Budget 2016 – Key Points

The economy

Britain is forecast by the Organisation for Economic Co-operation and Development (OECD) to be the fastest growing major advanced economy this year, with employment currently at a record rate of 74.1%. Where it was at one time the worst prepared to face a financial crisis, today it is seen as one of the best prepared.

The Office for Budget Responsibility (OBR) forecasts GDP growth of 2.0% in 2016 and employment to be 31.5 million in 2016 rising each year to 32.1 million in 2020. CPI is forecast to be below the 2.0% inflation target in 2016, returning gradually to 2.0% in 2018.

Income Tax

Personal Allowances

From 6 April 2016 there will be no higher age related personal allowance for people born before 6 April 1938 which means that the basic personal allowance for everyone will be £11,000. This will increase to £11,500 from 6 April 2017.

The amount of the basic personal allowance will, however, continue to be gradually withdrawn for all individuals (regardless of age) with ‘adjusted net incomes’ above £100,000 as provided for by section 35 of ITA. The rate of reduction is £1 of personal allowance for every £2 of income above the £100,000 limit so this will be fully withdrawn for those individuals with ‘adjusted net incomes’ of £122,000, or more.

From 2016/17, a spouse or civil partner who is not liable to income tax or not liable above the basic rate for a tax year will continue to be entitled to transfer up to 10% of their personal allowance (£1,100 in 2016/17) to their spouse or civil partner provided that the recipient of the transfer is not liable to income tax above the basic rate. The transferor’s personal allowance will then be reduced by up to £1,100 and the spouse or civil partner receiving the transferred allowance will be entitled to a reduced income tax liability of up to £220.

2016/17, however, also sees the introduction of two new tax-free income tax allowances: The £5,000 dividends allowance and a personal savings allowance for savings income which will be £1,000 for basic rate tax payers and £500 for higher rate taxpayers. Additional rate taxpayers will not have any personal savings allowance.

Despite being tax free though, any dividend or savings income that falls within these two new allowances will still count towards an individual’s basic or higher rate bands.

Rates and Thresholds

The main rates of income tax for the 2016/17 tax year will remain at 20% for basic rate taxpayers, 40% for higher rate taxpayers and 45% for additional rate tax payers.

In 2016/17, the 20% basic rate will apply to taxable income over the personal allowance up to the basic rate limit of £32,000, the 40% higher rate will apply to taxable income between £32,001 and £150,000 and 45% tax will apply to taxable income above £150,000.

The Chancellor also announced that from 6 April 2017 the basic rate limit will increase to £33,500 which, when added to the basic personal allowance of £11,500, will mean that the threshold above which higher rate tax will be paid will rise to £45,000.

In 2016/17, the 0% starting rate band for savings income will remain at £5,000 and there will also continue to be three rates of tax for dividends to the extent that the dividends received exceed the new £5,000 tax free dividend allowance.

From 2016/17, Dividends in excess of this allowance will be taxed at the following rates, depending on which tax band they fall in:

- Basic rate - 7.5%
- Higher rate - 32.5%
- Additional rate - 38.1%

The married couples allowance will remain at £8,355 with the minimum allowance also remaining at £3,220. However, this is only available where at least one of the parties to the marriage was born before 6 April 1935.

The blind person’s allowance will remain at £2,290.

Tax Collection

The Government announced in the March 2015 budget that it was committed to transform the tax system through digital technology and end the need for annual tax returns. In order to make further progress towards this transformation, the 2016 Budget announces that:

- From 2018 businesses, self-employed people and landlords who are keeping their records digitally and providing regular digital updates to HMRC will, if they wish, be able to adopt pay-as-you-go tax payments in order to help them better manage their cash-flow
- The government will explore options to simplify the tax rules for businesses, landlords, and the self-employed, to reduce administrative burdens and ensure that regular digital updates work smoothly

The government will consult on these measures in 2016, alongside publishing detailed proposals for other elements of the Making Tax Digital programme announced previously.

