

Emergency Budget Analysis

22 June 2010



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The full Budget document is available at http://www.hm-treasury.gov.uk/junebudget_documents.htm
Numbers in brackets [xx] refer to paragraph numbers in the Budget document. Analysis is given in italics.

1. VAT RISE TO HIT RETAILERS

[1.44, 2.90] The standard rate of VAT will increase from 17.5% to 20% from 4 January 2011. The budget makes no changes to the VAT zero-rating for household essentials, nor to the reduced rate of VAT that applies to certain goods and services. The increase is expected to raise £13.5bn a year by 2014/15.

The higher rate of Insurance Premium Tax will increase on 4 January 2011, from 17.5% to 20%, while the standard rate will increase from 5% to 6%. This will raise £0.5bn a year by 2014-15.

A rise in VAT was expected in the budget and will have a natural impact on consumers' willingness to purchase goods on which VAT is charged. This is not good news for retailers, and by extension landlords of retail property. With 12.6% of shops already standing empty, we could see more damage done to the high street.

However, on a positive note we are pleased to see the rise delayed until 4 January as this provides a reasonable window in which consumers can purchase big ticket items; it will provide retailers with enough time to get their houses in order ahead of the rise and, perhaps more importantly, it reduces the chances of an immediate slump in consumer confidence.

House builders will welcome the fact that they have avoided a VAT rise on new build properties, despite the Lib Dem manifesto suggesting it could have been a possibility.

It is disappointing that the opportunity was not taken to use VAT concessions to promote energy efficiency.

2. CAPITAL GAINS TAX RISE FOR HIGHER-RATE TAX PAYERS

[1.96] Capital gains tax will increase from 18% to 28% for higher rate tax payers from 23 June 2010. Basic rate taxpayers will continue to pay an 18% rate on their gains. The 10% CGT rate for entrepreneurial business activities will be extended from the first £2m to the first £5m of qualifying gains made over a lifetime. The annual exempt amount for CGT will remain at £10,100 for 2010-11.

The lower than expected increase in the CGT rate to 28% has allowed the government to avoid the need for complex taper or indexation relief provisions. This shows a welcome desire to keep things simple, although many will not be happy about the increase. Particularly, buy-to-let investors who have propped up the housing market over the last 20 years will suffer and this could hit the future supply of rented housing.

3. STAMP DUTY LAND TAX

[2.116] The Government will examine whether changes to the rules on stamp duty land tax on high value property transactions are needed to prevent avoidance in this area.

[1.111] Government will also review the stamp duty land tax relief for first time buyers taking into account its "impact on affordability and value for money".

[2.125] An additional 5% rate of stamp duty land tax will take effect for residential transactions worth over £1m from 6 April 2011 (March 2010 Budget).

[2.166] Legislation will be in the Finance Bill in the autumn to deal with claims to recover overpaid stamp duty land tax and petroleum revenue tax (March 2010 Budget).

The examination of SDLT avoidance follows up on a Liberal Democrat pledge, and is understood to relate to commercial property transactions as well as residential ones. Note that no formal consultation has been announced – but we will of course hope to be given the opportunity to discuss possible options and their likely practical implications for business with officials.

4. CORPORATION TAX REDUCED

[2.68, 2.69] The main rate of Corporation Tax will be reduced from 28% to 24% over four years. A 1% reduction will be implemented from 1 April 2011. Legislation will be in the Finance Bill introduced after the Budget, with further reductions in subsequent Finance Bills. The small profits rate of Corporation Tax will be reduced from 21% to 20% with effect from 1 April 2011, rather than rising to 22% as inherited by the Government.

[1.74] The Government will publish a Green Paper on business finance before the summer recess considering the range of finance options for businesses of different sizes including bank lending, equity and corporate debt. It will invite views from business, investors and lenders on priorities and approaches to enhancing the access of credit-worthy businesses to appropriate sources of finance.

The phased reduction in the main rate of corporation tax should allow most businesses to retain additional profits for future reinvestment, and is therefore a positive development. However, REITs will not benefit from this headline grabbing measure and the reduction in the rates of capital allowances (see below) means that they may emerge as net losers from these related measures.

It has not been made clear how lower rates of corporation tax will be paid for; a raid on tax relief for financing costs – trailed by the Tories last year – may yet re-emerge as a threat, but not before a Green Paper and due consultation.

