Budget 2016

On Wednesday 16 March 2016 the Chancellor George Osborne presented to Parliament his eighth Budget, his second following the election of a Conservative majority government in May 2015, together with the Office for Budget Responsibility's latest five-year forecasts for the economy and the public finances and an assessment of the Government's progress against its fiscal and welfare spending targets.

Since the November '15 forecast, four months ago, economic developments have been disappointing with the outlook for productivity growth and public finances looking much weaker, making the OBR's view of UK economic performance more pessimistic than before.

The most significant change is the OBR's judgement over potential productivity growth. This combined with historic data and a weaker global outlook means that the cash size of the UK economy is about 3% smaller at the end of their forecast than originally predicted.

The net effect is for the OBR's underlying forecast for public sector net borrowing to be around £11 billion a year worse on average over the next five years, which would have turned the £10 billion projected surplus of 2019-20 to a £3 billion deficit, extending 'austerity' by at least one year into the life of the next Parliament.

Economic growth slowed in 2015, the slowest annual growth since 2012, while remaining convincingly within historic norms at **2.2%**, down from 2.9% last year, 2014, while once again underpinned by further increasing consumer spending.

2010:	*2011:*	*2012:*	*2013:*	*2014:*	*2015:*
1.5%	***2.0%***	***1.2%***	***2.2%***	***2.9%***	***2.2%***

In February '16, the Organisation for Economic Co-operation and Development (OECD) lowered their GDP growth forecasts for most of the world's largest economies.

UK growth for 2016 was lowered to **2.1%** and this is still forecast to be the highest in the G7, but only just.

Modest economic growth combined with the continuing strong growth in the number of people in UK employment means that the productivity statistic fell sharply in the last quarter.

The pick-up in actual productivity growth in mid-last year seems now to have been a false dawn of the UK's trend productivity growth returning to pre-crisis levels (historically about 2%). UK productivity was (in 2014) 18% below the average of the rest of the 'G7 countries', the widest gap since at least 1991.

Although on course to breach the supplementary target to have debt falling as a share of GDP this year and beyond, and failing to hold spending on social security below a level capped July 2015, the OBR judges that the Government should (just) meet its 'fiscal mandate' of a budget surplus in 2019/20.

Notably this is by various 'accounting' and other measures: decreasing departmental spending; delaying measures for quarterly corporation tax payments; and controversially, reducing welfare spending, largely through tightening the disability benefits system by £1.3 billion annually.

Still Mr Osborne has only just a 50:50 chance of fulfilling this plan to deliver an annual surplus by the end of this Parliament, according to the director of the Institute for Fiscal Studies (IFS).

Outlook for economic growth: this looks 'materially weaker' than the OBR and others expected last November. They have revised real GDP growth down from an average of 2.4 per cent a year to **2.0 per cent for 2016.** The main reason is data published by the Office for National Statistics (ONS).

In November the OBR expected near term strong growth in consumer spending owing to rising inflation-adjusted household incomes. In part because of recent wage growth and partly through historically low inflation, at near zero. But annual growth in **average earnings**, which over the longer term should track the growth of productivity, has also weakened sharply, dropping from near 3% in the first half of 2015, slowing towards the end of the year back down to ***just below 2%.***

However, the **UK's labour market** continues to perform with increasing numbers employed (74.1%: **31.42 million people**), the employment rate is again at an historic high and the unemployment rate (at 5.1%) back to the pre-downturn average. The OBR report that the easing of real wage growth may in part reflect 'rising job flows into low-skilled occupations'.

Lower productivity growth means lower GDP growth, which then accompanies lower growth forecasts for labour income, profit growth, consumer spending and business investment. This, the OBR argues, leads in aggregate, to significantly reducing tax receipts; the OBR's rational for its changed view and judgement on the fiscal outlook.

Hence, expectation of increasing interest rates have weakened. **Interest rate** markets are suggesting that the Bank of England is not expected to raise interest rates until 2019 (a full decade after **Bank Rate** was initially cut to 0.5 per cent) and even that possibly a cut in rates is more likely that not in the near term.

Personal Tax

The Chancellor announced that he would increase both the income tax personal allowance to £11,500 and the higher rate threshold to £45,000 from April 2017 (the basic rate limit will be increased to £33,500). These are substantial tax changes, an annual Budget cost to the exchequer of £2.5 billion. The IFS estimate that this should stop the numbers paying higher rate tax from rising beyond 5 million, but will still be 2 million higher than in 2010.

