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# Budget 2011 KPMG Commentary

What it means for you

March 2011

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## Our view



**Anneli Collins**  
Head of Tax Policy

Today's Budget was in general a good budget for business, but there were a few offsetting disappointments. The forthcoming year will be very busy with consultations which have been announced in the Budget.

The further reduction in the main corporation tax rate to 26 percent from April 2011 will be welcomed by companies with larger profits, although it will have no impact on smaller businesses with profits below £300,000 whose corporation tax rate will be 20 percent from April 2011.

Legislation will be introduced in Finance Bill 2011 to exempt the profits of foreign branches of UK resident companies from corporation tax on an elective basis. The changes to the draft legislation should make it easier for companies such as some financial institutions that currently have losses in one or more of their branches to benefit from the regime.

Following consultation, the Government has announced that a number of changes are to be made to the Controlled Foreign Companies (CFC) interim improvements to make it easier for businesses to benefit from them. No further details have been provided at this stage. Similarly, the Government will continue to consult about the patent box with legislation expected in Finance Bill 2012.

Subject to obtaining state aid approval from the European Commission, the rate of additional deduction for expenditure on research and development by small or medium sized companies will be increased to 100 percent from 1 April 2011, giving a total deduction of 200 percent. Other changes will be made to simplify the relief.

A statutory residence test for individuals is being introduced to take effect from 6 April 2012. It is positive to have such a test but whether it will make determining residence more straightforward will depend on the precise test. More will be known after the consultation in June 2011.

There are three measures affecting non-domiciles to start from 6 April 2012 after a consultation document due in June. The annual £30,000 charge will be increased to £50,000 for those non-domiciles who have been resident for more than twelve years. There will be no tax charge if non-domiciles remit foreign income or gains to the UK for commercial investment in UK businesses. Technical simplification will be made to some aspects of the current rules for non-domiciles to remove undue administrative burdens.

The budget brought very welcome news for entrepreneurs by doubling the Entrepreneurs' Relief lifetime limit to £10million from 6 April 2011. There

have been no changes in the qualifying conditions but where the conditions are met this will be worth a maximum tax saving of £1.8million.

The government is proposing a range of changes that will affect the full range of state, public and private sector pension provision. Most of these measures are known only in outline at the present time, with detailed consultation to follow.

The Government has announced that it will consult on the potential integration of the operation of income tax and National Insurance Contributions (NIC). A consultation document will be published later this year. The Chancellor stated that any change would be complex and involve a wide range of policy and implementation issues. It will be a number of years before any merger could take place. In the long term this is likely to reduce the high costs of businesses running these two taxes side by side through the payroll.

The Government has confirmed that it will introduce new disguised remuneration rules to counter tax avoidance by employers and employees via the use of trusts and benefits such as loans. Following consultation, the Government have confirmed that they have amended the legislation to limit the impact on employers and individuals "where it is possible to identify arrangements that cannot be used for avoidance purposes". Employers will need to review very carefully all their remuneration arrangements which involve any party other than the employer to determine whether and to what extent they could be impacted.

The simplification of the tax system by the abolition of tax reliefs will help reduce its complexity. However, it will be important to consider the detail to ensure that significant benefits are not being taken away. Further consultation awaits.

The IR35 régime (the employment intermediaries' legislation) is being retained, following a review by the Office of Tax simplification. However, the administration is to be simplified, HMRC is to provide a dedicated helpline and set up a forum to engage with interested parties. It is hoped that these changes will ease the impact of IR35.

A number of rather minor announcements regarding VAT were made, many of which will not come into effect until 2012. Many consultations were also announced.

Two business sectors will be feeling hard done by today: the North Sea oil and gas producers who are paying for the reduced fuel duties on petrol and diesel by an increase in the supplemental charge from 20 percent to 32 percent. The proposed tax increases can only reduce the attractiveness of investment in the North Sea. The potential for this supplemental charge to be reduced if the oil price falls will be of no consolation to the UK's oil and gas producers.

Banks and building societies will be disappointed by the increase in the Bank Levy rates for 2012 and subsequent periods. Of particular concern will be the uncertainty that has been caused by two changes to the Bank Levy rates in successive months. UK headquartered banks are at a disadvantage to foreign banks, as they pay the banking levy on their worldwide balance sheets, rather than just their UK balances. With British

taxpayers as significant owners in two of the major banks, could this tending towards a tipping point where the UK banking sector is being put at a competitive disadvantage to banks overseas?

# Economic Implications



**Andrew Smith**  
Chief Economist

Theoretically this budget counts as broadly “neutral” since the main austerity measures were pre-announced last year. But in practice the fiscal stance is anything but. In 2011-12, current receipts are due to rise by one percent of GDP, reflecting principally increases in VAT and National Insurance Contributions, while spending cuts of a similar size are in the pipeline. In this context, these latest measures cancel each other out. The fuel duty reduction this year is worth almost £2bn but the chancellor is recouping this from North Sea producers.

Thus boxed in, this “budget for growth” has had to rely on relatively low cost efficiency measures aimed at improving the working of the economy, ranging from resuscitating enterprise zones, through de-regulation, to training and apprenticeships to combat youth unemployment. While welcome, supply-side improvements are no quick fix and take time and persistence to come to fruition.

The focus of deficit reduction is on spending cuts and tax rises, but it is also crucially dependent on a return to robust GDP growth. The fall in fourth quarter output has had a knock-on effect on the economic forecast for this year and next, but growth is projected to get back on track further out. To date, though, there is little evidence of the promised rebalancing of the economy. Consumer spending is certainly taking a back seat – this year’s forecast increase has been halved - but exports and business investment have yet to take off.

Slower growth and higher inflation - which is pushing up government spending faster than receipts – have already resulted in some slippage in the deficit reduction programme before it has really begun, but the OBR still thinks the Government is on track to eliminate the structural deficit by 2015-16.

As far as policy is concerned we are in uncharted waters with interest rates around zero. Perhaps the greatest risk is that the Chancellor’s strategy relies on monetary policy remaining loose to offset the tight fiscal stance - but this is outside his control and the MPC is becoming increasingly concerned about above target inflation.

# Public Sector Implications



**Alan Downey**  
Head of Public Sector

The Chancellor's ambitious budget for growth needs to be coupled with an equally ambitious programme of public sector reform.

Any plan for growth will only succeed if it also involves the transformation of our public services. Efficient and well-directed public sector spending can help to support and boost the private economy, not just by supporting it through a strong infrastructure and a well-educated workforce, but also by making Britain an attractive place to live and do business.

In a time of unprecedented cuts and a strong commitment on achieving challenging targets for spending reductions many public bodies may be tempted to reduce the frontline provision of services by cutting community health facilities, nurseries, services to older and vulnerable people, arts and cultural events, or programmes to increase labour participation. In order to stop public bodies taking the easy route to cuts and thereby harm the long-term competitiveness of the UK economy, the Government should not shy away from radical structural reform.

Over the last decade UK public bodies have fallen well behind private companies in productivity. According to the Office for National Statistics productivity in the public sector declined by more than 3% between 1997 and 2007, while among service providers in the private sector, it improved by more than 20% during that period. This has placed a huge and unnecessary strain on the whole UK economy. Reducing public spending alone will not increase efficiency – a radical reform must accompany the cuts.

Allowing the private and voluntary sector to participate in this process is critical. The chancellor rightly points out that the UK has one of the most innovative and creative business services sectors. It also has charities and voluntary organisations that are recognised world leaders in their respective fields. The government has the opportunity to benefit from this latent knowledge and enthusiasm by engaging these organisations in reform by stating the problems and allowing all providers - in-house, private or voluntary – to come up with new, innovative solutions rather than just contracting with them for 'doing the job'. Steps to improve procurement and to encourage small groups of public sector workers to establish employee-led mutuals are to be applauded, but they do not begin to address the more fundamental challenge.

Reform needs to cut across government departments – star chambers to police wayward overspenders or non-cutters will not solve the problem. Instead, commitment and leadership from No 10 and the Treasury in particular are needed to set out a more ambitious and sustainable path to driving public sector reform.

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# Tax Policy development



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The area of tax policy making has been high on the agenda since the Coalition Government came to power last year, and this year's Budget continues with this theme.

In June 2010's Emergency Budget, the Government published its framework for future tax policy, made an announcement of a consultation on a GAAR and initiated a consultation on tax policy. This was followed in December 2010 with the publication of the response to this consultation (including a draft framework agreement) and a draft protocol on announcements outside scheduled fiscal events.

In this year's Budget we see publication of a paper on "Tackling Tax Avoidance", finalisation of the protocol mentioned above and the introduction of tax simplification measures through the abolition of 43 tax reliefs (as recommended by the Office for Tax Simplification). The Government's stated aim of all of these documents and consultations is to reduce the volume and frequency of changes to the tax code and provide greater predictability and transparency in their plans for tax reform.

Whilst there has undoubtedly been much promotion of the area of tax policy over the last 10 months, there is more on the horizon: the publication of the finalised Tax Consultation Framework, consultations on the proposals in relation to removing the cash flow advantage of using perceived avoidance schemes, the review of high risk (legislative) areas and the GAAR study group completes its work by 31 October

# Tackling Tax Avoidance

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The Government has today pushed a paper setting out further information on its approach to tackling tax avoidance. This provides information on:

- An introduction to HM Revenue and Customs' (HMRC's) new anti-avoidance strategy: Prevention, Detection and Counteraction.
- Tackling avoidance at the root: The Government intends to address the behaviour of certain taxpayers entering into "high risk schemes" by removing the cash-flow advantage. The proposal is to encourage taxpayers entering into certain specifically identified schemes to pay disputed tax earlier than is currently required, or face an additional charge for late payment when it is found due.

In addition, the Government proposes a review of certain areas of the legislation which are regularly subject to tax avoidance. The first two areas identified are income tax losses and unauthorised unit trusts.

- Tackling avoidance through challenge and litigation with a commitment to allocate resource to those groups that present a higher risk or need more support, and a continued promotion of "real time" working.
- Finalisation of the "Protocol on unscheduled announcement of changes to tax law": Responses to the draft Protocol (published in December 2010) are provided, with details of the changes made to the draft listed.

## Who is affected?

Taxpayers who engage in what HMRC consider are tax avoidance schemes.

## Timing

A consultation document of the proposals to reduce the cash-flow benefits of avoidance will be published in May 2011, with a view to the development of legislation for inclusion in Finance Bill 2012.

No information on timing of other new consultations (e.g. review of income tax losses and unauthorised unit trusts legislation) is provided.

## Our view

The commentary provided by the Government in this document is largely consistent with previous announcements and with the approach that we have seen HMRC adopt in practice with many of our clients.

The finalisation of the "Protocol on unscheduled announcement of changes to tax law" is in line with the stated timetable on its publication in

draft last December. It is encouraging to see that changes have been made to address comments made during the consultation period.

The most controversial measure in the document is likely to be the proposal to remove the cash-flow advantage from using tax avoidance schemes by encouraging the early payment of disputed tax:

- Firstly, it will be critical to understand the criteria that the Government proposes to use to identify the schemes to fall into this regime. It is proposed that only specifically listed schemes will be subject to this proposal which goes some way to addressing concerns, but it will remain to be seen how widely this list may be drawn. The process for consulting on the inclusion of any given scheme should be transparent and the “independent advice” proposed should be sought from a variety of (truly independent) sources;
- Secondly, there must be a mechanism for ensuring that the taxpayer is fully and appropriately recompensed in the event that HMRC is not ultimately successful;
- Finally, it will also be key to understand the interaction of these proposals with current and ongoing enquiries which are in the process of negotiation.?

# Government response to Office of Tax Simplification review of reliefs

The Office of Tax Simplification published its final review of reliefs report on 3 March 2011, recommending the abolition of 47 tax reliefs. In Budget 2011 the Government has announced that it will abolish 43 reliefs, as set out below.

The following reliefs are to be abolished in Finance Bill 2011. Legislative references have been included for reference:

- Charities – transitional relief on distributions (s35 Finance (No2) Act 1997);
- Millennium Gift Aid (s48 Finance Act 1998);
- National Savings Bank ordinary account interest (s691 ITTOIA 2005);
- Payroll giving 10 percent supplement (s38 Finance Act 2000 and s146 Finance Act 2003);
- Exemption for certain assignments by seamen (s45 Finance Act 1945 and Reg 47D DGR 1939);
- Instruments relating to National Savings (s31 Finance Act 1953); and
- Transfers in relation to ships and vessels (Para 24(b) Sch13 Finance Act 1999).

The following reliefs are to be abolished in 2012, following a period of consultation:

- Payments to mariners to be discarded (Reg 123 SSCR 2001);
- Grants for giving up agricultural land (s249 TCGA 1992);
- Pool betting duty payments related to safety improvement at football grounds or for the arts (s139 CTA 2009);
- Mineral royalties (s319 ITTOIA 2005);
- Payments for the benefit of family members (s273 ICTA 1988, s609 ITEPA 2003 and s459 ITA 2007);
- Cycle to work days – provision of meals (Reg 3 SI 2002/205);
- Late night taxis (s248 ITEPA 2003; Para 5(c) Part 5 and Para 8(d) Part 10 Sch3 SSCR 2001);
- Luncheon vouchers (s89 ITEPA 2003 and Para 6A Part 5 Sch 3 SSCR 2001);
- Pools payment for football ground improvements (s126 Finance Act 1990);
- Pools payment for support for games (s121 Finance Act 1991);
- Disregard for certain apprentices and students coming to the UK (Reg 145(3) SSCR 2001);

- Assistance in identifying lost or stolen credit cards (Para 15 Part 10 Sch 2 SSCR 2001);
- Nationalisation schemes (s52 Finance Act 1946); and
- Tax reserve certificates issued by HM Treasury (s1283 CTA 1009).

A further set of reliefs will be abolished “after 2012”, with a final date for abolition to be set following consultation. A key item on this list is Land Remediation Relief (see our detailed commentary ‘Abolition of the tax relief given for the Remediation of Contaminated or Derelict Land’ in the Corporate Tax section below). The other reliefs in this group are:

- Class 1A NICs – Exemption for prescribed general earnings (Para 2(2)(b) Part 8 and Reg 40(4) Sch 3 SSCR 2001);
- Class 4 NICs – Allows deduction in next tax year of losses incurred in 1989/90 or the previous tax year where losses arise from income other than that from a trade, profession or vocation (Para 3 Sch 2 SSCR 2001);
- Deeply discounted securities – incidental expenses (s439(4) ITTOIA 2005);
- Life assurance premium relief (sections 266, 268-272, 274, 278 and Sch 14 ICTA 1988; SI 1997/1143; SI 1977/1144; SI 1978/1159; SI 1980/1947; and SI 1980/1948);
- Life assurance premiums paid by employers under E-FRBS (s266A ICTA 1988);
- Capital allowances – flat conversion allowances (Part 4A CAA 2001);
- Capital allowances – safety at sports grounds (s30-32 CAA 2001);
- Certain leases granted by registered social landlords (s128 Finance Act 2003);
- Disadvantaged area relief (s92 and Sch 30 Finance Act 2001)
- Exempt instruments (SI 1987/516);
- Partial relief for company acquisitions (s76 Finance Act 1986);
- Shared ownership transactions (s97 Finance Act 1980 and s54 Finance Act 1987);
- Transfers to registered social landlords (s130 Finance Act 2000);
- Visiting forces and allied headquarters (s74 Finance Act 1960);
- Disadvantaged area relief (DAR) (s57 and Sch6 and Para 26 Sch 15 Finance Act 2003 and SI 2001/3747);
- Angostura Bitters (s1(7) Alcoholic Liquor Duties Act 1979);
- Black Beer (s1(3)(a) Alcoholic Liquor Duties Act 1979);
- Compensation for mis-sold pensions (s148 Finance Act 1998);
- Harbour authorities (s221 TCGA 1992);
- Harbour reorganisation schemes (s993 CTA 2010);
- Transfers in relation to harbour reorganisation schemes (s45 FA 1966).



# Corporate Tax



**Jane McCormick**  
Head of Corporate Tax

Other than for the banking and oil and gas sectors, the corporate tax changes announced in the budget are broadly positive. The Chancellor announced that the main rate of corporation tax will now fall by two percent on 1 April 2011, to 26 percent rather than one percent as previously expected. This was a very welcome surprise. Also of note was the announcement that the proposed partial finance company exemption, to be included in the new CFC regime, will result in taxation of one-quarter (rather than one-third, as previously suggested) of the profits derived from overseas group financing arrangements. This will result in a UK effective tax rate of just 5.75 percent once the corporation tax rate falls to 23 percent in 2014. These measures are likely to increase the attractiveness of the UK to multi-national organisations and will hopefully prevent further high profile moves out of the UK to jurisdictions with tax regimes perceived to be more competitive.

On a less positive note the surprise increase in the oil and gas supplementary charge from 20 percent to 32 percent, effectively a windfall tax, is a huge blow to the oil industry and the proposed tax increases can only reduce the attractiveness of investment in the North Sea. Banks were also losers as the Chancellor announced an increase to the bank levy which, although small, is the second increase since the original levy proposals and some banks will be alarmed by the direction of travel.

While there were a number of headlines there was little detail on most of the measures announced in the Budget and, instead, we can expect a number of important consultation documents to be published in the months ahead. As expected we will be seeing consultations on full CFC reform, the proposed patent box and changes to the R&D regime in May. Also of note is a consultation on devolving corporate taxation to Northern Ireland due to be published on 24 March which may eventually result in a reduced tax rate for the region.

The coalition Government has introduced a new approach to tax policy making and in line with this policy draft clauses for the 2011 Finance Bill

were published in advance of the 2011 Budget on 9 December 2010. The structure of our commentary has changed to accommodate this new approach. All announcements relating to tax policy are set out in a separate section at the beginning of the commentary and then each tax section is ordered as follows:

- New measures not previously published in draft to be included in Finance Bill 2011.
- Measures to be included in Finance Bill 2012 or later.
- Measures to be included in Finance Bill 2011 that were published in draft on 9 December 2010 where changes to those draft clauses have now been announced in the Budget. Although this Budget commentary focuses on the changes that are to be made to those draft clauses, to help understand these changes our original commentary from December 2010 is replicated immediately after our comments on each measure. If no changes have been announced the measure has not been included in this commentary. A list of measures originally published on 9 December 2010 for which no changes have been announced at the Budget is included at the back of each section for completeness, and a full copy of our original commentary from December can be found [here](#).

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# New measures for Finance Bill 2011

# Corporation tax charge and main rate

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## Brief overview

It has been announced that the main rate of corporation tax will now fall by two percent on 1 April 2011, to 26 percent. The Finance Bill 2011 will also include a provision for a further one percent reduction to 25 percent on 1 April 2012. The further planned annual reductions, of one percent on both 1 April 2013 and 1 April 2014, will be legislated in subsequent finance bills.

The small profits rate of tax will fall by 1 percent to 20 percent on 1 April 2011.

Corporation tax rates for ring fence profits (those arising from oil extraction and oil rights in the UK and the UK continental shelf) will remain at 30 percent and 19 percent respectively.

## Key changes announced at the Budget

The main rate of corporation tax will be reduced by two percent on 1 April 2011; this was previously expected to be only a one percent reduction.

The Finance Bill 2011 will also legislate for a further one percent reduction on 1 April 2012. This year-on-year reduction had already been announced but it was unclear when it would be legislated.

The fraction for calculating marginal relief, where a company's profits fall between the small profits rate limit of £300,000 and the main rate threshold of £1,500,000, will be changed from 7/400 to 3/200, to reflect the reduction in the gap between the small profits rate and the main rate of corporation tax.

## Our view

This further reduction in the main companies rate will be welcomed by companies with larger profits, although it will have no impact on smaller businesses with profits below £300,000.

Whilst the inclusion, in the 2011 Finance Bill, of a reduction in the main tax rate from 1 April 2012 will provide greater certainty to businesses, the tax accounting implications will require detailed consideration.

## *What we wrote when the draft clauses were published 9 December 2010*

Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

### Summary of proposal

As previously announced, the main corporation tax rate will reduce from 27 percent (the rate for the financial year from 1 April 2011 – 31 March 2012) to 26 percent from 1 April 2012.

The Government is also consulting whether the pre-announced reductions to the main rate of corporation tax, reducing to 24 percent from 1 April 2014, should be also enacted in the Finance Bill 2011. If this were to happen, whilst perhaps providing greater certainty to business, the tax accounting implications would require detailed consideration

The small profits rate of tax will be reduced from 21 percent to 20 percent from 1 April 2011.

The corporation tax rates for ring-fence profits (profits arising from oil extraction and oil rights in the UK and the UK Continental Shelf) will remain at 30 percent and 19 percent respectively.

### Who is affected

All companies that pay UK corporation tax.

### Timing

The main rate of corporation tax rates will reduce to 26 percent from 1 April 2012 and the small profits rate from 1 April 2011.

### Our view

This confirms measures already announced in the June 2010 budget. The rate reductions will be welcomed by taxpaying companies. However, the potential tax benefit arising from the reduction in rates may be offset by the proposed capital allowance changes which take effect from 1 April 2012.

