BUDGET SUMMARY...

Briefing

April 2009

OVERVIEW

Leopards do not generally change their spots and that is certainly the case here. Making no apologies for the final abandonment of its manifesto promise, the Government has accelerated and increased its proposed top rate of tax, deprived those with high incomes of personal allowances and reduced the rate at which they obtain relief on pension contributions. The Government argues that these changes are justified in the light of current economic difficulties and that it is only fair to ask those best able to pay more to make an additional contribution for the benefit of the majority. However, as these changes will not affect more than a small percentage of taxpayers, and are unlikely to make an enormous overall contribution to the public sector finances, it is hard to avoid the suspicion that this is an old fashioned attempt to redistribute wealth buoyed up by the wave of public disenchantment with highly paid bankers. Similarly the application of the 50% rate to all trusts regardless of their income level despite representations seems evidence of the Government's continuing antipathy to trusts rather than an attempt to raise revenue. The denial of higher rate relief for pension contributions seems particularly arbitrary, and it would have been fairer to have capped relief, rather than withdrawing it altogether.

Against expectations there is to be no change to the rate of Capital Gains Tax. Whilst this may simply reflect the fact that an increase would be unlikely to generate much revenue in the current economic circumstances, the growing disparity between the rates of taxation of investment gains and income is difficult to justify and hard to envisage being sustained.

There are some highly disingenuous comments in the Budget Press Releases. The failure to admit clearly to the capping of higher rate relief on annual pension premiums is deeply questionable. The claim that increased levels of ISA investment for the over 50s is to help them prepare for retirement does not sit well with the restriction in the relief given for pension contributions for high income earners or the fact that all ISA investors will enjoy similar limits only six months later. Similarly, the proposal for HM Revenue & Customs ("HMRC") to produce a Charter is inconsistent with its increasingly adversarial attitude to taxpayers and the acquisition of ever more draconian powers.

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The current economic climate and the need to avoid wholesale failure of businesses has made the Government extend the provisions for loss relief and there are some helpful provisions for Capital Allowances. There are also changes to encourage investment in certain types of collective investment scheme, and some minor provisions to appease the Green Lobby. The taxation of foreign dividends and collective investment funds has been improved, clearly with the aim of making the UK more attractive to investors. Whether this will compensate for the consequences of the personal tax rises may be doubted.

While there are some generally helpful amendments to the complicated remittance rules affecting non-domiciled residents of the UK, these changes go nowhere near far enough to clarify the uncertainty caused by poor drafting and unnecessary complexity. It should be a cause of disquiet that so much ground has had to be covered in published correspondence between HMRC and the professional bodies which does not have force of legislation and is probably not admissible in a Court of law. There is a growing concern that HMRC prefers to use means other than legislation to define matters for precisely these reasons, encouraging legislation by regulation and practice statements, rather than by statute.

It may also be a cause of dismay to observe the increasingly adversarial attitude adopted by HMRC. This Budget announces further increases in HMRC's powers to enquire into taxpayers' affairs, impose penalties, and to publish the names and personal details of taxpayers who have "deliberately" understated tax due of more than £25,000. There are also provisions for taxpayers to be subject to continual reviews for five years, if after an enquiry they have received a penalty in excess of £5,000. While the language of the Press Releases emphasises that these provisions are for those who deliberately understate tax or fail to co-operate fully, in practice it is to be feared that these provisions will be used to intimidate less culpable taxpayers in investigation cases.

It remains to be seen whether this Budget will do anything for the frightening and rising level of public sector debt, the repayment of which is a major concern for the long term health of the economy.

1. CHANGES TO PERSONAL TAXES AND ALLOWANCES

From 6 April 2009 the personal tax allowance has increased from £6,035 to £6,475, and the age related allowances for those over 65 and 75 will be increased to £9,490 and £9,640 respectively. The 10% starting rate continues to apply only to savings income (excluding dividends) up to a limit of £2,440, providing that the individual's non savings income does not exceed £2,440. The 40% higher rate of tax will apply to income over £37,400. Full details of the rates and allowance for 2009/10 are given in the tax rate card.

From 6 April 2010 it has been announced that there will be substantial changes to personal taxation particularly for individuals with income in excess of £100,000. The basic personal allowance will be subject to a single income limit of £100,000. Where taxpayers' adjusted net income (explained below) is below this amount, they continue to be entitled to the full basic personal allowance. Where their adjusted net income exceeds the £100,000 income limit, the amount of the allowance will be reduced by £1 for every £2 of income above the limit.

Adjusted net income is calculated by taking an individual's total income subject to Income Tax, and deducting specified items such as trading losses, grossed up Gift Aid contributions and grossed up pension contributions.

From 2010/11 there will be three main rates of income tax: the basic rate of 20%, the higher rate of 40% and the additional higher rate of 50%, which will apply to taxable income in excess of £150,000. The Pre-Budget Report in 2008 contained an announcement that the additional rate would be set at 45% and introduced from 2011/12, but the rate has now been increased and the start date brought forward by a year.

