



TAX
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TAXline

TAXline supplement for members of the Tax Faculty, edited by Jane Moore

December 2009

PRE-BUDGET REPORT 2009

The Tax Faculty's summary of
the Pre-Budget Report, produced
by the Tax Faculty technical team.



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PRE-BUDGET REPORT 2009

The Tax Faculty's summary of the Pre-Budget Report 2009 has been produced by the Tax Faculty technical team.

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The Tax Faculty produces a range of technical information. All items published since January 2000 and selected items prior to that date, can be viewed on the website at www.icaew.com/taxfac where the information can be found under the heading 'Faculty Publications'.

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Editor: Jane Moore

PRE-BUDGET REPORT 2009



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1. OVERVIEW

We said in our Budget 2009 overview that if a week is a long time in politics, then the five months since the 2008 Pre-Budget Report (PBR) must have been the equivalent of a political lifetime, with major revisions downwards of growth and revenue forecasts. A further seven and a half months on, the outlook appears to have stabilised and there are some tentative signs that the worst of the recession may be past. However, the fallout will continue for years to come.

Last year the 2008 PBR growth estimate for 2009 was that GDP would be between -0.75% and -1.25%. The 2009 Budget revised this downwards to -3.5%. However, even that was too optimistic: the latest forecast in the 2009 PBR is that growth (or more properly shrinkage) in 2009 will now be -4.75%, apparently the largest reduction in GDP in 50 years.

The forecast growth for 2010 remains at +1.25%, the same as predicted in the 2009 Budget. It seems likely that growth will revert to being positive in the final quarter of 2009 and then into 2010, but recovery looks like being a slow business and the growth estimates still appear challenging.

The pressing need in this PBR was for the Chancellor to deliver a credible plan for addressing the UK's budget deficit – which we discuss in more detail below – without in the process killing any nascent recovery. Given that we are less than six months from a general election, this was always likely to be a highly political PBR with any painful measures kept back for the second half of 2010 and beyond. That appears to be what happened: the PBR 'Red Book' shows that in 2010/11 the changes announced will **increase** government borrowing by a further £1.2bn before a fiscal tightening from 2011/12 onwards.

Turning to income tax, the Chancellor resisted the temptation, widely trailed, that he would lower the £150,000 threshold at which the new 50% income tax would be payable. However, he said that in addition to the previously announced 0.5% rise in National Insurance (NIC) rates due to come into force from April 2011, the NIC rates would rise by a further 0.5% from that date. More changes are proposed to the restrictions on tax relief on pension

contributions for higher earners that were announced in the 2009 Budget. The provisions again appear highly complicated but in a change to the 2009 Budget proposals, employer pension contributions will now be taken into account in arriving at the £150,000 earnings limit.

The Government has introduced a one-off tax on bank bonuses. This will take the form of a payroll tax of 50% on the element of any bonus to be paid to employees which exceeds £25,000. On the face of it this appears a punitive measure, but one-off measures do little to provide stability and certainty and also reduce the UK's competitiveness. Further, given that considerable efforts will be put in to try and avoid the tax, the measure is surrounded by extensive anti-avoidance measures. It is difficult to escape the view that there must be better ways to address bank remuneration policy so that it is geared more closely to long-term earnings and any attendant risks.

Turning to small businesses, the message was much more positive than might have been expected in the circumstances. The proposed increase in the small companies' rate of corporation tax from 21% to 22%, due to take effect from April 2010, is deferred for a year. Further, the Chancellor announced an indefinite extension of the 'time to pay' arrangements for businesses struggling to meet their tax liabilities.

The drive to counter tax avoidance continues. A raft of targeted new measures were introduced and a further strengthening of the tax avoidance scheme disclosure rules.

On VAT, the Chancellor confirmed that the standard rate will revert to 17.5% on 1 January 2010. Retailers

will probably be disappointed with this but given the need to reassure the markets that the Government intends to reduce the budget deficit, a deferral of the start date would probably have sent out the wrong message.

That brings us neatly to the question of the UK's finances. In our 2009 Budget commentary, we mentioned the risk that the UK's credit rating would be damaged, the cost of government borrowing would rise and the risk of default would become much more likely. Since then, the concerns of commentators have increased and it was important that the Chancellor sent out a clear message that the UK has a credible plan to address the debt mountain.

In the event, the Chancellor set out a position that differed little from his assessment in the 2009 Budget, which on the face of it appeared slightly strange given that his prediction for 2009/10 GDP was significantly worse than he anticipated in April 2009. He stated that net borrowing for 2009/10 is now projected to rise to £178bn, only (if that's the right word!) £3bn more than the Budget 2009 estimate and rather less than the £200bn-plus deficit predicted by many commentators. Borrowing as a percentage of GDP is now projected to rise to over 70% in 2011/12 and to continue to rise to 77.7% in 2014/15, the end of the current projection period. Again, this was only slightly worse than the 2009 Budget estimate of 76.2%, but it is nevertheless far above the self-imposed 40% borrowing limit the Government set shortly after it took office in 1997 and it is also predicated on growth returning to 3.25% from 2011/12.

Whoever is in power after the 2010 election, they will have to take some tough decisions to avoid a financial crisis in UK plc. The tax rises announced so far will do little to plug the gap: there will have to be broadly-based tax increases (such as the increases in NIC) in order to make a major difference to the amount the Government spends and what it receives.

The Chancellor played his hand well but it is difficult to avoid the conclusion that the UK is stuck between a rock and a hard place

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In summary, with an election now less than six months away this was a highly political PBR. The state of the UK's finances remains a serious worry and clear and decisive action will be needed to get it under control. However, the Chancellor recognised the danger that tough medicine dispensed now could stifle the UK economy just as we appear to be pulling out of recession and hinder any attempts to get the UK's finances back into the black. The Chancellor played his hand well but it is difficult to avoid the conclusion that the UK is stuck between a rock and a hard place

2. RATES AND ALLOWANCES

The main rates and allowances for 2010/11 are summarised in the table on pages 6–7.

INCOME TAX RATES AND ALLOWANCES (PN02)

The income tax rates will be the same in 2010/11 as in 2009/10, with the addition of the 50% rate which will apply to income in excess of £150,000.

Income tax allowances and thresholds for 2010/11 have been frozen at 2009/10 levels. The Government notes that since these are usually linked to RPI, which has fallen, freezing them is of benefit to taxpayers in real terms.

CAPITAL GAINS TAX

The capital gains tax (CGT) rates and annual exemptions for 2010/11 were not mentioned in the PBR. No changes to the 18% rate were announced but we will have to wait until the Budget for more information.

NATIONAL INSURANCE RATES (PN02 AND PBRN01)

In his PBR speech the Chancellor announced a further 0.5% increase in the rates of NIC which will apply from April 2011. This is on top of the 0.5% increase already announced in last year's PBR. To ensure that the lowest earners are protected from the rise in NIC rates, the level at which people start to pay NICs will increase in April 2011 by £570 above the level previously announced. Those paying the standard employee rate and earning under £20,000 will pay less NICs overall as a result of these changes.

The rates and thresholds for NIC in the next two years will be as follows:

2010/11

NIC rates and thresholds will remain unchanged from the 2009/10 figures.

There are two exceptions to this. The Lower Earnings Limit, which determines access to state pensions and other contributory benefits, which will increase by £2 to £97 per week. The special Class 2 rate for volunteer development workers will increase by 10p to £4.85 per week.

2011/12

As a result of the 0.5% increase announced in PBR 2008 and the further 0.5% increase just announced:

- Classes 1 and 4 main rates will increase to 12% and 9% respectively.
- Class 1 secondary (ie employer) rate and Classes 1A and 1B will increase to 13.8%.
- The additional rates of Classes 1 and 4 will increase to 2%.

The primary (ie employee) threshold for Class 1 and lower profits limit for Class 4 will be increased by £570 more than the income tax personal allowance (this replaces the PBR 2008 announcement that they would be aligned). It should be noted that the secondary threshold is lower than the primary and this latest announcement means that they will differ by even more.

