Budget: 27 October 2021

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On 27 October 2021, Chancellor Rishi Sunak gave his second Budget speech of the year. As significant tax changes had been announced in the March Budget, this was widely expected to be more about spending than taxation. Many of these spending plans had been announced before the Budget, earning the Chancellor a rebuke from the Deputy Speaker.

Despite the huge costs of Covid, the Chancellor announced a 3.8% annual increases in spending for all government departments. He also said that he would start reducing taxes by the end of the current Parliament, due in 2024.

The Chancellor announced a new Charter of Budget Responsibility. Its main provision is that the government only borrows for infrastructure spending, and not for day-to-day spending.

The Budget also included a mass of economic data and statements of government policy. The general view is that the economy has recovered much better than expected. The better performance gave the Chancellor £35 billion of "headroom". He decided to spend about £15 billion of it, and use the other £20 billion to help get the public finances in order.

Yet there were still some significant tax announcements.

Personal tax

Basis period reform is to take place from 6 April 2024. This is a radical change that will see the end of traditional basis periods for income tax. It will also end overlap relief. The new system is called "tax year basis"

At present, the self-employed pay tax in arrears under what is called the current year basis. The new provisions will see the self-employed pay tax on the profits earned during the tax year, regardless of the accounting date. It will bring the self-employed into line with employees, landlords and investors.

The change starts to take effect in the tax year from 6 April 2023 to 5 April 2024. In this year, tax will be charged on the profits under the old basis, plus profits earned from the day after the accounting date to 5 April 2024 minus overlap relief. This means that taxpayers with accounting dates early in the tax year could find themselves with very large tax bills for that year. The government is considering allowing that additional tax to be paid over five years. The tax year basis starts from 6 April 2024.

These transitional arrangements differ markedly from 1994 when the income tax system moved from previous year basis to current year basis. Then, the government dealt with taxing two years in one year by taking the average of the two years. This allowed many tax planning opportunities which the government is clearly not prepared to allow again.

The HMRC press release states that the change takes place from 2023 with 2022/23 as the transition year. It is assumed that the Budget book has given the correct dates.

Income tax rates are unchanged from what has been previously announced. The 0% starting tax rate keeps its limit of £5,000. The individual savings account (ISA) limit remains at £20,000, and the junior ISA limit remains at £9,000.

It is reaffirmed that sole traders and landlords have an extra year to prepare for Making Tax Digital. This will now be introduced from 6 April 2024, except for general partnerships from 6 April 2025.

Capital gains tax rates are unchanged. The 30-day time limit for reporting disposals of UK property is extended to 60 days. This change applies from 27 October 2021. The 30-day limit has proved to be too short in practice.

National insurance rates for 2022/23 will be increased by 3.1%, apart from the upper earnings limit for class 1 national insurance paid by employees and their employers, and the class 2 and 3 rates. These are all unchanged.

The normal minimum **pension age** is to rise from 55 to 57 from 6 April 2028, as previously announced. This is the minimum age at which a pension scheme member may take benefits. The change does not affect police or other uniformed bodies. It does not change provisions allowing people to take benefits because of ill health. The age increased from 50 to 55 in 2010. The increase to 57 is in line with the increase in state pension age from 66 to 67 in 2028.

Emergency powers are to be given to ministers to allow income tax and national insurance reliefs to deal with disasters and national emergencies.

Business tax

The **annual investment allowance (AIA)** is a capital allowance that allows a business to deduct 100% of expenditure on most plant and machinery from its taxable profits. Since its introduction in 2008, it has applied at seven different limits ranging from £25,000 to £1 million. The limit was due to revert from £1 million to £200,000 on 1 January 2021. In March, this change was deferred by one year to 1 January 2022. It has now been deferred again to March 2023. This means that the annual investment allowance is £1 million for all periods from 1 January 2019 to 31 March 2023.

A company may claim 130% of expenditure under the new super-deduction for expenditure between 1 April 2021 and 31 March 2023. So AIA is only claimed when the super-deduction cannot be. As the super-deduction has no monetary limit, this is only likely to apply when the super-deduction cannot be claimed. This applies to expenditure by businesses that are not companies, such as partnerships and sole traders, and to company expenditure outside the two-year window for super-deduction.

Cross-border loss relief is abolished from 27 October 2021. This means that the limited right to claim UK tax relief for overseas losses is the same for EU countries as for non-EU countries.

Eight **Freeports** have been chosen from 18 applications in England. Freeports may have a "tax area" within them which qualifies for additional tax reliefs. These include structures and building allowance at 10% rather than 3%; 36 months exemption from some employer's national insurance; and 100% first year allowances on plant and machinery. Three Freeports have had tax areas agreed. They are in Humber, Teesside and Thames. They begin initial operations in November 2021.