# Increase in UK oil tax rate

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

From 24 March 2011 there will be an increase in the supplementary charge in respect of profits from oil and gas production in the UK and UK Continental Shelf from 20 percent to 32 percent.

In future years, where the oil price falls below a set trigger on a sustained basis, the Government will reduce the rate towards the original 20 percent rate on a staged and affordable basis. Government considers that a trigger price of USD\$75 per barrel would be appropriate but will set a final level and mechanism after seeking views of oil and gas companies and motoring groups.

Legislation will be introduced in Finance Bill 2012, to restrict tax relief for decommissioning expenses to the 20 percent rate of supplementary charge. The Government announced there will be no restrictions to decommissioning relief beyond this level for the lifetime of this Parliament.

It was stated that Government will work with the Industry with the aim of announcing further, longer-term certainty on decommissioning at Budget 2012.

## Who is affected

Upstream Oil and Gas producers operating in the UK.

## Timing

The new rules will take effect on or after 24 March 2011.

## Our view

The proposed tax increases can only reduce the attractiveness of investment in the North Sea. The potential for the tax rate to be reduced if the oil price falls will be of no consolation to the UK's oil and gas producers.

While the Chancellor spoke about making the UK a globally attractive place to do business this would not appear to apply to UK oil and gas production. With these announcements the effective rate for many North Sea fields has more than doubled in less than a decade.

It is disappointing that these measures were not discussed with industry; the rate change will come as a shock to oil and gas production companies in the UK.

# Capital Allowances – Short Life Assets

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The Finance Act 2011 will include provisions that will increase the period over which plant and machinery can be treated as a short life asset from four years to eight years.

## Who is affected?

Businesses investing in plant & machinery.

## Timing

The new rules will take effect from 1 April 2011 for corporation tax purpose and 6 April 2011 for income tax purposes.

## Our view

This measure is to be welcomed as this now gives businesses the option to elect in to the short life asset regime if the reality is that the plant and machinery will be scrapped or sold within eight years. This allows the tax treatment to be aligned with the economic benefit the business receives.

The administrative burden that is attached to electing for short life asset treatment needs to be considered as part of this change. It would be helpful for the business community if a 'light touch' is adopted by HM Revenue and customs to the increase in short life asset elections that will result as a consequence of this change.

# Increase in rate of relief for Research and Development (R&D) expenditure by small or medium enterprises (SMEs)

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

In his recent report "Ingenious Britain" Sir James Dyson called for the R&D reliefs for SME companies to be more generous. The Government has responded positively to this suggestion. Their aim is to increase the amount of expenditure by SME companies on research and development, in anticipation of the economic benefits that will arise.

The rate of deduction from taxable profits for SME companies incurring qualifying R&D expenditure is to be increased from 175 percent to 200 percent from April 2011, and to 225 percent from April 2012.

By 2013/14 the cost of this additional relief is estimated at £105m per annum.

Loss making companies can surrender losses resulting from qualifying R&D expenditure for a payable credit. Despite the increase in the rate of the enhanced deduction it is not intended to materially increase the amount of payable credit to loss making companies so the percentage at which losses can be surrendered for cash will be reduced to keep the value of the payable credit at roughly the same level.

## Who is affected?

SME companies that are eligible for R&D tax relief.

For R&D purposes only, the SME limits are:

- less than 500 staff; and
- either turnover below €100m or gross balance sheet assets below €86m on an annual basis.

## Timing

It is intended that the 200 percent rate will take effect from 1 April 2011, and the 225 percent rate from 1 April 2012, subject to European Commission (EC) State Aid approval. HM Revenue and Customs (HMRC) hope this will be forthcoming so long as the overall limits on State Aid intensity are observed. In this context the announced reduction in the rate of Vaccine Research Relief for SMEs, and then its removal, is intended to demonstrate to the EC that the overall State Aid limits will not be breached.

Where a measure requires State Aid approval this is usually brought into force by a Statutory Instrument if the approval is not received in advance of enactment of the Finance Act.

### **Our view**

This is a valuable increase to the incentive for SMEs carrying out R&D. The cash value of the relief will increase from 21 percent of qualifying expenditure currently, to 26 percent from 1 April 2011, and to 31.25 percent from 1 April 2012, assuming mainstream corporation tax rates apply.

# Sale of Lessor Companies – Preventing Avoidance

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

Changes are to be made to the sale of lessor companies legislation in response to disclosures of tax avoidance schemes.

## Who is affected

Companies carrying on a business of leasing plant or machinery alone or in partnership.

## Timing

The measures will take effect when:

- there is a change in the ownership of a lessor company (or a change in a partner company's interest in a leasing business) on or after 23 March 2011; or
- there is a transfer of a business of leasing plant or machinery on or after 23 March 2011 where under current law the assets would be treated as sold at market value.

The option to elect out of the sale of lessor companies charge will be withdrawn with effect from 23 March 2011.

Where a company has elected out of the charge in respect of a change of ownership prior to 23 March 2011, the measures will affect the disposal value of plant or machinery to be brought into account for Capital Allowances purposes on a disposal event taking place on or after 23 March 2011.

## Our view

The purpose of the sale of lessor companies legislation is to prevent the deferred profits of a lessor company not being brought fully into account for tax purposes following a sale of the company.

The legislation works by bringing the deferred profits of the lessor company into charge at the time of the sale. Immediately following the sale a matching relief (equal to the charge) is given to the lessor company to prevent double taxation of the deferred profits. Any loss that derives from the relief cannot be carried back to earlier accounting periods.

The changes have been introduced in response to disclosures of tax avoidance schemes which seek to ensure that lessor companies could be sold without suffering the "full" charge.

The arrangements that are being countered seek to:

- exclude plant or machinery from the current definition of "qualifying leased plant or machinery";
- manipulate the values of PM (plant or machinery) and TWDV (tax written down value) in the formula  $PM - TWDV$  (which determines the amount brought into charge);

- take advantage of the current definition of “market value”—for example, where an asset diminishes in value quickly but is still able to generate substantial rentals; and/or
- take advantage of the option to elect out of the sale of lessor companies charge.

Whilst we appreciate that the changes have been made to prevent abuse of the sale of lessor companies regime, we consider that the changes are much more complicated than they needed to be.

There appears to be a degree of duplication in the changes made, with both specific changes made to the definition of PM as well as an extension to the anti-avoidance provisions that currently deal with the manipulation of balance sheet figures to now encompass (inter alia) the amount of PM.

The changes appear to have closed various tax loopholes, but have also made the sale of lessor companies legislation even more complicated.

The withdrawal of the election is a negative move and raises the issue as to why the measures do not include a tax avoidance purpose test. Instead, these complicated measures apply both to tax-motivated and ordinary commercial transactions.

# Anti-avoidance targeted at structured leasing of plant and machinery

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

As announced on 9 March 2011, Finance Bill 2011 is to contain legislation designed to prevent double capital allowances being available as a result of a particular lease refinancing structure.

The planning involved a long funding finance lessee of plant or machinery. Such a taxpayer is deemed to own, and to have incurred qualifying expenditure ("QE") on, the leased assets for capital allowances purposes. QE is the present value of the lessee's minimum lease payments ("PVMLP"). The double allowances arose because a put option was granted by the lessee to the lessor. The guaranteed amount (i.e. the put price) qualified as part of the lessee's PVMLP. The lease would terminate and the asset would be acquired by the lessee, pursuant to the exercise of the put option by the lessor. The lessee's disposal value on termination of the lease would be reduced, reflecting the payment of the put price (inter alia) as an amount paid under the lease. The lessee's QE as purchaser also would reflect the put price paid.

Thus the allowances given to the lessee - qua lessee - were not clawed back, and new allowances were awarded in addition. In the case of a relatively short lease term, the assets would have retained most of their value, and the benefit would be tantamount to a double principal deduction.

## Who is affected

Lessees of plant and machinery where the lessee provides a guarantee to the lessor.

## Timing

The new rules will take effect from 9 March 2011. Transactions completed where the put option was exercised prior to 9 March 2011 should not be affected.

## Our view

This was a structured transaction which gave rise to a tax effect which was not intended under the legislation. It is not surprising that it has been closed down for the future.

The drafting of the blocking legislation is wide; it denies allowances in respect of payments which give rise to other tax relief, even if the result of that other relief is not a double tax deduction. The changes thus appear to impact innocent transactions involving a long funding finance lease of plant or machinery where the lessee provides a guarantee to the lessor in many commercial forms. The effect in such circumstances may be to cause a deferral of tax relief.

# Stamp Duty Land Tax (SDLT) anti-avoidance

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

Three legislative changes are made to block SDLT avoidance schemes:

- Sub-sale relief is specifically blocked where it might apply in combination with the alternative property finance reliefs.
- It will not be possible to qualify as a “financial institution” for the purposes of the alternative property finance reliefs simply by holding a consumer credit licence.
- The market value rule for exchanges of property can no longer result in a reduction of tax compared with a charge made on the normal basis of actual consideration paid.

## Who is affected

Purchasers of UK real estate.

## Timing

The new rules take effect from 24 March 2011.

## Our view

It is unsurprising that further action has been taken to block SDLT schemes. The measures are technical and specifically targeted and therefore should not impact on the general application of the SDLT rules or make them more complex.

The changes to the alternative property finance reliefs are clearly coherent with the policy intention that these reliefs are designed to prevent multiple charges to SDLT rather than complete exemption.

# Stamp Duty Land Tax (SDLT) reform of rules for bulk purchases

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

Changes are to be made to introduce a new relief for purchasers of residential property who acquire more than one dwelling. Currently SDLT is charged at the rate applying to the total price paid for a portfolio of properties. Where the total exceeds £500,000 then the four percent rate applies. The new relief will reduce the rate of SDLT on the purchase of multiple residential properties by relating it to the mean price, i.e. the total divided by the number of properties. The minimum rate of tax will be one percent.

## Who is affected

Property investors, residential property funds, and developers.

## Timing

The new rules will take effect from the date the Finance Bill 2011 receives Royal Assent.

## Our view

This is a positive announcement and will help property investors and large-scale purchasers such as pension and life funds to purchase batches of unsold properties for private rent. This in turn should have a knock-on effect on the private rented market by encouraging investors back into the market.

Property developers and house-builders should indirectly benefit as it will make their stock more attractive to prospective purchasers, by reducing the tax cost of making an investment or establishing a residential property fund.

# Stamp Duty and corporation tax treatment of alternative finance investment bonds

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

Unintended potential adverse consequences for the tax and regulatory treatment of alternative finance investment bonds (AFIBs) were created by the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) Order 2010 which came into effect on 24 February 2010.

The order was meant to align the treatment of AFIBs with conventional debt securities, but had the effect of creating a category of instrument (where such instruments were not listed or traded, or where the interest on them exceeded a normal commercial rate) that did not qualify for the stamp duty loan capital exemption and companies issuing them were unable to benefit from the special corporation tax regime for securitisation companies.

A second order rectified the position from 16 February 2011 but retrospective legislation will be introduced to ensure that it applies with effect from the date of the original order i.e. 24 February 2010.

## Who is affected

Companies who have issued AFIBs between 24 February 2010 and 16 February 2011 and those who have acquired interests in AFIBs during that period.

## Timing

The new rules will take effect retrospectively from 24 February 2010.

## Our view

This is a positive measure which will help to remove confusion and uncertainty in relation to stamp duty and the special corporation tax regime that has arisen in the financial markets following the making of the Financial Services and Markets Act order.

# Corporate gains: de-grouping charges anti-avoidance

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Impact on taxpayer			
Positive	Neutral	Negative	Both positive and negative

## The issue

Where transferor and transferee leave a group as associated companies and join another group which the transferee subsequently leaves, the de-grouping charge originally did not apply.

The existing legislation (Ss179(2A) TCGA) prevented advantage being taken of this by providing that the de-grouping charge still applied if there was a connection between the two groups. However, subsection (2A) only bites if this connection still exists at the time the transferee leaves the second group. It would therefore be possible to avoid the de-grouping charge by ensuring that the transferee did not leave the second group until after the two groups had ceased to be connected.

The legislation has now been tightened so that the de-grouping charge will also apply if and when the two groups cease to be connected.

## Who is affected

Anyone planning to use the associated companies exception to avoid de-grouping charges.

## Timing

The new rules will apply where the transferee leaves the first group on or after 23 March 2011.

## Our view

The proposed simplification of de-grouping charges (which will result in their being allocated to the share vendor as additional proceeds for the disposal of shares where the degrouping arises in consequence of a share disposal) is likely to mitigate the impact of this further tightening. However, where the Substantial Shareholding Exemption is not in point it will ensure that the charge continues to apply.

# UCITS IV: Management Company Passport

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

**The issue**

UK Fund Managers will be able to manage undertakings for collective investment in transferable securities (UCITS) funds in other member states without creating any adverse tax consequences in the UK for those funds.

**Who is affected**

UK fund managers authorised to provide services to UCITS funds.

**Timing**

The measure will take effect from the date of Royal Assent of the Finance Bill 2011.

**Our view**

Enabling UK fund managers to manage UCITS funds established in another EEA state without creating any adverse UK tax consequences for those funds will improve the competitiveness of the UK funds asset management industry.

The Government has also announced that it will introduce regulations to amend the Genuine Diversity of Ownership conditions to enable the establishment of Master-Feeder structures, which are permitted under UCITS IV. This will remove one of the technical concerns raised by the funds industry to the establishment of Master-Feeder structures.

Following consultation to commence in June 2011, the Government also announced that it will legislate in the Finance Bill 2012 to introduce a tax transparent fund vehicle, which would be suitable for a UK domiciled Master UCITS fund. This measure will help make the UK more competitive in attracting funds business.

# Oil licences and Intangible Fixed Asset (IFA) rules

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

**The issue**

Oil licences are specifically excluded from being treated as an IFA. However, companies would account for goodwill on some oil licence acquisitions.

Finance Bill 2011 is to ensure that the scope of the IFA rules excludes all goodwill and any intangible asset which relates to, derives from or is connected with an oil licence or an interest in an oil licence. This change would therefore mean that no goodwill amortisation or impairment charges would become deductible against income.

**Who is affected**

Upstream Oil and Gas producers operating in the UK.

**Timing**

The rules are to have effect from 23 March 2011.

**Our view**

Where goodwill was booked previously it could have been interpreted that the goodwill did not derive from the underlying identifiable oil licence. If it did derive from the oil licence then accounting policies would have often required the value of the oil licence itself to be reflected in the accounts at its fair value. Therefore it was possible goodwill could be seen as being something distinct from the oil licence with an income deduction arising for a transaction that otherwise would have been a capital expense. These rules clarify the treatment and no relief will be available.

# Mutual Assistance Recovery Directive

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

Legislation will be introduced in Finance Bill 2011 to enable the UK to implement the new Mutual Assistance Recovery Directive ("MARD") which was adopted by the EU on 16 March 2010.

## Who is affected

Taxpayers resident or present in the UK who have incurred tax liabilities in other EU member states.

## Timing

The new MARD is effective from 1 January 2012 and the Regulations implementing it in the UK will come into force on that date.

## Our view

The MARD replaces an earlier directive providing for Member States to assist each other in the recovery of tax debts and duties. The new Directive is more extensive in scope, covering all national taxes and duties, local duties and motor taxes. Among other things it also extends the scope for exchange of information without request and for tax administrations to carry out cross-border enquiries.

The Finance Bill will contain the necessary primary legislation to enable the new Directive to be implemented by Statutory Instrument. The detail of the new regulations will not be known until later in the year. It is hoped that the implementation of the new Directive will improve the cross-border collection of tax within the EU.

# Finance Bill 2011: Other new measures

## **Capital allowances – Energy Technology List**

The Energy Technology List in relation to Enhanced Capital Allowances will be updated by Treasury Order in the summer of 2011 with one new technology, certain energy efficient hand dryers. This is in line with previous years and allows taxpayers to continue to invest in qualifying plant and machinery that will attract a 100 percent First Year Allowance.

## **Vaccine Research Relief**

The main change to the Research & Development (R&D) relief has been the increase in the small and medium sized enterprises (SME) rate. Accompanying this is a restriction to the vaccine research relief for SMEs so that the overall State Aid intensity is not exceeded. This restriction will be to 20 percent from 1 April 2011 and to zero (for SMEs) from 1 April 2012.

## **Film Tax and Community Investment Relief**

The Government has confirmed that the future of two state aid reliefs which encourage UK investment will be secured, following re-notification to the European Commission. The first aid is film tax relief which applies to expenditure on British films. The second is Community Investment Relief, which provides tax relief to companies who invest in community finance institutions, set up to lend to businesses, social enterprises and individuals who may not be able to raise finance from high street banks.

## **Taxation of index linked Gilt edged securities**

The definition of a gilt edged security which qualifies for exemption for companies from a tax under the loan relationship rules is extended to include gilts referenced to the Consumer Price Index (CPI) as well as the retail price index (RPI). As the law currently stands, the security would have to be indexed by reference to the RPI to qualify for this treatment. The measure is intended to assist companies with hedging exposures to CPI movement.

## **Time to pay**

The Government has confirmed that HM Revenue & Customs' (HMRC's) Business Payment Support Service, which was launched in 2008 to provide advice and time to pay to viable businesses in temporary financial difficulty, will continue to operate.

## **Customer cost reduction announcement**

Since 1 April 2006 HMRC has set itself targets for reducing the administrative burdens on business of providing information both to itself and to third parties. HMRC has now announced that it will expand its narrow administrative burden target to include wider customer compliance costs whilst committing not to increase administrative burdens under the existing measure over this spending review period. This fits with HMRC's aim of improving its service and reducing business costs.

# New measures for Finance Bill 2012 or later

# Abolition of the tax relief given for the Remediation of Contaminated or Derelict Land

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The Government have confirmed that, as result of the review carried out by The Office of Tax Simplification (OTS), they intend to abolish the tax relief given for remediating contaminated or derelict land.

## Who is affected?

All businesses who incur expenditure on cleaning up brown field or derelict sites.

## Timing

No date has been given for abolition but it will be after 2012. The final date will be set out after consultation.

## Our view

The removal of the tax relief given for the Remediation of Contaminated or Derelict land is disappointing news. The rules, contained in CTA 2009 – Part 14, were subject to a lengthy and drawn out rewrite process only recently where the legislation was fine tuned from a previous version to be more targeted and focused. The legislation provides an enhanced deduction for companies cleaning up contaminated sites on the basis they were not (or not connected to) the original polluter.

It is recognised that the abolition being proposed was as a result of the OTS review. However, not all enhanced reliefs that were recommended for abolition have been accepted by the Government (for example Business Premises Renovation Allowance). The business community, with real estate assets ready for development, will need to consider their investment options if this relief has been factored into the viability of planned schemes. Additionally, for property developers, this will raise an interesting issue for those companies holding remediated property as stock, since relief will not be available until a sale goes through the profit and loss account.

# The extension of Business Premises Renovation Allowances

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

Business Premises Renovation Allowances (BPRA) will be extended for another five years and will now apply to qualifying expenditure incurred before the new expiry date, April 2017.

## Who is affected

Investors and potential occupiers who are converting or renovating a qualifying building in a disadvantaged area.

## Timing

The expiry date will be extended from April 2012 to April 2017 in Finance Act 2011.

## Our view

The extension to the date when BPRA can be claimed should be welcomed. Qualifying expenditure is eligible for a 100 percent capital allowance in the year the capital expenditure is incurred. As the building must be situated in a disadvantaged area and must be unused for at least one year before expenditure is incurred the allowances are very focused. This extension to the expiry date will mean that investor and potential occupiers will continue to be incentivised to invest in those disadvantaged areas.

# Loan relationships and derivative contracts (Disregard regulations) – exchange differences

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

**The issue**

Legislation is to be introduced, in statutory instruments, making three changes to the treatment of foreign exchange differences on loans and derivatives.

**Matching with own share capital**

Currently, there are rules which permit a company to match the exchange exposure on loan assets and derivatives with its own share capital (a process sometimes known as reverse matching). The effect of this is that the exchange differences on the loan/derivatives are never brought into account.

The rules are to be rewritten so that exchange gains and losses on loans and derivatives are ignored where they act to reduce the company's foreign exchange exposure in relation to its own preference shares, which are issued to non-connected entities and are accounted for as liabilities.

The changes will also allow for matching in wider circumstances if a clearance is obtained and an election is made. It is understood that this may apply where the preference shares are issued to a connected party.

**Matching with foreign currency partnership assets**

New rules are being introduced to allow a company partner to defer exchange differences on loans/derivatives where they reduce the economic exchange exposure in relation to foreign currency assets (such as shares) held by a partnership.

Currently, if the partnership itself enters into a loan/derivative to hedge foreign currency shares, HM Revenue and Customs (HMRC) accept that the company partner benefits from the deferral of exchange differences. It is understood that the new rules are intended to permit the company partner to benefit from the deferral when it enters into loans/derivatives to hedge any exposure not already dealt with in the partnership.