TAX CREDITS AND CHILD BENEFIT (PN02)

Most elements of Working Tax Credit (WTC) and Child Tax Credit (CTC), Child Benefit and Guardian's Allowance will increase by 1.5% from April 2010.

Exceptions are that the child element of CTC will rise by £20 above indexation (ie by £65 in total) and the threshold for receiving maximum CTC will increase to £16,190 in 2010/11. Some elements and thresholds for tax credits will remain unchanged.

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SUMMARY OF THE MAIN RATES AND ALLOWANCES FOR 2010/11

Income tax rates		National Insurance	
Basic rate	20%	<i>Rates are per week unless stated</i>	
on income up to	£37,400	Lower earnings limit, primary Class 1	£97
Higher rate	40%	Upper earnings limit, primary Class 1	£844
Additional rate	50%	Upper Accruals Point	£770
on income over	£150,000	Primary threshold	£110
Starting rate for savings income	10%	Secondary threshold	£110
on income within first	£2,440	Employees' primary Class 1 rate	
Lower dividend rate	10%	between PT and UEL	11%
Higher dividend rate	32.5%	above UEL	1%
Trust rate	40%	Employees' contracted-out rebate	
		Salary-related schemes	1.6%
		Money-purchase schemes	1.6%
		Married women's reduced rate	4.85%
		Employers' secondary Class 1 rate	12.8%
		Employers' contracted-out rebate	
		Salary related schemes	3.7%
		Money purchase schemes	1.4%
		Class 2 rate	£2.40
		Class 2 small earnings exception (year)	£5,075
		Special Class 2 rate for share fishermen	£3.05
		Special Class 2 rate for volunteer development workers	£4.85
		Class 3 rate	£12.05
		Class 4 lower profits limit (year)	£5,715
		Class 4 upper profits limit (year)	£43,875
		Class 4 rate between lower and upper profits limit	8%
		Class 4 rate above upper profits limit	1%

Income tax allowances	
	£
Personal allowance (age under 65)	6,475
Personal allowance (age 65–74)	9,490
Personal allowance (age 75+)	9,640
Married couple's allowance (age 75+)	6,965
Married couple's allowance minimum amount	2,670
Income limit for age-related allowances	22,900
Blind person's allowance	1,890

SUMMARY OF THE MAIN RATES AND ALLOWANCES FOR 2010/11

Tax credits

Working tax credit	£
Basic element	1,920
Couple and lone parent element	1,890
30 hour element	£790
Disabled worker element	2,570
Severe disability element	1,095
50+ Return to work payment (16-29 hours)	1,320
50+ Return to work payment (30+ hours)	1,965

Childcare element of the WTC

Maximum eligible cost	
for one child	£175 per week
for two or more children	£300 per week
Eligible costs covered	80%

Child tax credit	£
Family element	545
Family element, baby addition	545
Child element	2,300
Disabled child element	2,715
Severely disabled child element	1,095

Income thresholds and withdrawal rates

First income threshold	£6,420
First withdrawal rate	39%
Second income threshold	£50,000
Second withdrawal rate	6.67%
First threshold for those entitled to CTC only	£16,190
Income disregard	£25,000

Corporation tax

For financial year to 31 March 2011

Main rate	28%
Small companies' rate	21%
Upper profits limit	£1.5m
Lower profits limit	£300,000
Effective marginal rate	29.75%
Marginal rate fraction	7/400

Capital gains tax

Rate	TBA
Annual exemption	
For individuals, PRs and some trustees	TBA
For most trustees	TBA

Inheritance tax

Nil rate band	£325,000
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VAT

Standard rate of VAT	
To 31 December 2009	15%
From 1 January 2010	17.5%
Registration threshold	TBA
Deregistration limit	TBA

Note: items marked TBA have yet to be announced

3. PERSONAL AND EMPLOYMENT TAXES

TAXATION OF BANKING BONUSES (PBRN02)

There will be a one-off tax, the bank payroll tax, payable when banks operating in the UK pay bonuses in excess of £25,000 to their employees who are resident or working in the UK. The bank payroll tax will be 50% of that excess.

The bank payroll tax will apply to bonus payments made in the period from 9 December 2009 to 5 April 2010 inclusive and it will not be deductible for tax purposes. The tax will be payable by 31 August 2010. In his PBR speech the Chancellor estimated that the tax would raise a little over £500m which suggests that it will catch 'excess' bonuses of around £1bn, which in turn suggests a level of bonus much below those seen in previous years when they were well in excess of £5bn.

There is a targeted anti-avoidance rule to ensure that banks cannot award bonuses and escape the bank payroll tax. This will apply where there are relevant arrangements of which the main purpose, or one of the main purposes, is to reduce or avoid the liability to the bank payroll tax.

There will be a number of other anti-avoidance provisions among which will be measures to:

- Prevent employments being split to obtain multiple tax-free £25,000 bonuses.
- Prevent payments being made via intermediaries or using partnerships.
- Ensure benefits-in-kind, loans, future payments and non-cash payments are caught.

There are certain types of remuneration excluded from these provisions. These comprise regular salary or wages or a regular benefit, anything for which a contractual obligation to pay arose before 9 December 2009 and certain share-related awards.

There is a general overview of this measure in [PBRN02](#). In addition HMRC has published [Bank Payroll Tax – Technical Note, Draft legislation and Explanatory Notes](#).

Banks which have queries which are not answered by the information contained in the Technical Note are recommended to contact their HMRC Customer Relationship Manager.

The provisions introducing the bank payroll tax will appear in Finance Bill 2010.

FURNISHED HOLIDAY LETTINGS (PBRN24)

Budget 2009 brought with it the surprising news that the special rules which have applied to furnished holiday lettings (FHL) since 1984 were on the way out. As seems to be so often the case, the reason is that the rules as they were contravened EU State Aid because they only applied to UK property.

The FHL rules were therefore extended to all properties within the EC with immediate effect, with the warning that relief would be withdrawn altogether from April 2010.

The Tax Faculty, the CIOT and ICAS then went to HMRC and HM Treasury to explain why we felt that the rules should be retained, even if it meant restricting some of the benefits. We were (and still are) concerned that abolishing the rules would impose an additional burden on the hotel and tourist business. However, this is where we now find ourselves.

HMRC has published [draft legislation](#) for the repeal of the FHL rules and a document [Withdrawing the Furnished Holiday Lettings Rules from 2010-11](#) which explains in more detail how those who let furnished holiday accommodation will be affected by the repeal of the rules. There is also an [impact assessment](#). We have already made the point that the costs to businesses of having to prove that they were in fact 'trading' was why the legislation with more objective tests was introduced back in 1984. Sadly, the tax world has a short memory. For those businesses affected, the costs in this paper are likely to be considerably understated.

In summary, from April 2010, FHL businesses will indeed be property businesses still, but they will not be trades. As such, they will be just property income in the UK, or property income from overseas, and taxed in pools according to those respective rules.

The HMRC guidance document is helpful in that it covers most of the questions which an ongoing UK FHL letting business will ask. For example, for expenditure already incurred and in capital allowance pools, relief will continue to be given as before, except of course it will only be set against property income and cannot create losses for use elsewhere.

Another helpful point relates to capital gains reliefs already claimed. These will not be clawed back or immediately crystallise. For example, gains that have been held over under s 154, TCGA 1992, will not be treated as accruing on 6 April 2010 (or 1 April 2010 for companies) as a result of the repeal. The held-over gain will as before be treated as accruing on the earliest of:

- the date the asset is disposed of;
- the date the asset ceases to be used for the purposes of the FHL business; or
- the 10th anniversary of the acquisition of the asset.

There will however be questions which are not answered by this. Please send these to anitamonteith@icaew.com and we will ask for further clarification if necessary.

