Comment

Views on the Autumn Statement

The impact on big business

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Banks bear the brunt of the revenue raising measures.

Tenterhooks it is for another week: the Autumn Statement made passing reference to the new 'diverted profits tax' (aka the 'Google tax') to be levied at 25% on profits artificially diverted overseas from the UK by multinationals, but it looks like we will have to wait for the Finance Bill for the details. There was a little bit more on some related initiatives, including increased transparency on global tax bills through country by country (CBC) reporting and the tackling of hybrid mismatch arrangements. A new consultation on hybrids outlines measures designed to implement the G20/OECD recommendations. This includes the 'primary response/defensive rule' concept: in the classic case that an item is deductible in country A but not included as taxable income in country B, then a compliant country A should disallow the deduction; but, in the absence of country A compliance, country B should tax the income. This rule is – deliberately – supposed to operate objectively and be blind to which jurisdiction has lost revenue. The UK seemingly accepts that it would displace the existing UK anti-arbitrage regime (which incorporates a UK-focused motive test).

Looking at the numbers, it is noteworthy that the Google tax is predicted to raise an extra £1.355bn over the next five years. The CBC reporting and anti-hybrid stuff is designed to raise an additional £305m over the same period. Is that all? It is likely to be a drop in the ocean for the relevant sector over the same period. Compare and contrast the projected increase in tax take over the next five years as a result of the new banking loss restrictions – £3.485bn according to the Autumn Statement figures.

The prospect of a restriction on the use of a bank's carried forward losses had fallen off most people's radar. A number of jurisdictions introduced rules along these lines in the wake of the financial crisis, but the UK government declined to act. Nevertheless, it seems that the balance has been tipped by the possibility of banks availing themselves of losses attributable to the financial crisis, as well as the costs associated with 'subsequent misconduct and misselling scandals' – enough to push out corporation tax profitability by as much as 20 years. Banks are now facing new restrictions which will allow only 50% of a bank's future yearly profits to be sheltered by existing carried forward losses. The new rules kick in for periods beginning or deemed to begin on or after 1 April 2015. They contain a TAAR designed to disallow altogether the use of carried forward losses against profits arising from arrangements where the tax advantage outweighs the economic advantage – which is not quite a purpose-based test, despite sounding like one. In addition, there is an anti-forestalling rule which is separately focused on deliberate preemption of the new restrictions.

Also out of left field were the announcements to remove the scope (by amending corporate rather than tax law) for effecting public takeovers by way of cancellation schemes of arrangement to save stamp duty; and to close down 'B share schemes', being schemes which offer shareholders a choice of income or capital for tax purposes on a return of funds. B share schemes were thought to have been fairly safe, having even been cited in the GAAR guidance as falling on the acceptable side of the line, but clearly the softness of the target was too tempting when it came to rattling the kitty. These two measures are expected to bring in an extra £285m and £165m respectively over the next five years. If only we could all predict the levels of future M&A activity with such accuracy.

The private client perspective

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L'embarras des richesses.

A private client listening to the chancellor's Autumn Statement might have thought that there was little to affect him for good or ill. A closer look, however, suggests that the UK is to continue to be ever less welcoming to productive wealth, enterprise and expertise.

Those with comfortable incomes will not benefit from the increase in the personal allowance for 2015/16, whilst the chancellor's reference to the increase in the 'higher rate threshold' disguises the fact that the basic rate band is to be reduced once again. The chancellor extracted some political mileage from announcing once again the changes to the taxation of pensions, with which we are all now so familiar, and introducing minor new inheritance tax exemptions for emergency services and humanitarian personnel, which had already been well trailed in consultation documents.

Two sets of anti-avoidance provisions will further complicate the operation of the reliefs to which they apply. One will disallow losses otherwise deductible under ITA 2007 s 152 against miscellaneous income; and the other will prevent entrepreneurs' relief from applying to certain disposals of goodwill. Although the Autumn Statement says that the latter restriction will apply where the goodwill is transferred 'to a related close company', an examination of the draft legislation reveals that it will apply to any disposal of goodwill if the disponer is 'party to relevant avoidance arrangements'. The definition of such arrangements means that yet another costly uncertainty will be introduced into this already overcomplicated relief.