**Matching deferred proceeds on the sale of foreign currency shares**

Currently, a company can defer foreign exchange differences on loan/derivative liabilities where this reduces the economic exposure to exchange differences on share investments. The amount of the liabilities which can be matched in this way is limited to the accounts carrying value of the share investment or, if an election is made, to the underlying net asset value.

The rules are being amended to permit matching with the disposal proceeds of shares. Exchange differences on the loans/derivatives are deferred until the proceeds are received. At that time, the deferred

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exchange differences may be exempt if the disposal of the shares is exempt applying the Substantial Shareholdings Exemption.

#### **Who is affected**

Companies who have an exposure to taxable exchange differences on loans and derivatives.

#### **Timing**

Matching with own share capital – accounting periods beginning on or after 1 July 2011.

Matching of foreign currency partnership assets and the matching of deferred proceeds on the sale of foreign currency shares – accounting periods beginning on or after 1 January 2012.

#### **Our view**

In each case, the changes are expected to permit companies to manage their exposure to taxable exchange differences so that this more closely reflects the economic circumstances.

# Enterprise Investment Scheme (“EIS”) and Venture Capital Trusts (“VCTs”)

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

**The issue**

Subject to State aid approval the following increases will be introduced:

- the thresholds for the maximum size of qualifying company for both EIS and VCTs will increase with the employee limit being extended to fewer than 250 employees (currently fewer than 50 employees), and the size of gross assets being increased to no more than £15 million before investment (currently £7 million);
- the maximum annual amount that can be invested in an individual company will increase to £10 million (currently £2 million); and
- the annual amount that an individual can invest under the EIS will increase to £1 million (currently £500,000).

Measures will also be introduced to prevent those companies whose trade consists wholly or substantially in the receipt of Feed-In Tariffs or similar subsidies from qualifying unless commercial electricity generation commences before 6 April 2012.

**Who is affected**

Individuals subscribing for shares in qualifying EIS companies, VCTs and companies looking to qualify as EIS/VCT investee companies

**Timing**

The measures above will take effect from 6 April 2012.

**Our view**

This is a welcome move in that more companies will fall within the conditions to qualify as an EIS and VCT companies. This should result in more companies being able to attract investment. Individuals will also be able to benefit from increased tax relief as a result of the maximum annual investment being increased and therefore this is a positive measure.

# Charities and Charitable Giving

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

Changes are to be made to the Gift Aid donor benefit limits in respect of donations of £1,001 or more. Under the current rules where such a donation is made the donor can receive benefits in consequence of that donation with a value of up to five percent of the donation, subject to an overall limit of £500. This overall limit will be increased to £2,500.

A number of changes have also been announced which are intended to simplify the administration of Gift Aid, as well as encourage and support further charitable giving. These include:

- A Gift Aid style repayment for charities in respect of small donations. The new repayment will be claimable without the need to obtain Gift Aid declarations on donations of £10 or less, subject to a cap of £5,000 per year per charity. Charities will need to meet certain conditions in order to qualify to claim this new repayment.
- The introduction of a new online system for charities to register for and submit Gift Aid claims.
- Giving statutory effect to an existing Extra Statutory Concession under which HMRC currently make certain repayments of tax to charities outside of a tax return.
- Consultation will also be launched regarding the introduction of a tax deduction for taxpayers who donate works of art or historical objects of national importance to the State.

## Who is affected

Charities and their donors.

## Timing

The new rules for donor benefits will apply in respect of donations made on or after 6 April 2011 for individual donors, and for donations made in accounting periods ending on or after 1 April 2011 by corporate donors.

Other changes will be subject to consultation and will take effect in Finance Bill 2012 or later.

## Our view

These are positive changes which will help to reduce the administrative burden for charities in relation to Gift Aid. The new Gift Aid style repayment is good news for small charities who rely on small donations but who have until now been precluded from benefiting from Gift Aid due to the administrative costs.

# Solvency II and the Taxation of Life Insurance Companies (including changes to treatment of protection business)

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The Government has made announcements today which, following a formal consultation process which began in March 2010, sees a number of preliminary decisions being made on the direction of the tax regime for insurers to address upcoming changes being brought about by the advent of Solvency II from 1 January 2013. A further consultation is expected to take place in the near future to discuss the detail of these announcements.

The key announcements are as follows.

**Basis for taxation:** The Government has confirmed that the surplus reported in the Financial Services Authority (FSA) return will be replaced by the profit (or loss) before tax reported in the statutory accounts as the starting point for the tax computation.

Where a life insurer holds a Fund for Future Appropriations (FFA) under UK GAAP or Unallocated Divisible Surplus (UDS) under (International Financial Reporting Standards) IFRS, movements relating to these liabilities will be tax effective. The accounting position under Phase II of the IFRS project for Insurance Contracts is uncertain, and the tax position will be assessed when the accounting view becomes clearer.

**Policyholder bonuses:** Legislation to be introduced to confirm that policyholder bonuses should be treated as tax deductible, in line with the current position (case law provides that they are an appropriation of profit rather than a deduction in arriving at profit and thus such a provision is necessary).

**Policyholder tax:** Subject to further consultation, a proposal to base a deduction for policyholder tax borne by a life company on cash tax payable (at policyholder rates) and disregard deferred tax.

**Scope of I minus E regime:** The basis for taxing life insurers which are not taxed purely on their trading profits is known as the Income minus Expenses (I-E) regime which seeks to tax a life insurer on both shareholder profits and the policyholders' share of accruing investment return. At present, this (technically) applies to the whole of a company's life insurance business, although the income less expenses calculation only relates to basic life and general annuity business (BLAGAB) with a profits calculation for gross roll up business (GRB) being included in the taxable result. Going forward, the I-E basis (for BLAGAB) and the profits basis for GRB will be separated.

Categories of Long Term Business: As a result, both GRB and the third category of long term business for tax purposes, permanent health insurance (PHI) business, will cease to exist as separate categories. PHI business is already taxed on its trading profits based on accounting profit rather than FSA return surplus. Owing to the changes to GRB discussed above, since both GRB and PHI business will be taxed on their trading profits derived from the accounting profit, these categories will no longer be maintained separately. Consequently, long term business will be split between BLAGAB and another category (comprising current GRB, PHI and protection business written from 2013 onwards) taxed on a trading profits basis.

GRB dividends will continue to be taxed under the new regime. Consultation will be undertaken into the taxation of PHI business dividends.

Apportionment: Apportionment of income and gains to be made on a “factual commercial basis” insofar as possible, using an appropriate approach which can be agreed with HMRC Customer Relationship Managers (CRMs). A statutory rule will be put in place to cover scenarios where it is not feasible or appropriate to apportion on a factual basis.

Transitional Issues: Moving to an accounts basis of taxation for life insurers more in line with companies generally is expected to bring significant amounts into tax. The Government therefore proposes to introduce a number of transitional timing adjustments to spread the impact. Whilst it has recognised three broad categories which will require consultation of transitional measures, it also expects that it will be likely individual rules may also require specific measures.

The three broad categories the Government has identified are: deferred acquisition costs and deferred income reserves; untaxed surplus within Court schemes; and other residual transitional adjustments arising from timing differences in the recognition of profits for tax or from valuation differences. The first category will be dealt with simply by providing that there should be no double taxation or double deductions for amounts later recognised in the accounts when already taxed or relieved on an FSA Return basis. The other two categories will in effect be spread over ten years, although with a possible deferral for court schemes.

Carry forward of tax attributes on transition: GRB losses arising from the old regime and unused at the transition date will be available for carry forward against profits in the new combined GRB/PHI category. The Government intends to consult further as to whether pension business losses arising from the pre-2006 regime (before the amalgamation of various categories of business, including pension business took place) should continue to be streamed against future pension business profits.

BLAGAB trading losses which remain unused at the transition date will be available for carry forward against BLAGAB trade profits in carrying out the minimum profits test. The wording here is unclear and it is possible that only a proportion of the BLAGAB losses will be available. Consultation will take place on how this amount should be determined.

Excess BLAGAB expenses unused at the transition date will be available for carry forward into new regime I-E computations.

Treatment of Protection Business: Certain life insurance business which is described as “protection business” (broadly policies which provide no separate investment element) which is considered no longer appropriate for I-E treatment will be excluded from the I-E calculation. This business

will instead be taxed on a trading profits basis (see Categories of Long Term Business for further explanation).

The Government proposes to consult on detailed implementation, which will also address precisely how “protection business” should be defined. Only policies written on or after 1 January 2013 will be affected.

**Shareholder Fund Assets:** There is uncertainty as to whether the long term fund/shareholder fund distinction will continue to be a regulatory requirement under Solvency II, but the expectation is that it will not. In this eventuality, the Government proposes for the tax treatment of income and gains to be determined based on whether the underlying assets constitute fixed or circulating capital.

**Demutualisation Surplus:** The Government does not intend to make any special provision in relation to untaxed surplus originating in mutual companies and now held in proprietary companies following a scheme of demutualisation.

**Mutual Insurers:** No changes are expected to the taxation of mutual businesses.

**Transfers of Long Term Business:** The rules governing life insurance business transfers will be amended to be brought into line with general insurance.

For whole and part transfers of business between independent parties at arm’s length, accounting principles will be followed without adjustment.

Where transfers take place between connected parties, for the purposes of calculating trading profits, all profits and losses on the insurance contracts will be taxed as they emerge in the hands of the transferee. Accounting profits or losses attributable to the transfer will be disregarded.

Special provision will be needed where the transfer is to an entity outside the scope of UK taxation.

#### **Post 2013 Developments:**

**IFRS 4 Insurance Contracts Phase II:** It is currently unclear as to when the new standard will take effect (although this is not expected before 2014) or whether early adoption will be permitted. The Government has stated that it will consider issues relating to the tax impact of the new standard in conjunction with industry once the content and timing of IFRS 4 Phase II are clear.

**Future Court Schemes:** The Government intends to explore with industry whether there is a need for special rules to govern the tax treatment of profits whose distribution are restricted by schemes which may be put into place after the transition. Any such rules are not expected within Finance Bill 2012, and this point will not form part of the Solvency II consultation.

#### **Who is affected?**

Affects all companies carrying on life insurance business.

#### **Timing**

A further consultation is expected to take place from April 2011 with the aim of producing draft legislation to be included in the Finance Bill 2012.

It is intended for these measures to be effective as of 1 January 2013 to coincide with the expected commencement of the Solvency II regime.

#### **Our view**

This is a complete overhaul and rewrite of the life insurance regime.

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The transition to an accounts based tax regime should in principle, lead to a number of simplifications such as the narrowed focus of the I-E regime and the convergence in approach to taxation of GRB and PHI business.

However, the transition is not likely to be without its problems, particularly with regards to the potential acceleration of taxation of amounts which would otherwise have been deferred.

Furthermore, with the commencement of Solvency II fast approaching, it remains to be seen whether it will be possible to address the range of issues identified in such a limited timeframe.

The changes to protection business are likely to be popular with companies who cannot fully benefit from the existing tax treatment, but not with those who can.

# Insurance - Claims Equalisation Reserves

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

Claims equalisation reserves (CERs) are a means of smoothing the profit of an insurance company to mitigate the volatility of the business – particularly around catastrophes.

For corporate and partnership members of Lloyd's and general insurers, CERs are recognised for tax purposes such that movements in these reserves are brought into tax. The relief currently available to general insurers and Lloyd's members is based on the Financial Services Authority (FSA) regulatory rules on CERs.

Under the Solvency II Directive, it will no longer be possible to recognise CERs in regulatory terms; nor do International Financial Reporting Standards IFRS accounts permit them to be used. Following initial consultation already undertaken, the options proposed by the Government for dealing with this are to provide for continued tax relief or to ensure that the reserves are released over a transitional period of six years if relief is withdrawn. The Government has stated that it is minded to legislate for CERs to be retained for tax purposes provided that industry can make a sound case for the retention of such relief.

The intention is for a further consultation to take place to discuss this matter in greater detail.

The Government has also highlighted that, in any event, the case for maintaining a CER will be reviewed again when possible volatility implications of Phase II of IFRS 4 Insurance Contracts become clear.

## Who is affected

General insurers and Lloyd's corporate and partnership members recognising CERs for tax purposes.

## Timing

Further consultation is expected to take place over Summer 2011 although precise dates have not yet been confirmed.

## Our view

The outlook is very much dependent on the progression of the forthcoming consultation. Whilst the indications from the Government are promising, the onus is on the industry to justify the retention of CERs. However, it is encouraging that the Government intends to put a transitional arrangement in place in the event that CERs are not retained for tax purposes.

# Stop-loss and quota share insurance

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

HM Revenue and Customs have now changed their views on the timing of tax deductions in respect of stop-loss and quota share reinsurance premiums, after inviting comments following the previously unannounced amendments made to the Lloyd's manual in December 2009. HMRC now believes that the position under existing law is that member-level stop-loss premiums are admissible in accordance with the normal rules concerning trading profits. New rules will be introduced to align the timing for the deduction of expenses with the taxation of the profits to which the expenses relate.

## Who is affected

Corporate members at Lloyd's that enter into member-level reinsurance arrangements.

## Timing

The new rules will be included in Finance Bill 2012 following a period of informal consultation with interested parties. The guidance in the Lloyd's manual is to be updated shortly.

## Our view

This is an opportunity for HMRC to provide, through the legislative process, clarity to the timing treatment of reinsurance expenses for Lloyd's corporate members. The original legislation dates back to 1994 and is silent on the timing of relief for expenses, so it is refreshing to see proposed changes through legislation (following consultation) instead of just via changes to HMRC's Lloyd's manual or through enquiries to individual company tax returns. HMRC had originally announced it was their view that deductions would only be valid on a declarations basis from 1 January 2011, so this announcement and change of approach enables companies to continue to file on their current basis until the changes proposed for Finance Bill 2012 take effect.

# Future consultations and other measures

A feature of Budget 2011 is the announcement of consultations over the coming months in some key areas of the tax landscape. The consultations and future changes relevant to Corporation Tax are summarised below.

## CFCs

It has been announced that the proposed partial finance company exemption, to be included in the new CFC regime, will result in taxation of one-quarter (rather than one-third, as previously suggested) of the profits derived from overseas group financing arrangements. This will produce a relatively competitive regime, with a UK effective tax rate of just 5.75 percent once the corporation tax rate falls to 23 percent in 2014. A consultation document with further details on the new CFC rules is to be published in May 2011, followed by draft legislation in autumn 2011, for inclusion in Finance Bill 2012.

## Patent Box

As planned, the Government will continue to consult on Patent Box proposals. A consultation document will be released in May 2011 providing further details on how the new regime might be shaped. Legislation will be proposed for Finance Bill 2012.

## R&D

The government has been consulting on possible changes to the R&D tax relief regime and has indicated that it will be publishing a response document in May 2011. Specific measures which have been flagged up for further discussion and which are intended to be legislated for in 2012 are as follows:

- Removal of PAYE/NIC cap for SMEs claiming R&D tax relief payable credit – SME companies can surrender tax losses arising from R&D expenditure for a payable credit. The amount of payable credit is capped at the amount of the company's PAYE and NIC liability for the period. This proved to be an obstacle for companies which might be using subcontractors or agency staff to carry out their R&D, and also introduced complexity around checking PAYE payments under group arrangements or where PAYE payment periods did not line up exactly with accounting periods for Corporation Tax purposes.

Removal of the cap would be a welcome simplification, and removes an obstacle to claims by some loss making companies in a start up position, or without many staff.

- Removal of the de minimis level of qualifying R&D expenditure – In order to claim the R&D reliefs a company previously had to incur qualifying R&D expenditure of at least £10,000 per annum. This requirement is to be removed. This should open access to the relief to smaller R&D projects, which may be particularly relevant to smaller or start up enterprises.
- Relief for subcontracting parts of R&D projects – Currently, where Group company A subcontracts a part of its R&D project to Group

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company B, then Group company B can claim R&D relief so long as the work it carries out would have been R&D if carried out by Group Company A.

This measure means that within a group the parts of an R&D project can be carried out by different entities without each activity having to be R&D in its own right. So if one company was doing routine testing as part of another company's R&D project, it could still claim the R&D relief, even if considered by itself the testing did not amount to R&D.

This proposed measure would extend this treatment beyond members of a group to encompass third party claimants. The practical mechanics have not yet been fully decided.

### **Devolving corporate taxation to Northern Ireland**

The Government will publish a consultation paper on 24 March 2011, as part of their work with the Northern Ireland Executive to rebalance the Northern Ireland economy. This consultation will include the consideration of mechanisms for devolving the rate of corporation tax in Northern Ireland to the Northern Ireland Executive. The First Minister of Northern Ireland has previously called for a reduction in the corporation tax rate in Northern Ireland, to match the lower corporate tax rate in the Republic of Ireland. We await the detail of the consultation document.

### **Real Estate Investment Trusts (REITs)**

An informal consultation exercise will be undertaken to reduce barriers to entry to the REIT regime and to make it easier for investors to invest in REITs. In particular, this may help the creation of the long-awaited residential REIT since the UK residential investment sector is currently fragmented so would benefit from any measures to encourage newly created REITs.

The measures subject to consultation are:

- Introduction of a diverse ownership rule for institutional investors that will enable them to meet the close-company rules. While this is welcome it would be preferable if HMRC could start with a blank sheet of paper on this rule rather than just amend it for one investor class.
- Relaxation of the listing requirement and introduction of a grace period before the close company test needs to be met. This will help the introduction of "incubator" REITs.
- Abolition of the conversion charge for companies joining the REIT regime. This would be very welcome as the current two percent charge is a real barrier for potential new entrants.
- Allowing cash to be a good asset for the purpose of the 75 percent asset test. Again, this would really help new REITs raising money from investors as they will be able to make commercial decisions on when and how to spend the cash.
- Redefinition of financing costs for the interest cover test and extension of the time limit to comply with the distribution requirement.

It is intended that the informal consultation will be completed in time for any measures to be included in Finance Bill 2012.

### **North Sea Oil Tax**

Legislation will be introduced in Finance Bill 2012 to restrict tax relief for decommissioning expenses to the 20 percent rate of supplementary charge. See "Increase in UK oil tax rate".

## **UCITS IV: tax transparent fund vehicle**

Consultation is to commence in June 2011 to introduce a tax transparent fund vehicle. See “UCITS IV: Management Company Passport”.

## **Charities**

Consultations on various charity measures. See “Charities and Charitable Giving”.

## **Distributions working group**

HMRC has set up a working group with tax professionals to identify and help resolve remaining points of uncertainty surrounding the distributions legislation following the introduction of the distribution exemption on 1 July 2009. Further legislation was introduced in Finance (No.3) Act 2010 intended to clarify broadly that distributions paid out of reserves of a UK or foreign company created by a capital reduction should qualify for the distribution exemption and not be taxed as a part-disposal for capital gains purposes.

However, there are a number of practical points which remain uncertain in relation to dividends received by both individuals and corporates, including dividends in specie and certain foreign dividends such as those paid directly out of share premium or net assets. This area is particularly topical pending the publication of the Second Tier Tax Tribunal’s decision in the case of First Nationwide TC00339 which concerns whether a dividend paid directly out of the share premium of a Cayman company should be reclassified as a return of share capital.

These issues will be addressed by publishing comprehensive guidance or enacting legislation in Finance Bill 2012. If legislation is required the Government will consult on draft clauses in the autumn.

## **Tax treaties anti-avoidance**

The Government intends to introduce an anti-avoidance measure in Finance Bill 2012 to ensure that relief or exemption from UK tax is not given where a claim is made under the UK’s double taxation treaties and where arrangements have been made in relation to the claim to avoid UK tax. This measure will apply to UK resident individuals, trustees and companies and to overseas residents including where the latter are based in countries with which the UK does not have a double taxation treaty.

Such an approach would be in accordance with generally accepted international principles as set out by the OECD in the Commentary to its Model Tax Convention (e.g. in respect of Article 1) concerning the use of conduit companies and other artificial legal structures that have a main purpose of obtaining benefits under double taxation treaties. The Government will be consulting on this measure and it will invite representations on the draft clauses when they are published in the autumn.

## **Debt cap**

The Government has identified a number of practical issues with the debt cap rules, including the de minimis amount, which need to be addressed. It is proposed that, following further consultation, draft legislation will be published in autumn 2011, for inclusion in Finance Bill 2012. Hopefully, such changes will make the debt cap rules easier to apply and remove some of the anomalies that still exist.

### **Dishonest tax agents**

A consultation document entitled "Working with tax agents: the next stage" was published in December 2009 and was followed by draft legislation on deliberate wrongdoing by tax agents in February 2010. Subsequently there have been further informal consultations but no published documents. The informal consultations are to continue and a new consultation document and revised draft legislation are to be issued in July 2011.

### **Digital default consultation**

As part of its "One Click" programme designed to improve access to online services, the Government has announced that it will consult on how it will mandate use of the new online Registration Wizard for the main business taxes. The consultation will take place during summer 2011 with mandation coming into effect after August 2012.

