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UK TAX ALERT

SPRING BUDGET 2021

MARCH 2021

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On 3 March 2021, Chancellor Rishi Sunak delivered the Spring 2021 Budget. Unsurprisingly, the main focus of this Budget was on providing continued Covid-19 related support measures for the UK economy as the country embarks on the roadmap out of lockdown.

It was anticipated that the Chancellor's Budget day tax announcements might be limited, following the decision of the Government to hold a "Tax Day" on 23 March, when it plans to publish a range of documents relating to long-term changes in Government tax policy, which would usually have been published on Budget day. In addition, there was also speculation that the Chancellor would hold back many significant measures until the planned Autumn Budget later this year.

However, despite this, the Spring Budget did include some significant tax-related announcements. More detail will be available when the Finance Bill is published on 11 March.

We have summarised below the tax measures that are likely to be most relevant to our clients. It is not a comprehensive summary and does not cover (in particular) the COVID-19 support packages or measures primarily relevant to individuals, small businesses, or specific industries.

Tax Rates

Corporation Tax

Instead of a series of staggered corporation tax rate rises (as some had predicted), the Chancellor announced that the rate of corporation tax would rise from the current rate of 19% to 25%, with effect from 1 April 2023.

The current rate of corporation tax of 19% will continue to apply to smaller businesses, with profits of less than £50,000. Companies with profits between £50,000 and £250,000 will be taxed at the main rate of 25%, but will be able to claim marginal relief.

The increase to 25% will widen the effective tax rate differential between businesses structured as a UK company and businesses structured as an English limited liability partnership ("**LLP**") and the increased rate from 2023 is likely to be a factor in considering whether the LLP structure may be more suitable in appropriate circumstances.

Diverted Profits Tax

There will be a consequential increase in the main rate of diverted profits tax, which was introduced to address arrangements which are designed to erode the UK tax base through avoiding a presence in the UK or exploiting cross-border mismatches, from 25% to 31% to maintain the current differential of 6% between the rate of diverted profits tax and the main rate of corporation tax when the rate of corporation tax increases.

Bank Surcharge

The Government noted that the additional bank surcharge of 8%, when combined with the increase in the main rate of corporation tax to 25%, would make the UK taxation of banks uncompetitive and would risk damaging one of the UK's key exports. As such, the Government will review the bank surcharge and set out further details in the Autumn.

*Capital Gains Tax ("**CGT**")*

There had been much speculation concerning potential reform of the UK CGT regime in the run-up to the Budget, including increasing the rates of CGT or even aligning rates of CGT with rates of income tax. However, the Chancellor made no reference to an increase in CGT rates in his Budget day address. We will have to wait to see whether reform of the CGT regime will be addressed as part of the "Tax Day" later this month, or if it will feature in the Autumn Budget.

Other Rates

The Government has stood by its election commitment to its "Triple Tax Lock" (its promise not to raise rates of income tax, NICs or VAT).

Nor was there any change to the rates that apply to North Sea oil & gas companies (30% corporation tax and a 10% supplementary charge).

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Tax Losses

The period for which trading losses can be carried back against previous profits is extended from the current one year entitlement to a period of 3 years, with losses being carried back against later years first.

This extension will apply to trading losses made by companies in accounting periods ending between 1 April 2020 and 31 March 2022 and to trading losses made by unincorporated businesses in tax years 2020 to 2021 and 2021 to 2022. However, certain monetary limits apply. Notably:

- unincorporated businesses and companies that are not members of a corporate group will be able to obtain relief for up to £2 million of losses in each of 2020-21 and 2021-22;
- companies that are members of a corporate group will be able to obtain relief for up to £200,000 of losses in each of 2020-21 and 2021-22 without any group limitations; and
- companies that are members of a corporate group will be able to obtain relief for up to £2 million of losses in each of 2020-21 and 2021-22, but subject to a £2 million cap across the group as a whole.

There were also measures providing additional flexibility under the corporation tax loss relief rules.

Capital allowances

As a counterbalance to the tax rate increase, to incentivise investment the Government will introduce a new "super deduction" and 50% first-year allowances for capital expenditure.

Between 1 April 2021 and 31 March 2023:

- companies investing in qualifying new plant and machinery assets that currently qualify for the 18% main rate writing down allowances will benefit from a 130% first-year capital allowance; and
- companies investing in qualifying new plant and machinery that currently qualify for the 6% special rate writing down allowances will benefit from a 50% first-year allowance.

EU Interest and Royalties Directive

UK domestic law provisions which gave effect to the EU Interest and Royalties Directive (the "**EU IRD**") will be repealed in Finance Bill 2021. This will mean that, with effect from 1 June 2021, UK companies will not be able to rely on the provisions of the EU IRD to claim an exemption from withholding tax on intra-group interest or royalty payments, subject to the terms of the relevant double taxation agreement ("**DTA**"). In many cases the DTA will provide for a full exemption so this may have little practical significance. However, the terms of the relevant DTA will need to be examined in each case and a withholding tax may arise on certain payments out of the UK where the DTA rates in question do not reduce the withholding to zero.

OECD Mandatory Disclosure Rules

As we noted in our alert from 31 December 2020, in one of its first acts of divergence from EU-level measures post-Brexit, the Government published regulations which significantly reduced the scope of the EU Mandatory Disclosure Regime ("**DAC6**") in the UK. In its place, it is proposed to introduce a regime which aligns with the OECD's Mandatory Disclosure Rules, which facilitate global exchange of information on certain cross-border tax arrangements, to combat offshore tax evasion. The Government has confirmed that it will launch a consultation later this year on draft regulations to implement the OECD's Mandatory Disclosure Rules.

Hybrid mismatch rules

Various technical amendments were announced to the rules for hybrid mismatches to remove certain legislative anomalies and to ensure that the legislation operates proportionately and as intended. The detail of the amendments is expected when the Finance Bill 2021 is published on 11 March 2021.

The UK's hybrid mismatch rules need to be considered in relation to all structures involving

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UK companies financed with shareholder debt or equity with debt features. Very broadly, the rules aim to counteract certain arrangements that give rise to either a deduction for an entity under the rules of one jurisdiction without the corresponding recognition of income by another entity; or more than one deduction in respect of the same payment. Such outcomes are potentially counteracted where the mismatch arises as a result of some "hybridity", such as a "hybrid entity" (e.g. an entity treated as tax transparent in one jurisdiction but fiscally opaque in another) or a "hybrid instrument" (e.g. an instrument treated as equity in one jurisdiction but debt in another).

Avoidance, evasion and non-compliance

As has now become customary, the Chancellor noted the Government's commitment to continuing to develop proposals aimed at tackling tax evasion, tax avoidance and tax non-compliance. In particular, the Budget outlined certain measures with regards to:

- interest harmonisation and reform of penalties for late submission and late payment of tax;
- strengthening existing anti-avoidance regimes and tightening the rules designed to tackle promoters and enablers of tax avoidance schemes;
- amending the penalties that may be charged to people receiving "Follower Notices" as a result of using avoidance schemes; and
- strengthening the HMRC's civil information powers through the introduction of a "Financial Institution Notice".

Our tax team is available to discuss any of these issues with you and answer any specific questions you may have. If you would like more information about the topics raised in this briefing, please speak to your regular contact at Weil or to any of the authors listed below.

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