National Insurance

For 2016/17, the lower earnings limit for the purpose of primary class 1 NI credits will remain at £112 a week. The primary earnings threshold for class 1 employee NI contributions will also stay at £155 a week and the secondary earnings threshold for class 1 employer NI contributions will stay at £156 a week.

The Upper Earnings Limit (UEL) for primary and secondary Class 1 NI contributions remains aligned with the higher rate income tax limit, so for 2016/17 the threshold is £827 a week (£43,000 pa).

For 2016/17, it should also be noted that:-:

- The main rate of Class 1 NI contributions for employee's people will remain at 12%.
- The main rate of Class 4 NI contributions for the self-employed will remain at 9%.
- The additional rate of Class 1 and Class 4 NICs will remain at 2%.
- Class 2 NI contribution rates for the self-employed will remain at £2.80 a week and the small earnings exception for paying class 2 NI remains £5,965 pa.
- Class 3 (voluntary) NI contributions will also remain unchanged at £14.10 a week.

As far as the self-employed are concerned, the Chancellor also announced that:

- Class 2 NICs will be abolished from April 2018; and
- Class 4 NICs will be reformed so that self-employed individuals can continue to build entitlement to the State Pension and other contributory benefits, following the abolition of Class 2 NICs.

Changes to the NI treatment of termination payments (such as redundancy payments) were also announced which will mean that, from April 2018, whilst the first £30,000 of the payment will continue to be income tax free, the taxable portion in excess of £30,000 will also be subject to employer (but not employee) NI.

Capital Gains Tax

From 6 April 2016, the Capital Gains Tax (CGT) rate of 18% for non, starting rate and basic rate tax payers will be reduced from 18% to 10% and the 28% rate for higher and additional rate taxpayers (and most trusts) will be reduced to 20%. Private Residence Relief will continue to ensure that an individual's main home is not subject to CGT.

The annual exempt amount will remain at £11,100 (for individuals) and £5,550 (for most trusts).

The consumer price index (CPI) will continue to be used as the default indexation assumption for increasing the CGT annual exempt amount each year.

Entrepreneurs' relief will be extended to long term investors in unlisted companies. This will provide a 10% rate of CGT for gains on newly issued shares in unlisted companies purchased on or after 17 March 2016, provided they are held for a minimum of three years from 6 April 2016, and subject to a separate lifetime limit of £10 million of gains.

Inheritance Tax

The nil rate band will continue to be frozen at £325,000 until 2020/21.

The rate of IHT during lifetime remains at 20% and the rate on death remains at 40%.

Corporation Tax

For the 2016 financial year, the main rate will remain at 20%, giving a unified rate of 20% for all companies irrespective of the amount of profit they make.

Future reductions in this unified rate had already been announced: to 19% in 2017 and 18% in 2020 but Budget 2016 announces that the government will cut corporation tax further, so the rate will fall to 17% in 2020.

Insurance Premium Tax

The standard rate of Insurance Premium Tax (IPT) will be increased from 9.5% to 10%. This ensures that the impact of the rate increase is spread broadly across the entire general insurance industry.

IPT is a tax on insurers. However, if they do pass the cost of this rate increase onto their business and household customers, the average combined home and contents insurance would only increase by £1, and the average motor insurance premium by £2 per year.

All the revenue raised from this increase in IPT will be invested in flood defence and resilience measures.

VAT

There will be no change to the current VAT rate of 20%.

Stamp Duty

Residential additional properties

As part of the government's commitment to support home ownership and first-time buyers, the Autumn Statement 2015 announced that from 1 April 2016, higher rates of Stamp Duty Land Tax (SDLT) will apply to purchases of additional residential properties, such as second homes and buy-to-let properties. The higher rates will be 3 percentage points above the current SDLT rates and will apply to purchases of additional residential properties in England, Wales and Northern Ireland.

