



June 2010 budget: implications for employment, pensions and benefits

The budget contained few surprises from an employment, pensions and benefits perspective.

The increase in capital gains tax is less than had been feared and seems to have been influenced by a desire to maximise the amount of tax received while still encouraging capital investment.

Some had been concerned that bank payroll tax would be re-introduced. This did not happen but the government has announced that it will consult on a remuneration disclosure scheme.

This briefing gives a summary of the main points of interest.

Capital gains tax

From 23 June 2010, capital gains tax (CGT) will increase to 28 per cent for gains above the upper limit of the basic income tax rate band (£37,400). The link to the income tax rate reverts to the way CGT operated before April 2008. The rate will remain at 18 per cent where an individual's total income and taxable gains are less than the upper limit of the basic income tax rate band. If an individual's income is less than the upper limit of the basic rate band and his taxable gain would take him above the upper limit, that part of the taxable gain up to the upper limit will be taxed at 18 per cent and the balance above the upper limit will be taxed at 28 per cent. Trustees and personal representatives of deceased persons will be subject to CGT at 28 per cent.

Gains that arose before 23 June 2010 will be subject to CGT at 18 per cent and will not be taken into account when determining the rate of CGT applicable to gains arising on or after 23 June 2010.

The annual exempt amount remains £10,100 for 2010-11 and will continue to rise with inflation. In calculating the amount of gain that is subject to CGT (and so taken into account in determining the individual's total taxable gains and income), the annual exempt amount must first be deducted.

For example, assume an individual has taxable income of £20,000 and makes a gain of £15,100. The annual exempt amount is set against that gain, leaving £5,000 taxable. That amount must be added to the individual's taxable

income, giving a total of £25,000 – so the gain of £5,000 is subject to CGT at 18 per cent. If the individual's taxable income was £40,000, the total income and taxable gains would be £45,000 – so the gain of £5,000 would be subject to CGT at 28 per cent.

The government has also announced that the lifetime-gains limit for entrepreneurs' relief will be increased from £2m to £5m. Qualifying gains will be taxed at a rate of 10 per cent.

Despite the increase in the rate of CGT, the benefits of using share incentive schemes approved by HM Revenue & Customs (HMRC) remain (ie save as you earn, company share option plans, share incentive plans and enterprise management incentives (EMI):

- for lower rate taxpayers the position is unchanged and CGT will be charged at 18 per cent on gains above the annual exempt amount;
- higher rate taxpayers are also able to take advantage of the annual exempt amount and can arrange to sell shares over a number of years to use the annual exempt amount to maximum advantage, as well as transferring shares to their spouse or civil partner;
- for companies and employees, no national insurance contributions (NICs) are due on gains made under plans that are approved by HMRC (provided options are exercised within the relevant legislation). The relative benefit of HMRC-approved plans is reinforced by the previously announced 1 per cent increase in national insurance contributions (see below).

Personal allowances and national insurance thresholds

From 6 April 2011, the personal allowance for individuals aged under 65 will increase to £7,475 (currently £6,475). However, the basic rate limit will be reduced so that higher rate taxpayers (ie 40 per cent) do not benefit from this increase.

The threshold for employer's NICs will be increased by £21 per week above indexation. In addition, the upper earnings or profits limit will be reduced to align it with the higher rate threshold.

There is no change to the previously announced 1 per cent rise in NIC rates, all of which take effect on 6 April 2011. The revised rates are:

- employee's NICs on earnings between the primary threshold and the upper earnings limit – increased from 11 per cent to 12 per cent;
- employee's uncapped NICs on earnings above the upper earnings limit – increased from 1 per cent to 2 per cent; and
- employer's NICs – increased from 12.8 per cent to 13.8 per cent.

Enterprise management incentives

As previously announced, the requirement that a company granting EMI options must operate 'wholly or mainly' in the UK will be amended. Companies will now be able to operate an EMI scheme if they have a 'permanent establishment' in the UK. This amendment is needed to ensure EMI schemes comply with EU state aid guidelines.

Bank remuneration

To no one's surprise, banks will be hit with a bank levy. The joint statement by the UK, French and German governments states that the levy is proposed in light of the G20 agreement that 'the financial sector should make a fair and substantial contribution towards paying for any burdens associated with government interventions to repair the banking system or fund resolution in a financial crisis'.

The UK government has announced a levy on bank capital, rather than a return to bank payroll tax.

However, it also intends to consult on a remuneration disclosure scheme and to consider, with international partners, the costs and benefits of a financial activities tax on banks' profits and remuneration. At first sight, this focus on disclosure is slightly surprising given the disclosure regime (applicable to those earning £500,000 and above) planned in the draft regulations recently published under the Financial Services Act 2010.

In addition, the Financial Services Authority has been asked, as part of its review of its remuneration code, to:

- consider imposing more stringent requirements on the deferral and award of variable pay;
- examine mechanisms for strengthening the link between performance and remuneration to ensure that incentives are aligned with a firm's long-term performance; and
- consider how to vary capital requirements to offset risk in remuneration practices.

Restriction on pensions tax relief

The government has confirmed that it intends to restrict pensions tax relief but is considering doing this by lowering the annual allowance instead of introducing a relief charge.

The Finance Act 2010 would have introduced a 'high income excess relief charge' from 6 April 2011, which would have tapered away tax relief for individuals with a gross income of £150,000 or more. The government's provisional analysis suggests that the annual allowance may be lowered to somewhere between £30,000 and £40,000, but this will be decided only after consultation on the design of the new regime. Legislation to repeal the relevant parts of the Finance Act 2010 will be introduced before parliament's summer recess.

The government will not change the anti-forestalling regime, previously introduced to stop individuals accelerating pension contributions before the changes expected in April 2011.

Purchase of annuities for people aged over 75

The government intends to 'end the existing rules that create an effective obligation to purchase an annuity by age 75 from April 2011' and will release more detail on the changes in a consultation to be launched shortly.

Legislation for transitional arrangements is expected in the Finance Bill 2010 for those yet to secure an income who will reach 75 in the meantime.

Phasing out default retirement age

The government will consult on how quickly it will phase out the default retirement age (currently 65) from April 2011.

Provided the employer follows the correct procedures, it is possible to require an employee to retire at 65. Once the default retirement age is phased out, employers will have to consider age discrimination issues when terminating an employee's contract of employment.

Review of employment laws

The budget report states that each government department has been instructed to start a review of the employment laws for which it is responsible to ensure maximum flexibility, protect fairness and promote competition. Any changes to existing law will have to be made under the government's 'one-in-one-out' system for new regulation.

Proposed consultations

The government has confirmed that, as announced by the former Labour government, it intends to consult on the following areas:

- geared growth and employment-related securities – to develop proposals to ensure that employment income from employment-related securities that are used in geared growth arrangements is subject to income tax and national insurance contributions; and
- taxation of non-domiciled individuals – to consider whether changes should be made to the existing rules to ensure non-domiciled individuals 'make a fair contribution to reducing the deficit'.

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