There will also be three rates of tax for dividends. Dividends otherwise taxable at 20% will continue to be taxed at 10%, dividends otherwise taxable at 40% will continue to be taxed at 32.5% and dividends otherwise taxable at the new additional higher rate will be taxable at a new dividend rate of 42.5%. The same principle will apply to trustees, with the dividend trust rate increasing to 42.5% and the trust rate to 50% whatever the level of income.

2. UK PERSONAL ALLOWANCES AND RELIEFS FOR NON-RESIDENT INDIVIDUALS

The Personal Allowance and Blind Person's Allowance are available to individuals who are not resident in the UK as long as those individuals fall within one of the categories specified by statute. One of these categories is Commonwealth citizens. In order to comply with the Human Rights Act, this category is removed from 6 April 2009. However, in the majority of cases an individual resident in a Commonwealth country will be able to claim these allowances by virtue of the applicable Double Tax Treaty. Those affected are therefore limited to residents of 14 countries, the most significant being Bahamas, Cameroon, Mozambique and Tanzania.

3. PENSIONS

3.1 Limiting tax relief for high income individuals

Higher rate tax relief on pension contributions is to be restricted.

Currently, higher rate taxpayers have enjoyed tax relief on their pension contributions at their 40% marginal rate of Income Tax.

From 6 April 2011 higher rate tax relief on pension contributions made by individuals with an income in excess of £150,000 will be restricted or withdrawn. The withdrawal will operate by tapering away the higher rate tax relief where income exceeds this amount and higher rate tax relief will be lost altogether once an individual's income reaches £180,000.

To prevent individuals increasing their pension contributions before 2011, a complex set of anti-forestalling rules is proposed, to take immediate effect. These have the potential to catch individuals with an income above £150,000 in the relevant year or the preceding two years, who make contributions less frequently than quarterly or who increase pension scheme contributions (on or after 22 April 2009) in excess of their "normal regular savings". The provisions will apply to contributions made by the individual, his employer and any third party, so clearly advice should be taken where appropriate.

However, it appears that the rules will go far beyond preventing increased contributions. Despite the Press Release implying that individuals who continue with their normal patters of contribution will not be affected, this does not appear to be the case. "Normal Regular Savings" are defined as requiring contributions to be made quarterly or more frequently. Those accustomed to making annual contributions will therefore not qualify, and any contributions (even at identical levels to earlier years) in excess of £20,000 will be denied relief.

3.2 Taxation of payments from the Financial Assistance Scheme

The Government proposes to introduce legislation ensuring pension benefits accruing to individuals from the Financial Assistance Scheme ("FAS") are afforded the same tax privileges as Registered Pension Schemes. Broadly speaking, the FAS is a Government funded scheme to provide pension benefits for individuals whose defined benefit occupational schemes were unable to meet their pension obligations. Presently, pension benefits provided from the FAS are not afforded certain tax privileges (for example a tax-free lump sum), simply because the legislation affords such privileges only to Registered Pension Schemes. Legislation is proposed to ensure benefits from the FAS are treated in the same way as benefits from a Registered Pension Scheme.

3.3 Avoiding unintended tax consequences in relation to pension savings

Similar provisions are proposed in respect of insurance companies providing registered pension schemes who receive assistance from the Financial Services Compensation Scheme.

4. INCREASE IN ISA LIMITS

ISAs provide a tax beneficial way for individuals to invest, particularly those liable to higher rate tax. Although there is no deduction for the sum invested, thereafter the yield is not subject to Income or Capital Gains Tax. The amount which an individual can invest in an ISA in any tax year has always been restricted but the limits have gradually increased over the years generally in line with inflation.

Currently individuals are able to subscribe £7,200 per annum, of which one half (£3,600) can be saved in cash through one provider. The balance must be invested in shares or securities but can be with another provider. With effect from 6 October 2009, individuals aged 50 or over will be able to invest up to £10,200 in an ISA, of which one half (£5,100) can be saved in cash. These limits apply to funds introduced during the tax year 2009/10, but contributions made between 6 April and 5 October 2009 are restricted to current limits.

While this may encourage savings by those approaching retirement, it sits awkwardly with the restriction introduced for higher rate relief on pension contributions. Furthermore, the new limits will apply to all ISA investors, whatever their age, with effect from 6 April 2010, so the incentive for those aged 50 or over is modest indeed.

5. PERSONAL DIVIDENDS

Building on certain changes originally included in Finance Act 2008, for shareholdings of less than 10%, it has been announced that with effect from 22 April 2009, individuals with shareholdings of 10% or more in receipt of dividends from non-UK resident companies will become entitled to a non-repayable tax credit, subject to certain conditions.

Dividends received by individual shareholders are currently taxed at rates of 10% for basic rate and 32.5% for higher rate taxpayers. The non-repayable dividend tax credit reduces the effective rate of Income Tax on these dividends to 0% and 25% respectively.