Business rates are retained despite calls for them to be replaced, particularly for shops which are disadvantaged compared to online retailers. Many shops now pay no rates because of many reliefs already announced. Several changes were announced.

First, premises will be revalued every three years rather then five years.

Second, from April 2023, businesses will have a one-year exemption for any improvements they make. So if a hotel adds bedrooms, or a shop expands its premises, it will have a year before it pays the higher rate. Third, there will be a new green investment relief such as when a business premises installs solar panels. There are some further changes such as providing transitional relief when a revaluation leads to a large increase.

Business rates are calculated by multiplying the rateable value by a "multiplier". This is a lower figure where the rateable value is below £51,000. From 1 April 2020, the multiplier in England (outside City of London) has been 0.512, or 0.499 for small businesses (if they pay rates at all). These rates were not increased for 2021/22, and are again not increased for a further year to April 2023.

The hospitality sector, which was given a one-year holiday from business rates, will have a 50% reduction in rates for another year, 2022/23, to a maximum amount of £110,000.

Banks pay corporation tax at 8 percentage points above the corporation tax rate. As the current corporation tax rate is 19%, banks pay 27%. This is a pay back for banks being bailed out after the banking crisis of 2008/09.

From April 2023, the bank premium reduces to 3 percentage points when the corporation tax rises to 25%. So banks will see a small increase in corporation tax to 28%. The reduction in premium is to ensure that UK banks remain internationally competitive.

Many small banks, known as "challenger banks", have been set up to compete with the established banks. These banks are excluded from the premium. This Budget announced that the limit for these banks is increased to £100 million a year.

A new framework is being introduced for **asset-holding companies (AHCs)**. These are widely used by investment companies.

Insurance companies will be allowed to spread the additional tax incurred by adopting international accounting standard IFRS 17.

A new provision will allow stamp duty and stamp duty reserve tax to be amended in respect of **securitisations and insurance-linked securities.** This will allow the government to accommodate these new markets.

There is a collection of eight reliefs for **creative industries:** animation, children's television, films, high-end television, museums and galleries, orchestras, theatre, and video games. These can provide 25% relief from corporation tax if appropriate conditions are met. Some of these reliefs are time-limited.

The museums and galleries relief is extended by a further two years to 2024 as they have been obliged to close for much of the last year.

The reliefs for theatres and museums is currently 25% for touring productions and 20% for non-touring. These increase to 50% and 45% for one year from 1 April 2023.

Orchestra relief increases from 25% to 50% from 27 October 2021, reducing to 35% from 1 April 2023, and returning to 25% from 1 April 2024. For these purposes an orchestra is defined as a musical ensemble of at least 12 players at least half of whom are not electronically amplified. This is wide enough to include brass bands and dance bands.

Merchant shipping companies may elect voluntarily to pay **tonnage tax** based on the size of their fleet. This is an alternative to paying corporation tax on shipping activities. It was a condition that the ship had to fly the flag of an EU country. That is now changed. A ship may only come within tonnage tax if it flies the UK flag of the red ensign. The lock-in period is reduced from ten years to eight. Some other changes are made.

Indirect tax

Alcoholic liquor duty is thoroughly revised. This is an excise duty charged on drink that contains more than 1.2% alcohol by volume. It is charged as beer duty, cider/perry duty, wine duty and spirits duty. These are further subdivided. The tax dates from 1643 and contains many historic anomalies. The duty is charged at a fixed amount per hectolitre (100 litres). VAT at 20% is then charged on the total.

The objectives are to simplify and rationalise this tax. The 15 current rates are replaced by six. Duty will be related to the alcoholic strength of the drink rather than its nature. The break points will be 1.2%, 3.5%, 8.5% and 22%. Above 8.5% all drinks of the same strength will pay the same rate of duty, regardless of their nature.

Some drinks will become more expensive. These include strong red wines, fortified wines like sherry, and white cider. Most other drinks will reduce in price. Beer is expected to reduce by 3p a pint.

Sparkling wines will be taxed lower, at the same rate as still wines of the same strength. The reliefs for craft beers will extended to craft ciders. Duty on fruit ciders is reduced.

A new "draught relief" is introduced to reduce rates on draught beer by 5% if sold from a barrel containing at least 40 litres. The standard size of a UK beer barrel is 11 gallons which is 50.007 litres. The duty rates for beer, cider, wine and spirits are frozen for a further year.

Tobacco duties increase by inflation plus 6 percentage points from 27 October 2021.

VAT rates are unchanged. There are some specific changes in rules. An interim second-hand margin scheme is to be introduced in Northern Ireland for used motor vehicles supplied from Great Britain. The VAT exemption for dental prostheses imports is extended to include treatment by dental technicians.

The **HGV Road User Levy** is suspended for a further 12 months from August 2022.

Vehicle excise duty rates (road tax) for heavy goods vehicles are not increased for 2022/23. Rates for cars, vans and other vehicles are increased in line with inflation.