### **Bank Capital Instruments**

In response to the credit crisis, Banks will be required to hold significantly greater amounts of loss absorbing regulatory capital. This is likely to involve the creation of new types of contingent capital instruments that behave more like equity during times of stress. Examples are contingent convertibles (CoCos) and bail-in bonds. These capital instruments are likely to contain a number of features that make their tax treatment uncertain. HMRC have announced that a working group will be formed to explore the associated tax issues and consider whether legislative change may be required (likely in Finance Bill 2012). This is a welcome move. It will be important that tax law keeps pace with the emerging regulatory environment so as to reduce uncertainty for issuers and holders of new capital instruments.

### **Capital Allowances for the new Enterprise Zones**

The Government will consider introducing, in a limited number of cases, enhanced capital allowances to support the new enterprise zones. We presume the Government means a similar scheme to the previous Enterprise Zone Allowances where a 100 percent initial allowance was due on anyone incurring expenditure on a building or structure in a designated zone. It is noted the Government favoured bias is towards high value manufacturing and it will be very interesting on how this sector is defined.

### **Plant and machinery allowances in relation to Fixtures**

HMRC will publish a consultation document in May 2011 to introduce new rules that businesses must pool their expenditure on fixtures (fixed plant and machinery) in a building within a short period of acquiring the building in order to qualify for capital allowances. It is unclear why HMRC are looking to target fixtures only and this may mean we have a further complication on when you can pool assets dependant on if the plant and machinery has become a fixture or not.

### **Capital Allowances anti-avoidance rules**

Changes will be made to anti-avoidance legislation contained at Chapter 17 of the Capital Allowances Act 2001. The Government intend to replace the 'sole or main benefit' test with a more effective rule that is aligned to anti-avoidance rules elsewhere in the Taxes Acts. The clear inference is that the current drafting is not, in HMRC's view, achieving the desired effect. Recent history tells us that HMRC are likely to take a very prescriptive and mechanistic approach to perceived abuses. It is hoped

that the consultation that is being proposed (beginning in May 2011) on these changes will allow sufficient debate and scrutiny to ensure innocent transactions are not caught out by the proposed changes.

#### **Feed-in-Tariffs and Renewable Heat Incentives**

The Feed-in-Tariff (FIT) scheme was introduced in April 2010 and the Government is due to introduce the Renewable Heat Incentive (RHI) in the summer of 2011. Where the electricity and heat generation is carried on by a business then capital allowances may be due in respect of the generating equipment. The Government will be introducing legislation to clarify the capital allowances treatment of such expenditure to ensure a consistent approach. This is an area that should be relatively easy to clear up and we look forward to participating in the consultation which is due to commence in May 2011.

#### **Simplification of regulatory penalties**

The Government will be consulting on the range of penalties that HMRC can impose for failure to comply with regulatory obligations across the tax and duty regimes. It will publish a consultation document to consider options for simplification in June 2011.

# Revisions to measures published in Finance Bill 2011 draft clauses

# Bank Levy

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## Brief overview

The Bank Levy will be a tax based on total chargeable equity and liabilities of banks and building societies where these exceed £20bn. The Levy will be imposed with effect from 1 January 2011. Originally, reduced rates were to be applied for 2011. The Chancellor announced on 8 February 2011 an increase in the rates of Levy for 2011 so that for 2011 as a whole the Levy would be payable at the full rate.

## Key changes announced at the Budget

The Chancellor announced that the main rates for the Levy that apply from 1 January 2012 would be increased from 0.075 percent to 0.078 percent for short-term chargeable liabilities and from 0.0375 percent to 0.039 percent for long term chargeable equity and liabilities. It is expected that the change will raise additional revenue of approximately £100m in each full year to which it is applied.

## Our view

Banks and building societies will be disappointed by the increase in the Bank Levy rates for 2012 and subsequent periods. Of particular concern will be the uncertainty that has been caused by two changes to the Bank Levy rates in successive months.

## *What we wrote when the draft clauses were published 9 December 2010*

Impact on taxpayer			
Positive	Neutral	Negative	Both positive and negative

### Summary of proposal

In the June 2010 emergency Budget, the Chancellor announced the introduction of a Bank Levy, effective from 1 January 2011, in respect of certain equity and liabilities on banks' balance sheets. Following a consultation process which concluded on 5 October 2010, initial draft legislation was published on 21 October 2010, with further details of administration and collection procedures and anti-avoidance measures published more recently. The final draft legislation has now been published.

The Bank Levy will be charged based on total chargeable equity and liabilities reported in the relevant balance sheets of affected banks and building societies. For UK banking groups the levy will be imposed on the group's global consolidated balance sheet whereas for foreign banking groups the levy will be imposed on the UK group/subsidiary balance sheet and a proportion of the foreign bank's balance sheet where that foreign bank operates in the UK through a branch.

In determining chargeable equity and liabilities certain amounts may be excluded, the most important of which are Tier 1 capital, certain insured customer deposits and some insurance liabilities. Certain liabilities may also be reduced by netting against them certain assets or offsetting high quality liquid assets held for regulatory purposes.

The levy will be imposed at a rate of 0.0375 percent for long term liabilities (in excess of 12 months) and 0.075 percent for short term liabilities. A reduced rate applies for 2011 (0.025 percent for long term liabilities and 0.05 percent for short term liabilities).

The levy will not be charged on the first £20 billion of chargeable equity and liabilities and therefore many small banks and building societies would not expect to be affected.

According to the impact assessment the levy is designed to raise £2.6 billion annually from 2013-2014 and will be permanent.

### Who is affected

UK banks, banking groups and building societies, foreign banking groups operating in the UK through a permanent establishment or subsidiary and UK banks and banking sub-groups in non-banking groups. The definition of banking group is wider than pure banks and in some cases other financial institutions will need to consider whether they could fall within the definition.

### Timing

The Bank Levy will apply to periods of account ending on or after 1 January 2011. Where the period of account starts before 1 January 2011 the Bank Levy due is reduced on a pro-rata basis according to the part of the period falling before 1 January 2011. Going forward, the levy will be

payable quarterly in line with the regime for quarterly instalments of corporation tax.

#### **Our view**

The imposition of the Bank Levy is a controversial development and many banks will find it hard to reconcile its introduction with the UK's ambitions to maintain a competitive tax regime. However the consultation period has been productive and a number of changes to the original proposals will be welcomed. The legislation is lengthy and complex and banks and building societies will now need to work through the detailed provisions to determine the potential impact.

The most significant change is that the rates at which the levy will be imposed have increased for both short and long term liabilities. The lower rates for 2011 have also increased in both cases. It may be the case that the changes in the rates are designed to ensure the levy meets its revenue raising objectives following the changes made to the legislation during the consultation period. The most significant change has been the introduction of a £20 billion allowance rather than a £20 billion threshold, which is important for smaller and medium sized banks and building societies.

# Taxation of foreign branches

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## Brief overview

The Budget has confirmed that legislation will be introduced in Finance Bill 2011 to exempt the profits of foreign branches of UK resident companies from corporation tax on an elective basis. In addition, changes are to be made to the draft legislation published on 9 December 2010 following consultation. The revised draft legislation is not yet available.

## Key changes announced at the Budget

The transitional rules surrounding loss-making branches will be made more workable to allow more companies to enter the regime. It is anticipated this change will mean that a company's profitable branches will be able to benefit from the regime from the outset with loss-making branches being separately streamed until their losses are used up.

In addition, the anti-diversion rules which exclude a branch from the regime if it is used to divert profits artificially from the UK will be made more targeted and proportionate. These rules are currently based on certain key principles of the Controlled Foreign Companies (CFC) rules. It is anticipated the changes will make it easier to establish the motive test is met in relation to a foreign branch through, for example grandfathering measures for existing foreign branches that are currently within the charge to corporation tax.

There will also be specific legislation dealing with the computation of capital allowances where assets are used for the purposes of an exempt branch. Life assurance companies will now potentially be able to benefit from the exemption in respect of non-UK business written through their foreign PEs.

HMRC will also seek to address potential issues surrounding withholding tax on interest paid to exempt branches.

## Our view

The changes to the draft legislation should make it easier for companies such as some financial institutions that currently have losses in one or more of their branches to benefit from the regime. In addition, the further clarity around the anti-diversion rules should make it easier for companies to establish whether their foreign branches in low tax territories are eligible for the regime.

## *What we wrote when the draft clauses were published 9 December 2010*

Impact on taxpayer			
Positive	Neutral	Negative	Both positive and negative

### Summary of proposal

Following a discussion document earlier this year and detailed announcements contained in the Corporate Tax Road Map, the Government has published draft legislation for an exemption from corporation tax for foreign branch profits. This reflects their intention to make company taxation both more competitive and more territorial, in line with the distribution exemption introduced last year. The key features of the regime are as follows.

- The branch exemption will apply to branches in treaty and non-treaty countries, with the profits exempted being defined by reference to the individual treaty (provided this contains a non-discrimination article) or the OECD model treaty in other cases.
- No relief will be available for branch losses after a company enters the regime. When a company with historic loss-making branches opts in to the regime its branch profits will become exempt only once its total branches' tax losses in the immediately preceding six years have been matched by subsequent profits of its branches (excluding capital gains and losses). This six year period is extend back to include earlier years if very large (at least £50 million) branch losses have arisen since a date to be determined which be six years prior to the commencement of this new régime.
- In either of the above transitional situations, an appropriate amount of credit for any foreign tax suffered will be allowed. There does not appear to be a restriction on the offset of unrelieved foreign tax brought forward.
- The attribution of chargeable gains and losses to exempt branches will follow the principles of the relevant tax treaty or the OECD model as appropriate. Chargeable gains of close companies will remain fully subject to capital gains tax.
- Investment income will be included in exempt profits where the economic ownership of the assets generating the income lies with the branch rather than some other part of the enterprise. Branch exemption will not be available to a company whose business is wholly or mainly investment business.
- The usual treaty approach to capital attribution will broadly apply to establish the measure of the branch's profits based on the allocation of such equity and loan capital to the branch as it would reasonably be expected to have if it were a separate entity. HMRC will require the amount of capital attributed to a foreign branch to be adjusted if it is outside an appropriate arm's length range.
- Companies will also be expected to minimise the profits subject to tax in the branch country, e.g. by taking full advantage of the extent to which the treaty limits that territory's taxing rights through available claims and elections.

- Foreign branch exemption is not available for profits from international shipping and air transport but only to the extent that these activities are not taxed by the foreign jurisdiction due to the application of the relevant double tax treaty.
- Profits will not be exempt where they would be subject to a CFC apportionment if they arose in a foreign subsidiary. This should prevent taxpayers from exploiting the branch exemption to avoid the CFC rules. It will be achieved with legislation applying existing CFC rules to foreign branches but with a motive test, a lower level of taxation test and a *de minimis* level of profit as the only available carve-outs. These measures will then need to be repealed in 2012 when the new CFC regime is expected to take effect which will then apply equally to both foreign subsidiaries and exempt foreign branches. In addition, the election to join the regime will be deemed not to apply in computing a CFC's chargeable profits.
- Where a manufactured overseas dividend (MOD) is paid by a UK resident company in the course of a trade carried on by a foreign branch, the scope of existing UK withholding tax requirements will be reduced.

#### Who is affected

The proposals will potentially apply to all large companies with foreign branches and small and medium-sized companies with foreign branches in territories with which the UK has a double taxation agreement containing a non-discrimination article with the UK. They will be most relevant for industry sectors typically operating through foreign branch structures i.e. insurers, banks and oil and gas companies and are intended to create a level playing field across different business operating models.

#### Timing

The rules take effect next year from a date to be announced. It will be possible to elect into the regime from the start of the accounting period following the election. The election is on a company by company basis and irrevocable but can be revoked up to the filing date for the tax return for the first accounting period in which it would have effect. The existing double taxation relief credit regime continues to apply for companies not making the election.

For companies with calendar year-ends, the earliest effective start date will therefore be 2012. The start date for life assurance companies may be deferred further pending an ongoing reform of the taxation of such entities expected to be complete in 2013.

#### Our view

In overview, the proposals mean that companies with foreign branches will have considerable flexibility in choosing how they are taxed. The regime will be more favourable than the branch exemption operated by many other territories which often limit their exemption to treaty countries and have stringent loss claw-back rules.

As the regime will apply on an elective basis, taxpayers for which loss relief is more important, such as the oil and gas industry, can continue to apply the existing credit rules. However, the exemption is subject to the same protection against artificial diversion of profits as for foreign subsidiaries making it more complex to operate than previously hoped.

# CFC interim improvements

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## Brief overview

Following consultation, the Government has announced that a number of changes are to be made to the Controlled Foreign Companies (CFC) interim improvements to make it easier for businesses to benefit from them.

## Key changes announced at the Budget

Although it has been announced that a number of changes are to be made to the design of the new exemptions, no further details have been provided except that the new temporary exemption, which can apply for up to three years, will also be available to previously UK-headed groups if they return to the UK.

It has also been decided that the interim improvements will have effect for CFC accounting periods beginning on or after 1 January 2011 (except the extension of the transitional rules for holding companies, which will be deemed always to have had effect).

### Our view

It will be necessary to wait until Finance Bill 2011 is published on 31 March to see what changes are being made to the new exemptions. We will also need to wait to see whether the extension of the new temporary exemption actually results in any groups deciding to return to the UK.

It is helpful that the interim improvements are to be introduced sooner than was initially announced, allowing, for example, CFCs with 31 December year-ends to rely on the new exemptions one year earlier.

## *What we wrote when the draft clauses were published 9 December 2010*

Impact on taxpayer			
Positive	Neutral	Negative	Both positive and negative

### Summary of proposal

Finance Bill 2011 will include legislation to deliver a package of interim improvements to the CFC rules with the aim of making the rules more competitive ahead of full reform in 2012.

The draft legislation includes changes to the CFC rules in five areas:

#### New exemption for certain intra-group activities

A new exemption will apply to CFCs engaged in the provision or consumption of intra-group goods and services where there is little or no UK connection. Various conditions will need to be met in order for a full exemption to apply, including that no more than 10 percent of the CFC's gross income or expenditure is UK-related and no more than 5 percent of its gross income consists of finance/IP income. Full exemption will also apply, even if the proportion of transactions with the UK is between 10 percent and 50 percent, provided the CFC has sufficient staff based outside the UK and its profits do not exceed 10 percent of its relevant staffing costs (the so-called "safe-harbour").

There will also be a partial exemption mechanism under which it will be possible to apply to HMRC to agree a reduced CFC apportionment where the safe-harbour above is not met or if the amount of finance/IP income exceeds the 5 percent limit (provided that any IP income on its own does not exceed the 5 percent limit).

#### New exemption for exploitation of IP with no UK connection

A new exemption will apply to CFCs whose main business is to exploit IP where the IP and the CFC have minimal UK connection. Various conditions will need to be met in order for a full exemption to apply including that the relevant IP has not been held in the UK within the preceding 10 years and activities relating to the creation, maintenance or enhancement of the IP have not been carried on in the UK. The CFC must also not have a significant UK connection by reference to the extent to which funding of its main business is provided from the UK (other than by way of debt), the extent to which its gross income is derived from the UK and the extent to which it incurs expenditure on R&D or the creation, maintenance or enhancement of the IP carried on in the UK.

The partial exemption mechanism will again be available where the amount of finance income earned by the CFC exceeds the 5 percent limit.

#### New temporary exemption following acquisition or reorganisation

The current 'period of grace' approach is to be formalised and expanded to allow foreign companies coming under UK control for the first time as a result of an acquisition or reorganisation (including groups migrating to the UK) for a period ending 24 months after the end of accounting period in which the acquisition or reorganisation takes place. Thus, exemption will be available for up to three years.

The temporary exemption will apply on a company by company basis and a change in the main business or activities of a CFC will not affect the exemption unless, and to the extent, it erodes the UK tax base. In such circumstances, it will be possible to apply to HMRC to agree an apportionment which reflects only the profit relating to the change.

#### Improving the de minimis exclusion

For CFCs in a group which includes at least one large company, the de minimis limit is to be increased to £200,000 (proportionately reduced for periods of less than 12 months). The existing limit of £50,000 will continue to apply for groups which consist only of small and medium sized companies.

In addition, for all CFCs, the starting point for the computation of profits will be accounting profits calculated in accordance with GAAP, excluding capital gains/losses. For CFCs in a large group, the accounting profits will need to be adjusted in line with the transfer pricing rules (except where any such adjustment is less than £50,000). Anti-avoidance measures will prevent CFCs claiming the exemption where they are involved in arrangements undertaken purely to take advantage of the exemption.

#### Extending the transitional rules for superior and non-local holding companies

The transitional rules, included in Finance Act 2009, which allow certain superior and non-local holding companies to continue to satisfy the exempt activities test are to be extended for an additional 12 months to 1 July 2012 to cover the period to full reform.

#### Who is affected

UK companies with overseas subsidiaries.

#### Timing

It is likely that the changes (apart for the extension of the transitional rules for holding companies, which will be deemed always to have had effect) will have effect for CFC accounting periods beginning on or after 1 April 2011, although this is subject to further consultation with business.

#### Our view

The interim improvements, although limited, show we are moving in the right direction as regards reform of the CFC rules. The new intra-group activities exemption is particularly helpful in allowing companies involved in intra-group activities to be exempt under the CFC rules, although the rules are not straightforward. The non-UK IP exemption is much more restricted but it is at least a start in the development of a more favourable regime for IP.

# Investment companies – functional currency

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## **Brief overview**

Legislation is being introduced to enable investment companies to specify the currency in which their corporation tax computations are prepared.

This will be relevant where taxable profits and losses are based on accounting figures, such as for loans, but will not affect the computations of capital gains which will continue to be calculated in sterling.

## **Key changes announced at the Budget**

The scope of the rules is to be restricted so that companies will only be able to make an election where their main purpose is to make investments. However, if such a company makes an election, it is understood that this will apply to all its activities where the taxable profits are based on accounting figures.

In addition, the rules will make provision for newly incorporated companies. It is understood that this change is being made to enable such companies to make an election for their first period.

## **Our view**

The opportunity for investment companies to specify the currency to be used in their corporation tax computations is positive. It is expected that this will provide a useful technique to manage the exposure to taxable exchange differences, particularly in relation to loans and derivatives.

## *What we wrote when the draft clauses were published 9 December 2010*

Impact on taxpayer			
Positive	Neutral	Negative	Both positive and negative

*Negative for those who have entered into tax avoidance schemes, but with some beneficial simplification measures for other investment companies*

### Summary of proposal

The starting point for preparing corporation tax computations is that these must be computed in Sterling. However, computations are prepared in another currency where certain conditions are satisfied. This can, for example, be the case where the accounts are prepared in a non Sterling currency.

Legislation is to be introduced which will permit UK resident investment companies to designate the currency to be used.

- An election is required to be made before the first period of account for which it is to apply.
- It is possible to make further elections which will apply from the next period of account onwards.
- The election will continue to have effect until a further election is made or the relevant conditions (see below) cease to be satisfied. It is intended that an election can also be revoked with effect from the start of the next period of account.
- A currency may only be designated where either a significant proportion of the assets and liabilities of the company are denominated in that currency or a condition based on the rules for accounting consolidations is satisfied. If neither of these conditions are satisfied at some point in a period, the election ceases to have effect for that period and for subsequent periods.

There is an anti-avoidance measure which will exclude exchange gains and losses from loan relationships and derivative contracts arising in the first period of account in which the election is effective if these would not have arisen but for the election. This measure will also apply where there is a change in functional currency.

The application of the anti-avoidance measure is not entirely clear and it may need to be modified.

### Who is affected

Companies which have an unhedged exposure to tax on exchange differences arising on loans and derivatives.

### Timing

The rules will apply to periods of account beginning on or after 1 April 2011. It is possible to make and revoke elections from 9 December 2010 even though the legislation will not be enacted until Royal Assent for Finance Act 2011.

### **Our view**

The facility for investment companies to choose the currency in which computations are to be prepared is very welcome. Further work may be required to clarify the rules.

# Group mismatches – loan relationships and derivatives

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## **Brief overview**

Draft legislation was published on 6 December to counter transactions within a UK corporate group which derive a tax advantage from the mismatch through asymmetry in the treatment of either loan relationships or derivative contracts. Such arrangements are defined in the legislation as a 'group mismatch scheme' (GMS). There was a further period of consultation subsequent to the publication of the draft legislation.

## **Key changes announced at the Budget**

Amendments have been announced which clarify the circumstances in which the mismatch rules will apply. The amendments provide that only mismatches between companies within the scope of UK tax are within the new rules. The other amendments add a provision to one of the alternative qualifying conditions that to fall within the definition of a GMS the scheme must provide a tax benefit of at least £2m and also that a new objective test must be applied in recognition of a GMS (in addition to the existing subjective motive test) such that the scheme is more likely to produce a tax advantage than a tax disadvantage.

## **Our view**

It is pleasing to see the clarifications these changes make.

## *What we wrote when the draft clauses were published 9 December 2010*

Impact on taxpayer			
Positive	Neutral	Negative	Both positive and negative

### Summary of proposal

HMRC have received repeated disclosures of schemes designed to achieve a mismatch in the treatment of intra-group loan relationships and derivative contracts and, in March 2010, issued a discussion paper for a principles based approach to counter such arrangements. Draft legislation was issued on 6 December 2010 which reflects the outcome of the consultations. Comments on the approach adopted and the detail of the draft legislation are requested by 9 February 2011.