The tax credit will only be available if the source country of the dividend has a double taxation agreement with the United Kingdom and regulations will be introduced permitting HM Treasury to vary the list of qualifying and non-qualifying territories. Also, the legislation will include anti-avoidance measures to counter the use of conduit structures designed to secure a tax credit for dividend income originating in a non-qualifying territory.

6. DISTRIBUTIONS FROM OFFSHORE FUNDS

In a related development, it was announced that the non-repayable dividend tax credit would also apply to offshore funds which are largely invested in equities. This will apply to all holdings in offshore funds irrespective of ownership, with effect from 22 April.

However, where the offshore fund is invested mainly in interest bearing assets, individuals receiving distributions will be treated as having received interest rather than a dividend. The holding in interest bearing assets must exceed 60% before this rule can apply.

This change will not affect the taxation of UK investors in offshore funds which are transparent for the purposes of tax. In such cases, the investor is taxed on his share of the underlying fund income according to the type of income received and not on the distribution made.

7. FURNISHED HOLIDAY LETTINGS IN THE EUROPEAN ECONOMIC AREA

Landlords with rental income from UK property which qualifies as Furnished Holiday Lettings ("FHL") are currently treated for the purpose of certain UK tax reliefs as if they carried on a trade, including the ability to treat an FHL loss as a trading loss. A property will only qualify for this treatment if it satisfies certain tests. Until now, one of the FHL tests has been that the property must be situated in the UK. It is now apparent that a distinction between UK and European properties may not be compliant with European Law. As a result, the rules will be applied to all qualifying properties within the European Economic Area ("EEA") until 5 April 2010. There are various conditions and advice should be taken where it is felt that a foreign property may qualify.

The normal time limit for amending an individual's Self-Assessment Return is one year after the 31 January following the relevant tax year. However, in this case, HMRC have indicated that they will accept late amendments to 2006/07 Returns up to 31 July 2009. If any individuals have losses on rental properties in the EEA which may qualify for the FHL rules, advice should be sought as to whether to file amended Returns and claim a repayment of tax.

From 6 April 2010, the FHL rules will be repealed for all properties irrespective of their location.

8. NON-DOMICILIARIES - THE REMITTANCE BASIS

8.1 New de minimis limit for requirement to file a Tax Return

Applying retrospectively from 6 April 2008, certain individuals will not be required to file a Self-Assessment Tax Return solely because they are in receipt of foreign employment income. This exemption from the requirement to file a Tax Return will only apply where their overseas employment income is less than £10,000 and is subject to a foreign tax. The exemption also covers overseas bank interest of such an individual, if less than £100, and also subject to a foreign tax.

8.2 Exempt Assets

The exemption from tax for certain remittances (for example works of art on public display) introduced by Finance Act 2008 only applied to assets purchased using Relevant Foreign Income (broadly interest and dividends). These exemptions will be extended to include assets purchased using both foreign chargeable gains and foreign employment income, and

this extension is retrospective, applying from 6 April 2008.

8.3 De minimis exemptions from claims for the remittance basis

From 6 April 2008 a "short-term" resident (who has been in the UK for fewer than seven of the previous nine tax years) was not required to claim the remittance basis (and so complete a Tax Return) if he had made no remittances to the UK, but this only applied if he had no UK source income or gains (of any amount). With retrospective effect from 6 April 2008 there will be no requirement to make a formal claim for the remittance basis if there are no remittances in the year, provided UK income and gains amount to less than £100, and have been taxed at source.

8.4 Remittance Basis and Trusts

Certain transitional provisions will be amended to make clear that a remittance has not occurred in certain circumstances where assets have been acquired by settlor-interested trusts out of income that arose before 6 April 2008, in line with the provisions that apply to income arising to individuals.

The rules regarding the interaction of the remittance basis and the anti-avoidance provisions that apply to settlor-interested trusts are to be clarified, but no specific details have yet been published.

8.5 Gift Aid and the £30,000 Remittance Basis Charge

A specific provision will be introduced to make clear that the £30,000 tax charge can be used to "frank" donations made under the Gift Aid scheme. This will apply from 6 April 2008.

8.6 Minor anti-avoidance amendments

An amendment is to be made to the definition of a relevant person to make clear that subsidiary companies are caught by these provisions.

The provisions regarding the amount remitted when only part of a set or collection (for example part of a stamp collection) is brought to the UK are to be amended to increase the amount treated as remitted.

8.7 Statement of Practice on offshore accounts containing employment income for not ordinarily resident employees

HMRC issued a new Statement of Practice in March 2009 (SP1/09) confirming the continuation of their historic treatment of employment income received by an individual who is not ordinarily resident in cases where earnings subject to apportionment between UK and foreign duties are paid into a foreign bank account. It is intended that this treatment will be given a statutory basis in Finance Act 2010.