One can at least be thankful that the government appears to be retreating from its mean spirited proposal to restrict non-residents' entitlement to the personal allowance and to have seen the folly of its proposals for the 'simplification' of the inheritance taxation of settlements. The government is at last to take the professional bodies advice to 'target avoidance through the use of multiple trusts', rather than introduce a single settlement nil-rate band. Ominously, though, it is also to 'simplify the calculation of trust rules'. One feels that something has been lost in translation here.

Putting aside these more minor matters, the major items affecting private clients will significantly increase the burden of taxation on them. It is always politically easy to propose some new fiscal impost on the 'rich', but this incremental approach allows governments to avoid considering how one quantifies the overall burden of taxation on productive wealth and how one determines what it should be. One more straw will not break the camel's back, because this useful metaphorical beast of burden always has the option of taking itself to more hospitable countries.

In spite of former promises to introduce some stability into the taxation of non-domiciliaries, the remittance basis charge is to be altered and its burden significantly increased. The charge on those who have been resident for 12 out of the last 14 years will increase to £60,000 and a new charge of £90,000 will be imposed on those who have been UK resident for 17 of the last 20 years. Most significantly, the government will also consult on making the election apply for a minimum of three years. This last proposal will markedly increase the costs of the remittance basis to those who realise a one-off capital gain or income amount, providing an increased incentive for them to move abroad just when they are most likely to do so.

Non-domiciliaries are also likely to be disproportionately affected by the chancellor's proposal to increase the ATED in respect of residential properties worth more than £2m by 50% above inflation.

In proposing to impose penalties on transactions to which the GAAR applies, the chancellor has stolen an idea of Mr Miliband's – one is not sure whether that is a good source in which to find one's fiscal innovations. If enacted, it will further increase the expensive burden which the GAAR imposes just as much on taking advice on commercial transactions as on 'egregious tax avoidance'.

The introduction of a banded rate system to SDLT on residential properties to replace the slab system – which, it appears, will continue to apply for other SDLT purposes – widens still further the gap between what is rapidly becoming two separate systems of SDLT. It also shifts significantly the burden of SDLT onto those who own larger properties. The result is that any property costing more than £937,500 will bear an increased amount of SDLT. A property costing £1.5m will bear £18,750 more tax than under the current rules and one costing £5m will bear £163,750 of additional tax.

After a detailed examination, therefore, the chancellor is unlikely to have pleased very many private clients. Surely, however, one cannot but admire the chutzpah of a man who can claim to have 'set a course to restore stability' and to 'get on top of our debts', who actually plans to increase public spending in every year of his five-year planning horizon and intends to spend more than he receives for the next three fiscal years, adding £126bn to the nation's already grotesquely swollen national debt – a man who plans to return to basic fiscal prudence only at a time which is comfortably far away in the future.

Compliance, enforcement and appeals

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Examining the conspicuous absentees.

In an Autumn Statement which in general contained a lot more than had been expected, there was probably less than had been expected in relation to compliance and enforcement. In fact, it was the matters that were 'conspicuous by their absence' that are perhaps most worthy of comment.

The main items that had been anticipated were the post-consultation proposals in relation to the direct recovery of debt (DRD), the principles of which had been announced in the Budget in March and consulted on over the spring and early summer. However, HMRC 'jumped the gun' by making an announcement on 24 November 2014 which 'watered down' the original proposals significantly. In particular, new safeguards were announced, including one which provides HMRC with a requirement (described as an 'opportunity'!) to meet and personally identify the debtor, confirm it is their debt, explain to the debtor what they owe and why they are being pursued – and discuss their proposals for payment. Other provisions include options to resolve the debt, including offering a 'time to pay' arrangement to the debtor and identifying 'vulnerable debtors'.