The focus of the rules is on the term “relevant tax advantage” which means a post tax economic profit made by the group, from a scheme, which arises as a result of asymmetries in the way group entities treat debits and credits from loan relationships/derivative contracts. The definition covers situations where the asymmetry relates to the timing of debits and credits as well as to their amounts.

For example, if a loan between two UK group companies is structured so that the borrower obtains relief for the cost of borrowing but the lender is not taxed on the corresponding income, the tax saving would represent an economic profit resulting in a relevant tax advantage (provided this is more than negligible).

If the provisions apply, profits or losses from the loan relationships and derivative contracts are left out of account in all of the group companies which are party to the scheme. The intention is that the tax advantage is eliminated but no disadvantage is created.

The legislation is not intended to affect all intra-group loans/derivatives. It is targeted at schemes where, at the outset, it is practically certain that there will be a relevant tax advantage or the main purpose or one of the main purposes for entering into the scheme is the chance of securing a relevant tax advantage.

Some key points arise from the draft provisions.

- The rules will apply provided that it is practically certain that the scheme will produce a tax advantage. It will be necessary to make an assessment of this at the outset of the scheme.
- The provisions can apply even if there is no tax avoidance motive.
- It is intended that the rules will not apply where the asymmetry is as likely to produce a loss as a profit. An example of this is where a loan is made between two UK group companies which have different functional currencies, where one of the companies will recognise exchange differences.
- The scope of the rules includes the determination of chargeable profits for CFC purposes.

**Who is affected**

Groups which are involved in schemes where there is an asymmetrical UK tax treatment of loan relationships and derivative contracts involving group companies.

**Timing**

The rules will apply to schemes whenever entered into (including before 6 December 2010) but only in respect of profits and losses which relate to a time on or after Royal Assent to Finance Bill 2011.

**Our view**

This is principles based anti avoidance legislation with the intention of avoiding the need to legislate in a targeted manner in response to disclosed structures. The rules are potentially far-reaching and the opportunity to make representations should not be missed.

# Accounting derecognition of loan relationships and derivatives

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## **Brief overview**

Draft legislation was published in December 2010 amending legislation which counters arrangements by which a tax advantage is obtained through application of accounting 'derecognition' rules as applied to loan relationships or derivative contracts. The draft legislation required the 'derecognised' amount to be brought into charge. The draft legislation was effective from 6 December 2010 but an opportunity for consultation was provided.

## **Key changes announced at the Budget**

As a consequence of the consultation some amendments have been made to the draft legislation.

The amendments affect companies which engage in arrangements to derecognise loan relationships/derivative contracts in the accounts to secure a tax advantage.

The effect of the amendments is to apply the legislation to debits which arise from the derecognition of creditor loan relationships and derivative contracts and ensure that the legislation can only apply in circumstances in which the company with the loan relationship or derivative contract remains a party to the loan or derivative. The amendments will also ensure that the full difference between the fair value of a derecognised derivative amount and the accounts value is brought into charge.

The amendments apply from 6 December 2010, other than the basis for measurement of the quantum of benefit caught, which applies from 23 March 2011.

## **Our view**

The amendments clarify the circumstances of application of the rules and their operation.

## *What we wrote when the draft clauses were published 9 December 2010*

Impact on taxpayer			
Positive	Neutral	Negative	Both positive and negative

### Summary of proposal

Legislation was published on Monday 6 December 2010 to counter avoidance schemes involving the derecognition in the accounts of loan relationships and derivative contracts. Where the arrangements have a tax avoidance motive, the changes may require the recognition of income or deny relief for debits.

The starting point for the taxation of profits and losses from loan relationships and derivative contracts is the accounting treatment. The Government has legislated a number of times to counter arrangements which result in the non-recognition of income for accounting and tax purposes. Earlier this year, it was recognised that countering such arrangements by targeting specific schemes has not been effective, because further variations of the planning are subsequently developed. Accordingly, a technical note with draft legislation was published in July setting out a more principles- based approach and the legislation which has been published reflects the resulting consultations.

Amendments have been made to the existing legislation which counters derecognition planning (for loan relationships in sections 311/312 CTA 2009 and for derivatives in sections 599A/599B CTA 2009) broadly in line with the draft legislation published in July. The effect of the provisions applying is that the accounts must be adjusted, for tax purposes, to bring into charge amounts on the assumption that the whole loan relationship/derivative is recognised in determining the company's profit or loss for the period.

There are some significant changes to the draft legislation.

- The provisions will only apply where the main purpose or one of the main purposes of the arrangement is to obtain a tax advantage. It is expected that that this will "carve out" situations where a normal commercial transaction results in a loan relationship or derivative not being recognised for accounts purposes e.g. carrying derivatives off balance sheet in "old UK GAAP" companies which have not adopted IFRS or FRS 26.
- A company will now be treated as being a party to a loan asset for the purposes of this legislation even though it has disposed of its rights e.g. under a contract for the sale and repurchase of a loan.
- New provisions (for loan relationships in section 455A CTA 2009 and for derivative contracts in section 698A CTA 2009) are being introduced to deny relief for debits which arise on the derecognition of creditor loan relationships/derivative contracts, where those debits arise from arrangements of which the main or one of the main purposes is to obtain a tax advantage.

For example, where a group member agrees to transfer the right to cash receipts from a loan asset as a subscription for shares in another

group company, this may be accounted for as a credit to the loan asset and debit to the carrying value of the investment in the recipient of the shares. In these circumstances, the debit may be deductible (under section 320 CTA 2009). The new legislation would deny this deduction..

#### **Who is affected**

Companies where amounts in respect of loan relationships and derivatives are not fully recognised in the accounts as a result of tax avoidance arrangements.

#### **Timing**

The new rules apply to amounts accruing from 6 December 2010.

#### **Our view**

This is targeted anti avoidance legislation in respect of disclosed structures. It is welcomed that, following consultation, the measures are restricted to arrangements which have a main purpose of obtaining a tax advantage.

# Finance Bill 2011: Other previously announced measures

Draft clauses for the 2011 Finance Bill were published in advance of the 2011 Budget on 9 December 2010. Significant changes to these draft clauses announced in this Budget have been detailed above. Minor changes are as follows:

## **Tonnage Tax leasing**

The December 2010 draft legislation included minor changes to the capital allowances available to lessors of ships to UK tonnage tax companies. Essentially the rates of 20 percent for the first £40 million of expenditure on a ship and 10 percent for the next £40 million are replaced by linking the first £40 million to the rate otherwise available (this is likely to be the special rate for expenditure on or after 1 January 2011) and linking the next £40 million to the special rate. The new rules now extend to expenditure incurred on or after 1 January 2011 under an agreement preceding 1 January 2011.

It is not yet clear whether there will be any change to the position in 2011 and subsequently for expenditure incurred before 1 January 2011. The current rates of 20 percent and 10 percent given in the tonnage tax rules would need to be adjusted to reflect the prevailing main and special rates as these are expected to change on 1 April 2012. However, whilst the 20 percent rate has to date tracked the main rate, the 10 percent rate has not tracked the long life asset/special rate.

## **Modernisation of tax rules for investment trust companies**

There were minor revisions that do not affect the substance of the legislation. Draft regulations will be published towards the end of April 2011 setting out the detailed operational rules relating to the application process and obligations imposed on approved investment trusts.

## **Data-gathering powers**

Following the consultation document and draft legislation issued in December 2010, there will be a small amendment to the data-gathering legislation to make clear that documents requested by a notice need only be provided if they are within the possession or power of the person to whom the notice is sent. A consultation response document is to be published on 31 March 2011.

## **Oil and gas minor measures**

A reinvestment relief was introduced in Finance Act 2009 that provided for an exemption from chargeable gains for certain disposals of UK Oil and Gas assets where the company incurred expenditure on, broadly, offshore assets. Following consultation in early 2011 the draft legislation has been slightly amended to ensure it will allow the reinvestment to be made by incurring expenditure on exploration, appraisal and development activities.

The reinvestment relief application to exploration, appraisal and development activities is effective from 24 March 2010.

### Corporate capital gains simplifications: degrouping charges

There are some minor drafting changes to clarify the intent of the draft legislation to simplify the rules for the calculation of capital gain degrouping charges for companies. Other changes also cover the situations where companies leave a group as a result of a share for share exchange and where there are minority investors in a company that leaves a REIT group.

No details have been included in this commentary on those draft clauses published in December for which no changes have been announced. The corporate tax measures to be included in Finance Bill 2011 not covered in this Budget commentary are as follows:

- Small profits rate: associated companies
- Capital Allowances – Reduction in writing down allowances
- Capital Allowances – Reduction in Annual Investment Allowance (AIA)
- Corporate Capital Gains (Simplification): Value Shifting
- Corporate Capital Gains (Simplification): Pre-entry Losses
- Group mismatches – convertible loans
- Reform of Stamp Duty Reserve Tax on Collective Investment Schemes
- OECD Transfer Pricing Guidelines
- Changes to Accounting Standards for Leases
- Life assurance apportionment rules
- A copy of our commentary on the draft Finance Bill (including these measures) can be found [here](#).'

# Other 2011 New Measures

## **Finance Bill 2011: Other new measures:**

### [Taxation of index linked Gilt edged securities](#)

The definition of a gilt edged security which qualifies for exemption for companies from a tax under the loan relationship rules is extended to include gilts referenced to the Consumer Price Index (CPI) as well as the retail price index (RPI). As the law currently stands, the security would have to be indexed by reference to the RPI to qualify for this treatment. The measure is intended to assist companies with hedging exposures to CPI movement.

### [Vaccine Research Relief](#)

The main change to the Research & Development (R&D) relief has been the increase in the small and medium sized enterprises (SME) rate. Accompanying this is a restriction to the vaccine research relief for SMEs so that the overall State Aid intensity is not exceeded. This restriction will be to 20 percent from 1 April 2011 and to zero (for SMEs) from 1 April 2012.

## **Other announcements**

### [Capital allowances – Energy Technology List](#)

The Energy Technology List in relation to Enhanced Capital Allowances will be updated by Treasury Order in the summer of 2011 with one new technology, certain energy efficient hand dryers. This is in line with previous years and allows taxpayers to continue to invest in qualifying plant and machinery that will attract a 100 percent First Year Allowance.

### [Film Tax and Community Investment Relief](#)

The Government has confirmed that the future of two state aid reliefs which encourage UK investment will be secured, following re-notification to the European Commission. The first aid is film tax relief which applies to expenditure on British films. The second is Community Investment Relief, which provides tax relief to companies who invest in community finance institutions, set up to lend to businesses, social enterprises and individuals who may not be able to raise finance from high street banks.

### [Time to pay](#)

The Government has confirmed that HM Revenue & Customs' (HMRC's) Business Payment Support Service, which was launched in 2008 to provide advice and time to pay to viable businesses in temporary financial difficulty, will continue to operate.

### [Customer cost reduction announcement](#)

Since 1 April 2006 HMRC has set itself targets for reducing the administrative burdens on business of providing information both to itself and to third parties. HMRC has now announced that it will expand its narrow administrative burden target to include wider customer compliance costs whilst committing not to increase administrative burdens under the existing measure over this spending review period. This fits with HMRC's aim of improving its service and reducing business costs.



## Indirect Tax



**Gary Harley**  
Head of Indirect Tax

This was a Budget comprising a lot of rather minor announcements as far as VAT was concerned, many of which will not come into effect until 2012. Many consultations were also announced.

The widely predicted changes to the Low Value Consignment Relief turned out to be rather less draconian than had been anticipated, as the threshold has only been reduced by £3 (to £15) for now (wef 1 November 2011). Under current EU law, the UK could have reduced the limit to £9. The possible sting in the tail here though is the announcement that the UK is looking to agree a derogation from the EU law which could further limit the relief.

The UK found out, again, that when it comes to indirect tax, we are not an island. The previous announcement that Air Passenger Duty was to change at some point from a per passenger tax to a per plane tax has foundered on this rock, as the UK has established that this approach would be illegal under international law. APD is to be frozen until April 2012. At present passengers on private jets are exempt from APD since they do not pay for a ticket – consultations will take place over the next 12 months regarding the application of APD to passengers on such flights.

There was some relief for the hard pressed motorist in the Budget though. The duty on road fuel will decrease by 1p a litre from 6pm on Budget Day. The planned increase next month will be postponed until 1 January 2012 when the duty rate will increase by just over 3p a litre. This is only a temporary and small respite but given the enormous increase in fuel prices over the last few months, due to inflation and the increase in the cost of oil, it will be welcome.

The coalition Government has introduced a new approach to tax policy making and in line with this policy draft clauses for the 2011 Finance Bill were published in advance of the 2011 Budget on 9 December 2010. The structure of our commentary has changed to accommodate this new approach. All announcements relating to tax policy are set out in a separate section at the beginning of the commentary and then each tax section is ordered as follows:

- New measures not previously published in draft to be included in Finance Bill 2011.
- Measures to be included in Finance Bill 2012 or later.

Some measures to be included in Finance Bill 2011 were published in draft on 9 December 2010. A full copy of our original commentary from December can be found [here](#).

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# New measures for Finance Bill 2011

# VAT: Low Value Consignment Relief

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The reduction of the value eligible for low value consignment relief from £18 to £15.' Currently it is possible to import goods from outside the EU free of VAT and duty where the value of those goods is below £18. A number of online retailers benefit from these provisions and supply goods, including CDs, DVDs, office stationery, and other items easily posted to customers in the UK. In such cases the customers are the importer of record rather than the supplier.

HMRC have been concerned that this practice distorts competition for high street retailers unable to set up operations outside the UK. They have been keen to limit its application and have sought to litigate the issue.

The reduction in rate is to be accompanied by engagement with the EU Commission to agree, if possible, the terms of derogation from the EU law which would further limit the application of the relief in the UK.

## Who is affected?

Online and high street retailers of goods of low value.

## Timing

The new rule takes effect from 1 November 2011.

## Our view

Some form of measure to limit low value consignment relief was anticipated in this budget. The EU law provisions would have permitted a reduction in the relief value down to £9. The measure will impact the price point for CDs and DVDs predominantly but save in more exceptional circumstances will not have a great impact.

The consultation seeking derogation is perhaps more significant. Other EU countries had already been granted derogations to exclude mail order imports from the relief. It is unclear what form of derogation HMRC might seek.

# Fuel Duty rates

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The Chancellor announced a temporary decrease by one pence per litre (ppl) from 6 pm on Wednesday 23 March, and deferred the planned April increase to 1 January 2012 when the main fuel duty rate will increase by 3.02 ppl. The Chancellor also announced the abolishment of the inherited fuel duty escalator which will be replaced by a fuel stabiliser system.

There will also be decreases to non road fuels, bio fuels for road use, biofuels and bioethanol. Natural gas and liquefied natural gas (LPG) for road use will be reduced by 1.45 pence and 1.43 pence per kg respectively, to maintain the differential with road fuels in pence per litre equivalents.

The decrease in duty on aviation gasoline by 0.65 to 0.3770 ppl will take effect from 6pm on Wednesday 23 March.

Biodiesel made from waste cooking oil will continue to benefit from a 20ppl duty differential until 31 March 2012.

## Who is affected?

Manufacturers, importers, distributors, retailers and consumers of fuel products

## Timing

The new rates will take effect on and after 6pm 23 March and on and after 1 January 2012.

## Our view

The unexpected decrease in fuel duty rates will be welcomed by businesses and consumers. However the measure is only likely to provide temporary respite from the January 2012 increase. The introduction of a fuel stabiliser system may counterbalance the volatility of fuel prices but with no guarantees that the system will see pump prices fall.

# Alcohol: Duty Rates

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

Legislation will be introduced for the proposed increases on duty rates for alcohol. Duty rates for all alcoholic drinks will increase by two percent above inflation. As anticipated, the Chancellor confirmed the changes to the beer duty regime by introducing a new additional duty on high-strength beers (above 7.5 percent abv) to be twenty five percent of the general beer duty rate along with the introduction of new reduced rate of duty on lower strength beer (at or below 2.8 percent abv and above 1.8 percent abv) to be fifty percent of the general beer duty rate.

## Who is affected?

This will affect manufacturers, importers, distributors, retailers and consumers of alcoholic beverages.

This year's changes will have the following impact on retailing prices equivalent to:

- 54 pence on a 70cl bottle of spirits at 37.5 percent abv;
- 4 pence on a pint of beer;
- 15 pence on a 75cl bottle of wine

## Timing

The increase takes effect on 28 March 2011 while the new duty on high and lower strength beer takes effect on 1 October 2011.

## Our view

The increase in alcohol excise duty rates is in line with expectation and confirms the Government's plan to continue with the inherited alcohol duty accelerator. The increase is significant and will have a damaging impact on the brewing industry and pubs. All these increases will be unpopular in the business and ultimate consumers will be faced with a new increase in the retail price in addition to the recent increase of the VAT rate to 20 percent. The introduction of a new tax band for low strength beer and additional high strength beer demonstrate the Government's commitment to influence consumers to move to low strength beer

# Increase in rates of duty on tobacco products

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

Legislation will be introduced in the Finance Bill to increase the rates of duty on tobacco products imported into the UK or manufactured in the UK.

This will result in the following changes being made to the duty rates on tobacco products:

- cigarettes: an amount equal to 16.5 percent of the retail price plus £154.95 per thousand cigarettes;
- cigars: £193.29 per kilogram;
- hand-rolling tobacco: £ 151.90 per kilogram; and
- other smoking tobacco and chewing tobacco: £84.98 per kilogram.

This year's changes will have the following impact on retail prices equivalent to :

- 33 pence to 50 pence to a packet of cigarette;
- 67 pence to a packet of hand-rolling tobacco;
- 10 pence to a packet of 5 small cigars; and
- 17 pence to a packet of pipe tobacco.

## Who is affected?

This rate increase will affect manufacturers, importers, wholesalers, retailers and consumers of tobacco products.

## Timing

The increase takes effect at 6pm on 23 March.

## Our view

This change is in line with expectations although we were not expecting an amendment to the structure of cigarette duty. The Government is clearly committed to maintaining high rates of tobacco duty and in reducing the price gap between different tobacco products.

# Amusement machine licence duty (AMLD) and gaming duty revalorisation

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

Changes are to be made to increase Amusement Machine Licence Duty (“AMLD”). The changes will increase AMLD in line with inflation and raise the gross gaming yield bandings for gaming duty.

## Who is affected

Casino operators, bookmakers, bingo halls, “amusement arcades” and similar operators here in the UK.

## Timing

The new AMLD rates will be charged for any licence applications that are received by HMRC after 4pm on 25 March 2011. The gross gaming yield bandings used to calculate gaming duty must be used for any accounting periods starting on or after 1 April 2011.

## Our view

These changes will increase the costs of affected businesses. However the impact of the changes will be relatively short lived with the industry expecting far reaching changes as part of HMRC’s review of AMLD.

# Climate change levy: reform of Climate Change Agreements

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The reduced rate of Climate Change Levy (CCL) enjoyed by those who have entered into CCAs is to be reduced from 35 percent to 20 percent on electricity only.

The Climate Change Agreements (CCA) scheme, which was due to expire in 2013, is to remain in place until 2023.

DECC is to consult on simplifying the CCA scheme. This consultation exercise will take place during 2011.

## Who is affected

Energy intensive businesses that have entered into Climate Change Agreements.

Gas and electricity utilities; suppliers of solid fuels and liquefied petroleum gas.

## Timing

The reduced rate will be reduced to 20 percent in April 2013.

## Our view

Energy intensive businesses will be pleased by an early return to the reduced CCL rate of 20 percent on electricity following the increase to 35 percent on 1 April 2011.

The retention of the CCA scheme will also be welcomed by those businesses that benefit from it. It will be interesting to see what the consultation exercise brings, given that there has been much talk of simplifying the wide range of taxes and policy measures that impact upon energy.

# Climate Change Levy: Recycling Services

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

**The issue**

The current state aid approval for Climate Change Levy (CCL) exemption for taxable commodities used in recycling aluminium and steel expires on 31 March 2011. The government intends to suspend the exemption, thereby removing the risk that those who benefit from the exemption may have to repay illegal state aid.

The exemption will remain suspended unless and until state aid approval is granted by the European Commission.

**Who is affected?**

Recyclers of aluminium and steel who currently benefit from exemption from CCL.

Energy suppliers who are registered for CCL and who will be required to deal with the CCL accounting consequences.

**Timing**

The exemption will be removed from 1 April 2011.

It will be re-instated via secondary legislation if state aid approval is granted.

**Our view**

It is regrettable that state aid approval has not yet been obtained by the Government as the suspension of this exemption will result in increased costs for recycling businesses. There will also be administrative costs for energy suppliers.

# Climate Change Levy: Certain Forms of Transport

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The current state aid approval for Climate Change Levy (CCL) exemption for taxable commodities used in transport expires on 31 March 2011. The government intends to suspend the exemption for rail freight services and passenger services, where the operator does not hold a Public Service Obligation, thereby removing the risk that those who benefit from the exemption may have to repay illegal state aid.