SEAFARERS' EARNINGS DEDUCTION (PBRN23)

The seafarers' earnings deduction is available to individuals who work on ships and are ordinarily resident in the UK. It can give 100% UK tax relief for earnings from carrying out duties as a seafarer wholly or partly outside the UK during an eligible period.

Legislation is to be introduced in the Finance Bill 2010 to extend the availability of this deduction from 6 April 2011 to seafarers who are EU or EEA residents.

WORKPLACE CANTEENS EXEMPTION AND SALARY SACRIFICE (PBRN25)

The tax exemption for workplace canteens will be restricted from 6 April 2011. The exemption in s 317, ITEPA 2003 will not apply when used in conjunction with salary sacrifice or flexible benefit arrangements. The Government explains that these arrangements enable a minority of employees to buy canteen meals out of pre-tax/NIC income. The exemption will continue to apply for subsidised canteens that are available to all employees.

HMRC intends to produce draft legislation in the New Year.

COMPANY CAR AND VAN BENEFITS

The Government has introduced the following measures to support and encourage low-carbon transport.

Company car benefits for lower emissions (PBRN26)

A new lower 10% band will be introduced from 6 April 2012 for company cars with CO₂ emissions of up to 99g/km. From this date the taxable benefit on employees and the Class 1A NIC charge on employers for cars with these emissions will be calculated at 10% of the list price (adjusted for taxable accessories) and qualifying low emissions cars (QUALECs) will no longer exist as a separate category.

These measures replace the 2009 Budget proposals to remove from 6 April 2012 the 10% category for cars emitting less than 120g/km of CO₂ and extend the system of bands so that they increase by 1% point with every 5g/km CO₂ from 10%.

Electric cars: benefit-in-kind changes (PBRN27)

The company car benefit for electric cars will be reduced to nil from 6 April 2010 for five years. This will affect both the employee benefit and the Class 1A NIC charge on employers.

Electric vans: benefit-in-kind changes (PBRN28)

Vans provided to employees and directors for their private use are currently subject to a flat rate charge of £3,000. A new nil rate benefit for electric vans will be introduced for a five year period from 6 April 2010. This will affect both the employee benefit and the Class 1A NIC charge on employers.

Fuel benefit changes: cars and vans (PBRN29)

From 6 April 2010 the fuel benefit charge multiplier for calculating the fuel benefit where free fuel is provided to an employee or director will increase as follows:

Cars: from £16,900 to £18,000

Vans: from £500 to £550

INCOME TAX TREATMENT OF SHARED LIVES CARERS (PBRN22)

A Shared Lives carer is someone who, in their own home, cares for up to three individuals who have been placed with them under a local authority Shared Lives placement scheme. The category includes adult placement carers.

The income from providing Shared Lives care is taxable (generally as the income of a trade, profession or vocation). HMRC currently allows various non-statutory deductions and exemptions for adult placement carers. Income tax relief is now to be put on a statutory footing for all Shared Lives carers, in a similar way to the existing relief for foster carers.

The new rules will apply from 6 April 2010. Shared Life carers will have a tax-free allowance per household, comprising a fixed £10,000 per tax year and weekly amounts of either £200 or £250 for each adult placed with them. If the carer's total receipts from caring are less than the total allowance for the year, the income will be tax free. If the total receipts exceed the allowance the carer can choose either to be taxed on the excess or to work out their profits based on the usual rules for businesses.

ADULT PLACEMENT CARERS AND CGT MAIN RESIDENCE RELIEF (PBRN16)

An adult placement carer is a person who looks after an adult under a placement scheme with a local authority. The carer does the work in their own home and is paid by the local authority, and the earnings are taxable under the usual rules for a trade, profession or vocation (though subject to certain exemptions).

One or more rooms in the carer's home may be used exclusively for the caring activity – in fact the local authority contract may require this. As a result, the CGT exemption for an only or main residence may not apply to that part of the house when the carer comes to sell it. This is because private residence relief (PRR) is not available for any part of a property used exclusively for business.

This restriction on PRR is removed for disposals on or after 9 December 2009. The fact that part of the home is occupied by an adult in care will not make it ineligible for PRR. Legislation will be included in Finance Bill 2010. HMRC has published draft legislation and an explanatory note **Capital Gains Tax: Private Residence Relief: Adult Placement Carers**.

This will be a very welcome relief for carers who undertake what is essentially a social service, without appreciating that it could land them with a CGT liability on their own home.

4. PENSIONS AND SAVINGS

RESTRICTION OF PENSIONS TAX RELIEF FOR HIGH INCOME INDIVIDUALS

Changes have been made to the pensions anti-forestalling legislation for 2009/10 and 2010/11. In addition, the Government has published its proposals for the post-April 2011 pensions tax relief regime for high income individuals (PBRN19).

The changes are given in PBRN18 and PBRN19 and there is also a detailed document *Implementing the restriction on pensions tax relief* available at www.hm-treasury.gov.uk/prebud_pbr09_consult_pensions.htm.

Anti-forestalling: background

In the 2009 Budget, the Chancellor announced that from 6 April 2011 those on incomes of £150,000 or more would have tax relief on their pension contributions reduced. To prevent taxpayers obtaining a tax advantage by manipulating their income and pension contributions in advance of the introduction of the new rules, 'anti-forestalling' provisions were introduced for 2009/10 and 2010/11.

Anti-forestalling: the December 2009 changes (PBRN19)

It has been announced that the anti-forestalling provisions will now apply to individuals whose 'relevant income' (as defined for these purposes – see below) is £130,000 or higher, rather than to those with incomes of £150,000 or higher. However, tax relief on pension contributions made after 8 December 2009 will be reduced only where the individual has changed their existing pattern of pension contributions and total contributions in the tax year exceed £20,000 (or over £30,000 in certain circumstances).

The reduction in tax relief is effected by way of a 'Special Annual Allowance' charge which:

1. In 2009/10, charges tax at 20% on pension contributions to which it applies (which can mean that the contribution attracts no tax relief where the charge applies because income was more than £130,000 in previous tax years).
2. In 2010/11, will charge tax at a rate such that the tax relief is reduced to, rather than by, 20%.

Due to the 'look-back' rules, anyone with relevant

income of £130,000 or more in any of the tax years 2007/08, 2008/09, 2009/10 or 2010/11 will potentially be within the anti-forestalling legislation, some of whom would not previously have been.

Details of the calculation of relevant income for these purposes are set out in para 2, Sch 35, Finance Act 2009. It is, broadly, total income less losses less Gift Aid plus pension contributions made (grossed up if paid net) plus post 21 April 2009 salary sacrifices for employer pension contributions.

The post 5 April 2011 pensions tax relief regime (PBRN18)

Further to the Chancellor's 2009 Budget announcement about the reduction in tax relief for high income individuals, the detailed proposals have now been published for consultation. Unlike the anti-forestalling provisions, the proposals apply to all relevant pension contributions made on or after 6 April 2011 and not just to contributions made in excess of arrangements which were in force previously.

The post 5 April 2011 pensions tax relief regime: who may be affected?

The proposals introduce two further definitions of income and individuals will have tax relief on pension contributions restricted if their:

1. Pre-tax income is £130,000 or more. Pre-tax income for these purposes is before pension contributions and charitable donations have been deducted. And
2. Gross income is £150,000 or more. Gross income is pre-tax income as at 1 above plus pension benefits provided for them, typically employer pension contributions.

We are pleased however to note that the draft legislation applies only where income in the tax year exceeds the thresholds and does not require pre-tax and gross income of the previous two years to be considered as well.

The draft proposals would mean that those with:

1. Pre-tax income of less than £130,000 will not be affected by the rules regardless of the size of employer contributions.
2. Pre-tax income of between £130,000 and £150,000 will only have tax relief on pension contributions reduced if their employer pension contribution takes their gross income to £150,000 or more.

3. Gross income of between £150,000 and £180,000 will obtain tax relief on pension contributions of between 20% and their marginal tax rate by way of a tapering mechanism.
4. Gross income of £180,000 or more will be given relief at the basic rate (20%).