5. CAPITAL ALLOWANCES REDUCED

[2.75, 2.76] From April 2012, the rate of capital allowances on the general pool of plant and machinery will be reduced from 20% to 18%, and the rate of allowance on the special rate pool of plant and machinery will be reduced from 10% to 8%. The Annual Investment Allowance will be reduced from £100,000 to £25,000 from April 2012.

The reduction in the rates of capital allowances is not welcome, but is not unexpected. Fortunately, the Government has responded to our argument that this is the wrong point in the cycle to reduce incentives to invest, and the reduction (which is relatively modest) will only take effect from April 2012. We hope to discuss the impact on REITs and their mandatory distribution obligation with officials over the coming weeks. No announcement has been made about ECAs, so the assumption is that they remain unchanged for the moment.

6. BUSINESS RATES

[2.82] Legislation will be introduced to cancel backdated business rates bills eligible for the 8-year schedule of payments scheme, including for businesses in ports, for newly assessed properties that were split from a larger rateable property.

[2.150] The level of small business rate relief in England will be temporarily increased for one year, from 1 October 2010, giving full relief for eligible businesses occupying premises with a rateable value of up to £6,000 and tapering relief to £12,000. (March 2010 Budget)

News on relief from empty property rates was absent from the Emergency Budget.

Good news for ports, but nothing for those struggling to cope with empty property rates, despite pre-election sympathy from leading Tories and Lib Dems. We would expect the temporary relief for low-value empty properties at least to be revisited in the Pre-Budget Report.

7. REITS TO ISSUE STOCK DIVIDENDS

[2.156] Changes will be made in the Finance Bill introduced in the autumn to allow UK-REITs to issue optional stock dividends as part of their property income distribution requirement.

Enabling REITs to issue stock dividends allows them to maximise the cash retained in the business and therefore encourages the long term growth of REITs and the recapitalisation of the sector. We welcome the Government's decision to implement this revenue neutral but business-friendly measure, and believe that it will enhance the competitiveness of the UK's REIT regime and help promote development, regeneration and employment.

8. PENSIONS INCREASE

[1.107, 1.108] Government will increase the basic State Pension by a "triple guarantee" of earnings, prices or 2.5%, whichever is highest, from April 2011. CPI will be used as the measure of prices, as for other benefits and tax credits. It will protect other benefits for older people, such as Winter Fuel Payments.

Linking pensions to earnings may be a good thing for the property industry as an investment asset class, and perhaps particularly for large-scale investment in housing, which has not had any other encouragement from this Budget, given the relationship between property income and earnings.

9. REGIONAL DEVELOPMENT AGENCIES ABOLISHED

[1.89] Regional Development Agencies will be abolished through the Public Bodies Bill to be replaced by Local Enterprise Partnerships where demanded by business and locally-elected leaders. A White Paper in the summer will consider options for business rate and council tax incentives that would allow local authorities to reinvest the benefits of growth into local communities, and promote the role for a simplified planning consents process in specific areas where there is need for business growth.

The scrapping of RDAs has been well flagged. With regeneration activity around the country at a standstill what really matters now is what the Government plans to do to re-energise development that can stimulate the economic growth that the country needs. Giving local authorities rate and council tax incentives to promote development will help but much more innovative thinking is needed. The new Enterprise Partnerships will need to achieve greater coordination of large capital spending programmes to ensure their regenerative benefits are fully utilised and promote a more proactive approach by councils and public bodies to facilitating and, where feasible, 'de-risking' regeneration schemes.

At a time in which few projects stack up in conventional development appraisals, tax increment financing (TIF) represents one approach that the Government should wholeheartedly approve. TIF allows the upfront cost of infrastructure to be paid for out of the rate income that new developments generate.

10. HOUSING BENEFIT REFORM

[1.102, 2.50-7] The Government will introduce a package of reforms to Housing Benefit from April 2011 onwards. This includes changing the percentile of market rents used to calculate Local Housing Allowance rates, and uprating these rates by CPI from 2013-14, capping the maximum Local Housing Allowance payable for each property size, time-limiting the receipt of full Housing Benefit for claimants who can be expected to look for work, and restricting Housing Benefit for working age claimants in the social rented sector who are occupying a larger property than their household size warrants.