9. COLLECTIVE INVESTMENT SCHEMES

9.1 Venture Capital Schemes

The Enterprise Investment Scheme ("EIS"), Corporate Venturing Scheme ("CVS") and Venture Capital Trust ("VCT") scheme are long standing arrangements which provide tax incentives designed to promote investment in unlisted trading companies. A range of technical measures has been announced, with the aim of improving all three schemes and enhancing their appeal.

As regards the EIS, four modifications to the existing rules are proposed. Currently 80% of the funds raised from an issue of shares must be employed for the purposes of the company's trade within 12 months (or within 12 months of the commencement of trading, if later) with the balance being employed during the succeeding 12 months. For EIS shares issued after 21 April 2009, there will be a requirement for 100% of the funds raised to be employed within two years of the date of issue of the shares, or the commencement of trading as appropriate.

For share subscriptions after 21 April 2009 it will no longer be necessary for non-EIS funds raised at the same time as an EIS share issue to be utilised within the same two year period.

The other two modifications affect EIS investors. For share subscriptions in 2009/10 and later years, there will no longer be a restriction on the amount of relief which can be carried back to the previous tax year. Hitherto, carry back relief has been limited to half of any subscriptions between 6 April and 5 October, with an overall restriction of £50,000.

The final change corrects an anomaly and ensures that on a "share for share" exchange involving the disposal of EIS shares in respect of which Capital Gains Tax Deferral Relief has previously been claimed, a charge to tax arises only on the deferred gains.

As regards the CVS and VCTs, the existing 80:20 rule for the employment of funds raised (mirroring that in the EIS code) is to be replaced by a requirement for 100% of the funds raised to be employed for trading purposes within two years, or, if later, within two years of trading commencing. Again, the change applies to any shares issued after 21 April 2009.

9.2 Chargeable Gains and Offshore Funds

A new provision will be introduced (to have effect from 1 December 2009) to treat certain offshore funds that are constituted as contractual arrangements as opaque for Capital Gains Tax purposes. This will mean that investors will only be charged to Capital Gains Tax on disposals of interests in such funds, and not on the

underlying transactions undertaken by the funds. This new provision will not apply to funds constituted as companies or unit trusts (which are treated as companies). Except in the case of interests exceeding 10% in what would otherwise be closely held companies, such funds are already treated as opaque for Capital Gains Tax. It will also not apply to partnerships, which will in general continue to be treated as transparent.

9.3 Offshore Funds

As previously announced and following extensive consultation, a new definition of what constitutes an offshore fund for the purposes of the Offshore Income Gain legislation is to be introduced. The rules will adopt the terminology of "Reporting" and "Non-Reporting" Funds. The new definition will be "characteristics based" as opposed to the current definition which is based on the definition of a "collective investment scheme" contained in the Financial Services and Markets Act 2000. There will be "grandfathering" provisions to cover funds that will change status following the change in the definition.

In addition, as also previously announced, changes to the Offshore Income Gain provisions will be introduced through regulations.

This new regime for offshore funds will take effect from 1 December 2009. This represents a delay and may indicate that earlier proposals are to be substantially revised.

9.4 Authorised Investment Funds (AIFs) and Investment Trust Companies (ITCs)

There are two related provisions designed to allow a more tax efficient streaming of income from interest-bearing investments to the investors in AIFs and ITCs.

Both AIFs and ITCs are liable to Corporation Tax on their taxable income but, in broad terms, enjoy exemption from tax on capital gains. Distributions to most UK resident investors are treated as dividend income and, where the investor is a higher rate taxpayer, the applicable rate is 32.5% (subject to a non-repayable 10% tax credit). Thus, effectively, interest income is taxed within the fund and the net profit distributed is then subject to further tax at investor level.

Broadly parallel revisions for each type of fund are proposed.

Thus AIFs will, from 1 September 2009, be permitted to make an election to be treated as a Tax Elected Fund ("TEF"). When distributing income to investors, TEFs will be required to differentiate between distributions out of dividend income (which is not taxable at fund level) and distributions out of interest income. The TEF will then receive a Corporation Tax deduction for the interest distribution. The net effect will be to enable a TEF to distribute its interest to investors gross, without suffering Corporation Tax at fund level. Although the UK investor will pay Income Tax on the interest distribution at the main Income Tax rate rather than the dividend rate, overall net income for the investor will be enhanced. An overseas investor would, in most cases, pay no UK tax on the distribution. This brings the treatment of the fund's interest income into line with that of its dividend income and the investor is treated effectively as having received it directly.

Similar provisions will be introduced for ITCs.

This measure is helpful in maximising the post-tax return on interest income for investors in UK authorised funds and is to be welcomed. In particular, it will enable UK funds to compete on level terms with foreign funds which have enjoyed similar treatment. However, only AIFs which "meet certain conditions" will be eligible to make the election and it remains to be seen what these conditions are.

As already observed, AIFs are subject to tax on their income profits, which would include the profit from trading transactions and not just passive investment income. However, it is not always clear whether a profit on a transaction falls to be treated as a capital gain or a trading profit, when there is a bewildering range of short and medium term investment opportunities.

