK tax purposes; a technical consultation concerning this change will be published later in 2015
- individuals born in the United Kingdom with UK-domiciled parents will no longer be able to claim non-UK domiciliary status (for example, if the individual leaves the United Kingdom and acquires a domicile of choice in another jurisdiction) while they are UK resident

- UK residential property, including that held indirectly via an offshore structure owned by a non-UK domiciliary, will, regardless of its residence status, be brought into the scope of inheritance tax; a consultation on these proposals will be launched later in 2015.

Banking tax reform

The Summer Budget announced a “long-term roadmap” on bank taxation, involving a phased reduction of the bank levy rate from 0.21 percent falling gradually to 0.10 percent from January 2021, but also the introduction of a new “corporation tax surcharge” in the form of a supplementary tax at a rate of 8 percent on banks’ corporation tax profit. This profit will be calculated before the use of existing carried-forward losses, but the supplementary tax will not apply to the first £25 million of profit within a group.

Pensions tax relief

The government proposes to introduce, from April 2016, a taper to an individual’s annual allowance (currently £40,000 per year) for pension savings tax relief. The taper may apply to those individuals with adjusted annual incomes, including pension contributions, exceeding £150,000. For every £2 of adjusted income more than £150,000, the annual allowance will be reduced by £1, down to a minimum of £10,000.

Consultation regarding the taxation of performance-linked rewards paid to asset managers

The UK government has launched a consultation regarding the criteria for determining when fees arising to fund managers are to be taxed as income, rather than capital, as part of plans to legislate on the issue with effect from 6 April 2016.

The UK government intends to legislate to introduce a default rule that all performance-linked rewards paid to asset managers will be taxed as income with carve-outs for specific activities and arm’s-length co-investments. The UK government has set out two main options for introducing these rules:

- establishing a “white list” of investment activities that will be charged to tax as chargeable gains
- establishing a “holding period” test so that capital treatment is available in circumstances where fund managers are granted a stake in underlying long-term investments.

Reform to dividend taxation

The Summer Budget also contained the abolition of dividend tax credits for individuals and the introduction of a new tax-free £5,000 dividend allowance, which will take effect from 1 April 2016.

The new system of dividend taxation is likely to represent a material increase in tax for additional rate taxpayers holding large equity portfolios. Dividend income in excess of the £5,000 tax free allowance will be taxed at the following effective tax rates:

- basic rate: 7.5 percent (2015-2016 effective rate: zero)
- higher rate: 32.5 percent (2015-2016 effective rate: 25 percent)
- additional rate: 38.1 percent (2015-2016 effective rate: 30.56 percent).

Stamp duty land tax seeding relief for property authorised investment funds and co-ownership authorised contractual schemes

It was announced that, as part of the Finance Bill 2016, legislation will be introduced to grant stamp duty land tax (SDLT) seeding relief for the transfer of existing property portfolios into a property authorised investment fund (PAIF) or an authorised contractual schemes (ACS) and, subject to resolving potential tax avoidance issues, to amend the SDLT treatment of co-ownership ACSs so that SDLT is not payable on transactions in units.

Insurance premium tax: standard rate to be increased

As part of a bid to increase the tax revenue raised by insurance premium tax (IPT), the UK government has announced that the standard rate of IPT is to be increased from 6 percent to 9.5 percent. This is an unpopular move and has been criticised by industry commentators as a "stealth tax." However, it is expected to raise an estimated £1.5 billion a year and is anticipated to have the largest financial impact of any of the measures introduced as part of the Summer Budget. The new standard rate will be due on premiums treated as received on or after 1 November 2015, except where insurers operate a special accounting scheme. For operators of special accounting schemes, the new standard rate will apply to premiums relating to risks covered by contracts entered into on or after 1 November 2015. From 1 March 2016, the new standard rate will apply to all premiums, regardless of when the contract was entered into.

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