CITY AM UK

What will Rishi Sunak's Budget mean for personal taxes?

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6.3.2020

With a commitment to leave rates for income tax, national insurance and VAT unchanged, the new Chancellor may be looking for other areas to raise tax in March's Budget – possibly in capital gains tax and inheritance tax. In addition, the Conservative Party manifesto contained commitments to "review and reform" entrepreneurs' relief (ER) as well as to "redesign the tax system so that it boosts growth, wages and investment and limits arbitrary tax advantages for the wealthiest in society." It is not clear what advantages the Conservatives had in mind, but it seems reasonable to assume that personal tax will be an area where they want to focus some change. What are the key aspects?

Capital gains and entrepreneurs' relief

It is not clear how wide-ranging the proposed "review and reform" of ER will be. However, both the Office for Tax Simplification (OTS) and the Institute for Fiscal Studies have suggested that the relief is expensive and does little to encourage investment. The suggestion is that the relief is given at the wrong point in the life cycle of a business – with more support needed at the start of a business's life.

Current rumours suggest a consultation considering reform of the relief will be announced in the Budget. If this is the case, it is likely that any fundamental changes will take place at a later date, perhaps in April 2021 or even beyond. However, we cannot rule out the possibility of either a more immediate change to the relief or of anti-forestalling measures to prevent people taking action now to lock into the relief. One possibility, for example, would be to reduce the lifetime limit from its current level of £10 million back to the original £1 million which applied when it was first introduced in 2008. There has even been some recent speculation that the relief could be scrapped altogether.

More broadly, with a need to increase the tax take and within the constraints of the triple lock, Rishi Sunak may decide to increase the rate of capital gains tax across the board. This could be portrayed as a way of "reducing tax advantages for the wealthiest in society".

Possible inheritance tax changes

Another area where we might expect a significant announcement is inheritance tax. The report by the Office of Tax Simplification (OTS) published in July 2019 suggested a number of reforms to inheritance tax including a reduction in the length of the look-back period for lifetime giving from seven to five years and the abolition of taper relief; possible changes to business property relief (BPR) rules to align them to CGT reliefs; proposals that the CGT uplift on death could be removed where an asset qualifies for relief from IHT; and changes to the way the nil rate band is offset against lifetime transfers.

The OTS review was limited in scope and only considered reforms to the existing inheritance tax regime. More wide-ranging in scope was the recently published All-Party Parliamentary Group (APPG) report on reforms to inheritance tax (see below). This suggested a complete overhaul of IHT with a much-reduced tax rate (of 10-20%) accompanied by the abolition of all reliefs apart from gifts to one's spouse/civil partner and to charity. Under these proposals the annual allowance would increase to £30,000 but all lifetime gifts would be taxable above that level. The nil rate band would remain at current levels but only apply on death. The APPG report also suggested the abolition of the capital gains tax-free uplift on death – meaning that those inheriting assets would also inherit their base cost and would likely need to be capital gains tax when the assets are eventually sold.

It seems likely that there may be a consultation announced in the Budget to look at reform of IHT, but it is possible that the Government may wish to implement some of the OTS suggested reforms more immediately.

Changes to trusts

A consultation on the reform of the taxation of trusts closed last February and the responses have not yet been published. It is possible we will see some further progress in this area at the Budget. The consultation considered transparency, fairness and simplicity, including consideration of whether the IHT regime for trusts was fair when compared to that for individuals. It also considered other changes to trust taxation, including potentially removing principal private residence relief for trustees.

The APPG report on IHT also explored some possible changes to inheritance tax for trusts, including an annual charge for discretionary trusts and a limit to the length of time a trust may remain "excluded property" when established by a non-UK domiciled individual.

Property taxes

The Conservative Party manifesto promised to introduce an additional SDLT surcharge for non-residents of 3%. A previous proposal to introduce the surcharge at 1% has already been the subject of a consultation and we expect some announcement with regard to this in the Budget.

In recent days there has also been press speculation around the introduction of a mansion tax. The two possibilities being considered are said to be either the introduction of some form of annual levy, or of an additional band or bands of council tax.

Pension changes

The Government has been consulting on changes to the NHS pension scheme to help address concerns that pension tax charges are causing senior clinicians to retire early or change their working habits, negatively impacting patient care. There has been speculation that the Budget may announce changes to the tax rules themselves, possibly by amending the threshold tests for the annual allowance taper. It is recognised that this would merely reduce the scale of the problem and not address the issue itself (which can be further compounded by the Lifetime Allowance limit). It is unlikely that any changes to the pension rules would be limited to doctors.

In addition to any changes to the annual allowance taper, there have been renewed calls for a wider review of pension tax relief. Suggestions have included a flat rate of relief (at a rate between the existing income tax basic rate and higher rate) or simply removing higher rate relief. Given that there was no consensus on changes at the time of the last consultation under George Osborne, it seems unlikely that major changes will be made without further discussion but the cost of pension relief (and its existing anomalies) does make pensions an area which the Government may want to focus on.

Weighing up the options

There are certainly plenty of possible personal tax changes for a new Chancellor to consider. Rishi Sunak's recent appointment as Chancellor adds to the uncertainty around Budget and increases the chances that any substantial changes may be postponed to an autumn Budget later in the year. We wait with interest.