It is now proposed that secondary legislation will be introduced to publish a "white list" of transactions which, when carried out by a "qualifying AIF", will not be characterised as trading. The same "white list" can also be relied upon by an "equivalent offshore fund", which will be concerned to differentiate between capital gains and income in order to meet its obligations under the new "reporting fund" regulations (the introduction of which is described at 9.3 above).

There are, however, two caveats. The list can only be relied upon by a "qualifying AIF", or an offshore equivalent. To qualify, the fund will need to meet a "genuine diversity of ownership" condition. Although there are as yet no details, this will probably exclude Private Authorised Unit Trusts or Private OEICs.

Secondly, there is clearly a concern that access to the "white list" may prompt financial traders, such as banks and securities dealers, to route their transactions through AIFs. Financial traders holding interests in "white listed" AIFs and offshore equivalents will therefore be required to bring realised and unrealised profits in such funds into their own trading accounts.

Publication of detailed regulations will assist in clarifying HMRC's view as to what types of investment

transactions they regard as constituting a trading activity. It will be interesting in due course to see how "diversity of ownership" is to be defined.

10. INHERITANCE TAX

The nil-rate band has increased from £312,000 for 2008/09 to £325,000 for the current 2009/10 tax year. It will increase again to £350,000 for 2010/11. These increases were set in FA 2006 and FA 2007.

In January of this year, the European Commission requested the UK to amend its "discriminatory" legislation which restricted Inheritance Tax relief for agricultural property to qualifying assets situated in the UK, the Channel Islands and the Isle of Man. The Government has responded in the Budget by expanding the scope of Inheritance Tax Agricultural Property Relief and Woodlands Relief to qualifying property situated anywhere in the European Economic Area ("EEA"). Such property also qualifies for Capital Gains Tax Hold Over Relief.

Claims may be made for relief retrospectively in relation to any Inheritance Tax paid on EEA situated agricultural property within the last six years, ie on or after 23 April 2003. The earliest deadline for reclaiming Inheritance Tax will be 21 April 2010. Retrospective claims for Capital Gains Tax Hold Over Relief since 2003/04 can also be made, although the deadline for this year will be 31 January 2010.

11. CHARITIES

11.1 Substantial Donor Regulations

Certain transactions between charities and "substantial donors" which take place within a six year period following a qualifying donation will result in a tax charge arising as if the expenditure was for non-charitable purposes. The definition of a "substantial donor" is to be amended so as to increase the level of donations required to qualify. The current threshold of £100,000 in any six year period will increase to £150,000. The annual threshold of £25,000 remains.

12. ANTI-AVOIDANCE

12.1 Employment Income

Following an announcement by the Financial Secretary to the Treasury on 13 January 2009, it has been confirmed that legislation will be introduced to block a range of tax avoidance schemes designed to create employment-related liabilities and losses. The schemes have sought to take advantage of the statutory relief for losses incurred by an employee, which are eligible for relief against income of the year of loss, the previous year, or both. Techniques have included contrived employments coupled with the deliberate triggering of artificial damages or compensation liabilities. They will be blocked in relation to losses incurred after 11 January 2009 (regardless of when the arrangements which resulted in the loss were entered into), but do not affect claims to employment loss relief made on or before that date.

The new restrictions on employment tax relief are subject to a motive test. They will not operate where the arrangements giving rise to a loss claim were not made with the purpose of avoiding tax.

12.2 Life Assurance Policies

Following an announcement on 1 April 2009, legislation will be introduced to counter avoidance schemes which have sought to create Income Tax losses from offshore life insurance policies. The stated aim is to put "beyond doubt" that tax relief is not available in respect of such policies, and to bring their treatment fully into line with that of life policies written by UK insurers.

The new rules will apply to any assignments or surrenders of offshore life insurance policies after 5 April 2009. There will also be transitional provisions for the tax year 2008/09, in order to prevent a claim for Income Tax relief in respect of transactions taking place after the 1 April 2009 announcement.

13. BUSINESS TAX

13.1 Dividends received by UK Companies

The Government has confirmed the introduction of a tax exemption for most foreign dividends received by UK companies. This will apply to dividends and other distributions received on or after 1 July 2009.

Foreign dividends received by UK companies are currently chargeable to Corporation Tax, with credit given for any foreign tax withheld from a dividend, and (for shareholdings of 10% or more) for foreign tax charged on the profits out of which the dividend is paid (underlying tax). Currently UK dividends received are generally exempt from Corporation Tax. The new rules will exempt from UK tax all foreign and UK dividends which fall into an "exempt class". It seems clear that this will exempt foreign dividends derived from shareholdings of more than 10%. It is not clear whether it will also apply to smaller shareholdings. However, the exemption will apply to all UK companies, regardless of size.

13.2 Worldwide Debt Cap

The Government has confirmed the introduction of a "Worldwide Debt Cap", which will restrict the tax deduction available for interest payable by UK members of a group of companies to the consolidated gross finance expense of that group. The debt cap will apply to finance expenses payable in accounting

periods beginning on or after 1 January 2010, and will only apply to companies in "large" groups.