For the self-employed, from 2018, Class 2 National Insurance contributions will be abolished, which apparently will give a tax cut of more than £130 annually to three million people.

Significantly raising the tax cost, as previously announced, new dividend tax rates, a Dividend Allowance and a Personal Savings Allowance come into force from 6 April 2016.

Loans to participators are to be taxed at a rate of 32.5% from April 2016. Historically, private companies could make a loan to a shareholder in preference to a dividend, which under the current tax rules could be advantageous, as the tax rate on such a loan is 25%, whilst a dividend would be taxed at up to 38.1%. This announcement brings the rate on these loans in line with the tax a higher rate taxpayer would pay on a dividend.

Capital Gains Tax (CGT)

In a surprise move, from 6 April 2016 CGT rates will be reduced from 18% to 10% for basic rate taxpayers, and from 28% to 20% for higher rate taxpayers. Although these reduced rates will not apply to gains on the disposal of residential property. Entrepreneurs' Relief is extended to shares held for 3 years in unlisted trading companies (other than by officers and employees), with an effective rate of 10%.

Non-UK residents disposing of UK residential property are not required to file a non-resident CGT return if for a disposal of residential property which takes place for no gain or loss, or on the grant of a lease for no premium to an unconnected person in a bargain at arm's length.

Non-UK domiciled (non-dom) individuals

Government is undertaking major reforms of non-UK domicile taxation. It was announced that non-doms who become deemed UK domiciled under the new rules can rebase their non-UK assets for CGT purposes to market value from 2017 so as to be only subject to UK CGT on future not past growth in value.

Pensions and savings

A new £1,000 allowance will apply to both property and trading income from April 2017 aimed at 'the micro-entrepreneurs'.

The total amount that can be saved each year into an ISA will be increased from £15,240 to £20,000 from 6 April 2017. Also from 6 April 2017, any adult under age 40 will be able to open a new 'Lifetime ISA'. Up to £4,000 can be saved each year until the **age of 50** and a 25% bonus will be received from the Government. This Lifetime ISA can be used to buy a first home or saved until age 60 and then used as retirement income, otherwise a 5% charge will apply and the bonus will be withdrawn if the funds are taken out for any other reason. Income and gains within the ISA are tax free in the usual way.

Corporate taxes

The new unified rate of corporation tax will remain at 20% for Financial Years 2015 and 2016 and will be reduced to 19% from April 2017, furthermore the Budget announced a larger than expected reduction to 17% from April 2020.

A further cut in the main CT rate, already the lowest rate in the G20, was a demonstration of Government's desire to make the UK attractive to multinationals. The headline rate will have been cut from 28% to 17% in a decade.

Tax deductibility of corporate interest

In a significant change and widely predicted, the Chancellor announced restrictions to the tax deductibility of corporate interest expenses from April 2017, as recommended by the OECD. These should have no impact on smaller businesses.

Business rates

The conclusions to the Government's review of the business rates system has resulted in a large permanent increase in the small business rates relief. 600,000 smaller businesses will be affected. The Chancellor announced changes coming into force from April 2017:

- Business property with rateable value of £12,000 and below (replacing the £6,000 threshold) will receive 100% relief.
- Businesses with a rateable value between £12,000 and £15,000 will receive tapered relief.

The standard business rates multiplier is to be reduced for rateable values below a new threshold of £51,000.

From April 2020, the indexing of business rates will be by reference to the consumer price index, replacing RPI, and this should reduce amounts paid. However, it is also proposed for more regular valuation reviews, every three years.

Changes to Stamp Duty Land Tax

From 17 March 2016, commercial Stamp Duty Land Tax (SDLT) on the acquisition of non-residential (or mixed-use) properties changes from a 'slab' to a 'slice' system, with VAT-inclusive consideration over £250,000 subject to SDLT at 5%.

These changes to SDLT should increase the overall amount of tax paid, but for acquisitions of commercial property less than £1.05 million (including VAT where applicable) the SDLT liability will be lower. A benefit to smaller businesses, while larger occupiers under rental leases will also suffer if the net present value of rent exceeds £5 million.

There will be no relief for businesses from the **3% SDLT surcharge** that applies to the purchase of residential properties from 1 April 2016. Investors, traders and developers buying residential properties will now face unexpected SDLT.

Employee's termination payments

The Government has announced a tightening of the income tax exemption and an introduction of employer NICs on termination payments over £30,000, representing an increased cost for employers.