Following consultation, the government announced in Budget 2016 that it has decided that:

- To help those moving in difficult circumstances, purchasers will have 36 months rather than the originally proposed 18 months to either claim a refund from the higher rates or before the higher rates will apply, in the event that there is a period of overlap or a gap in ownership of a main residence; and
- There will be no exemption from the higher rates for significant investors, and the higher rates will apply equally to purchases by individuals and corporate investors

Commercial Property

Currently, SDLT rates on freehold and lease premium transactions operate on a slab system, where one tax rate is due on the entire transaction value.

From 17 March 2016, the slab system will be replaced by a slice system in order to ensure that SDLT is instead payable on the portion of the transaction value which falls within each tax band.

The new rates will therefore be 0% for the portion of the transaction value between £0 and £150,000; 2% between £150,001 and £250,000; and 5% above £250,000. As a result of this change, all freehold and lease premium transactions below £1.05 million will pay the same or less in SDLT.

A new 2% rate for rent paid under a non-residential lease will also be introduced where the net present value of the rent is above £5 million. All leasehold rent transactions up to £5 million will remain unaffected.

Pensions

In addition to announcing that the 25% tax free pension commencement lump sum will continue to be available, a number of minor changes are being made to the pensions tax rules to ensure that they operate as intended following the introduction of pension flexibility in April 2015. In summary, these changes will mean that:

- A serious ill-health lump sum can now be paid from crystallised pension funds
- Where a serious ill-health lump sum is paid to an individual who is 75 or over, this will now be taxed at the individual's marginal rate for income tax, rather than at a flat rate of 45%.
- Dependant children, under age 23, in receipt of a dependants capped or flexi-access drawdown pension will be able to continue to be able to take an income from that drawdown pension after their 23rd birthday, without incurring unauthorised payment charges (thus aligning the tax treatment for a dependant with that of a nominee)
- Lump sum death benefits can now be paid to a charity, tax free, if the death occurs before the age of 75

Whilst not announced in the budget it should also be noted that the following changes will also take effect from 6 April 2016:-

Tapered Annual Allowance

The annual allowance for tax relieved pension savings will be reduced for those individuals with 'adjusted income' of over £150K.

For individuals with 'adjusted income' over £150K the standard £40K annual allowance will be reduced by £1 for every £2 of income they have over £150K. This is subject to a maximum reduction of £30K so individuals with 'adjusted income' of £210K or more will have a £10K annual allowance.

If, however, an individual has 'threshold income' of £110K or less, then even if their 'adjusted income' exceeds £150K they will not be subject to the tapered annual allowance.

Lifetime Allowance

From 6th April 2016, the lifetime allowance for pension contributions that can benefit from tax relief will reduce from £1.25 million to £1 million. The lifetime allowance will be indexed to increase annually in line with CPI from 6 April 2018.

To counteract this reduction though, individuals can apply for 'Fixed Protection 2016' to preserve an entitlement to the higher £1.25m lifetime allowance provided (broadly) they do not accrue further pension benefits after this date. Individuals with total pension rights valued at greater than £1m as at 5 April 2016 can also apply for 'Individual Protection 2016.'

Over 96% of individual's currently approaching retirement have a pension pot worth less than £1 million, so this change will affect only the wealthiest pension savers.

State Pensions

The Basic State Pension for people with an adequate national insurance record who attain SPA *before* 6 April 2016 will increase from £115.95 to £119.30 a week for a single person and from £185.45 to £190.80 a week for a couple.

The minimum income guarantee for Pension Credit will also be increased from £151.20 to £155.60 a week for a single person and from £230.85 to £237.55 a week for a couple.

For anyone reaching SPA *on or after* 6 April 2016, however, the complex existing state pension system will be replaced by a simpler, single-tier state pension, called the New State Pension. For people with an adequate national insurance record, the full rate of the New State Pension in 2016/17 is set at £155.65 a week.

The Budget announced no further changes to the planned increases in State Pension Age which will be equalised at age 65 for men and women in November 2018 and will then rise from 65 to 66 for both men and women in October 2020.