From the headlines ahead of the Budget we knew that welfare was likely to be a focus for cost reductions by Government. This afternoon's announcement shows the scale of the Government's ambition to reduce this cost – the local rents for Local Housing Allowance being sliced back considerably to the thirtieth percentile for the area – rather than the LHA rates being equivalent to the market rents for PRS properties as is the case at the moment.

This is a massive reduction and unless landlords reduce their rents, will result in a shortfall that LHA tenants will have to make up themselves.

One issue that has not been raised, and is one we believe will lead to cost savings for the Government, is the introduction of choice as to whether LHA is paid to the landlord. Currently the practice is to pay it to the tenant, which leads to cases of rent not being paid and leakage.

11. ENERGY TAX FRAMEWORK

[1.77] Government will assess how the energy tax framework can provide the right incentives for investment, alongside wider market reforms. In the autumn, the Government will publish proposals to reform the climate change levy in order to provide more certainty and support to the carbon price. Subject to consultation, the Government intends to bring forward relevant legislation in Finance Bill 2011

It remains to be seen how exactly a reformed Climate Change Levy would be used to shore up the price of carbon, which has been subject to instability particularly at the EU Emissions Trading System level. Though we are generally supportive of fiscal instruments which are directed toward

the end user of energy, the Government will need to take great care not to artificially stimulate the price of carbon to unsustainable levels in the advent of the first auction of carbon allowances under the CRCEES in 2013.

12. GREEN INVESTMENT BANK

[1.78] Government will put forward detailed proposals on the creation of a Green Investment Bank, following the Spending Review, to help the UK meet the low-carbon investment challenge.

All political parties agreed on the introduction of a Green Investment Bank in their manifestoes but differed on its scope. The BPF believes that the most effective function of a Green Investment Bank would be to help to finance the transition from an electrical grid which is dependent upon fossil fuels to one which relies on greener sources of energy in greater proportions. It should also be used to finance “exemplar” projects to establish whether outstanding energy efficiency commands a market premium. However, it remains to be seen from where the seed funding for such a bank would be found, particularly against the backdrop of today’s austerity Budget.

13. GREEN DEAL FOR HOUSEHOLDERS

[1.79] - A “Green Deal” for households will be launched through legislation in the Energy Security and Green Economy Bill, to help individuals invest in home energy efficiency improvements that can pay for themselves from the savings in energy bills. The Government will also continue to progress work on creating green financial products to provide individuals with opportunities to invest in the infrastructure necessary to support the green economy.

14. OTHER SUSTAINABILITY MEASURES

[1.121] – Government will explore the creation of a fair fuel stabiliser. The Chancellor will ask the Office for Budget Responsibility to undertake an assessment over the summer of the effect of oil price fluctuations on the public finances. Informed by this assessment, the Government will examine options for the design of a fair fuel stabilizer.

[2.127-8, 2.130, 2.132, 2.137] The Budget also confirms some previous announcements that Government will: include nitrous oxide gases in the EU Emissions Trading System from 2011; reduce the discount from the climate change levy for industries participating in a climate change agreement from 80 to 65% in April 2011, and increase the climate change levy in line with inflation; increase the standard rate of landfill tax by £8 per tonne on 1 April 2011 until at least 2014, and introduce a floor so that that the rate will not fall below £80 per tonne until at least 2020; increase aggregates levy to £2.10 per tonne in 2011; introduce an enhanced capital allowance for zero-carbon goods vehicles from April 2010.

15. INFRASTRUCTURE

[1.83] The Budget confirms the establishment of Infrastructure UK to lead work within HM Treasury to enable greater private sector investment in infrastructure, and improve the Government’s long-

term planning and delivery. In the autumn, the Government will publish a national infrastructure plan that will set out goals for UK infrastructure.

16. PRIVATE RENTED SECTOR

This did not feature in the budget, although we understand that the Government will publish responses to the HM Treasury consultation later in the summer, and we will continue to consider all the issues raised.

17. DEREGULATION

[1.65] Government has announced that it will reduce regulatory costs by introducing a one-in-one-out system for new regulations. The Department for Business, Innovation and Skills will publish more detail in July 2010. All regulation scheduled for introduction over the coming year will be scrutinized by a Reducing Regulation Committee. Regulations will cease to be law after seven years unless Parliament has confirmed they are still necessary or they were set to have a longer timeframe. All employment laws will be reviewed by their relevant departments.