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Clients&FriendsMemo

UK Budget 2020 – Key Tax Measures

12 March 2020

The Chancellor of the Exchequer delivered the United Kingdom ("UK") Budget for 2020 on 11 March 2020. The Budget was delivered against a backdrop that very few people could have anticipated at the commencement of the year. The Government's long term focus of re-orienting the UK away from the European Union, as a result of Brexit, is now overshadowed by the global pandemic of Covid-19. Despite this dramatic political environment, the measures in the Budget relating to taxation are, by contrast, almost reassuringly down-to-earth. Those measures deliver a consistent message of the UK being a top-tier jurisdiction in which investment can be made efficiently, alongside a careful eye being kept on the competitiveness of the UK's tax policy environment. In this regard, of note is the continuation of the corporation tax rate of 19 per cent. for the 2020/2021 tax year, still relatively low compared to many EU member states' equivalent corporate income tax rates, and the forthcoming review of the taxation of certain elements of the UK's fund industry. The Chancellor also announced a second budget to be delivered in the Autumn to coincide with the completion of the Government's review of business rates. This would also likely present a further opportunity for setting out the Government's post-Brexit tax policy.

In this Client and Friends Alert we have outlined the key tax measures that we expect to be of interest to Cadwalader's clients and friends.

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Limited Liability Partnerships ("LLPs")

The UK government has announced that it will legislate both prospectively and retrospectively in Finance Bill 2020 to "put beyond doubt" that LLPs should be treated as general partnerships under the legislation relating to the taxation of partnerships. Prior to this announcement, an LLP would be treated as being tax transparent – and, effectively, taxed as a general partnership – where it was carrying on a business with a view to profit. The proposed legislative change will ensure that HMRC can continue to amend LLPs members' tax returns where the LLP operates *without* a view to profit, thereby correcting a potential weakness in the legislation. As a result, HMRC will be able to amend the returns of LLP members even if the LLP is argued to be operating "without a view to profit" – as might be the case in certain structured arrangements.

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Wide-ranging review of the UK fund industry

The UK government will undertake a review of the UK's legislative regime for funds during 2020, covering direct and indirect tax as well as relevant areas of regulation. The review will consider the possibility for legislative changes based on policy objectives, which are likely to be aligned with the post-Brexit environment for investment in UK-managed funds. The review will include a consultation on whether changes to the tax treatment of intermediate holding companies used by funds to hold assets might result in the UK being a more viable location for such companies, as opposed to companies located in other European jurisdictions such as Ireland or Luxembourg. This is likely to have considerable importance for alternative funds that commonly make real-estate, credit and private equity investments through intermediate asset holding companies. As part of this review, the government has said that it will consider the VAT treatment of fund management fees, in respect of which the UK is sometimes perceived to offer a less attractive VAT regime compared to other comparable jurisdictions. We will be following developments in respect of the Government's review during the course of 2020.

Counteracting tax avoidance

The government has announced that it will legislate in Finance Bill 2020-21 to take further action against those who promote and market tax avoidance schemes. Of particular note is the announcement that enhanced information powers will be added to HMRC's existing regime to tackle "enablers" of tax avoidance schemes, including the imposition of penalties to be applied "without delay" for multi-user arrangements, resulting in anyone enabling tax avoidance arrangements that are later defeated facing a penalty of 100 per cent of the fees they earn.

Enhancements are also promised by the Government to ensure promoters fulfil their obligations under the Promoters of Tax Avoidance Scheme regime, including where HMRC has alleged those promoters have tried to abuse corporate structures to get around the rules, or have staged allegedly spurious legal challenges to disrupt the process by which HMRC scrutinises promoters. The government has also announced that it will legislate to make additional changes to the UK's General Anti-Abuse Rule, or "GAAR", so the GAAR can be used more effectively (or, in the phrase of HMRC, "as intended") to tackle avoidance using partnership structures.

Finally, in an eye-catching measure, the Chancellor announced in Parliament that the government will publish a call for evidence in the spring of 2020 on raising standards for tax advice. The government has stated that it will seek evidence about providers of tax advice, and the current standards upheld by tax advisers, in order to give taxpayers more assurance that the advice they are receiving is reliable. This development will be interesting to monitor, particularly in line with the existing standards for providers of taxation advice which are published by professional associations, such as the Chartered Institute of Taxation.

Digital Services Tax

The Government has previously confirmed that it would press ahead with the introduction of a digital services tax (**"DST"**), notwithstanding requests from the US to defer such measures and France's deferral of the collection of taxes under its own DST. The introduction of a UK DST

was again confirmed in Budget 2020 and will come into effect from 1 April 2020. The UK DST is intended to apply to search engines, social media services and online marketplaces with group worldwide revenues of more than £500 million and where more than £25 million of these revenues are derived from UK users. The UK DST will apply at the rate of 2 per cent. subject to a £25 million allowance.

