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United Kingdom – Summer Finance Bill 2015 Published

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The U.K. government's Summer Finance Bill 2015 ("SFB 2015") was published on 15 July 2015[1]. The Bill incorporates the changes announced in the Summer Budget 2015 (see GMS *Flash Alert* 2015-083 (10 July 2015). Measures affecting individuals – including globally mobile employees – include, a further increase to the U.K. personal allowance, new threshold for the upper limit of the basic rate tax band, and a tax "lock" on increases in the rates of income tax, VAT, and National Insurance contributions (NIC).

The SFB 2015 does not include draft legislation on the changes to the U.K. tax rules for individuals considered to be domiciled outside the United Kingdom. This is expected to be published after the summer recess of Parliament in conjunction with the consultation document due on this issue. In the meantime, for further details on these changes and the expected legislation, please see GMS *Flash Alert* 2015-088 (17 July 2015).

Why This Matters

There are several measures of note for international assignees and their employers. It is important that the potential additional costs arising from these measures are considered and budgets adjusted accordingly. Where appropriate, payroll administrators should be planning for adjustments to withholdings.

Employers should also consider whether it is appropriate to communicate the changes to those assignees who are potentially affected by the changes proposed in SFB 2015, and the proposed changes to the rules on non-U.K. domiciled individuals.

Provisions are being put in place to ensure that the rates of income tax, National Insurance Contributions (NIC or U.K. social security), and VAT do not rise above their current levels during the life of this Parliament. This will provide employers with certainty in respect of the marginal rates of U.K. tax over the next five years.

Summer Finance Bill's Main Measures in Detail

Personal Allowance Increase and Indexation

In the Summer Budget, a further increase (over and above those announced in the Budget in March 2015) was announced to the U.K. personal allowance (PA). From 6 April 2016, the PA will increase from GBP 10,600 to GBP 11,000. It will rise again from 6 April 2017, to GBP 11,200. These increases have been legislated for in SFB 2015. For individuals earning over GBP 100,000, the PA continues to be phased out by GBP 1 for every GBP 2 by which income exceeds GBP 100,000.

Further increases in the PA (up to GBP 12,500) have been promised. Legislation also included in SFB 2015 provides that once the PA reaches the promised level it is increased in line with the national minimum wage so that anyone working for 30 hours per week and earning the minimum age will not pay any income tax.

Higher Rate Threshold Increase

The upper limit for the basic rate tax band (that is, the income level at which taxpayers start to pay tax at 40 percent) was set to increase to GBP 31,900 in April 2016 (making the higher rate threshold GBP 42,700 when including the tax free personal allowance). Legislation is included in SFB 2015 to implement further increases in this threshold announced in the Summer Budget. The new threshold will be GBP 43,000 from 6 April 2016.

Tax Lock

Legislation is included in the SFB 2015 to ensure that the rates of income tax, NIC, and VAT cannot rise above those in force for 2015/16 (that is, the current U.K. tax year). There are also provisions to ensure that the upper earnings limit for NIC cannot rise above the threshold at which higher rate tax begins to be paid. For information, the upper earnings limit for NIC is the level at which employee contributions decline from 12 percent to 2 percent. This measure will therefore mean that individuals will not be required to pay 40-percent tax and 12-percent NIC on the same income.

KPMG Note

This measure was one of the election promises made by the Conservatives and therefore its inclusion in SFB 2015 is no surprise. It is interesting to note that capital gains tax is not included within the tax lock, especially given that gains are charged to tax at 18 percent or 28 percent compared to the top rate of income tax of 45 percent.

Pensions – Restriction of Annual Allowance

In the Summer Budget, it was announced that individuals with income of over GBP 150,000 will have their Annual Allowance (AA) for pensions reduced (briefly, the AA is the level of pension savings in a year that benefit from full tax relief). Legislation is included in SFB 2015 to enact this.

The AA will remain at GBP 40,000 for individuals with income of less than GBP 150,000, but will then be reduced by GBP 1 for every GBP 2 by which income exceeds the GBP 150,000 limit until the AA reaches GBP 10,000. The GBP 10,000 is reached at an income level of GBP 210,000. To the extent that the adjusted AA is exceeded, an AA charge will arise which is taxed at the individual's marginal rate of tax.