13.3 Controlled Foreign Companies (CFCs)

The CFC (superior and non-local) holding company exemptions, and Acceptable Distribution Policy ("ADP") exemption will be removed for accounting periods starting on or after 1 July 2009 with provision made for accounting periods that straddle this date. However, the exemption for non-local and superior holding companies may be available for qualifying companies in a transitional form until 1 July 2011.

13.4 Treasury Consents

The existing Treasury Consent legislation requires companies to obtain approval from HM Treasury before undertaking certain transactions involving subsidiary companies resident outside the UK. The legislation includes a criminal sanction for non-compliance.

The Government has announced that, for transactions undertaken on or after 1 July 2009, the existing legislation will be repealed, and that in its place a post-transaction reporting requirement will be introduced that will apply to transactions with a value of at least £100m. Companies will be required to make a report of the relevant transaction within six months.

13.5 Capital Allowances

The Chancellor announced that, for a one year period, any business (ie company, individual or partnership) will be able to claim a First Year Allowance ("FYA") of 40% for expenditure on general plant and machinery. This expenditure would normally attract a writing down allowance of only 20%.

The FYA will apply to qualifying expenditure incurred (with no upper limit) in the 12 month period beginning 1 April 2009 for the purpose of Corporation Tax, and 6 April 2009 for the purpose of Income Tax. Special rate expenditure (long life assets and expenditure on integral features), cars and assets for leasing will not be eligible for FYAs.

13.6 Small companies' rate of Corporation Tax

Companies with profits chargeable to Corporation Tax lower than £300,000 are currently liable to Corporation Tax at 21%. This was due to be increased to 22% from 1 April 2009, but this plan has been abandoned, and hence the 21% rate will continue in force for the time being.

13.7 Extension of carry-back loss relief

The temporary window to permit companies to carry back losses of up to £50,000 for three years has been extended from November 2009 to November 2010.

13.8 Release of a trade debt between connected companies

It was announced that, on the release of a trade debt between connected companies, the loan relationship rules will now apply to the debtor company as well as to the creditor company. This means that if the debtor company is connected with the creditor, a tax charge will no longer arise on the debt release. This change will apply to releases of trade debts that take place on or after 22 April 2009.

13.9 Interest payable between connected companies

Currently, a UK debtor company is not permitted a tax deduction for interest payable to a connected non-UK creditor on an "accruals" basis. A tax deduction is only available on a "paid" basis. However, the Government has now announced that a tax deduction will be available on an "accruals" basis for company accounting periods beginning on or after 1 April 2009, provided that that the creditor is not resident in a "non-qualifying territory" (broadly, a tax haven).

13.10 Personal accountability of senior acounting officers of large companies

The Government has proposed to make senior accounting officers of "large" companies personally accountable if they fail to maintain accounting systems which are adequate to ensure accurate tax reporting. This new legislation, to be introduced in Finance Bill 2009, will require a large company to notify HMRC of the identity of its "senior accounting officer", and for that person to:-

- Establish and monitor accounting systems that are adequate for accurate tax reporting; and
- Certify this annually or specify any inadequacies, and confirm that these have been notified to the company's auditors.

Penalties will be introduced for careless or deliberate failure to comply with these new rules. These penalties will be chargeable personally to the senior accounting officer, as well as to the company.

13.11 Other business tax changes

Minor technical changes were announced to the tax rules relating to the sale of lessor companies, the impact of preference shares on group relief, the calculation of foreign denominated losses, the reallocation of chargeable gains within groups, the rate of double tax relief on dividends, and the definition of "goodwill" within the intangible assets regime.

A large number of targeted anti-avoidance provisions were announced in the Budget to shut down tax avoidance schemes that involved convertible bonds, derivative contracts, sale and leasebacks, foreign

exchange matching, transfers of income streams, disguised interest, manufactured interest, manufactured overseas dividends, and the repayment of foreign tax.

14. EMPLOYEE LIVING ACCOMMODATION

Subject to a limited number of exceptions for certain categories of job-related accommodation, directors and employees are subject to Income Tax on the benefit of living accommodation provided by reason of their employment. The quantum of the annual benefit-in-kind is ascertained by applying a formula linked to the cost of providing the accommodation, normally a percentage of the capital cost if owned or the rent paid by the employer if leased.

Certain employers have sought to minimise the tax charges for employees by entering into arrangements involving lease premiums coupled with a reduced rent. In order to counteract this, changes are to be introduced for leases entered into or extended after 21 April 2009. The new rules will apply to leases of 10 years' duration or less which are accompanied by the payment of a lease premium. In such cases the premium will be spread on a time basis over the term of the lease and a pro-rata element will be taxed in each year, aggregated with any rent actually paid for that year. However, the anti-avoidance rule will not apply to leases on properties used mainly for a business purpose by the employer and only partly as employee accommodation.