The exemption will remain suspended unless and until state aid approval is granted by the European Commission.

## Who is affected?

Operators of rail freight services and a limited number of passenger rail services which do not hold a Public Service obligation.

Energy providers who are registered for CCL and who will be required to deal with the CCL accounting consequences.

## Timing

The exemption will be removed from 1 April 2011.

It will be re-instated via secondary legislation if state aid approval is granted.

## Our view

It is regrettable that state aid approval has not yet been obtained by the Government as the suspension of this exemption will result in increased costs for rail operators. There will also be administrative costs for energy suppliers.

# Carbon Price Floor

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The Climate Change Levy (CCL) exemption for solid fuels, gas and LPG used in the electricity generation process is to be removed.

The above commodities are to be subject to a 'carbon price support rate' based on carbon content which will create in essence a carbon price floor.

As oil used in electricity generation is not subject to CCL, the fuel duty which can be reclaimed will be subject to a restriction in order to create the same effect.

## Who is affected?

- Businesses that supply fossil fuels to generators of electricity.
- Generators of electricity using oils that currently reclaim fuel duty.
- Indirectly, all electricity consumers.

## Timing

The new rules will take effect from 1 April 2013.

## Our view

The announcement is not surprising as this proposal has long been seen as a key part of the Government's desire to increase the proportion of green taxation.

It is pleasing that the Government has taken a variety of stakeholders' views into account following last year's consultation on the subject.

It is interesting to note that the Government believes that only 40 percent of the cost will be borne by households. Whilst the impact for some businesses will be mitigated by the increase in the Climate Change Agreement discounts, the indirect impact on electricity prices will inevitably create a further cost for all businesses.

# Aggregates Levy Rate

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

**The issue**

The increase in aggregates levy from £2 per tonne to £2.10 per tonne that was due to take effect from 1 April 2011 will be repealed. This will have a minor positive impact on all aggregate producers in the UK but is intended to benefit those in Northern Ireland in particular. This is seen as compensating Northern Irish aggregates producers for the suspension of the aggregates levy credit scheme under which they were able to claim an 80 percent credit in respect of aggregates levy declared to HMRC.

The aggregates levy credit scheme was suspended from 1 December 2010 following a judgment by the European General Court in a case brought by the British Aggregates Association. The UK government plans to reintroduce the scheme as soon as possible, subject to state aid approval from the European Commission.

The rate will rise to £2.10 per tonne on 1 April 2012.

**Who is affected?**

Quarry companies and others subjecting rock, sand or gravel to its first commercial exploitation.

**Timing**

The planned increase on 1 April 2011 will not now take place.

Aggregates levy will rise to £2.10 per tonne on 1 April 2012.

**Our view**

This is an interesting approach to compensating Northern Irish businesses that have seen a real increase in their aggregates levy burden since the aggregates levy credit scheme was suspended in December 2010. It is unlikely to have a major impact on any registered aggregate producers.

# Mutual Assistance Recovery Directive

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

Legislation will be introduced in Finance Bill 2011 to enable the UK to implement the new Mutual Assistance Recovery Directive ("MARD") which was adopted by the EU on 16 March 2010.

## Who is affected

Taxpayers resident or present in the UK who have incurred tax liabilities in other EU member states.

## Timing

The new MARD is effective from 1 January 2012 and the Regulations implementing it in the UK will come into force on that date.

## Our view

The MARD replaces an earlier directive providing for Member States to assist each other in the recovery of tax debts and duties. The new Directive is more extensive in scope, covering all national taxes and duties, local duties and motor taxes. Among other things it also extends the scope for exchange of information without request and for tax administrations to carry out cross-border enquiries.

The Finance Bill will contain the necessary primary legislation to enable the new Directive to be implemented by Statutory Instrument. The detail of the new regulations will not be known until later in the year. It is hoped that the implementation of the new Directive will improve the cross-border collection of tax within the EU.

# Indirect Tax: Other measures

## **VAT: revalorisation of registration and deregistration thresholds**

The measure increases the annual taxable turnover threshold which determines whether a person must be registered for VAT from £70,000 to £73,000. The taxable turnover threshold which determines whether a person may apply for deregistration will be increased from £68,000 to £71,000. The registration and deregistration threshold for relevant acquisitions from other EU Member States will also be increased from £70,000 to £73,000. These thresholds will apply thresholds on or after 1 April 2011.

## **VAT: revalorisation of fuel scale charges**

The VAT fuel scale charges will be revalorised. The new fuels scale charges will have effect from 1 May 2011.

## **Vehicle excise duty uprating**

From 1 April 2011, Vehicle Excise Duty (VED) rates will increase by indexation except VED rates for heavy goods vehicles which will be frozen in 2011-12. The overview of tax and legislation also confirmed discount rates for Euro VI reduced pollution certificates (RPCs) will remain the same as for previous Euro standards. RPCs will be available for Euro VI standard vehicles from 1 January 2012 until 31 December 2016, applying to vehicles purchased before the standard becomes mandatory. The RPC will be backdated for Euro VI vehicles purchased before 1 January 2012. All Euro VI vehicles will return to standard VED rates when their tax disc naturally expires from 31 December 2016.

# New measures for Finance Bill 2012 or later

# Compulsory online registration and tranche 2 of online filing of VAT returns

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

**The issue**

Mandatory online VAT registration/deregistration and notification of changes.

Removal of registration threshold for businesses making taxable supplies in the UK but not established in the UK.

Mandatory online filing of VAT returns and electronic payment of VAT.

**Who is affected?**

Businesses requiring to register/de-register/notify changes in relation to VAT.

All businesses making taxable sales in the UK which are not established in the UK and not already VAT registered in the UK.

Existing VAT registered businesses with a VAT exclusive turnover under £100,000.

**Timing**

From 1 August 2012:

All VAT registration/de-registration and notification of changes must be completed online

The VAT registration threshold for businesses not established in the UK will be removed

For VAT periods beginning on or after 1 April 2012:

Mandatory online filing of VAT returns and electronic payments will be extended to include the second tranche of existing VAT customers (VAT exclusive turnover under £100,000).

**Our view**

The details of these measures are subject to further consultation, but are in line with the “Digital Agenda” set out in the Minister for the Cabinet Office’s statement of 23 November 2010.

# VAT Status of public bodies

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

UK law will be amended to ensure that UK law properly reflects the EU position around the treatment of supplies by public bodies. The VAT Directive states that where public bodies engage in activities and transactions as public authorities, (i.e. where they are carrying out their statutory duties) they are not taxable persons. This generally means VAT is not due on the income generated from these activities as non taxable persons do not charge VAT. However where the public bodies carry out these duties in competition with the private sector, the Directive requires that they should be taxable persons, if treating them as non taxable persons would lead to "significant distortions of competition". UK law at present does not wholly reflect the Directive in this area.

## Who is affected?

Public bodies (local authorities, government departments etc)

## Timing

Draft legislation will be issued in the autumn with a view to bringing in the legislation in the Finance Bill 2012.

## Our view

The long running Isle of Wight case (which considers whether local authorities act as taxable persons or not when operating off street car parks) has clearly shown the difficulties that surround the correct treatment of many of the activities that public bodies are obliged to offer or provide, but where no monopoly for the public body exists. Often both private and public sector may ostensibly offer the same services, but target wholly different markets and charge very different prices, wholly irrespective of VAT considerations. Some clearer tests that will help determine whether such supplies by public bodies are within the scope of VAT or not would be welcome. In cases where the public and private sectors are competing for the same market the private suppliers will welcome a level playing field, and where they are not, the public sector will be glad to be relieved from the burden of having to collect and declare VAT.

# VAT Grouping: Enactment of provisions currently with an ESC

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

Extra Statutory Concession (“ESC”) number 3.2.2 (“The Measure”) reduces the value of supplies and therefore the tax potentially due on services imported by VAT Groups from overseas group members under section 43.2A VATA 1994. The Measure (i.e. both the “old” ESC and “new” Statute) values the imported supplies by reference to the value of supplies purchased by the overseas group member which would have been taxable if supplied in the UK.

However, as an ESC any taxpayer prevented from applying the concession could only challenge through a judicial review. From 2012 this administrative relief is now a statutory relief and enforceable as such.

Section 43.2A was an anti-avoidance measure introduced by Finance Act 1997. It sought to tax supplies that had been first routed-out of the UK (to an overseas branch of a member of a partly exempt VAT Group) without VAT and subsequently brought back into the UK (again without VAT) via the VAT Group. A strict application of the measure would not only tax the supplies initially routed out of the country but also any value added by the overseas branch. Thus the ESC was required to ensure that section 43.2A was proportionate (i.e. caught only the abuse it sought to block) and therefore valid. The removal of the ESC and the enactment of similar provisions is part of the continuing program to rationalise ESCs following the House of Lords decision in Wilkinson which commenced a couple of years ago. The Government’s own assessment of budget measures suggests (as expected) that the change is fiscally neutral.

## Who is affected?

Theoretically: Partly exempt VAT Groups. Practically: Nobody.

## Timing

Finance Bill 2012

## Our view

As part of the program designed to move away from the “tax by statute, don’t tax by concession” philosophy historically employed by HMRC, the measure is to be welcomed.

# Diplomatic privilege

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

Extra statutory concessions (ESCs) to be replaced by legislation in 2012.

## Who is affected

Diplomatic missions, international bodies, visiting NATO forces, and UK taxpayers supplying goods and services to these bodies.

## Timing

Legislation will be introduced in 2012, no further details available.

## Our view

The VAT Directive requires Member States to relieve these supplies from VAT. The UK has to date applied these reliefs through ESCs rather than by way of legislation. However the Wilkinson case confirmed that the taxpayer should not "untaxed" by concession in cases where the UK law would expect tax to be due. Accordingly these concessions need to be withdrawn.

However as the reliefs they contained are mandatory under EU law, which is binding on the UK, the UK has to legislate to replace the concessions.

Additionally the UK will legislate to allow for the UK tax relief envisaged by the EU European Research Infrastructure consortia Regulation.

# Air Passenger Duty

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

Air passenger duty is to be frozen at its current rate following the increase in November 2010. An increase of APD rates by RPI in April 2011 will be deferred until April 2012.

Subject to further consultation, the Government proposes to extend APD to include passengers aboard aircraft with an authorised take-off weight in excess of 5.7 tonnes where APD is not already payable ('business jets'). The specific definition of flights which will be covered by the new tax will be determined in light of consultation evidence and responses (i.e. there are likely to be exemptions for emergency and public services flights etc).

## Who is affected?

Travel industry firms and airline operators. Executive fliers (or their employers) will be affected by APD on business jets once this is implemented.

## Timing

The increase of APD rates by RPI will take effect from April 2012.

## Our view

Following the increase in air passenger duty in 2010 this was not an unexpected measure given the strength of protest from the airline industry. This is not a preliminary step towards charging APD on a per plane (as opposed to a per person) basis since this would be illegal under International Law (according to the Chancellor). Further consultations will take place over the next 12 months regarding the implementation of the new APD rules on private jets.

# Future consultations

A feature of Budget 2011 is the announcement and continuation of consultations over the coming months in some key areas of the tax landscape. The consultations relevant to Indirect tax are summarised below.

## **VAT Cost Sharing Exemption**

The 2011 Budget referred to the ongoing consultation on the UK implementation of the VAT cost sharing exemption. The exemption could be used by organisations such as charities, universities and housing associations wanting to make efficiency savings by working together to achieve economies of scale. A formal consultation was previously expected last year but was delayed.

## **Tackling VAT fraud on imported road vehicles**

This new consultation follows a joint HMRC-DVLA initiative to combat VAT fraud on road vehicles brought into the UK. The proposal is that from 2013 vehicles entering the country for permanent use on UK roads will have to be notified to HMRC online before the vehicle is registered with the DVLA.

This will require individuals and non-VAT registered businesses to pay the VAT at the time of notification. VAT registered customers will continue to make payment through their VAT return. It is anticipated a formal consultation document will be issued in May 2011 with a view to announcing in Finance Bill 2012.

# Revisions to measures published in Finance Bill 2011 draft

# Finance Bill 2011 – previously announced measures

Draft clauses for the 2011 Finance Bill were published in advance of the 2011 Budget on 9 December 2010. Any substantial changes to these draft clauses announced in this Budget have been detailed above. The indirect tax measures to be included in Finance Bill 2011 where no major changes have been made and which are not covered in this Budget commentary are as follows:

- Taxation of Gaming Machines
- VAT Zero Rating: Splitting of Supplies
- VAT Change of treatment of business samples
- Refunding irrecoverable VAT costs incurred by academies
- Duty on high and low strength Beers
- Exceptional Rates of Vehicle Excise Duty for Certain Heavy Goods Vehicles.

A copy of our commentary on the draft Finance Bill (including these measures) can be found [here](#).



## Employee Issues



**Jayne Vaughan**  
Head of Employee Tax

From an employer perspective this year's Budget contained a number of "big ideas" with the detail to follow later. But equally, the Government's new rules on "Disguised Remuneration" are complicated and will potentially impact on employers from 6 April 2011 (if not before). It will be important for employers to take stock in terms of both the Finance Bill, which will be published next week on 31 March 2011, and a number of consultation documents that will be published over the summer. In this respect this Budget leaves a number of open questions and further work to do.

The most significant immediate concern is the new anti-avoidance legislation on "Disguised Remuneration". The Budget documents have confirmed HMRC's intention to amend the legislation where there are unexpected results without an avoidance motive, but given the complex nature of the legislation, it appears inevitable that there will remain hard edges and unintended consequences. Employers will have to carefully review their remuneration arrangements where third parties are involved to see whether they fall foul of the new rules. And they may well want to approach HMRC to confirm that they are not inadvertently impacted.

Another big idea, albeit not new, is the review of non-domicile taxation. In the June 2010 Emergency Budget, the Government confirmed that it would review the taxation of non-domiciled individuals and the ongoing uncertainty has been harming the UK's competitiveness. The Government has recognised that the remittance basis rules are a disincentive to invest in the UK and intend to modify the rules to address this. On the other hand the remittance basis charge is to be raised to £50,000 for individuals who have been resident for 12 or more years. A consultation document will be issued in June with a view to implementing these reforms from April 2012. The Government has also stated there will be no further changes to these rules during the period of this Parliament.

There is also the announcement that there will be a statutory residence test. Currently there is no single statutory test for tax residence in the United Kingdom. An individual who is in the UK for 183 days or more in a tax year will be UK resident. Someone who spends no time in the UK in a tax year is unlikely to be resident. In other cases HMRC and, if necessary, the courts determine a person's residence status from case law principles. Recent cases have demonstrated the real difficulties that can arise.

Again a consultation document will be issued in June with the aim to introduce a statutory residence test from April 2012. The devil will be in the detail but the hope is that the test will provide certainty over an individual's residence status, whilst being sufficiently practical to enable employers to meet their PAYE obligations with the minimum of administrative costs.

The Government has also responded to the suggestion by the Office of Tax Simplification ("OTS") of a merger of income tax and NIC by announcing a consultation that will take place later this year. A merger makes sense from the point of view of administration but may be difficult to achieve in practice. The Government confirmed that the intention is for this to be a simplification and not a revenue raising measure. They also confirmed that NIC is not to be extended to individuals of State pension age and not levied on pensions, savings and dividends.

The Government also responded to the OTS report on IR35. The Government has decided to retain this because it cannot put substantial tax revenue at risk. This will disappoint those who were hoping for the abolition of IR35.

Other changes announced include a tweaking of the company car scale charge rates to encourage greater use of lower CO2 emission vehicles and an increase in the car fuel benefit scale charge. The HMRC Authorised Mileage Allowance Payments for business journeys in privately owned cars have been increased from 40p a mile to 45p a mile for the first 10,000 miles. This change will take effect from 6 April 2011. This rate has remained at the previous 40p a mile level for some few years and with significantly increasing fuel costs this change will be welcomed.

The coalition Government has introduced a new approach to tax policy making and in line with this policy draft clauses for the 2011 Finance Bill were published in advance of the 2011 Budget on 9 December 2010. The structure of our commentary has changed to accommodate this new approach. All announcements relating to tax policy are set out in a separate section at the beginning of the commentary and then each tax section is ordered as follows:

- New measures not previously published in draft to be included in Finance Bill 2011.
- Measures to be included in Finance Bill 2012 or later.
- Measures to be included in Finance Bill 2011 that were published in draft on 9 December 2010 where **substantial** changes to those draft clauses have now been announced in the Budget. Although this Budget commentary focuses on the changes that are to be made to those draft clauses, to help understand these changes our original commentary from December 2010 is replicated immediately after our comments on each measure. If no changes have been announced the measure has not been included in this commentary.

If only minor changes, or no changes at all, have been made to the measure published in December, the measure has not been included in this commentary. Instead, two lists can be found at the end of this section: one detailing those measures where minor changes have been made and a second listing those which are unchanged. A full copy of our original

commentary from December, which covers those measures, can be found [here](#).

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# New measures for Finance Bill 2011

# Response to OTS report on IR35

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

The Government has considered the Office of Tax Simplifications (OTS) report published on 10 March which included comment on IR35 and have decided to retain IR35. The legislation is contained at Chapter 8, Part 2 of ITEPA 2003 but is commonly known as IR35 and applies in situations where an end user contracts with a Personal Service Company (PSC) for the services of a contractor (Director of the PSC). Broadly IR35 applies where the relationship between the end user and the contractor, ignoring the contract with the PSC, would be viewed as an employment relationship.

## The issue

The OTS put forward three suggested options for revising the IR35 legislation one of which was to remove IR35 totally. In the past IR35 has received much criticism regarding the difficulties in applying the legislation and particularly that this relies on the definition of employment in determining when IR35 will apply. There has also been some criticism that IR35 had not brought in the extra tax revenues expected whilst increasing costs for contractors as they defended themselves against IR35.

The Government has considered the options put forward by the OTS and decided that it cannot put substantial tax revenue at risk and are, therefore, retaining IR35. They appear to have recognised some of the difficulties of administering IR35 and are going to provide greater clarity on what they consider is within IR35. They also intend to simplify the administration for all with specialist teams to look at the high risk cases, provide a dedicated helpline and in addition propose to set up a forum to engage with interested parties to monitor the HMRC revised approach. This is intended to clarify what IR35 will cover and thereby reduce the costs of contractors due to incorrect IR35 determinations.

## Who is affected?

This will affect many individuals who supply their services via their own PSC including both UK and non UK PSC's where the work is carried out in the UK. In particular it will impact industries such as IT and construction etc where historically significant numbers of contractors have provided services via a PSC.

## Timing

The Government has committed to making these improvements to IR35 but has not yet published a timescale.

## Our view

This decision will be disappointing for a number of individuals affected by IR35 who may have thought the complete abolition of IR35 was a better outcome. The proof will be in the changes that HMRC bring forward and if they are able to simplify the application of the IR35 legislation. It has yet to be determined if the HMRC teams are able to apply this fairly and consistently. It is welcome that HMRC intend to set up a forum to engage

with those affected and the hope will be that this forum will enable any potential problems to be resolved quickly. It is yet to be seen what impact, if any, these proposed changes will have on the tax receipts.

# Company car tax rates 2013/14

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

**The issue**

The Government have announced an increase in the ‘appropriate percentage’, used to calculate the employees’ benefit in kind, for all vehicles with CO2 emissions between 95g/km and 219g/km by one percent with effect from 6 April 2013.

Zero emission cars will remain at zero percent and ultra low emission cars with emissions up to 75g will remain at five percent.

**Who is affected**

Any employees being provided with company cars by their employer with CO2 emissions between 95g/km and 219g/km.

**Timing**

The new rules will take effect from 6 April 2013.

**Our view**

This is an extension of the Government’s drive toward low emission company vehicles. Zero emissions cars will remain at zero percent and ultra low emissions cars with emissions up to 75g will remain at five percent. The CO2 level for the company car tax benefit in kind calculation generally reduces year on year and the Government announce any changes in advance so drivers can continue to make an informed decision about the company vehicle they choose.

# Changes to the benefit in kind of private fuel provided to company car drivers

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

HM Revenue & Customs ('HMRC') has confirmed that the tax and Class 1A NIC costs of providing private fuel to company car drivers will be increasing from 6 April 2011. From this date, the fuel benefit multiplier will increase from its current rate of £18,000 to £18,800. This amount is multiplied by the appropriate benefit in kind percentage for the company car (which is based on the car's CO2 emissions).

## Who is affected

Employers will be affected as their Class 1A NIC costs will increase, as will employees, as the tax they pay on this benefit in kind will increase.

## Timing

This change will take effect from 6 April 2011.

## Our view

The impact of this measure is negative as it will increase the Class 1A NIC costs on the employer of providing private fuel as well as increase the tax the employee will be liable to pay.

# Authorised Mileage Allowance Payments ('AMAP') rate changes

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The Government announced in the 2011 Budget that the AMAP rates for own car and cash allowance drivers will increase from 40p per mile for the first 10,000 miles to 45p per mile for business mileage undertaken. This is the first increase in AMAPs since 2002. The change will be effective from 6 April 2011.