The post 5 April 2011 pensions tax relief regime: employer contributions

The reduced tax relief applies both to employee pension contributions and to employer (and other) pension contributions made for employees. In the case of employer contributions, in addition to contributions made to schemes, increases in benefits accruing to employees under retirement benefits schemes will also be taken into account. Although it is fairly straightforward to quantify pension contributions made to Defined Contribution ('money purchase') schemes, it is less easy to value those relating to Defined Benefit (including 'final salary') schemes. Much of the consultation document relates to this valuation issue and also the additional burdens the new regime generally will place on employers and pension scheme managers.

As tax relief is generally given at source on employer contributions, employees may be liable to large amounts of tax which will be collected through self assessment. HMRC is consulting on the practical implications of this and ways in which the tax charge may be spread where this is appropriate.

The post 5 April 2011 pensions tax relief regime: special cases

HMRC is also consulting on the following three issues:

1. Practical issues arising from the application of the rules for members of overseas pension schemes.
2. Application of pensions tax relief restriction in the year in which benefits are drawn.
3. The effect of the restriction where an employee has received a termination payment.

VENTURE CAPITAL SCHEMES

The EIS and VCT schemes received approval from the EC as State Aids on 29 April 2009. That approval was subject to a number of changes being made. **Draft legislation** is now published which:

- applies an additional requirement that to qualify under either scheme, a company must not be in difficulty;
- replaces the requirement for a company to carry on its qualifying trade wholly or mainly in the UK, with a new requirement that the company must have a permanent establishment in the UK;
- replaces the requirement that a VCT's shares must be included in the official UK List, with a requirement that their shares must be traded on an EU regulated market; and
- changes the rules governing the amount of a VCT's investment which must be held as equity.

The draft legislation also redefines a small business to be one based on the definition set out by the EC. The proposed new condition focuses on the substance of the economic activity comprising, or including, the company's qualifying business activity, and requires that the enterprise engaged in the substantial economic activity is a small enterprise.

The new definition is intended to make the relief more targeted to genuine small businesses.

EIS COMPANIES IN PARTNERSHIP

HMRC has published a separate Technical Note, **Enterprise Investment Scheme (EIS) and Partnerships**, setting out its view that under s 183, ITA 2007, companies carrying on their qualifying activity in partnership do not qualify under the EIS.

In simple terms, s 183 requires that the trade has to be carried on by the company which issued the shares or its 90% subsidiary. Where the trade is carried on by the company in partnership or by a limited liability partnership of which the company is a member, the condition is breached.

HMRC recognises that this change of view may have adverse implications for companies which had intended carrying out a trade in partnership. While we do not know how many companies are currently in the process of applying for relief, it seems to us that there may be cases where a business seemed to qualify but

may now need to be restructured. HMRC intends to consult on the consequences of this and on whether there is now a need to cater for some partnership arrangements by revising the law. We would be interested to hear from members with particular cases which will either suffer from this interpretation or where changes in these rules would help. Email anita.monteith@icaew.com

ALTERNATIVE FINANCE ARRANGEMENTS

The Government will continue to adapt tax rules on alternative (Islamic) finance in response to market developments, and will issue guidance on the VAT treatment of Islamic bonds (known as 'sukuk').

It is also considering changes for alternative property refinance arrangements that do not include payment of interest so they have the equivalent tax treatment to conventional loans.

5. TAX CREDITS AND STATE BENEFITS

TAX CREDITS: NOTIONAL ENTITLEMENT

Apart from the increase in rates and thresholds, there are two small but important changes to the tax credits system.

The Government are going to introduce the so-called 'notional entitlement' procedure. This is a technical-sounding term for a practical and helpful approach to tax credits claims when changes in a couple or single status are reported late.

When a couple splits up or one partner dies, or a single person becomes part of a couple, the change brings any current tax credit claim to an end. The newly-single person or new couple must make a new claim. Such changes must be reported to HMRC within one month, but often people delay, perhaps due to the stress of their situation or because it is hard to tell exactly when a relationship has ended. Meanwhile a tax credits overpayment may be building up from the date the old claim technically ended, but a new claim can only be backdated by three months. When the situation comes to light, the claimant can find themselves in financial difficulty. For some time, representative bodies (led by the voluntary sector but including the Tax Faculty) have been pressing Government to reduce the overpayment in this situation by offsetting the amount of tax credits which

would have been paid if the change had been reported and a new claim made on time, ie to take account of the 'notional entitlement'.

HMRC has now agreed to this and will apply it from January 2010. Further details will be set out later in guidance.

TAX CREDITS: WTC FOR THOSE AGED 65-PLUS

The working hours requirement for Working Tax Credit (WTC) is either at least 30 hours a week, or at least 16 hours a week in certain circumstances. Older people currently have to meet the 30 hours rather than the 16 hours requirement unless they have dependent children or qualify for a disability element or for the 'return to work' element (for those aged 50-plus who have been on benefits).

To provide more support to older people who wish to stay in work, people aged 65 and over will from April 2011 be able to claim WTC if they work at least 16 hours a week (regardless of whether they have dependent children etc).

STATE PENSION

The state pension will be increased by 2.5% from April 2010, giving a full basic state pension of £97.65 per week. Pension credit will be increased to £132.60 a week for single pensioners and £202.40 for couples from April 2010.

These benefits are normally linked to increases in the RPI, so would not have gone up at all on that basis.

6. BUSINESS TAX

BUSINESS PAYMENT SUPPORT SERVICE

HMRC's Business Payment Support Service (BPSS) was introduced in the 2008 PBR. The idea is that HMRC will support compliant viable businesses through periods of temporary difficulty by giving them time to pay their tax. This has so far enabled over 160,000 businesses to spread over £4bn of tax.

It is confirmed (para 4.5 of the PBR 'Red Book') The BPSS will continue for as long as it is needed.

INDEPENDENT BUSINESS REVIEWS

The BPSS has proved extremely popular and many businesses have undoubtedly benefited, although the rules were tightened up rather after the initial euphoria.

However, in the last six months HMRC has received in excess of 150 time to pay (TTP) requests for £1m or more. Clearly these larger amounts need rather more checking which itself costs more, as indicated by the **impact assessment** which accompanies this announcement.

With effect from April 2010 a business applying for time to pay a debt of £1m or more will need to engage, at their own expense, a suitably qualified professional adviser to carry out an Independent Business Review (IBR) in support of its application.

HMRC will be consulting informally on the best way to implement this measure.

ELECTRIC VANS: CAPITAL ALLOWANCE CHANGES (PBRN30)

There will be a new 100% capital allowance for the purchase of new, unused (not second-hand) electric vans. This will apply to expenditure on or after 1 April 2010 for companies and on or after 6 April 2010 for other businesses subject to income tax.

Note that the introduction is subject to confirming compatibility with EU State Aid rules.

R&D TAX RELIEF FOR SMES (PBRN06)

Until now, it has been necessary for a SME company which has claimed research and development (R&D) tax relief to itself hold any intellectual property arising from that R&D.

It was announced in the 2009 PBR that this condition will not apply to any expenditure incurred in accounting periods ending on or after 9 December 2009.

Draft legislation and an explanatory memorandum have also been published.

EMPTY PROPERTY RATE RELIEF

The temporary increase in the threshold at which an empty property becomes liable for business rates has been extended for a year. For financial year 2010/11, empty properties with a rateable value of less than £18,000 will be exempt from business rates.

FALSE SELF-EMPLOYMENT IN CONSTRUCTION

A summary of responses to the consultation on *False Self Employment in Construction* will be issued in the New Year. The Government says it is committed to addressing this problem and 'will continue to work with stakeholders to develop a legislative solution that is well targeted' (para 5.95, PBR 'Red Book').