DSTs generally were borne out of proposals for reform of the international tax system, and in particular, the digital economy. Whilst there is broad consensus that the international tax system should be reformed, there are divergent views as to the approach that such reform should take. In particular, the OECD and G20 are considering options for reform that would address the digitalisation of the broader economy and are hoping to present a "unified approach" by July 2020.

In light of the UK's departure from the EU and the negotiation of trade agreements, including with the US, it will be interesting to see how the introduction of UK DST impacts upon these issues.

UK Property

As has come to be expected, a number of announcements in the Budget 2020 were focussed on the taxation of UK property.

Non-residents acquiring residential property

Following a consultation process which ran until 6 May 2019, non-UK residents (including individuals, companies, trusts and partnerships) purchasing residential property in England and Northern Ireland (noting that land taxes in Scotland and Wales are devolved) will be subject to a stamp duty land tax ("**SDLT**") surcharge at the rate of 2 per cent. to take effect from 1 April 2021. A summary of responses to the consultation are due to be published shortly and transitional rules may apply to contracts exchanged before 11 March 2020 (i.e. Budget day) but which complete, or are substantially performed, after 1 April 2021. This surcharge will take the possible top rate of SDLT for overseas purchasers to 17 per cent. (when combined with the existing 3 per cent. surcharge for second properties).

This SDLT surcharge was less than the 3 per cent. rate that some had anticipated, although more than the 1 per cent. rate that had initially been proposed in the consultation process. The Government intends to allocate the estimated £140 million that will be raised over a five-year period from this surcharge to help fund policies to reduce rough sleeping.

VAT Domestic Reverse Charge

The Government reiterated that the introduction of the VAT domestic reverse charge for building and construction services will be delayed until 1 October 2020 (from the previously announced start date of 1 October 2019).

Whilst the "reverse charge" rules usually apply in a cross-border context, the domestic reverse charge procedure will require UK customers who receive supplies of construction services from

UK suppliers to account for the VAT component. This measure is intended to utilise the reverse charge collection mechanics in a way which addressed VAT fraud arising where suppliers fail to account to HMRC for the VAT in respect of supplies made.

Non-resident companies with UK property income

The Government has also announced that legislation will be introduced in Finance Bill 2020 to smooth the transition of non-UK property companies carrying on a UK property business or otherwise deriving UK property income from the income tax regime to the corporation tax regime. Specific amendments will be made to address transitional issues identified in relation to the interaction with the loan relationships and derivative contract rules as well as relief for pre-commencement financing costs.

Amendment to the calculation of Banking Surcharge

The Budget has introduced, with immediate effect from 11 March 2020, an amendment to the calculation of surcharge profits for the purposes of Banking Surcharge.

The Banking Surcharge is a charge of 8 per cent. on the profits of banks, levied in addition to corporation tax. Surcharge profits, on which Banking Surcharge is chargeable, are calculated on the same basis as for corporation tax, other than having some further reliefs disregarded. For the purposes of corporation tax, a bank can elect to transfer allowable losses from a non-banking company in the same group to the bank (such losses, "**transferred-in losses**") so that the transferred-in losses can be used to reduce the bank's chargeable gains. Under the current legislation, for the purposes of surcharge profits, such election would be disregarded in relation to those transferred-in losses used to reduce future chargeable gains, but not those transferred-in losses used to reduce chargeable gains arising in the same year as the transferred-in losses.

The Budget has addressed this inconsistency, such that banks can no longer use transferred-in losses to reduce in-year surcharge profits.

This measure has immediate effect, applicable to allowable losses that are deducted from chargeable gains accruing on disposals made on or after 11 March 2020. Legislation will be introduced in Finance Bill 2020 to bring this measure into law.

Crown Preference

The measure of making HMRC a secondary preferential creditor (ranking before floating charge holders and unsecured creditors) in respect of certain tax debts held by a business was originally announced at Budget 2018 and scheduled to take effect from 6 April 2020.[1] Budget

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[1] We have previously written a Brass Tax article on Crown Preference as announced at Budget 2018, "*Squeezing Until the Pips Squeak: The UK Government's Reinstatement of Crown Preference.*" For further information, please visit: https://www.cadwalader.com/brass-tax/index.php?nid=4&eid=24

2020 has delayed the commencement of this measure to 1 December 2020 and has extended this measure to Northern Ireland.

Under the current law, HMRC is an unsecured creditor. In order to ensure that fewer of those taxes paid by employees and customers but temporarily held in the hand of a business will go to other creditors when the business goes into insolvency, the previous UK government announced that it will make HMRC a secondary preferential creditor in respect of these taxes. Therefore, the reform will only affect those taxes collected and held by businesses on behalf of other taxpayers, including VAT, PAYE Income Tax, employee National Insurance contributions, student loan deductions and construction industry scheme deductions. For the same reason, HMRC will not be a secondary preferential creditor in respect of taxes owed by the business itself, such as corporation tax and employer National Insurance contributions.

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