This will help provide additional relief for many motorists required to use their own vehicle for business travel. The AMAPs will remain at 25p per mile for business travel after the first 10,000 miles.

## Who is affected

All employers and employees who reimburse/undertake business travel.

## Timing

The new rules will take effect from 6 April 2011.

## Our view

The impact of this measure is positive and will provide employees who undertake business mileage with additional relief for these journeys for the first 10,000 miles. This measure will help temper the recent rise in the cost of fuel.

# Mutual Assistance Recovery Directive

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

Legislation will be introduced in Finance Bill 2011 to enable the UK to implement the new Mutual Assistance Recovery Directive ("MARD") which was adopted by the EU on 16 March 2010.

## Who is affected

Taxpayers resident or present in the UK who have incurred tax liabilities in other EU member states.

## Timing

The new MARD is effective from 1 January 2012 and the Regulations implementing it in the UK will come into force on that date.

## Our view

The MARD replaces an earlier directive providing for Member States to assist each other in the recovery of tax debts and duties. The new Directive is more extensive in scope, covering all national taxes and duties, local duties and motor taxes. Among other things it also extends the scope for exchange of information without request and for tax administrations to carry out cross-border enquiries.

The Finance Bill will contain the necessary primary legislation to enable the new Directive to be implemented by Statutory Instrument. The detail of the new regulations will not be known until later in the year. It is hoped that the implementation of the new Directive will improve the cross-border collection of tax within the EU.

# New measures for Finance Bill 2012 or later

# Statutory definition of residence

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

*Positive to have such a test, but the broader effect depends on the definition used.*

## The issue

The current case law principles for determining whether an individual is resident in the UK are unclear and complex. A statutory residence test will be introduced.

## Who is affected

This is relevant for all taxpayers who do not spend all of their time in the UK.

## Timing

The Government will consult on this issue in June. Legislation implementing the new statutory test for residence will be included in Finance Act 2012 to take effect from 6 April 2012.

## Our view

Whether the new legislation will make it more straightforward in determining an individual's residence status will depend on the precise test which results from the consultation in June. A simple objective test based on days of presence in the UK would be welcome.

# Changes to the Taxation of Non-Domiciled Individuals

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The previous Government introduced sweeping changes to the taxation of non-UK domiciled individuals ("non-doms") in Finance Act 2008. The taxation of non-doms will be further reformed as follows:

- The annual £30,000 charge will be increased to £50,000 for those non-doms who have been resident in the UK for twelve or more years and who wish to be taxed on the remittance basis. The £30,000 annual charge will continue for those individuals who have been resident in the UK for at least seven years but fewer than twelve years.
- The tax charge will be removed for non-doms who remit foreign income or gains to the UK for the purpose of commercial investment in UK businesses.
- Technical simplification will be made to some aspects of the current rules to remove undue administrative burdens.

## Who is affected

These changes will affect non-domiciled individuals. In particular it will affect those non-doms who have been resident in the UK for twelve or more years.

## Timing

The Government will issue a consultation document in June. Legislation implementing these changes will be included in Finance Act 2012 to take effect from 6 April 2012.

## Our view

The increased charge to £50,000 will be a real cost to some individuals. However, the other changes are welcome, in particular the assurance that the Government plans no other substantive changes to the taxation of non-doms for "the remainder of Parliament" and the technical simplification of some aspects of the current rules. The ability for non-doms to bring foreign income and gains to the UK to invest in UK businesses is an encouraging step.

# Income tax and NIC reform

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The Government has announced that it will consult on the potential integration of the operation of income tax and National Insurance Contributions (NIC).

## Who is affected

Individuals liable to and who account for income tax and NIC such as employers, employees and the self-employed. The Government has said that it is not the intention to extend NIC to individuals above State Pension age or to other forms of income such as pensions, savings and dividends.

## Timing

A consultation document will be published later this year. The Chancellor stated that it will take a number of years to complete the consultation.

## Our view

The Chancellor has now announced a review/consultation on integrating the operation of income tax and NIC. In line with the stated aim of the Budget, the Chancellor said this was intended to be a simplification and not a tax raising measure.

The merger makes a lot of sense from an administrative perspective particularly for employers. The two regimes work in a similar way in as much as they both tax earned income but there are very significant areas of inconsistency around how they operate. For many years, the administration of both the income tax and NIC systems has been run by one government department (HM Revenue and Customs), but it often appears to employers that separate organisations administer the two systems. For example, frequently, guidance issued only covers tax or NIC, but not both.

NICs are currently only applied to earned income whereas income tax is generally applied to all income. So merely merging the two rates would make no difference to the take home pay of most employees. However, the recent Office of Tax Simplifications (OTS) report stated that 'The income tax and NIC treatment of benefits varies, with some exempt from both income tax and NIC (e.g. cycle to work), some exempt from income tax only (e.g. pension contributions), some exempt from NIC only (e.g. payments in respect of lost and stolen credit cards) and some exempt from neither (e.g. health insurance). This creates confusion for both taxpayers and employers....'. Qualifying termination payments attract income tax above £30,000 (and, in certain cases more) but no NIC and there are other similar examples of different approaches being taken. The two systems cannot be merged without some give and take at this level unless we are to end up with an extremely complex combined system.

The implication on the UK's tax competitiveness should also be considered if a merger of the two charges resulted simply in an abolition of NIC and a correspondingly higher headline income tax rate. Although the overall tax take may stay unchanged, the change in headline rates could create a negative perception issue for the UK compared to other countries

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which charge a social security tax separate from income tax. To the unsophisticated investor, this could, for example, make UK plc seem uncompetitive when compared to other European neighbours.

It is, at present, unclear how a merged system would interact with the UK's double taxation treaties and reciprocal social security agreements including the European Union agreement.

The Government have also said that they will maintain the contributory principle and reflect this in any changes that it brings forward. This will inevitably create a tension with the desire to simplify but, nevertheless, we welcome the Government's intention to revisit the issue of merging income tax and NIC and argue that this will have real potential to reduce administrative burdens on employers.

# Pension schemes

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The Government is proposing a range of changes that will affect the full range of state, public and private sector pension provision. Most of these measures are known only in outline at the present time, with detailed consultation to follow:

**State pensions and contracting out:** The Government wants to simplify the state pension system and plans to issue shortly a consultative green paper setting out its proposals. These will include a measure to move to a single-tier, flat-rate state pension of around £140 per week in today's terms. Such a move would entail the abolition of the state second pension and defined benefit contracting out (with an increase in National Insurance contributions for previously contracted-out schemes of 3.4 percent for employers and 1.4 percent for employees). This would not affect existing state pensioners and there would be some protection of SERPS and state second pension already accrued. There are no further details at present, and the Chancellor indicated that such changes could entail a lengthy transitional period. However this change is now very clearly on the agenda for this Parliament.

**Public service pensions:** The Government has accepted Lord Hutton's recommendations as a basis for consultation with public sector workers and their representatives. It will set out more detailed proposals in autumn 2011. It has emphasised that the Hutton recommendations should be treated as a package and that it does not wish to see "cherry-picking". The discount rate for unfunded public service pensions should be based on the long-term expectation of GDP growth; a discount rate of three per cent above CPI will therefore be adopted under this methodology for future valuations. This change in the discount rate will not lead to an increase in member contribution rates beyond those already announced.

**Employer asset-backed pension contributions:** The Government will consult on measures to limit the amount of tax relief available to employers when they make asset-backed contributions to their defined benefit pension schemes, so that the tax relief accurately reflects the increase in fair value of pension plan assets. A consultation paper will be issued this spring, with legislation in Finance Bill 2012. We understand from HMRC that the intention is not to attack legitimate arrangements which irrevocably pass value to scheme trustees, but it does have concerns with structures that include contingent payments.

**State pension age (SPA):** The Government will make proposals for an independent ongoing review of longevity that will deliver automatic increases in SPA as longevity increases.

## Who is affected?

The changes are likely to affect, to varying degrees, all individuals who are currently planning for their retirement. Public sector employers will be particularly affected, as will private sector employers who still offer contracted-out defined benefit schemes.

### **Timing**

No clear timing has been stated for implementation of the main measures but the changes to state pensions are unlikely to start having effect before the end of the current Parliament.

### **Our view**

Clearly, these measures could have a profound influence on the way we provide for retirement in the UK. Abolition of defined benefit contracting will force further scheme design changes on employers and very likely accelerate still further the decline of defined benefit provision. We await further details with interest and look forward to making our views known during consultation.

# Revisions to measures published in Finance Bill 2011 draft clauses

# Disguised Remuneration

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The Government announced on 9 December 2010 that anti-avoidance legislation will be introduced in Finance Bill 2011 concerning third party arrangements used to avoid, reduce or defer liabilities to income tax and NICs on rewards from employment or to avoid restrictions on pensions tax relief.

A new income tax charge will apply where a third party provides an employee with reward, recognition or a loan in connection with the employee's employment. The Government say that third party arrangements that do not amount to tax avoidance will be excluded "in so far as this is possible without creating additional avoidance risks". In particular, this is to apply to genuine deferred remuneration arrangements common in the financial services sector and which last less than five years and genuine commercial arrangements for the provision of employee car ownership schemes.

The legislation will also apply to pension arrangements involving third parties (which they generally do) and which are used in addition to, or instead of, registered pension plans and where, at present, the rules on the annual and lifetime allowances do not apply.

The legislation will apply to arrangements involving trusts or other third parties and where (i) sums or assets are "earmarked" for employees, (ii) loans are provided to employees (iii) assets are made available to employees or (iv) sums or assets are paid or provided to employees. The legislation will apply equally to remuneration and retirement benefit arrangements, but not to payments otherwise chargeable to tax as pension income.

The new charge will be based on the full amount of any sum of money made available or the higher of the cost or market value where an asset is used to deliver the reward.

The amount will count as a payment of employment income and the employer will be required to account for PAYE accordingly.

The Government invited representations on this measure over the period until 9 February 2011, and on 21 February published a series of FAQs addressing a number of points that were raised.

The Government have confirmed that they have amended the legislation to limit the impact on employers and individuals "where it is possible to identify arrangements that cannot be used for avoidance purposes". The amendments cover "the protection of rewards by group companies, share incentive arrangements and genuine deferred remuneration arrangements". The Government have also confirmed that existing pension savings will be excluded.

The Government note that they regard certain arrangements caught by these new measures as not, in any event, effective under the current law and say they will continue to challenge such arrangements.

## Timing

The new rules will take effect from 6 April 2011 but anti-forestalling rules will apply to the payment of sums (including loans) to employees, and in certain other circumstances, between 9 December 2010 and 5 April 2011.

Regulations will be published shortly to apply NICs to amounts chargeable to income tax under the new rules.

## Our view

The Government say that approximately 5,000 employers and 50,000 employees will be affected by these measures with a yield to the Exchequer of some £750 million in 2011-12 and subsequent years to 2015/16.

Whilst it is understandable that the Government wishes to clamp down on perceived areas of tax avoidance and is concerned about potential tax leakage through the use of pension arrangements falling outside of the registered regime, there was much concern expressed during the consultation period about the very wide scope of the draft legislation that was published on 9 December 2010.

The FAQs that were published on 21 February 2011 sought to allay this concern by referring to a number of the hard edges and unintended consequences of the new rules and confirming, as the Government now reaffirm, that the draft legislation will be appropriately amended.

Our real concern, however, is the very wide range of circumstances in which third parties are involved in the provision of reward to employees, whether this be in relation to share plans, pension plans, medical insurance cover, relocation assistance etc. This applies equally, if not more so, to international assignees posted to the UK from abroad. Whilst there are a number of prescribed exceptions there will inevitably still be numbers of commercial arrangements which will not tick all the required boxes.

Although the Government say they will, for the most part, exclude group companies from the definition of third parties, this is with the caveat that this will not be so where there are "additional avoidance risks". Whilst we can understand this approach at a conceptual level, the reality is that employers will need to review very carefully all their remuneration arrangements which involve any party other than the employer alone (and whether this is another group company or otherwise) and to determine whether, and if so how, they could be impacted. Indeed employees may well want to approach HMRC to confirm the position since the consequences of inadvertently getting it wrong will be very unwelcome to both employers and employees alike.

# Finance Bill 2011: previously announced measures

Draft clauses for the 2011 Finance Bill were published in advance of the 2011 Budget on 9 December 2010. Any substantial changes to these draft clauses announced in this Budget have been detailed above. The employee issues measures to be included in Finance Bill 2011 where no or only minor changes have been made are as follows:

## Measures with no changes

- Employer-Supported Childcare: Changes to the “Open Generally” Condition
- Expenses paid to MPs

## Measures with Minor changes

Removing the effective requirement to annuitise by Age 75

Changes to remove unintended differences between pensions and lump sums

- Restricting pensions tax relief – changed to include provision to oblige pension schemes to pay the tax charge on a member’s behalf, with an appropriate reduction in the member’s benefit, if the tax charge arising in a scheme is more than £2,000
- Changes to Tax Reliefs for Employer-Supported Childcare
- Minor technical change
- Security for Payment of PAYE
- Regulations will be amended to ensure that the time to pay regulations are considered before a security is enforced.

A copy of our commentary on the draft Finance Bill (including these measures) can be found [here](#).



# Personal Tax



**David Kilshaw**  
Private Client Chairman

The 2011 Budget measures relating to individuals can be seen at least in part as meeting some of the Government's main policy objectives.

## **Reducing the fiscal deficit**

Limiting future indexation of most tax reliefs and allowances to the CPI rather than the RPI will, on the basis that the former is usually a lower measure, represent an effective tax increase over time (albeit that for the time being the Government is continuing to pursue its policy of increasing the personal income tax allowance by substantially more than the normal indexation basis, at least for basic rate taxpayers).

The Government announced specific areas for anti-avoidance measures, and a framework for tackling tax avoidance in general was published for consultation, with a view to protecting current and future tax revenues.

However, most of the tax and national insurance increases coming into force from 6 April 2011 had already been pre-announced and therefore there was less pressure to introduce further tax increases in this Budget.

## **Encouraging enterprise and competitiveness**

The lifetime allowance for entrepreneurs' relief is being doubled to £10 million and the tax benefits of investment in EIS qualifying companies are being enhanced as a means of encouraging and rewarding entrepreneurial activity.

The retention of the remittance basis of taxation for non-UK domiciled individuals (albeit with an increased annual charge of £50,000 for those resident here for 12 years or more), and the ability to remit on a tax free basis foreign income and capital gains for investment in UK businesses can also perhaps be seen as part of the same agenda.

## **Big Society**

Changes to the administration of the Gift Aid scheme which will benefit both small and large donors, and an enhanced IHT relief for charitable bequests (reducing the effective IHT rate from 40 percent to 36 percent), are intended to encourage donations to charity.

## **Tax simplification**

The announcement of a possible merger of the operation of Income Tax and National Insurance Contributions ("NIC") would represent one of the most substantial tax reforms of the past half century. The difficulties with this are recognised by the Government and it is regarded as a long term project. There are clear potential benefits in administration from merging the systems, but there are many issues to consider, such as the

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interaction with the benefits system, and whether a merged system would apply to income that is not subject to NIC – for example, pensions and investment income.

The announcement of an intention to proceed with a statutory residence test could represent the opportunity to give certainty on a difficult issue that has led to an increasing amount of litigation in recent years. However, there is no detail on the Government's preferred approach and it could well be the case that it will be no simpler to determine UK residence than under the current rules.

### Conclusion

The mix of policy objectives and the fiscal pressures facing the Government mean that the Budget is a "mixed bag" with good and bad news, and some indications of major reforms to the tax and national insurance systems.

The coalition Government has introduced a new approach to tax policy making and in line with this policy draft clauses for the 2011 Finance Bill were published in advance of the 2011 Budget on 9 December 2010. The structure of our commentary has changed to accommodate this new approach. All announcements relating to tax policy are set out in a separate section at the beginning of the commentary and then each tax section is ordered as follows:

- New measures not previously published in draft to be included in Finance Bill 2011.
- Measures to be included in Finance Bill 2012 or later.
- Measures to be included in Finance Bill 2011 that were published in draft on 9 December 2010 where **substantial** changes to those draft clauses have now been announced in the Budget. Although this Budget commentary focuses on the changes that are to be made to those draft clauses, to help understand these changes our original commentary from December 2010 is replicated immediately after our comments on each measure. If no changes have been announced the measure has not been included in this commentary.
- If only minor changes, or no changes at all, have been made to the measure published in December, the measure has not been included in this commentary. Instead, two lists can be found at the end of this section: one detailing those measures where minor changes have been made and a second listing those which are unchanged. A full copy of our original commentary from December, which covers those measures, can be found [here](#).

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# New measures for Finance Bill 2011

# Entrepreneurs' Relief - increase in lifetime limit

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The lifetime limit on gains qualifying for Entrepreneurs' Relief has been doubled from £5million to £10million. Tax payers who have already used the £5million lifetime limit will be able to benefit from the increased threshold and receive and apply the relief to another £5million of qualifying gains after 5 April 2011.

## Who is affected?

Individuals and trustees of settlements who have qualifying gains.

## Timing

The new rules will take effect from 6 April 2011.

## Our view

This is a welcome increase to encourage enterprise. Entrepreneurial share owners will now be able to benefit from an additional £900,000 tax saving under the new limit. This will bring the maximum, total value of the relief to £1.8 million for higher rate tax payers. Qualifying gains are subject to capital gains tax at 10 percent.

It is important to note that the criteria have not been relaxed and therefore to qualify for the relief individuals broadly need to hold five percent of the voting rights and rights to assets on a winding up in an unquoted trading company for which they work. They also have to have held the shares for at least a year.

The increase in relief is not retroactive; any gains made before 6 April 2011 in excess of the previous limit will not benefit from the additional relief. The increased limit will be available for future qualifying gains after 5 April 2011.

# Enterprise Investment Scheme (“EIS”)

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

**The issue**

The rate of income tax relief given under EIS will increase from 20 percent to 30 percent of the amount subscribed for shares in qualifying companies. Further changes to the qualifying company thresholds will also apply from 6 April 2012. See section below regarding measures to be included in Finance Bill 2012 or later for further details.

**Who is affected?**

Individuals subscribing for shares in qualifying EIS companies.

**Timing**

The increased rate of income tax relief will take effect from 6 April 2011.

**Our view**

The EIS was introduced to encourage individuals to invest in smaller, higher risk UK companies to assist them in raising finance. The increased income tax relief given to individuals subscribing for shares in EIS companies should promote further investment into smaller enterprises and the increased relief received by investors is a welcome measure.

# Personal Tax: Other measures

To be included in FB2011

## **Abolishment of certain reliefs following OTS review**

The Government intends to implement some of the findings from the review carried out by the Office of Tax Simplification (OTS) earlier in the year. It intends to abolish 43 reliefs in total which have outgrown their use, are poorly targeted or have limited benefit versus the administrative burden required to implement.

Seven of the reliefs to be abolished will be included in Finance Bill 2011 and comprise reliefs which are completely redundant so will not have any effect on taxpayers or the Government. One such example is the proposed repeal of Millennium Gift Aid Relief given that it only applied to donors and charities until 31 December 2000.

The balance of the reliefs is likely to be abolished over the next couple of years after a period of consultation as some still have ongoing application such as tax relief for late night taxis and the special tax regime for mineral royalties.

For a full list of reliefs to be abolished see the Tax Policy section of our full commentary.

## **Donations of tax repayments through Self Assessment tax return**

It has been possible since 2005 for taxpayers to donate their tax repayments direct to a nominated charity through their Self Assessment tax return. However on the basis that this facility has been little used and HMRC consider that it is vulnerable to fraud, it is to be withdrawn for the tax return for 2011/12 and subsequent years, and for any repayments made in respect of earlier years on or after 6 April 2012.

# New measures for Finance Bill 2012 or later

# Income tax and NIC reform

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The Government has announced that it will consult on the potential integration of the operation of income tax and National Insurance Contributions (NIC).

## Who is affected

Individuals liable to and who account for income tax and NIC such as employers, employees and the self-employed. The Government has said that it is not the intention to extend NIC to individuals above State Pension age or to other forms of income such as pensions, savings and dividends.

## Timing

A consultation document will be published later this year. The Chancellor stated that it will take a number of years to complete the consultation.

## Our view

The Chancellor has now announced a review/consultation on integrating the operation of income tax and NIC. In line with the stated aim of the Budget, the Chancellor said this was intended to be a simplification and not a tax raising measure.

The merger makes a lot of sense from an administrative perspective particularly for employers. The two regimes work in a similar way in as much as they both tax earned income but there are very significant areas of inconsistency around how they operate. For many years, the administration of both the income tax and NIC systems has been run by one government department (HM Revenue and Customs), but it often appears to employers that separate organisations administer the two systems. For example, frequently, guidance issued only covers tax or NIC, but not both.