TAX AND ACCOUNTANCY: CHANGES TO ACCOUNTING STANDARDS ON FINANCIAL INSTRUMENTS (PBRN05)

The International Accounting Standards Board (IASB) is proposing a number of changes to IAS 39 *Financial Instruments: measurement and recognition*, due to take effect in 2010. These changes will affect the way in which financial instruments such as loans, securities and derivatives are treated for accounts which are prepared under IFRS. The UK's Accounting Standards Board will make corresponding changes to the equivalent UK accounting standard FRS 26 *Financial Instruments*.

The IASB has issued, or is proposing to issue, Exposure Drafts proposing changes in four main areas of IFRS 39, as follows:

- the way that financial instruments are classified and measured for accounting purposes;
- when they are recognised on the balance sheet;
- how impairment losses are quantified; and
- how hedging arrangements should be accounted for.

Because the tax treatment of such instruments is based on the accounting treatment, changes to the accounting rules will have implications for the tax rules on loans, derivatives and repos (sale and repurchase agreements).

Legislation will be introduced in Finance Bill 2010 to respond to these changes by inserting a power to amend the loan relationships and derivative contracts rules by way of secondary legislation. The amendments will be limited to those necessary to ensure the rules continue to operate fairly and efficiently where companies adopt the modified accounting standards. The regulations will have effect for company accounting periods ending on or after 1 January 2010. However, the IASB has also proposed that companies should be able to adopt certain of the accounting changes retrospectively, in which case any tax changes will also be applied retrospectively.

7. COMPANY TAX

SMALL COMPANIES' RATE

The small companies' rate of corporation tax will continue at the current rate, 21%, for the year beginning on 1 April 2010. The planned increase to 22% has been deferred for a year until 2011/12.

ENTERPRISE MANAGEMENT INCENTIVES

The Enterprise Management Incentives (EMI) rules require a qualifying company's activities to be 'wholly or mainly' in the UK. This will be changed so that a company will need only a 'permanent establishment' in the UK.

The EMI legislation is designed to allow smaller companies to grant share options with tax and NIC advantages to their employees. It is aimed at smaller, higher-risk companies to help them recruit and retain key employees. In order to qualify for the scheme, a company has to meet various conditions with respect to its size, independence and trading activities.

Such schemes have to comply with the European Commission's guidelines and treaties regarding the provision of State Aid. The Commission has agreed to grant EMI State Aid approval until April 2018 subject to this change being made. **Draft legislation** has been published.

The change will have effect in relation to EMI options granted on or after 6 April 2010.

FILM TAX RELIEF (PBRN07)

Where a film company produces a film over more than one accounting period, a quirk in the legislation currently restricts the available tax credit in a way which was not intended.

Film tax relief allows an additional deduction based on UK expenditure by companies on the production of films qualifying as culturally British. Losses sustained in production can be surrendered for a payable tax credit.

Draft legislation has been published to correct the quirk and revise the calculation of the amount surrenderable for this tax credit to the lesser of:

- the available qualifying expenditure, and
- the loss for the period, plus any unsurrendered loss brought forward.

The new rules will apply to accounting periods ending on or after 9 December 2009.

FOREIGN COMPANY PROFITS: THE DEBT CAP RULES (PBRN04)

The debt cap rules are being introduced for accounting periods beginning after 1 January 2010 as a safeguard to ensure that while dividends from overseas subsidiaries will now be exempt from UK tax there may be a limit on the amount of interest that will be deductible from UK profits. This is designed to prevent groups of companies 'overloading' the UK with debt. The provisions restrict the deductibility of interest in the UK where the UK financing costs exceed the financing costs of the worldwide group.

During the course of the consultations on these measures the Government accepted that if the legislation in Finance Act 2009 could be improved then this would be done in Finance Act 2010. The Financial Secretary to the Treasury **announced** various changes in a statement in the House on 9 November 2009.

The detailed legislation and explanatory notes have now been **published**.

The proposed changes include:

- Eliminating mismatches in the application of the 'gateway test' caused by different accounting treatments of the same debt in single entity accounts and consolidated accounts.
- Excluding securitisation companies from the debt cap rules.
- Eliminating mismatches between the computation of UK financing costs and worldwide financing costs where borrowing is undertaken by a partnership, including a limited liability partnership.
- Restricting the allocation of disallowances under the debt cap to group companies which are dual resident investment companies.
- Allowing other companies to elect that no disallowance shall be allocated to them.
- Amending the definition of a group treasury company to prevent an anomalous result where other companies in the group have income from treasury activities.
- Including guarantee fees received from other group companies in a company's financing income.
- Widening the definition of a collective investment scheme to prevent the automatic exclusion of overseas partnerships which are, legally, bodies corporate.

CONTROLLED FOREIGN COMPANIES

The overhaul of the controlled foreign company (CFC) regime, first introduced in 1984, was initially going to be an integral part of the 'foreign company profits' changes. However because of considerable resistance to the initial proposals in June 2007 the CFC changes were disconnected from the other proposals. They have been the subject of further consultation during the summer of 2009 after HMRC published a policy principles document in July 2009. In the July document it was stated that the policy underlining the new CFC regime will be to distinguish between profits genuinely earned overseas and those which represent an artificial diversion of profits from the UK.

Paragraph 4.59 of the 'Red Book' confirms that the Government will publish its CFC proposals early in 2010.

FOREIGN BRANCH PROFITS

When the first consultation document on foreign company profits was published in June 2007 the decision was taken only to deal with the position of groups of companies with subsidiaries operating abroad. The taxation of other entities, which means in the main the banks, was left for future consideration.

Paragraph 4.60 of the 'Red Book' now indicates that the Government is going to 'engage with business to identify and explore issues relevant to any potential future rule changes' in relation to foreign branch taxation.

PATENT BOX REGIME

The Government will consult during 2010 on the introduction of a 'patent box' regime for UK companies with effect from 1 April 2013. The intention is that there will be a reduced corporation tax rate of 10% for income from patents registered from that date. There are no detailed proposals available at the moment but HM Treasury has suggested that the eventual cost of this new regime could be £1.3bn. See paragraph 4.40 of the 'Red Book' for brief details.

8. IHT AND TRUSTS

IHT NIL RATE BAND (PBRN20)

The amount of the IHT nil rate band will be frozen at £325,000 for 2010/11. The provision in Finance Act 2007 setting the nil rate band at £350,000 from 6 April 2010 will be repealed.

This means that the maximum total nil rate band for an estate where the personal representatives can claim a transfer of unused nil rate band from the dead person's previously-deceased spouse or civil partner will remain at £650,000.

ANTI-AVOIDANCE: IHT CHARGES ON TRANSFERS INTO A TRUST (PBRN21)

The Government is introducing legislation to counter two tax avoidance schemes designed to avoid IHT charges on transfers into a trust.

HMRC has published draft legislation and explanatory notes in a document entitled **Inheritance tax avoidance**.

The two situations where the new measures apply are:

- Where a person transfers property into a trust in which they (or their spouse or civil partner) retains a future interest, or where a person purchases a future interest in a trust.

There will be a chargeable event for IHT purposes when the future interest comes to an end and the person becomes entitled to an actual interest under the trust. If that future interest is given away before the person becomes entitled to an actual interest, it may be immediately chargeable to IHT.

- Where a person purchases an interest in possession in a trust at full value.

Such an interest will be treated as part of the purchaser's estate for IHT purposes. If the interest comes to an end during the purchaser's lifetime, there may be an immediate charge to IHT.

The changes apply to transfers into trust and the purchase of interests in trusts on or after 9 December 2009.

The Government intends also to explore what more can be done to identify and reduce the avoidance of IHT charges on trusts so that legislation does not have to be done on a piecemeal basis, while making sure any methods adopted are workable, effective and do not cause undue burdens (para 5.80 of the 'Red Book').

9. VAT AND DUTIES

17.5% STANDARD RATE FROM 1 JANUARY 2010

The Chancellor confirmed that the standard rate of VAT will return to 17.5% on 1 January 2010. This is in line with his stated intention when the rate went down temporarily to 15% from 1 December 2008.

Despite much speculation, the change has not been delayed, nor has the standard rate been put up to something higher than 17.5%, or the scope of VAT extended to raise revenues.