In addition, the window for debtors to object to DRD has been extended from 14 to 30 days, with funds being 'frozen' during this period but not transferred to HMRC – and a right to appeal against DRD to the County Court on specified grounds.

Given the level of objections to the original proposals (although surprisingly the consultation elicited only 124 responses), it can at least be said of HMRC that it 'listened' in relation to DRD – and the revised proposals should be given a cautious welcome.

The second conspicuous absentee was any further word on the proposals for a strict liability offence in relation to tax evasion, which were announced by the chancellor in a speech a few weeks after the Budget and then the subject of a consultation which closed on 31 October 2014. Revised proposals had been widely expected in the Autumn Statement. It is entirely possible that these may emerge over the next couple of weeks – or even in January 2015. One might divine from the absence of this measure that the results of the consultation were 'negative', particularly with regard to safeguards – as one assumes they were in relation to DRD. It is also fair to say that it is now unlikely that the new offence will be enacted in the course of the current parliament, given that revised proposals (probably with further limited consultation) followed by draft legislation will need to be published first.

There was, however, something in relation to offshore evasion. The HMRC consultation entitled *Tackling offshore tax evasion: Strengthening civil deterrents*, which closed on 31 October 2014 was followed up with an announcement that, in advance of the implementation of a new global standard for the automatic exchange of financial information for tax purposes, the government will increase the amount and scope of civil penalties for offshore tax evasion. The existing offshore penalties regime will be extended to include inheritance tax and will apply to domestic offences where the proceeds are hidden offshore (these measures will be introduced with effect from 1 April 2015). There will also be a new aggravated penalty of up to a further 50% for moving hidden funds to circumvent international tax transparency agreements (with effect from royal assent of the next Finance Bill, presumably on the dissolution of Parliament in April 2015). There was also a reference to a review of 'incentives' for obtaining information on offshore tax evaders – possibly further 'amnesties' or even (shock, horror!) financial incentives for 'whistleblowers'? However, it is difficult to see how this might work in practice when the common reporting standard will lead to the release of the identity of defaulters in any event.

We were also promised (yet) more consultations next year on the introduction of further deterrents for serial tax avoiders; penalties for tax avoidance cases where the GAAR applies; and the reinforcement of DOTAS by updating hallmarks, removing 'grandfathering' provisions for existing schemes. This is along with a new 'task force' for policing the DOTAS regime – presumably in part to address concerns that the accelerated payment rules applicable to DOTAS arrangements might encourage non-disclosure.

A figure of £5bn was mentioned in the chancellor's speech as being recoverable from 'measures tacking avoidance and evasion' – and one assumes that a portion of this is what the proposed measures will be expected to bring in. Again, we can expect them ahead of the Budget in March 2015 – having regard to the fact that Parliament will be dissolved shortly afterwards. Any 'firm' proposals and draft legislation will not be expected until after the next Parliament convenes in May 2015.

Finally, a rare very positive move which will be welcomed both by HMRC and (sensible) taxpayers. It has long been a bugbear of those trying to resolve disputes that it is extraordinarily difficult to litigate a disputed aspect of a self-assessment return whilst other aspects remain 'open' and under enquiry. It can lead to delays running on for years. The current cumbersome process (requiring both parties' consent) for the referral of a single issue to the tribunal has never worked in practice. Buried in the small print is a proposal to consult on giving HMRC the power to close one aspect of an enquiry whilst leaving others open. Provided that this is backed by a commensurate provision enabling taxpayers to apply to the tribunal for a direction that HMRC should issue a closure notice in relation to a single aspect, this is a very welcome measure which will speed up the resolution of disputes. One hopes it will help to clear the current unacceptable backlog of open enquiries. It might, however, mean that the tribunals become even busier than is currently envisaged as a result of accelerated payment notices etc. and the impact of HMRC's litigation and settlement strategy.

The impact on SMEs

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A mixed bag for SMEs.