SPA will then rise from 66 to 67 between April 2026 and April 2028 with further increases likely to be in line with increased longevity.

Salary Sacrifice

The government has expressed concern about the growth of salary sacrifice schemes as clearance requests for salary sacrifice arrangements from employers to HMRC have increased by over 30% since 2010. The government is therefore considering limiting the range of benefits that attract Income Tax and NI advantages when they are provided as part of salary sacrifice schemes.

The government has stated, however, that it intends for pension saving, childcare and health-related benefits (such as Cycle to Work) to continue to benefit from Income Tax and NIC relief when provided through salary sacrifice arrangements.

Enterprise Investment Schemes (EIS) and Venture Capital Trusts (VCT)

The subscription limits and tax reliefs available for both EIS and VCT investments remain unchanged.

This means that 30% income tax relief will continue to be made available on investments up to £1m into an EIS and £200,000 into a VCT and the usual CGT reliefs remain unchanged. EIS shares will continue to be IHT exempt after just 2 years of ownership.

50% income tax relief will also continue to apply for investments of up to £100,000 into a Seed EIS.

Help to Save

To help the people who find it hardest to save, the government will introduce a new Help to Save scheme. This is aimed at those on low incomes who wish to regularly set aside some of their income.

The scheme will be open to 3.5 million adults in receipt of Universal Credit with minimum weekly household earnings equivalent to 16 hours at the National Living Wage, or those in receipt of Working Tax Credit. It will work by providing a 50% government bonus on up to £50 of monthly savings into a Help to Save account.

The bonus will be paid after two years with an option to save for a further two years, meaning that people can save up to £2,400 and benefit from government bonuses worth up to £1,200. People will be able to use the funds in any way they wish.

Individual Savings Accounts

Adult ISAs

In 2016/17, the annual ISA allowance will remain at £15,240. From 6 April 2017, the annual ISA allowance will then increase to £20,000.

Junior ISAs

The annual subscription limit for junior ISAs will remain at £4,080 in 2016/17. It is unclear at this stage whether the Junior ISA limit will also be raised from 6 April 2017.

The Lifetime ISA

From April 2017, people under the age of 40 will be able to open a Lifetime ISA and contribute up to £4,000 in each tax year. The government will then provide a 25% bonus at the end of the tax year on the contributions that have been made. This means that anyone who saves the maximum amount in the tax year will be subject to a £1000 bonus. Savers will be able to make contributions from the age of 18 up to the age of 50.

The Lifetime ISA aims to help young people save flexibly for the long-term throughout their lives. It will help them to simultaneously save for a first home or for their retirement, without having to choose one over the other.

Opening a Lifetime ISA will work in the same way as opening any other ISA, as will saving into one. Individuals will also be able to transfer their Lifetime ISA in line with the existing ISA rules.

There will however be some additional rules to consider:

- Any contributions into a Lifetime ISA will form part of the overall £20,000 ISA limit that will come into force in April 2017.
- Individuals will be able to contribute into a Lifetime ISA and receive the 25% Government bonus up to the age of 50.
- The Government Bonus will be paid on contributions of up to £4,000 per year. This is essentially £1 from the Government for every £4 the individual invests.
- Individuals will be able to transfer funds from other ISA's as a way of funding their Lifetime ISA.
- Where people choose to withdraw savings from the Lifetime ISA to make a first home purchase, they will be able to withdraw up to 100% of their balance including the Government bonus. Their withdrawal can be put towards a first home located in the UK with a purchase value of up to £450,000. There will be an initial holding period of 12 months from the account opening before withdrawals can be made for a home purchase.
- When saving for retirement, full or partial withdrawals can be made from the age of 60 and will be paid free of tax. Any remaining funds will receive interest and investment growth tax free.

Whilst the purpose of the Lifetime ISA is to encourage long term saving for buying a home or saving for retirement, the Government have also stated that they want to ensure that people can access their money for any other purposes. This will however incur a 5% charge, and the bonus element of the fund returned to the Government.