There will be a period of grace for certain businesses trading across the midnight deadline on 31 December 2009 to charge the lower rate until either when they close, or if earlier, 6.00am on 1 January.

FLAT RATE SCHEME UPDATE (PBRN33)

The rates used in the VAT Flat Rate Scheme will be updated from 1 January 2010 so that they are based on the 17.5% rate and reflect the latest data about different business sectors. Virtually all sectors will face an increase (as a result of the increase in the standard rate) but some sectors' increases will be bigger than others.

Further guidance on the changes to the flat rate scheme, including a full table of rates, can be found in PBRN33.

CONSULTATION ON LATE PAYMENT AND FILING PENALTIES

HMRC has issued a **consultation document** *Meeting the obligations to file returns and pay tax on time: Draft legislation and commentary* on the subject of penalties for the late payment and filing of returns relating to indirect taxes and excise duties.

The consultation document sets out the draft legislation and the explanatory notes relating to the penalties to which a taxpayer will be liable if they fail to submit certain returns or pay certain amounts of tax on time.

The paper seeks views on draft legislation to bring the remaining taxes and duties administered by HMRC into the same late filing and late payment penalty regime as was introduced for most direct taxes by Finance Act 2009. This will extend the regime to VAT, insurance premium tax, aggregates duty, climate change levy, landfill tax and excise duties.

HMRC recognises that these regimes have a wider range

of periods to which filing and payment obligations may apply, and plans to develop the penalty models to accommodate these differences, based upon the same principles as contained in Finance Act 2009. The draft legislation does this by suggesting two separate forms of penalty:

- Penalties for returns and payment periods that are between six and two months (such as VAT and the environmental taxes).
- Penalties for returns and payment periods that are less than two months long (such as some excise duties).

If you have any comments regarding the consultation that you would like to be included in the Tax Faculty's response, please send them to neil.gaskell@icaew.com by the end of January 2010.

CONSULTATION ON EXCISE MODERNISATION AND COMPLIANCE CHECKS

HMRC has issued a **consultation document** *Excise: Modernisation and Compliance Checks: the next stage* regarding the modernisation of its legal powers to check compliance within excise regimes.

The areas covered by the consultation include information and inspection powers, record-keeping and aligned time limits for making assessments and claims in relation to compliance checks, excise modernisation and a review of associated customs law. It is aimed at anyone involved in dealing with duties in alcohol, tobacco, energy products, gambling and air passenger duty.

BINGO DUTY

Bingo duty will be reduced to 20% at Budget 2010.

LANDLINE DUTY

There will be a new landline duty of 50p per month on UK landlines, from 1 October 2010. This is designed to generate funds to pay for the improvement of broadband services. HMRC and the Department for Business, Innovation and Skills will consult shortly on the implementation of the new duty.

10. ENVIRONMENTAL TAXES

BIOFUELS DUTY (PBRN31)

The differential duty rates for biofuels will end in 2010/11. This confirms what was announced in the 2008 Budget.

Legislation will be introduced in Finance Bill 2010 to amend the duty rates for biodiesel and bioethanol for road use from 1 April 2010, alongside changes to other duty rates for hydrocarbon oils and alternative fuels. Secondary legislation will be introduced to maintain the 20p per litre duty differential for biodiesel produced only from waste cooking oil for a period of two years

CLIMATE CHANGE LEVY (PBRN32)

The reduced rate of the climate change levy (CCL) will increase from 20% to 35%. The change will apply from 2011/12, ie to supplies of taxable commodities made on and after 1 April 2011.

LOW-CARBON TRANSPORT

The Government has introduced a number of measures to support and encourage low-carbon transport, covered elsewhere in this summary.

11. ANTI-AVOIDANCE

PROTECTING TAX REVENUES

The Government has for the first time published an official estimate of the extent of the direct tax gap. It has published a document **Protecting Tax Revenues 2009** which sets out the measures that HMRC has taken, and is taking, to tackle the overall tax gap.

There is then a further publication **Measuring Tax Gaps 2009** which contains estimates of all tax gaps. The 'gap' in indirect taxes has been estimated officially since 2001. The estimate of the overall size of the UK net tax gap in 2007/08 is £40bn including both indirect and direct taxes and is about 8% of the theoretical tax liability.

Finally in paragraph 5.76 of the 'Red Book' there is the announcement that a new Hidden Economy Advisory Group is to be set up to consider what actions HMRC can take to increase the number of people that make the transition from the hidden to the formal economy.

The Government also announced measures to tackle offshore evasion of which the New Disclosure Opportunity and the Liechtenstein Disclosure Facility were announced in the months leading up to the PBR.

DISCLOSURE OF TAX AVOIDANCE SCHEMES

The disclosure of tax avoidance schemes (DOTAS) regime was introduced in 2004 and the Government estimates (see Box 5.4 in the 'Red Book') that it has contributed to the closure of over £12bn in avoidance opportunities.

The Government has now issued a consultative document **Disclosure of Tax Avoidance Schemes**, for comment by 19 February 2010, with five proposals to strengthen the scheme. The proposals are:

1. A change to the trigger point for disclosure of marketed schemes to ensure early disclosure.
2. An information power to require that persons who introduce scheme promoters to clients identify who the promoter is.
3. Enhanced penalties for failure to comply with a disclosure obligation.
4. A requirement for a promoter to provide HMRC with a periodic list of clients to whom they have issued Scheme Reference Numbers.
5. Revised and extended hallmarks for the types of arrangements that have to be disclosed.

DOTAS AND SDLT (PBRN35)

In addition, following a consultation over the summer, regulations will be introduced to extend DOTAS to require the disclosure of certain stamp duty land tax (SDLT) schemes that concern residential property with a value in excess of £1m. Users of SDLT schemes for both residential and commercial property will be required to report the use of these schemes to HMRC. The relevant regulations will be laid before Parliament in the New Year and will come into effect no later than 1 April 2010.

RISK TRANSFER SCHEMES (PBRN08)

Measures will be introduced with effect from 1 April 2010 to restrict loss relief on certain group hedging transactions such that losses are limited to the real economic losses suffered by the group concerned, are ring-fenced, and can only be offset against profits from the same arrangements.

INSURANCE PREMIUM TAX (PBRN015)

New measures will be introduced with effect from 9 December 2009 to prevent the avoidance of insurance premium tax (IPT) on insurance provided to individuals by splitting the premium between two contracts, one being predominantly for the administrative charges (which would not attract IPT).

The Government has **published** draft legislation and explanatory notes on these IPT proposals.

STAMP DUTY AND SDRT (PBRN17)

In a case involving HSBC Holdings the European Court of Justice ruled that it was contrary to the Capital Duty Directive and the free movement of capital for the UK to charge when shares are issued into an EU clearing service or depositary receipt system. These are commonly used for trading shares in foreign jurisdictions.

There are exemptions for subsequent transfers between clearance services and depositary receipt systems.

It is now proposed to introduce provisions in Finance Bill 2010, with effect to transfers made on or after 1 October 2010, to ensure that where securities enter a clearance service or depositary receipts scheme without stamp duty or stamp duty reserve tax (SDRT) being due in accordance with the ECJ decision, a subsequent transfer of those securities to a clearance service or depositary receipts scheme will no longer benefit from the current exemption which is designed to prevent a double charge.

SIMPLIFYING TRANSACTIONS IN SECURITIES LEGISLATION

HMRC has **issued** a consultation response document following the recent consultation on simplifying the 'transactions in securities' legislation. ICAEW Tax Faculty response to that consultation was published as **TAXREP 56/09**.

The aim of this anti-avoidance legislation is to prevent the extraction of profits from companies which results in shareholders obtaining an 'income tax advantage' where the transaction is, in broad terms, tax-motivated rather than commercially driven.

In our response to the consultation we wrote that:

A large part of the transactions in security legislation is now out of date and its very wide potential application means that it can 'catch' straightforward company sales

etc which results, currently, in there being far too many clearance applications.