Hitherto, it has been standard planning for a sole trader or partner incorporating a business to take advantage of the scope for selling goodwill to the new company at market value. The gain would normally benefit from entrepreneurs' relief (ER) and (provided the goodwill was created after 2002) amortisation relief would normally be available to the company. Very few will have considered such planning to have been 'tax avoidance'. But apparently they were mistaken; for it is in the name of 'countering avoidance' that henceforth (for transactions undertaken on or after 3 December) ER is to be denied to the individual and amortisation relief to the company.

On the other hand, there is good news on the ER front as well. Until now, the crystallisation of a gain – which has previously been deferred by use of the enterprise investment scheme or social investment tax relief – has (completely illogically) not been capable of qualifying for ER. A taxpayer has had to choose between taking ER and deferring the gain. It is now very sensibly proposed that if the original gain would have qualified for ER had it not been deferred by reinvestment, it will also (to the same extent) qualify for ER when it crystallises at a later date. This will benefit gains that are deferred on or after 3 December but, disappointingly, not the crystallisation after that date of gains deferred before then.

Reforms to stamp duty – essentially replacing the 'slab' system with a banding system – are primarily targeted at owner-occupiers, but will also benefit developers and investors (provided of course that they are not within the penal rules applying to non-natural owners of 'expensive' residential property). It is regrettable that the changes do not also apply to commercial property: firstly, because having decided that a 'cliff-edge' system is inequitable it seems odd to want to preserve it for non-residential transactions; and secondly, because of the complexity now introduced where a single transaction has both residential and non-residential elements.

The best that can be said for the enhancement to R&D tax relief (up from 225% to 230%) is that it is at least better than reducing it; but the introduction of an advance assurance scheme for small businesses making their first R&D claim is likely to be of more practical significance. And the introduction (from April 2015) of a new corporation tax relief for the production of children's television programmes is likely to be of real help to small businesses operating in that field.

As widely leaked, ahead of the Autumn Statement, the government is to review the future structure of business rates with a view to reporting by Budget 2016. Meanwhile, temporary sticking plaster solutions include extending the doubling of small business rate relief to April 2016 and increasing to £1,500 the existing business rates discount for shops, pubs, cafes and restaurants with a rateable value below £50,000.

HMRC proposes to review arrangements whereby the use of 'umbrella company' structures permits employment intermediaries to afford tax relief for home-to-work travel for some temporary workers. Employers will perhaps be delighted or aggrieved, depending on whether they use the arrangements themselves or see them as unfair competition. But most employers will be unequivocally happy to see the prospective adoption of many of the recommendations made by the Office of Tax Simplification on simplifying the rules for employee benefits and expenses.

A view from the OTS

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Simplification is on the agenda.

It was gratifying that the OTS's work on competitiveness was mentioned in the Autumn Statement, and in the context of most of our recommendations being taken forward. The main Budget documents had more to say on our work, as did a letter from the financial secretary (to be published on our website).

Competitiveness review: Our recent report on improving the competitiveness of the UK tax administration came up with 58 recommendations and 51 are being taken forward. Many of our ideas were far reaching structural measures, such as moving taxable profits closer to accounting profits and abolishing the trading/investment income divide. Rightly, the commitment is to consider the ideas properly, not make precipitate changes.

It is very good to see that such ideas will be taken seriously and that a significant number of our points will definitely be taken forward – including the idea of a post-implementation review of RTI and the need for full 'on or before' reporting.

Employee benefits and expenses (EBE): The four measures consulted on in the wake of our main EBE report – abolishing the £8,500 threshold; replacing dispensations with relief for allowable business expenses; a trivial benefits exemption; and a framework for voluntary payrolling – are all going ahead. These will make a real difference to the administrative burdens around P11D reporting. There are other recommendations that need taking forward, especially widening PAYE settlement agreements which I am constantly told needs actioning.

Accommodation benefits and termination payments: We reported separately on these and made the case for simplification through reform, though we readily acknowledged that these are complex and sensitive areas. The letter from the financial secretary to the Treasury (FST) says the government will consider the issues, but these were never going to be areas for quick action.