Research and development attracts generous tax relief. A business can claim up to 230% of the expenditure against taxable profits. For companies not yet making profits, this allowance can be exchanged for a cash payment of 13%.

The scope of research and development is widened to include data and cloud computing costs.

Despite these generous reliefs, much of this research and development is not benefiting the UK. So tax reliefs will "refocus the reliefs towards innovation in the UK". There will also be changes to prevent abuse of the relief. Further details will be published later.

Air passenger duty (APD) is reformed so that duty on internal UK flights is halved.
The new APD for domestic flights is £6.50.

A new long haul charge is added. At present there are two bands for journeys below 2,000 miles and those above. A third band will be introduced of more than 5,500 miles. Rates for the three bands will be £13, £87 and £91 for economy passengers.

A new **residential property developer tax** is introduced from April 2022, as previously announced. The tax is charged on profits that companies and corporate groups derive from UK residential property development. The tax is 4% on profits Exceeding £25 million a year. The sums raised will be applied to building safety remediation, such as removing fire-risk cladding.

Hydrocarbon oil duty is not increased for the twelfth consecutive year. Suppose petrol or diesel costs £1.44 a litre. One sixth of that amount, 24p, is VAT. Another 58p is duty (57.95p to be precise). That means that the tax is 82p a litre. The petrol itself only costs 62p.

This duty and other taxes related to road fuel (such as income tax charges for company cars) yield £30 billion a year. The government has yet to say how this loss of revenue will be recovered when we are all driving electric cars.

HMRC is being provided with an additional £292 million over three years to tackle **tax evasion.** A further £55 million is allocated to tackle abuse of the coronavirus schemes. HMRC also receives additional funding to make the tax computer system more comprehensive and robust.

No Budget is now complete without **anti-avoidance measures.** This Budget reaffirms provisions already announced that give HMRC more powers over promoters of avoidance schemes. These include freezing their assets and even closing them down.

Non-tax matters

There were some significant announcements in non-tax matters.

The **national living wage** rate increases by 6.6% to £9.50 an hour. This is paid to all workers aged 23 and above. Other national minimum wage rates are:

- 21 to 22 years old: from £8.36 to £9.18
- 18 to 20 years old: from £6.56 to £6.83
- 16 to 17 years old: from £4.62 to £4.81
- apprentice rate: from £4.30 to £4.81
- accommodation offset: from £8.36 a day to £8.70. (The Budget statement says this rate is "per hour", but this is assumed to be a mistake.)

The withdrawal rate for **universal credit** is to reduce from 63% to 55%. This change is to be introduced no later than 1 December 2021. The work allowance is also increased.

Universal credit is a means-tested social security benefit paid to those with little or no income. The government sets out maximum awards for claimants to receive. There are certain allowances and disregards. If a person's income from all sources does not exceed this figure, he or she receives the full amount of benefit. If their income does exceed this amount, the benefit is reduced by the withdrawal rate. In other words, for every extra £1 they earn, they lose 63p in benefit.

This can lead to very high marginal tax rates if the withdrawal is viewed as a tax (as the Chancellor did in his speech). If a person on average income or even national minimum wage earns an extra £100, he may pay another £20 income tax and £12 national insurance, leaving him or her with a net increase of £68. If the worker is receiving universal credit, 63% of that £68 (which is £42.84) is reduced from their universal credit. The net benefit of a £100 pay rise to a claimant is £25.16. In effect they have paid tax at 75%.

When universal credit was first proposed, the withdrawal rate was to be 55%. It was introduced at 65% and then reduced to 63%. In our example, 55% of the additional £68 is £37.40. So the claimant would receive a net benefit of £30.60. The effective tax rate has reduced from 75% to around 70%. A claimant keeps an extra 8p for each additional £1 earned.

The work allowance is also increased by £500 a year. These two changes mean that all universal credit claimants will receive at least another £1,000 a year, which just happens to be the amount withdrawn when the coronavirus supplement was withdrawn.

These changes help universal credit claimants who have income. Neither change helps claimants who have no income.

The Budget also sets a new date of March 2025 for completing the migration from old means-tested benefits to universal credit. The original completion date was 2017 but has repeatedly been put back.

The **recovery loan scheme** is extended to 30 June 2022 to ensure that lenders continue to support small and medium-sized businesses.

Spending commitments include £5.9 billion of capital expenditure for the National Health Service, although this includes money already announced. There are also large commitments for education, justice, defence, housing, local government, energy, employment, environment and transport. Many spending plans are given in detail such as better roadside toilets for lorry drivers and a new Beatles centre in Liverpool.

A new **Multiply** programme aims to improve numeracy skills.

Foreign aid was reduced from 0.7% to 0.5%. The Chancellor confirmed that it will return to 0.7% by 2024.