In the consultation response document, the Government states that it will carefully consider the responses and intends to make certain technical changes to reflect some of the concerns raised by respondents. It is envisaged that these changes will be included in the Finance Bill 2010 or shortly afterwards.

The Government also states that it will consider repealing the whole of the legislation for corporate shareholders, although this needs further consideration and is unlikely to take place until after Finance Bill 2010.

ANTI-AVOIDANCE: SIMPLIFYING UNALLOWABLE PURPOSES TESTS

The UK's direct tax legislation contains over 200 purpose tests which are typically intended to determine whether taxpayers are entitled to take advantage of the availability of a particular favourable tax treatment. These separate tests can be constructed very differently and use widely differing terminology.

In principle, bona fide commercial transactions will qualify for the beneficial treatment available whereas uncommercial tax-motivated transactions will not, with the consequence that any tax advantages are denied. However, the experience of many taxpayers is that these unallowable purpose tests can be complicated, widely drafted and highly subjective, with the result that there can often be a lack of clarity as to whether innocent transactions might inadvertently be caught by anti-avoidance rules.

HMRC has **issued** a discussion response document concerning proposed simplifications to the various unallowable purpose tests contained within the direct tax legislation. The intention is that a new framework could be adopted in the summer of 2010.

OTHER ANTI-AVOIDANCE MEASURES (PBRN09–PBRN14)

The Government also announced that legislation will be introduced in Finance Bill 2010, with effect from 9 December 2009, to cover the following arrangements:

- Life insurance companies: apportionment of income and gains (PBRN09)
- Sale of lessor companies: consortium arrangements (PBRN11)

- Capital allowances – transfer of benefit (PBRN12)
- Plant and machinery leasing (PBRN13)
- Index-linked gilt-edged securities (PBRN14).

In addition there will be provisions in Finance Bill 2010 to give a lessor company an option to elect that the immediate charge that would otherwise arise under Sch 10, Finance Act 2006 is collected on the profits of the leasing business following the sale (PBRN10).

12. POWERS, COMPLIANCE AND APPEALS

HMRC POWERS REVIEW

We have come to expect a hefty package of documents from HMRC's modernisation of powers programme at Budget and PBR time, and this month's PBR did not disappoint. Further consultations and response to earlier ones have been published on the following:

1. Working with tax agents
2. Tackling offshore evasion
3. Bulk and specialist information powers
4. Interest: working towards a harmonised regime (for corporation tax and petroleum revenue tax)
5. Meeting the obligations to file returns and pay tax on time (for indirect taxes and excise duties)
6. Modernisation and compliance checks: the next stage (for excise duties)

Items 5 and 6 are covered in the VAT and duties section, the first four are discussed below.

WORKING WITH TAX AGENTS

The story so far

In the 2009 Budget HMRC published a consultation paper *Working with tax agents*. The document was very much a 'starter for 10' and considered a number of areas for possible reform, including:

- possible new penalties on agents who make careless errors;
- greater sanctions against tax agents who have been deliberately non-compliant, including possible penalties, reports to professional bodies and closer monitoring and risk assessment; and

- whether tax agents should be registered with HMRC.

The paper also recognised that tax agents play a vital role in the delivery of the tax system and that the overwhelming majority of tax agents advise their clients appropriately and calculate the right amount of tax.

The Tax Faculty's response was published as TAXREP 48/09 and since then we have continued discussions with HMRC.

The latest proposals

HMRC has now published a further consultation document *Working with tax agents: the next stage*, together with a related impact assessment.

The latest consultation document reflects the continued dialogue. The earlier suggestions about a possible tax agents' registration scheme have now been dropped (not that HMRC was keen on this idea in the first place) and the latest document now focuses on the following areas:

- disclosure to professional bodies;
- dealing with deliberate wrongdoing by tax agents; and
- dealing with high volume agents.

Disclosure to professional bodies

The April 2009 consultation document discussed the role of professional bodies in maintaining and improving standards, whether the existing statutory gateway which allows HMRC to disclose bad work by agents is sufficient, and whether there is a need for a less formal and more flexible gateway designed to help agents improve without the need to invoke formal disciplinary procedures.

HMRC's conclusion is that the existing gate in s 20, Commissioners of Revenue and Customs Act 2005 is sufficiently wide to allow public interest disclosures at a lower level. It is proposed that:

- where HMRC identifies a problem area, it would first raise the concerns with the agent to see if the problem can be resolved;
- in some cases, the tax agent may wish to approach their professional body to seek help;
- if the problem persists or the member does not wish to engage with HMRC, HMRC will seek to take formal steps to disclose details to the professional body; and

- where there is clear evidence of conduct likely to result in exclusion from membership of the professional body, HMRC might decide to make an immediate disclosure to the professional body.

Where a tax agent is not a member of a professional body, HMRC would seek to discuss the matter with the agent but if the concerns could not be resolved it would then consider invoking other sanctions.

Deliberate wrongdoing by agents

Proposals in this area take up a considerable portion of the consultation document. HMRC is at pains to make clear that these proposals are aimed at serious problems such as fraud or dishonest evasion where the behaviour of the agent could result in prosecution – they are not aimed at agents who operate in accordance with professional standards but might make mistakes.

HMRC already has a number of powers in this area over and above the ability to prosecute. These include the ability to fine an agent who knowingly prepares an incorrect tax return up to £3,000 (s 99, TMA 1970) and the ability in certain defined cases to seek access to the agent's working papers (s 20A, TMA 1970). HMRC sets out a number of suggestions for extending these existing powers.

- To make it easier for HMRC to access the working papers of tax agents who have been involved in deliberate wrongdoing. Under current rules HMRC can only proceed under s 20A if the agent has been successfully prosecuted or been fined under s 99. These requirements would be removed but any approach would need to be authorised by a tribunal.
- Possible tax-geared penalties imposed on agents involved in deliberate wrongdoing, with a suggested minimum penalty of £5,000 and a maximum of £50,000 but subject to mitigation for unprompted/prompted disclosure in line with the penalty rules in Sch 24, FA 2007.
- Possible 'naming and shaming' of the agent along similar lines to the new rules in s 94, FA 2009.

High volume agents

The April 2009 consultation document highlighted HMRC's concerns about certain tax agents who submit large volumes of tax repayment claims which on investigation often have little or no merit. HMRC is concerned to address problems in this area while

respecting the rights of bona fide agents who submit valid claims. HMRC proposes that:

- it would issue a direction to the agent requiring them to verify information included in the repayment claim on a bulk basis;
- if that direction was not complied with, the repayment claim would lapse; and
- in certain circumstances any repayment would only be made to the taxpayer and not the agent.

These powers would be subject to safeguards including the need for authorisation by a tribunal.

Next steps

HMRC invites comments on the above proposals. The deadline is 3 March 2010. The Tax Faculty will be putting in a submission in due course and we would very much welcome comments from members. Please send them to Frank Haskew at frank.haskew@icaew.com.

TACKLING OFFSHORE EVASION

Notable among the consultation documents is *Modernising Powers, Deterrents and Safeguards: Tackling Offshore Tax Evasion* with an accompanying **impact assessment**.

HMRC is proposing a package of deterrents and new tools to help HMRC tackle offshore tax evasion. This includes a new notification requirement for certain new offshore bank accounts and a tougher penalty regime for offshore non-compliance. HMRC is also inviting comments on possible reforms to the information provided by non-resident trusts.

The proposal for a notification requirement is as follows. Some individuals who have bank accounts in certain jurisdictions would be required to notify them to HMRC. Depending on the jurisdiction, this would either apply to all bank accounts or to bank accounts where the balance was over £25,000. Notification would be required within 60 days of the accounts becoming notifiable. Failure to comply would attract an initial fixed penalty, followed by a period of daily penalties and then tax-gearred penalties. The penalty would be in addition to the penalties for under-declaration, so that in the most serious cases the aggregate penalty could be as high as 200% of the evaded tax. There is no indication when this proposal would be implemented.

