Tax Alert
July Budget 2015

July 8, 2015

The Chancellor delivered the first Budget of the new government this afternoon. We have set out below a summary of the main tax announcements, based on the information which has been released so far. In many cases, only limited information has been given at this stage. If you wish to discuss any of the following, please contact me or your usual Weil contact and we would be happy to assist.

Carried Interest

- **Carried Interest**: changes to the taxation of carried interest received by individual members of a fund manager team have been made, effective today. Under the new regime all carried interest returns will be taxed as capital gains (previously carried interest was commonly taxed at the tax rate, and on the tax principles, appropriate to the nature of the underlying profits going to pay the carried interest). However, the "deductions" available in determining the gain which is subject to tax are to be limited to, in broad terms, amounts actually paid for the carry by the relevant individual (such amounts are usually de-minimis) whereas previously the partnership structures used by fund managers enabled them to access what was known as "base cost shift" such that the amount taxable as a gain was less than the actual economic gain.
- **Further consultation on carried interest**: the government is now consulting on changes to the (new – see above) rules relating to carried interest. The proposal being consulted on would treat all performance based awards received by an individual investment manager as taxable, at income tax rates, with managers who manage funds that conduct transactions that are "investment" in nature eligible for capital gains rather than income tax treatment. Any changes arising as a result of this consultation are unlikely to affect the taxation of carry received by managers of traditional private equity, infrastructure or core real estate funds. Instead, the proposals appear to be aimed at managers of hedge funds and "short term" debt funds. It is unclear at present whether the proposals would result in additional tax on carry being payable by managers of non-core (i.e. value add and opportunistic) real estate funds.

Business tax

- **Corporation tax rate**: the main rate of corporation tax will be reduced to 19% from 1 April 2017 and further reduced to 18% from 1 April 2020.

- **Bank Levy**: the Budget sets a long-term roadmap for the taxation of banks, involving three steps:
  - the introduction of a new tax on banking sector profit from 1 January 2016, at a permanent rate of 8% (the "**Bank Tax Surcharge"**);
  - a phased reduction of the bank levy rate, from the existing rate of 0.21% to 0.18% from January 2016, 0.17% from January 2017, 0.16% from January 2018, 0.15% from January 2019, 0.14% from January 2020 and 0.10% from January 2021; and
  - a change in the bank levy's scope from 1 January 2021, meaning that UK headquartered banks will be levied on their UK balance sheet liabilities only.

Under the Bank Tax Surcharge, taxable profits will be calculated on the same basis as for corporation tax, but with some reliefs (e.g. losses arising before 1 January 2016) added back.

- **Corporation tax payment date**: companies with annual taxable profits of £20 million or more will, for accounting periods beginning on or after 1 April 2017, be required to pay corporation tax in quarterly instalments in the third, sixth, ninth and twelfth months of their accounting period; this effectively brings forward payment dates by four months. Where companies are part of a group, the £20 million threshold will, as it applies to each company, be divided by the number of companies in the group.
- **Controlled foreign companies and loss restriction**: from today, the government will restrict the availability of loss relief under the controlled foreign companies (CFC) regime. In broad terms, the CFC regime imposes a tax charge on a UK parent company where profits of the CFC can be attributed to it in accordance with the applicable legislation. The government will introduce new rules that prevent UK companies from reducing or eliminating such a CFC charge by offsetting UK losses.

Insurance premium tax rate: the standard rate of insurance premium tax will increase from 6% to 9.5% from 1 November 2015 followed by a four month concessionary period.

Personal tax

- **Income tax thresholds**: the income tax **personal allowance** will increase to £11,000 from April 2016 with a further increase to £11,200 from April 2017, the **basic rate threshold** will increase to £32,000 from April 2016 with a further increase to £32,400 from April 2017 and the **higher rate threshold** will increase to £43,000 from April 2016 with a further increase to £43,600 from April 2017.
- **Dividend tax**: from April 2016, the dividend tax credit will be replaced by a new tax-free dividend allowance of £5,000 a year (which is in addition to the tax-free personal allowance – see above). Effective dividend tax rates (i.e. in respect of any amount which exceeds the £5,000 allowance) will also be increased, from 0% to 7.5% for basic rate taxpayers, from 25% to 32.5% for higher rate taxpayers and from 30.56% to 38.1% for additional rate taxpayers.
- **Pensions – tapered annual allowance for top earners**: individuals with incomes above £150,000 (including pension contributions) will have their annual allowance for tax relieved pension contributions (currently £40,000) tapered to as low as £10,000 per tax year from 6 April 2016. The rate of reduction is £1 for every £2 by which income (including pension contributions) exceeds the £150,000 threshold, such that individuals with an income of £210,000 or more will have an annual allowance of only £10,000. To ensure the measure is focussed on the higher rate and additional rate taxpayers, those with income (excluding pension contributions) below £110,000 will not be subject to this tapered annual allowance.
  - UK non-domiciles ("non-doms"): anyone resident in the UK for more than 15 of the last 20 tax years will be deemed to be domiciled in

the UK for all tax purposes and as such will be subject to (i) inheritance tax on their worldwide assets and (ii) tax on their worldwide income and capital gains, and unable to claim the remittance basis of taxation. Further, individuals born in the UK to parents domiciled in the UK, and who have gained a foreign domicile under general law, will no longer be eligible to claim non-dom status whilst resident in the UK. Non-doms will also no longer be able to shelter UK residential properties from inheritance tax by holding them through offshore structures. These changes will take effect from 6 April 2017.

Litigation

- Court judgment interest rate: legislation will be introduced in the upcoming Finance Bill 2015 to disapply the current 8% interest rate on judgment debts (including pre-existing judgments) relating to a taxation matter, and instead apply the late payment interest rate (currently 3%) where HMRC is the **creditor**, and the Bank of England base rate plus 2% where HMRC is the **debtor**.

And finally, there was some bad news for private landlords today:

- Tax deductions on mortgage interest expense incurred by individual landlords of residential property will be restricted to the basic 20% rate of income tax. Currently, landlords are able to claim tax relief for their interest payments at the rate of income tax they pay (e.g., additional-rate taxpayers are currently able to get 45% tax relief on the mortgage interest they are paying). This restriction will be phased in over four years, starting from April 2017.
- From April 2016, the automatic 10% "wear and tear" allowance against rental income will be abolished, and residential landlords will instead only be able to deduct the actual cost of replacing furnishings.

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