15. CHANGES TO COMPANY CAR TAX FROM 2011/12

Where a car is made available to an employee for his or her personal use a taxable benefit arises. The benefit is calculated by applying the appropriate percentage to the list price of the vehicle, based upon its CO_2 emission figure.

From 2009/10 the starting rate of 15% will apply to all petrol vehicles with a lower threshold CO_2 emission figure of 135g/km, and this will increase by 1% for every 5g/km above 135g/km to a maximum of 35% on vehicles with a CO_2 emission of 235g/km and above. The appropriate percentage is increased by 3% for diesel vehicles but the maximum of 35% still applies.

For 2010/11 the lower threshold CO_2 emission figure will be reduced to 130g/km and for 2011/12 it will be further reduced to 125g/km.

The lower rate of 10% (13% for diesels) continues to apply to vehicles with a CO_2 emission of 120g/km and below.

From 2011/12, the £80,000 price cap will be abolished and there will be no upper limit.

The current discounts for cars using various alternative fuels will be discontinued from 2011/12, but electrically propelled cars will continue to be taxed at 9% of their list price.

16. VALUE ADDED TAX (VAT)

With effect from 1 May 2009 the VAT registration threshold will be increased to £68,000 and the de-registration threshold will be increased to £66,000.

From 1 May 2009 there will be a simplified procedure for those wishing to opt to tax (apply VAT to supplies in relation to) land and buildings on which they have made previous exempt supplies.

Legislation will be introduced to counter schemes that take advantage of the current 15% VAT rate for goods and services to be supplied after the re-institution of the 17.5% rate on 1 January 2010.

There will be technical changes for businesses involved in supplying services to or receiving services from other member states of the EU. These changes will be phased in over a period of three years with effect from 1 January 2010. The most significant change that will take place from 1 January 2010 will be for those businesses that supply services to customers registered for VAT in other member states of the EU. From 1 January 2010 the supplier will have to complete an additional declaration known as an "EC Sales List" (ESL) for each calendar quarter, declaring the customer's VAT registration number allocated in the customer's EU member state and value of the supplies made.

A further announcement by the Chancellor affects dealers in second-hand vehicles. An extra-statutory concession assists dealers who do not retain evidence of both selling and purchase price of a vehicle by allowing the VAT on the sale to be accounted for on the profit margin. With effect from 1 April 2010 this extra-statutory concession will be withdrawn and in future if a dealer fails to retain evidence of both the selling and purchase price, VAT will be due on the full selling price.

17. STAMP DUTY LAND TAX (SDLT)

The temporary increase in the SDLT threshold introduced in September 2008 for an initial one year period has been extended until the end of 2009. Residential property worth not more than £175,000 is exempt from SDLT for transactions made before the end of the year. After that date the threshold will revert to the previous level of £125,000.

18. HMRC POWERS AND PROCEDURES

18.1 Review of HMRC powers, deterrents and safeguards

Changes are to be made following consultation as part of the ongoing work of the Review of HMRC's Powers, Deterrents and Safeguards and Tax Administration project. The Government's aim is to provide a modern framework of law and practice for HMRC. The changes are to be introduced on a staged basis, commencing with the date on which the 2009 Finance Act receives Royal Assent.

18.2 Payment, Repayments and Debt

Three changes relate to payments of tax. Firstly, voluntary managed payment plans will allow taxpayers to spread their Income Tax or Corporation Tax payments equally over a period straddling the normal due dates. Secondly, HMRC will have the power to collect small debts through the PAYE system. Finally, HMRC is to be given power to require companies and businesses to provide contact details for people who owe tax.

18.3 Compliance

The 2008 Finance Act contained provision for new compliance requirements. These included powers to obtain information and documents, requirements for record keeping and changes to time limits for assessments and claims. These provisions are to be extended to other taxes including Inheritance Tax and Stamp Duty Land Tax.

The new framework includes the power to inspect statutory records required by the record keeping legislation, and to visit business premises and inspect records and assets. These changes will commence from a date to be announced by Treasury Order, expected to be 1 April 2010.

The time limits for claims are to be aligned, generally adopting a four year period. Many Income Tax and Capital Gains Tax claims need to be made within five years following the 31 January after the end of the relevant tax year; this period will be reduced to four years from the 31 January. These time limit changes will be subject to a transitional period and are not expected to become fully operative until 1 April 2011.

18.4 Penalties

The 2008 Budget announced the Government's intention to introduce a single penalty regime applying to all taxes administered by HMRC.

The 2007 and 2008 Finance Acts introduced a new penalty regime for errors in documents. For Income Tax purposes, this will apply to tax returns for 2008/9 onwards. Penalties are fixed as a percentage of potential lost revenue. The percentage depends on whether the error was "careless" (up to 30%), "deliberate but not concealed" (up to 70%) or 'deliberate and concealed' (up to 100%).

New announcements deal with late payment of tax and late filed returns. Broadly, the same penalties will apply to the main taxes including Income Tax, Corporation Tax, Stamp Duty Land Tax, Inheritance Tax and pension schemes, with modifications for PAYE and construction industry schemes.