Under the tougher penalty regime, offshore non-compliance, whether careless or deliberate, would be subject to penalties at the same scale as deliberate domestic non-compliance. This would mean that the minimum penalty would be 20% of the undeclared tax even where a full unprompted disclosure was made, and penalties would be as high as 70% even where no concealment is involved. These penalties would apply for tax periods commencing on or after 1 April 2011 but HMRC have also said that they intend to seek penalties at similar levels for earlier years on the basis that the non-compliance is deliberate.

BULK AND SPECIALIST INFORMATION POWERS

HMRC has published a summary of the responses to the consultation earlier in 2009 on *Bulk and specialist information powers*, together with proposals for the next steps.

The two key themes emerging from the responses were:

- the opportunity should be taken to update the bulk powers; and
- there should be more dialogue with data-holders, particularly about how powers are exercised in practice.

HMRC proposes to bring forward new legislation and will include a draft in a second consultation document that will be issued in due course. In order that the new legislation applies to all duties administered by HMRC, it is presently envisaged that the bulk powers will be put into a new Schedule modelled on Schedule 36 to FA 2008. That Schedule will identify particular groups of data-holders and detail the information that may be sought from each group. It is possible that some of the detail may go into regulations.

INTEREST: WORKING TOWARDS A HARMONISED REGIME

The FA 2009 rules harmonised the plethora of rules that applied for late paid/repaid tax but excluded corporation tax (CT) and petroleum revenue tax (PRT). It was proposed that provisions to harmonise rules for these two taxes would be included in the Finance Act 2010. HMRC has published a consultation document setting out draft legislation and related commentary on how this would be done.

The draft legislation proposes that CT and PRT will be

brought within the harmonised interest rules by way of amendments to the FA 2009 rules rather than separate but parallel legislation as envisaged at an earlier stage in this process.

The interest regime applicable to quarterly interest payments will remain unchanged.

The deadline for comments is 3 March 2009.

ENFORCEMENT OF JUDGEMENTS IN LITIGATION

Paragraph 5.87 of the PBR 'Red Book' contains a statement that 'HMRC is to apply a more consistent approach to the collection of debts in litigation'.

Where an appeal has been decided in a court or tribunal but there is a further appeal, HMRC must repay overpaid tax where there is a judgment in favour of a taxpayer, even though that judgment is subject to appeal. However where there is a judgment in its favour, HMRC does not consistently collect the tax before the appeal is heard. Accordingly, HMRC has decided to adopt the approach that payment of the tax will normally be required in all such cases.

The change of practice will take effect in relation to all decisions made by the tribunals or courts on or after 1 April 2010.

We are concerned that having to pay the tax might prove a barrier to justice for some appellants, and intend to discuss this with HMRC to find out more about how the new approach will be applied.

13. ADMINISTRATION AND OTHER ISSUES

CODE OF PRACTICE ON TAXATION FOR BANKS

The Government issued a consultation document in June 2009 with a view to introducing a voluntary code of practice on taxation for banks. Responses were required by the end of September and the ICAEW Tax Faculty submitted a representation, **TAXREP 50/09**.

The code, with a few minor amendments from the June 2009 draft, is now going to be introduced and the Government 'expects all banks operating in the UK to adopt the principles set out in the code'. In practice banks should first consider the implications of the code and then take a corporate decision, following their normal governance procedures, to adopt the code and communicate that decision to HMRC.

The actual code itself contains only a few amendments to the June 2009 draft and it keeps to the four main heads contained in the draft code, namely:

- Overview
- Governance
- Tax planning
- Relationship between the bank and HMRC.

Details are contained in the **consultation response** document, which contains the final version of the code, and the **Supplementary Guidance Note**.

The overview states that:

The Government expects that banking groups, their subsidiaries, and their branches operating in the UK, will comply with the spirit, as well as the letter, of tax law, discerning and following the intentions of Parliament.

This means that banks should:

- *adopt adequate governance to control the types of transactions they enter into;*
- *not undertake tax planning that aims to achieve a tax result that is contrary to the intentions of Parliament;*
- *comply fully with their tax obligations; and*
- *maintain a transparent relationship with HM Revenue and Customs.*

The most contentious of the above requirements is for banks 'not to undertake tax planning that aims to achieve a tax result that is contrary to the intentions of Parliament'. The ICAEW remains concerned that achieving this may prove problematic, particularly when Parliament is quite often unclear as to precisely what a particular piece of legislation is targeting. The consultation response document suggests that:

banks answer the question of whether the [particular] transaction is contrary to the 'intentions of Parliament' in practice by asking whether the tax consequences of a proposed transaction are too good to be true.

The final version of the code no longer includes an obligation for banks to disclose, in advance, details of a transaction where they have doubts that it may be contrary to the intentions of Parliament. The code now lays down that if the banks have doubts they 'may discuss the plans in advance with HMRC' but there is not an obligation to do so.

The Supplementary Guidance Note makes clear that if a bank does not adopt the code, or adopts but does not implement the code properly, then that bank will not be considered low risk and is likely to face additional scrutiny from HMRC.

Only the 76 banks managed within the Large Business Service of HMRC need sign up to the full code. The other banks, which are stated to be 180 banks and 49 building societies, need only adopt the 'overview' part of the code.

EXTRA-STATUTORY CONCESSIONS: MORE TO BE ENACTED OR WITHDRAWN

The decision in the *Wilkinson* case (*R v HM Commissioners of Inland Revenue ex parte Wilkinson* [2005] UKHL 3) clarified the extent of HMRC's administrative discretion to make concessions which fall outside the strict statutory position. HMRC has therefore been reviewing its concessions and withdrawing those which it believes are outside its administrative discretion. In some cases legislation is being introduced to give statutory effect to the concession.

As part of the continuing review, HMRC has identified nine concessions which it believes are obsolete and which will be withdrawn with effect from 9 December 2010 (see **Withdrawal of extra statutory concessions – technical note**). If the effect of the withdrawal of the concession is likely to cause difficulties, taxpayers are invited to discuss these with HMRC.

The concessions to be withdrawn (with the tax or taxes to which each relates) are:

3.37 VAT– Welfare agencies pending social registration (VAT)

A45 – Life assurance: variation of term assurance policies (IT)

A47 – House purchase loans made by life offices to staff of insurance associations (IT)

B7 – Benevolent gifts (IT and CT)

C27 – Life assurance business: calculation of investment return and profits (CT)

F1 – Mourning: as a funeral expense (IHT)

F2 – Property of Roman Catholic religious communities (IHT)

VAT Ofsted Inspections (VAT)

The ring fence: interaction of finance costs and transfer pricing (Tonnage Tax)

Draft legislation has also been put forward in **Extra statutory concessions: third technical consultation on draft legislation** to enact the following concessions:

A10 – Lump sums paid under overseas pension schemes (IT)

A31 – Life assurance premium relief by deduction: pre-marriage policies: premium relief after divorce (IT)

A51 – Repayment supplement: life assurance premium relief (IT)

A81 – Termination payments and legal costs (IT)

C4 – Trading activities for charitable purposes (IT and CT)

Qualifying life assurance policies – reinstatement within 13 months (IT)

4.5: Insurance premium tax: arrangements for discounted insurance (IPT)

Comments are invited on whether the draft legislation gives legislative effect to the tax treatment afforded by the concession. Tax Faculty members should send any views to angela.williams@icaew.com.

EQUITABLE LIABILITY (PBRN34)

Under the practice of equitable liability, where a taxpayer in self-assessment has not submitted a tax return and has missed all deadlines to displace HMRC's determinations of their liability, HMRC will still forego any tax that is legally due but which the taxpayer can show is excessive.

The 2009 Budget contained a proposed to abolish this concession. However, following representations from a number of bodies (including the Tax Faculty) and individuals, the Government has re-considered and has confirmed that the practice of equitable liability will be incorporated in legislation.

We do not yet know the start date or details of the new legislation. Until then the existing practice will continue.

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