Tax penalties: Our recent short report on penalties is acknowledged and we look forward to hearing more about our recommendations.

Partnerships: We are continuing to work on aspects of this subject and will soon be publishing a final report. In the meantime, progress is being made on a number of our ideas, including streamlining the process of reporting partners' and the partnership's income.

Share schemes: It is disappointing that two of our more radical ideas around share schemes – the 'marketable security' and 'employee shareholding vehicle' – are not going forward. We were surprised that HMRC's consultations attracted limited comment – we heard a lot of requests for the measures. But overall there has been a good programme of reforms in the share schemes area based on our recommendations.

One of our projects that didn't get a mention was the work we did on tax reliefs. But listening to the speech I was struck by the fact that we'll need to update – again – our list of reliefs, which currently stands at 1,140 … and rising!

Economic view

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Five more years of pain.

The chancellor stuck to his guns in the Autumn Statement, confirming there could be five more years of pain to come on public spending to restore the budget to surplus before 2020.

The Office for Budget Responsibility (OBR) has raised its real GDP growth forecasts slightly to 3% this year and 2.4% next year (see table below), almost exactly in line with our own projections published last month. But this is offset by slower than previously expected growth in the following three years, due to the ongoing malaise in the Eurozone and shrinking spare capacity in the domestic UK economy. Nonetheless, growth of around 2–2.5% in the medium term would still be a respectable performance, close to the UK's historic trend growth rate and consistent with unemployment settling at just over 5%, similar to pre-recession levels.

Comparison of key OBR forecasts at the time of the 2014 Budget and the Autumn Statement

GDP growth (%, calendar years)	2014/15	2015/16	2016/17	2017/18	2018/19
Budget (March 2014)	2.7	2.3	2.6	2.6	2.5
Autumn Statement (Dec 2014)	3.0	2.4	2.2	2.4	2.3
CPI inflation (%, calendar years)					
Budget (March 2014)	1.9	2.0	2.0	2.0	2.0
Autumn Statement (Dec 2014)	1.5	1.2	1.7	2.0	2.0
Public sector net borrowing (£ billion)*					
Budget (March 2014)	86	68	42	16	-4
Autumn Statement (Dec 2014)	91	76	41	15	-4

**Excluding borrowing of public sector banks (on revised ESA 2010 definitions)*
Source: OBR

The planned severe spending cuts in the next parliament impose a drag on UK growth in the medium term, although this negative impact should be offset by lower interest rates than would be possible without this continued austerity.

The OBR has also revised down its inflation projections over the next couple of years, which is good news for consumers but less good for tax revenues, as these are related to growth in cash terms. Wage growth is expected to pick up gradually over time, but there is still a long way to go before the sharp fall in real wage levels since the onset of recession is made up. This tends to keep down income tax receipts throughout the forecast period.

Overall, tax receipts are projected to be around £25bn lower in 2018/19 than the OBR forecast at the time of the Budget in March. But this is offset almost exactly by lower public spending, primarily on debt interest but also on welfare payments and departmental spending to a lesser degree.

As a result, as the table shows, public borrowing is higher than previously forecast this year and next, but then falls faster than expected over the following two years. In 2018/19, after four more years of austerity, the budget is projected to be back in surplus by around £4bn, almost exactly the same as the projection in March.

Given the short-term borrowing overshoot, any giveaways in the Autumn Statement (e.g. from stamp duty changes and raising the income tax personal allowance) were at least matched by takebacks, such as the restrictions on loss relief for banks and anti-avoidance measures. Overall, there was a small net fiscal tightening, relative to previous plans up to 2018/19, but not enough to have a major impact on the economy. In addition, the chancellor pencilled in another year of spending cuts in 2019/20.

In summary, therefore, the chancellor had good news to announce on jobs and growth, and some welcome help for small businesses and buyers of less expensive homes. But his central message was that we have five more years of pain to come on public spending. ■