Implementation will require changes to computer systems and will be made over a number of years, starting with the penalties for the late payment of PAYE, from April 2010. The provisions will be brought into effect by Treasury Orders which will specify the dates from which they have effect.

Penalties for late filing are to include a £100 penalty (whether or not the tax has been paid); daily penalties of £10 per day for returns more than three months late, running for a maximum of 90 days; and penalties of 5% of tax due if the returns are six months late, and again at 12 months.

Penalties for late payment include 5% of the amount unpaid, and will generally apply one month after the due date; and further penalties of 5% of any amounts of tax remaining unpaid at six and 12 months.

The PAYE penalties will depend on the number of defaults in any 12 month period. The taxpayer will not receive a penalty on the first occasion of default, but a second late payment and any subsequent failings in the period will attract a penalty of 2% of the tax unpaid rising to 5% of the tax unpaid.

18.5 Tribunals

Although not part of the Budget speech, it is worth noting the new system of tax tribunals which commenced on 1 April 2009.

Previously, most appeals on tax matters were heard by the General and Special Commissioners. A specialist tribunal heard appeals on certain anti-avoidance provisions, and the VAT and Duties Tribunal dealt with indirect tax. Each tribunal had its own rules and procedures.

On 1 April 2009 the four tax tribunals were abolished, and their functions transferred to a new two tier tribunal system. The taxpayer will now be responsible for making an appeal on any tax matter; in contrast to the previous position where HMRC controlled the process on direct tax matters.

The First-Tier tribunal has a dedicated Tax Chamber to consider appeals against HMRC decisions. There will be a right of appeal, with permission from the First-Tier Tax Chamber, to the Finance and Tax Chamber in the Upper Tribunal. This is made up of High Court judges as well a specialist tax judiciary. Appeals from the Upper Chamber are to be the Court of Appeal.

18.6 Reclaiming overpaid Income Tax, Capital Gains Tax and Corporation Tax

New legislation is introduced which will amend the means of reclaiming overpayments of Income Tax, Capital Gains Tax and Corporation Tax where there is no other statutory route. Currently the legislation for error or mistake claims allows an individual five years 10 months to reclaim tax owing to a mistake in the Tax Return. From 1 April 2010 repayments must be claimed within four years and rules will be introduced to regulate the grounds for any claim. The current restrictions on the right of appeal will be removed, allowing an appeal to the courts on the same grounds as appeals against other tax decisions.

18.7 Interest Harmonisation

New legislation will create a harmonised interest regime for all taxes and duties administered by HMRC (initially with the exception of Corporation Tax and Petroleum Revenue Tax, which will be introduced in Finance Bill 2010) and Class IV National Insurance contributions. This system will apply to underpaid tax and refunds of overpaid tax, and this will provide for the automatic setting of rates calculated by reference to the Bank of England base rate. The new regime will be brought into effect at varying stages as HMRC's computer systems are updated, from April 2010 onwards.

18.8 Publishing the names of deliberate tax defaulters

Under the new taxpayers' compliance regime, HMRC will have the power to publish the names and details of taxpayers who are subject to a penalty for either deliberately understating tax due (including overstating claims or losses), or deliberately failing to notify HMRC when required to do so, if the tax at risk exceeds £25,000. Only those taxpayers who have been penalised for deliberate defaults or concealment under the new penalty regime will have their details published, and not simply those taxpayers who are penalised for failing to take reasonable care.

There will be an exemption for taxpayers who make a full unprompted disclosure of the default, or make a full prompted disclosure to HMRC within a specified time. The publication is subject to a right to appeal. If a taxpayer's details are published, they will be listed on HMRC's website within 12 months of the penalty becoming final and will remain there for 12 months.

In addition, taxpayers who incur a penalty of £5,000 or more will be required to submit more information on their Tax Returns for up to five of the following years.

19. HMRC CHARTER FOR TAXPAYERS

Legislation will be introduced requiring HMRC to prepare and maintain a Charter which will set out the standards of behaviour and values to which HMRC will aspire in dealing with taxpayers and others. The legislation will require the Commissioners of HMRC to report annually on HMRC's performance in meeting the standards in the Charter. HMRC plans to launch the Charter by Autumn 2009.

20. NEW OFFSHORE DISCLOSURE FACILITY

A new disclosure opportunity is announced for taxpayers with unpaid tax relating to offshore accounts. The window will run from Autumn 2009 to March 2010 and will give an opportunity to disclose any unpaid liabilities with a lower level of penalty than might otherwise be applied under the normal rules. The level is yet to be announced. Interest will remain chargeable without mitigation.

BUDGET SUMMARY...

This Briefing Note provides a commentary on those parts of the Budget which we think will be of specific interest to our clients and contacts.

The information contained in this briefing does not constitute advice and is intended solely to provide the reader with an outline of the provisions. It is not a substitute for specialist advice in respect of individual situations.

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