For these purposes, there is a special definition of income based on an "adjusted income" which will include, amongst other items, the value of employer pension contributions. Under the new rules, the position should be reviewed for anyone whose earnings (net of pension contributions) are over GBP 110,000 to ascertain whether their adjusted income exceeds GBP 150,000. Complex transitional provisions will apply.

This measure will take effect from 6 April 2016.

An anti-avoidance provision prevents the use of salary sacrifice under arrangements made on or after 9 July 2015, to reduce the individual's threshold income for the purposes of calculating the restriction.

KPMG Note

The interaction between the phase-out of the AA and the phase-out of the PA appears to have some important consequences for individuals whose net income is above GBP 110,000 and whose adjusted income is above GBP 150,000.

The result of the phase-out appears to be that for individuals who are affected by both, the phase-out of the AA and the PA for every additional GBP 2 of salary is subject to an effective tax rate of 80 percent. Although the number of people to be affected by this is unknown, KPMG LLP (U.K.) is seeking clarification on whether this is the intended policy objective.

Withdrawal of Higher Rate / Additional Rate Relief for Mortgage Interest

Under current rules, individual owners of residential property who rent the property out are normally able to deduct the full interest costs from borrowings in respect of their property-business. This is in contrast to interest paid on borrowings undertaken to fund the purchase of a property to be used by an individual as a residence (in respect of which no deduction is allowed for interest paid).

SFB 2015 includes a restriction on the available relief for owners of residential rental property carrying mortgages, which will be phased in from 6 April 2017. This will operate as follows:

- 2017/18 – 75% interest full deduction: 25% interest relieved at basic rate of income tax;
- 2018/19 – 50% interest full deduction: 50% interest relieved at basic rate of income tax;
- 2019/20 – 25% interest full deduction: 75% interest relieved at basic rate of income tax;
- 2020/21 – 100% interest relieved at basic rate of income tax.

The basic rate relief on interest will be given as a tax reduction in the individual's tax computation for the year, rather than as a deduction from the rental profit. The tax reduction will be 20 percent of the lower of the interest affected, the rental profits, and the individual's income (excluding savings and dividend income) for the year. Where the affected interest exceeds the rental profits in a year, the excess will be carried forward for potential relief in subsequent tax years.

KPMG Note

These changes will affect only those individuals who are liable to higher or additional rates of income tax. The proposal indicates that it will apply only to individual property owners and it remains to be seen whether the rules will also apply to properties owned through trusts and other entities that pay income tax on rents. U.K. companies letting residential property, which are subject to corporation tax on their profits, would not seem to be affected. This creates a potential mismatch in the treatment of loan interest for different forms of property business.

It also appears that the basis on which relief is calculated will mean that for "higher earners," the amount of the mortgage interest relief that is given at 20 percent will not reduce profit. It will therefore not reduce income for the purposes of the pension relief restriction. This would appear to be a further disadvantage to such individuals, particularly where they are also affected by the restriction on personal allowances.

Footnote:

1 See: http://www.publications.parliament.uk/pa/bills/cbill/2015-2016/0057/16057.pdf .

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Labor Law and International Assignments Survey for You to Take

We invite you to take a brief survey prepared by the Legal Services team* within the KPMG International member firm in Germany. This is a benchmarking survey regarding multinational organizations' global labor law awareness and practices. To take the survey, click here.

The aim of this short survey is to gain insight and provide benchmarks on global labor law practices and considerations in the context of international assignments. This will enable organizations to keep abreast of trends in this oft-overlooked area and to identify market-standard practices of benefit to both the organization and the assignee.

The survey is also accessible on mobile devices and should take no longer than 10 – 15 minutes to complete.

The closing date for the survey is Friday, 14 August 2015. Results can be provided upon request.

** There are Legal Services teams present in over 50 KPMG International member firms around the world, working along-side Global Mobility Services tax and immigration professionals to help employers make sense of and stay compliant with the labor rules and practices that apply to their assignees working in a cross-border context.* ***Please note that KPMG LLP (U.S.) does not offer services related to matters of labor law.***

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