

UK Autumn Budget 2018 – the key measures impacting business

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The Chancellor, Philip Hammond, has delivered the Budget 2018. Announcing that the era of austerity was coming to an end, whilst retaining the need for fiscal discipline, his headline grabbing announcements in the business arena include a new Digital Services Tax and a tightening of the requirements for entrepreneurs' relief.

Our tax experts pick out below eight key measures that will have a significant impact on businesses and wealthy individuals doing business in the UK.

New Digital Services Tax

Taxation of digital business is an issue of significant public interest, with a perception, fanned by the popular press, that large search engines, social media platforms and online marketplaces generate significant revenues from the UK but do not pay their "fair share" of tax. In order to bring the UK tax system up to date with the digital economy, the Chancellor announced a new tax intended to reflect the value such large businesses derive from UK users.

From April 2020, the government proposes to introduce a new tax, similar to that recently introduced in Spain. It will be a 2% tax on the revenues of certain digital businesses to ensure that the amount of tax paid in the UK is reflective of the value they derive from their UK users. Broadly, the tax will apply to revenues from those activities that are linked to the participation of UK users, subject to a £25 million per annum allowance. It will only apply to groups that generate global revenues from in-scope businesses of more than £500M per year.

The government remains committed to G20 and OECD discussions on potential future reforms to the international corporate tax framework, and will only apply the DST until an appropriate long-term solution is in place.

Is the Chancellor jumping the gun or plugging the gap with his new digital services tax aimed at tech giants? He rightly recognises that this needs to be a global initiative, but he is tired of waiting and wants to introduce something now. The new tax will no doubt be complex to administer, likely be replaced by the OECD global solution in due course, and is not be expected even by the Chancellor to raise much revenue.

Entrepreneurs' Relief

The Chancellor did not, as some had anticipated, announce the abolition of entrepreneurs' relief. However, he did tighten the requirements.

To encourage longer-term investment, from 6 April 2019 the minimum period throughout which the qualifying conditions for relief must be met will be extended from 12 months to 24 months.

In another change, in addition to the current requirement to hold at least 5% of the company's ordinary share capital (by reference to nominal value) allowing the individual to exercise at least 5% of the voting rights, from

29 October 2018 shareholders must also be entitled to at least 5% of the distributable profits and net assets of a company to claim the relief. This is intended to address a perceived abuse of the current rules where individuals can benefit from entrepreneurs' relief without having a material economic interest in a company. This is likely to be a significant problem for certain PE managers. Careful structuring may be able to ameliorate the effects of the new rules in certain cases.

Tax Relief for IP

Following a short consultation, the government will seek to introduce targeted relief for the cost of goodwill in the acquisition of businesses with eligible intellectual property from April 2019. With effect from 7 November 2018, the government will also reform the de-grouping charge rules, which apply when a group sells a company that owns intangibles, so that they more closely align with the equivalent rules elsewhere in the tax code.

New Structures and Buildings Allowance (SBA)

The Chancellor announced a new Structures and Buildings Allowance (SBA) for new non-residential structures and buildings. Relief will be provided on eligible construction costs incurred on or after 29 October 2018, at an annual rate of 2% on a straight-line basis.

The new tax relief for expenditure on new and improved non-residential structures and buildings is to be welcomed in principle. However 2% per annum, spread over 50 years and against a backdrop of a 17% corporation tax rate, appears to be too little to move the dial.

Protecting taxes in insolvency

In what we see as a retrograde step, from 6 April 2020 HMRC will once again be a preferred creditor, this time in relation to VAT, PAYE Income Tax, employee NICs, and Construction Industry Scheme deductions. This is despite a large body of work being carried out in the past by the Law Commission and insolvency bodies, which led to the removal of crown preference for VAT and direct taxes since it often resulted in struggling but salvageable businesses being driven into the ground by an overzealous HMRC. The rules will remain unchanged for taxes owed by businesses themselves, such as Corporation Tax and employer NICs.

This measure is likely to lead to greater complexity in restructuring, securitisations and financings generally, but particularly in whole business securitisations (or similar arrangements).

Hybrid Capital Instruments

Certain corporate debt instruments (known as hybrid capital) have some equity-like features. The government will introduce new rules for the taxation of such instruments, to ensure that they are taxed in line with their economic substance, taking into account new Bank of England requirements for loss absorbency. Generally speaking, this measure should improve the position for taxpayers by making interest deductibility more certain and thus issuance of such instruments may increase, particularly in a PE context. The new rules will also eliminate mismatches between the tax treatment of instruments used to raise funds externally and those used to on-lend such funds internally within a group. The rules will cover issues by companies in any sector and replace current rules covering regulatory hybrid capital instruments issued by banks and insurers.

New tax introduced on offshore receipts in respect of intangible property

As announced at Autumn Budget 2017, the government is introducing legislation in Finance Bill 2018-19 to tax income from intangible property held in low-tax jurisdictions to the extent that it is referable to UK sales. This measure will come into effect from April 2019. Following consultation, the government is making changes to ensure that the measure is effective, appropriately targeted and robust against abuse. These include collecting the tax by directly taxing offshore entities that realise intangible property income in low-tax jurisdictions, rather than through applying a withholding tax.

Personal Tax

The income tax Personal Allowance will increase to £12,500 for tax year 2019/2020. The basic rate limit will be increased to £37,500 for 2019/2020. As a result, the higher rate threshold will be £50,000 in 2019/2020.

The Capital Gains Tax annual exempt amount will increase to £12,000 for individuals and personal representatives and £6,000 for trustees of settlements for tax year 2019/2020.

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