NICs are currently only applied to earned income whereas income tax is generally applied to all income. So merely merging the two rates would make no difference to the take home pay of most employees. However, the recent Office of Tax Simplifications (OTS) report stated that 'The income tax and NIC treatment of benefits varies, with some exempt from both income tax and NIC (e.g. cycle to work), some exempt from income tax only (e.g. pension contributions), some exempt from NIC only (e.g. payments in respect of lost and stolen credit cards) and some exempt from neither (e.g. health insurance). This creates confusion for both taxpayers and employers....'. Qualifying termination payments attract income tax above £30,000 (and, in certain cases more) but no NIC and there are other similar examples of different approaches being taken. The two systems cannot be merged without some give and take at this level unless we are to end up with an extremely complex combined system.

The implication on the UK's tax competitiveness should also be considered if a merger of the two charges resulted simply in an abolition of NIC and a correspondingly higher headline income tax rate. Although the overall tax take may stay unchanged, the change in headline rates could create a negative perception issue for the UK compared to other countries

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which charge a social security tax separate from income tax. To the unsophisticated investor, this could, for example, make UK plc seem uncompetitive when compared to other European neighbours.

It is, at present, unclear how a merged system would interact with the UK's double taxation treaties and reciprocal social security agreements including the European Union agreement.

The Government have also said that they will maintain the contributory principle and reflect this in any changes that it brings forward. This will inevitably create a tension with the desire to simplify but, nevertheless, we welcome the Government's intention to revisit the issue of merging income tax and NIC and argue that this will have real potential to reduce administrative burdens on employers.

# Changes to the taxation of non-domiciled individuals

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The previous Government introduced sweeping changes to the taxation of non-UK domiciled individuals (“non-doms”) in Finance Act 2008. The taxation of non-doms will be further reformed as follows:

- The annual £30,000 charge will be increased to £50,000 for those non-doms who have been resident in the UK for twelve or more years and who wish to be taxed on the remittance basis. The £30,000 annual charge will continue for those individuals who have been resident in the UK for at least seven years but fewer than twelve years.
- The tax charge will be removed for non-doms who remit foreign income or gains to the UK for the purpose of commercial investment in UK businesses.
- Technical simplification will be made to some aspects of the current rules to remove undue administrative burdens.

## Who is affected

These changes will affect non-domiciled individuals. In particular it will affect those non-doms who have been resident in the UK for twelve or more years.

## Timing

The Government will issue a consultation document in June. Legislation implementing these changes will be included in Finance Act 2012 to take effect from 6 April 2012.

## Our view

The increased charge to £50,000 will be a real cost to some individuals. However, the other changes are welcome, in particular the assurance that the Government plans no other substantive changes to the taxation of non-doms for “the remainder of Parliament” and the technical simplification of some aspects of the current rules. The ability for non-doms to bring foreign income and gains to the UK to invest in UK businesses is an encouraging step.

# Statutory definition of residence

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

*Positive to have such a test, but the broader effect depends on the definition used.*

## The issue

The current case law principles for determining whether an individual is resident in the UK are unclear and complex. A statutory residence test will be introduced.

## Who is affected

This is relevant for all taxpayers who do not spend all of their time in the UK.

## Timing

The Government will consult on this issue in June. Legislation implementing the new statutory test for residence will be included in Finance Act 2012 to take effect from 6 April 2012.

## Our view

Whether the new legislation will make it more straightforward in determining an individual's residence status will depend on the precise test which results from the consultation in June. A simple objective test based on days of presence in the UK would be welcome.

# Income tax rate limits, personal allowances, CGT annual exempt amount and IHT nil rate band

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The tax free personal allowance for individuals under 65 years old will increase by £630 to £8,105 in 2012/13. There will be an equivalent reduction in the basic rate limit to £34,370.

The underlying indexation basis for direct taxes and National Insurance will change from the Retail Price Index (RPI) to the Consumer Prices Index (CPI) from 6 April 2012.

However the income tax personal allowances and limits that are subject to indexation will be increased in line with the RPI for 2012/13.

The capital gains tax (CGT) exempt amount will increase by £500 to £10,600 from April 2011 in line with statutory indexation. The underlying indexation basis for the CGT annual exempt amount will change from the RPI to the CPI from 6 April 2012.

The IHT nil rate band will be frozen at the current level of £325,000 until 5 April 2015. Thereafter CPI will be used as the indexation basis for increases in the band.

## Who is affected

This is potentially relevant for all taxpayers.

## Timing

The changes will take effect from 6 April 2012.

## Our view

While it is encouraging that lower paid workers will benefit from an above inflation increase in the personal allowance, the higher rate threshold remains unchanged so that higher rate tax payers gain no extra benefit from the increase in the personal allowance.

The change in the default indexation basis from the RPI to the CPI was not unexpected as the Government had already introduced this for certain pension and other purposes. The effect will be to increase the yield of income tax as the CPI usually increases by less than RPI.

The continued freeze on the IHT nil rate band will potentially increase the number of estates being charged to IHT over time, subject to movements in asset and property values.

# Reduction in inheritance tax rate for charitable giving from estates

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

A reduced rate of inheritance tax (IHT) will be applied where 10 percent or more of a deceased's net estate is donated to charity. This provision will apply for deaths occurring on or after 6 April 2012. The proposal will be subject to consultation on the detailed implementation of the measure.

The precise detail is awaited, but it may encourage some individuals to donate or to donate more to charity from their estates, and may also benefit other beneficiaries of estates through reducing the net cost of specific charitable bequests.

## The issue

The net estate of a deceased person after all available reliefs and exemptions (including spouse exemption, nil rate band and specific reliefs) is subject to IHT at 40 percent. Gifts to charity from an estate are exempt from the charge to IHT.

The Budget proposes that a further incentive to leave assets to charity is introduced. This is that where an individual leaves 10 percent or more of their net estate (after all reliefs and exemptions) to charity, the rate of IHT on the remaining estate is reduced from 40 percent to 36 percent. This is a 10 percent reduction in the overall rate of tax charged on the net estate. The Chancellor announced that the benefit of this reduction will be passed to the charity rather than to increase the estate passing to the other beneficiaries of the estate. It is not yet clear what the precise mechanism for passing the benefit to the charity will be.

## Who is affected

There may be an added incentive for certain individuals to leave assets from their estate to charity as the net cost of this may be reduced.

Charities would benefit from any increase in the number of bequests left to them, and also from the additional tax saving if this is passed to them as suggested by the Chancellor.

The other beneficiaries of estates may benefit through a reduction in the net cost to the estate of leaving a specified sum to charity.

However as we have no detail on these new rules, their precise impact cannot yet be determined.

## Timing

The new rules will take effect for deaths occurring on or after 6 April 2012. The Government is to consult on the precise implementation of the rules and how they would interact with other IHT rules that apply to an individual's net estate.

### **Our view**

The measure is intended to encourage gifts to charity from estates, but much more detail is required on how this might work in practice before it will be possible to determine its likely effects, and any impact on behaviour.

# Enterprise Investment Scheme (“EIS”) and Venture Capital Trusts (“VCTs”)

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

**The issue**

Subject to State aid approval the following increases will be introduced:

- the thresholds for the maximum size of qualifying company for both EIS and VCTs will increase with the employee limit being extended to fewer than 250 employees (currently fewer than 50 employees), and the size of gross assets being increased to no more than £15 million before investment (currently £7 million);
- the maximum annual amount that can be invested in an individual company will increase to £10 million (currently £2 million); and
- the annual amount that an individual can invest under the EIS will increase to £1 million (currently £500,000).

Measures will also be introduced to prevent those companies whose trade consists wholly or substantially in the receipt of Feed-In Tariffs or similar subsidies from qualifying unless commercial electricity generation commences before 6 April 2012.

**Who is affected**

Individuals subscribing for shares in qualifying EIS companies, VCTs and companies looking to qualify as EIS/VCT investee companies.

**Timing**

The measures above will take effect from 6 April 2012.

**Our view**

This is a welcome move in that more companies will fall within the conditions to qualify as an EIS and VCT companies. This should result in more companies being able to attract investment. Individuals will also be able to benefit from increased tax relief as a result of the maximum annual investment being increased and therefore this is a positive measure.

# Charities and charitable giving

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

Changes are to be made to the Gift Aid donor benefit limits in respect of donations of £1,001 or more. Under the current rules where such a donation is made the donor can receive benefits in consequence of that donation with a value of up to five percent of the donation, subject to an overall limit of £500. This overall limit will be increased to £2,500.

A number of changes have also been announced which are intended to simplify the administration of Gift Aid, as well as encourage and support further charitable giving. These include:

- A Gift Aid style repayment for charities in respect of small donations. The new repayment will be claimable without the need to obtain Gift Aid declarations on donations of £10 or less, subject to a cap of £5,000 per year per charity. Charities will need to meet certain conditions in order to qualify to claim this new repayment.
- The introduction of a new online system for charities to register for and submit Gift Aid claims.
- Giving statutory effect to an existing Extra Statutory Concession under which HMRC currently make certain repayments of tax to charities outside of a tax return.
- Consultation will also be launched regarding the introduction of a tax deduction for taxpayers who donate works of art or historical objects of national importance to the State.

## Who is affected

Charities and their donors.

## Timing

The new rules for donor benefits will apply in respect of donations made on or after 6 April 2011 for individual donors, and for donations made in accounting periods ending on or after 1 April 2011 by corporate donors.

Other changes will be subject to consultation and will take effect in Finance Bill 2012 or later.

## Our view

These are positive changes which will help to reduce the administrative burden for charities in relation to Gift Aid. The new Gift Aid style repayment is good news for small charities who rely on small donations but who have until now been precluded from benefiting from Gift Aid due to the administrative costs.

# Personal Tax: Other measures

To be included in FB2012 or later

## **Gifts of art**

The Government is to consider the introduction of a tax reduction for individuals who donate works of art or historical objects of national importance to the State. However, there will be a consultation on the proposal and no further details are available as to the precise tax relief available and the conditions applying.

# Revisions to measures published in Finance Bill 2011 draft clauses

# Disguised remuneration

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Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

## The issue

The Government announced on 9 December 2010 that anti-avoidance legislation will be introduced in Finance Bill 2011 concerning third party arrangements used to avoid, reduce or defer liabilities to income tax and NICs on rewards from employment or to avoid restrictions on pensions tax relief.

A new income tax charge will apply where a third party provides an employee with reward, recognition or a loan in connection with the employee's employment. The Government say that third party arrangements that do not amount to tax avoidance will be excluded "in so far as this is possible without creating additional avoidance risks". In particular, this is to apply to genuine deferred remuneration arrangements common in the financial services sector and which last less than five years and genuine commercial arrangements for the provision of employee car ownership schemes.

The legislation will also apply to pension arrangements involving third parties (which they generally do) and which are used in addition to, or instead of, registered pension plans and where, at present, the rules on the annual and lifetime allowances do not apply.

The legislation will apply to arrangements involving trusts or other third parties and where (i) sums or assets are "earmarked" for employees, (ii) loans are provided to employees (iii) assets are made available to employees or (iv) sums or assets are paid or provided to employees. The legislation will apply equally to remuneration and retirement benefit arrangements, but not to payments otherwise chargeable to tax as pension income.

The new charge will be based on the full amount of any sum of money made available or the higher of the cost or market value where an asset is used to deliver the reward.

The amount will count as a payment of employment income and the employer will be required to account for PAYE accordingly.

The Government invited representations on this measure over the period until 9 February 2011, and on 21 February published a series of FAQs addressing a number of points that were raised.

The Government have confirmed that they have amended the legislation to limit the impact on employers and individuals "where it is possible to identify arrangements that cannot be used for avoidance purposes". The amendments cover "the protection of rewards by group companies, share incentive arrangements and genuine deferred remuneration arrangements". The Government have also confirmed that existing pension savings will be excluded.

The Government note that they regard certain arrangements caught by these new measures as not, in any event, effective under the current law and say they will continue to challenge such arrangements.

## Timing

The new rules will take effect from 6 April 2011 but anti-forestalling rules will apply to the payment of sums (including loans) to employees, and in certain other circumstances, between 9 December 2010 and 5 April 2011.

Regulations will be published shortly to apply NICs to amounts chargeable to income tax under the new rules.

## Our view

The Government say that approximately 5,000 employers and 50,000 employees will be affected by these measures with a yield to the Exchequer of some £750 million in 2011-12 and subsequent years to 2015/16.

Whilst it is understandable that the Government wishes to clamp down on perceived areas of tax avoidance and is concerned about potential tax leakage through the use of pension arrangements falling outside of the registered regime, there was much concern expressed during the consultation period about the very wide scope of the draft legislation that was published on 9 December 2010.

The FAQs that were published on 21 February 2011 sought to allay this concern by referring to a number of the hard edges and unintended consequences of the new rules and confirming, as the Government now reaffirm, that the draft legislation will be appropriately amended.

Our real concern, however, is the very wide range of circumstances in which third parties are involved in the provision of reward to employees, whether this be in relation to share plans, pension plans, medical insurance cover, relocation assistance etc. This applies equally, if not more so, to international assignees posted to the UK from abroad. Whilst there are a number of prescribed exceptions there will inevitably still be numbers of commercial arrangements which will not tick all the required boxes.

Although the Government say they will, for the most part, exclude group companies from the definition of third parties, this is with the caveat that this will not be so where there are "additional avoidance risks". Whilst we can understand this approach at a conceptual level, the reality is that employers will need to review very carefully all their remuneration arrangements which involve any party other than the employer alone (and whether this is another group company or otherwise) and to determine whether, and if so how, they could be impacted. Indeed employees may well want to approach HMRC to confirm the position since the consequences of inadvertently getting it wrong will be very unwelcome to both employers and employees alike.

# Tainted charity donations

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## Brief overview

The consultation on the draft Tainted Charity Donations rules has resulted in a number of welcome amendments to the legislation. Whilst the rules remain broadly as set out in the draft Finance Bill as published in December 2010, amendments have been made to ensure that the new rules will operate as intended and minimise the impact on charities. The key changes to the Tainted Charity Donations rules are:

**Condition B** – this now focuses on “financial” advantages.

**Condition C** – there is now also an exemption for relevant housing providers (this is something that KPMG specifically pushed for whilst part of the HMRC Working Party looking at these provisions)

A shorter transitional period with the repeal of the substantial donors provisions from April 2013 (previously the repeal would not have been until April 2015)

We understand that HMRC are to continue to consult on the practical impact of the new rules and will propose amendments for the future where necessary.

## *What we wrote when the draft clauses were published 9 December 2010*

Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

### Summary of proposal

New rules will be introduced to replace parts of the existing Substantial Donors legislation (found at Sections 502 – 510 CTA 2010 for charitable companies and Sections 549 – 557 ITA 2007 for charitable trusts).

The Tainted Charity Donations rules will adopt a purpose test approach and will apply to treat an otherwise relievable charitable donation as a “tainted donation” where certain conditions are met. There are three conditions which must each be met in order for a donation to be tainted and these can be summarised as follows:

**Condition A** – there is a donation and arrangements which would not have been made or entered into independently of one another.

**Condition B** – the main purpose, or one of the main purposes, of the arrangements is to obtain an advantage directly or indirectly from the charity for the donor (or any person connected with them at the relevant time).

**Condition C** – the donor is not a qualifying charity owned company.

The new rules are intended to deny tax relief to the donor where the donation is treated as a tainted donation. In addition to the loss of tax relief in respect of the tainted donation, a tax charge may also arise for individual donors (but not corporate donors) in cases where the donation would have otherwise been eligible under the Gift Aid scheme.

### Who is affected

All organisations entitled to UK charity tax reliefs and their donors (whether individuals or corporate donors).

### Timing

The new rules will take effect in respect of donations made on or after 1 April 2011.

The Substantial Donors legislation will remain in force, but will be disapplied in certain circumstances in relation to pre-existing substantial donors. No new substantial donors will be created as a result of donations made on or after 1 April 2011.

### Our view

We continue to recognise and support the need for anti-avoidance legislation where this ensures that the valuable tax reliefs available to charities are not abused. However, the existing Substantial Donors legislation has placed a significant administrative burden on charities and has the potential to catch innocent transactions.

We therefore welcome the new Tainted Charity Donations rules which, where applicable, will deny tax relief to the donor rather than penalise the charity.

The introduction of a purpose test means that these new rules should not catch donors seeking to make genuine charitable donations. In addition the new rules should not catch arrangements which, although connected to a donation, do not result in the donor (or any connected person) obtaining an advantage from the charity. Broadly, speaking an advantage will not be obtained from the charity where the arrangement involves a transaction carried out on arm's length terms.

# Removing the effective requirement to annuitise by age 75

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## **Brief overview**

It was previously announced that the Finance Bill 2011 will remove the requirement to take an annuity at age 75 years from April 2011.

## **Key changes announced at the Budget**

Some differences in the rules for the pensions and lump sums payable before and after age 75 have been identified at the consultation stage and changes will be made in the Finance Bill 2011 to remove such differences.

## *What we wrote when the draft clauses were published 9 December 2010*

Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

### Summary of proposal

The draft legislation confirms previously announced proposals to remove pensions tax rules from April 2011 that currently require members of registered pension schemes to secure an income, usually by buying an annuity, by age 75.

Currently, members of defined contribution pension schemes may, as an alternative to buying an annuity on retirement, take income prior to age 75 in the more flexible form of “unsecured pension” or, after age 75, “alternatively secured pension” (ASP). ASP is considered to be very restrictive and is subject to heavy tax charges. The new measures, in effect, will abolish ASP and allow a modified form of unsecured pension to continue beyond age 75.

The maximum income that an individual may withdraw from most unsecured pension funds will be capped at 100 per cent of the equivalent annuity that those funds could buy. The cap must be reviewed at least every three years until age 75, after which reviews must be carried out annually.

However, the cap will not apply at all to individuals who can demonstrate that they have secured a lifetime pension income of at least £20,000 a year. These members will be able to access the whole of their drawdown funds as pension income with no annual limit.

The tax rate for all lump sum death benefits is to be set at 55 per cent – except where the member dies before age 75 without having taken a pension, in which case the benefit will remain tax-free. (Note that this is a worsening of the position for those who die before age 75 having already taken a pension income, where the rate of tax is currently only 35 per cent.)

Individuals making a withdrawal from unsecured pension funds when they are resident outside the UK for a period of less than five full tax years will be liable for UK income tax on that withdrawal in the tax year in which they become UK resident again.

From 6 April 2011, inheritance tax will not typically apply to unsecured pension funds remaining when the individual dies – even if this occurs after reaching age 75. But IHT will continue to apply where the pension scheme trustees have no discretion regarding the payment of lump sums on death and certain other lump sums.

### Who is affected

Members of registered pension schemes.

### Timing

The new rules will take effect from 6 April 2011.

### **Our view**

We welcome the measure as offering members more flexibility in choosing how to draw their retirement income and removing the arbitrary variation in tax treatment around the pivotal age of 75.

Each defined contribution scheme can determine whether they wish to offer unsecured pensions. Members of schemes which do not offer this facility (which would include all defined benefit schemes) would need to transfer their pension rights to a new scheme in order to take advantage of the new rules.

# Restricting pensions tax relief

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**Brief overview**

On 14 October 2010 the Government announced that the annual allowance for tax relief on pension savings for individuals will be reduced from £255,000 to £50,000 from 2011-12, and the lifetime allowance will be reduced from £1.8m to £1.5m from 2012-13.

**Key changes announced at the Budget**

Following consultation, there will be provisions in the Finance Bill 2011 to enable individuals with annual charges in excess of £2,000 from a pension scheme to elect for their liability to be met from their pension benefit.

## *What we wrote when the draft clauses were published 9 December 2010*

Impact on tax payer			
Positive	Neutral	Negative	Both positive and negative

### Summary of proposal

Under legislation put in place by the previous Government, pensions tax relief would be restricted for those with gross incomes of £150,000 and above from tax year 2011/12 onwards. The new, coalition, Government is pressing ahead with an alternative which instead restricts pensions tax relief through a reduction in the existing allowances.

The annual allowance (AA) sets a limit on the tax-relieved pension savings that an individual can make in a tax year. It will reduce from £255,000 to £50,000 from April 2011 and will remain at that level until at least 2015/16. Full marginal rate tax relief will be available on pension savings up to the allowance, and any excess will be taxed at the individual's marginal rate.

All contributions (employee and employer) to money purchase pension arrangements count towards the AA. For defined benefits arrangements, the annual accrual of benefit valued using a factor of 16:1 counts towards the AA.

There will be an exemption from the AA in cases of death, serious ill-health (life expectancy of under a year) and where an individual is suffering from ill-health such that they are not expected to be able to work again in any capacity.

The Government is expecting individuals, employers, and pension schemes to adapt their behaviour to stay within the AA wherever possible. To help individuals avoid a charge, where their savings exceed the AA in a given year unused allowance from up to three previous years will be available to offset against the excess pension savings. Carry-forward will be available against an assumed AA of £50,000 for the tax years 2008/09, 2009/10 and 2010/11.

Even with the above, there will still be some individuals who exceed the AA and the tax charge could be substantial. So the Government is also consulting on options for pension schemes to meet part of the tax charge on the member's behalf, with an appropriate reduction in benefit.

The lifetime allowance (LTA) sets a limit on the value of the tax-relieved pension savings arising effectively on retirement. It will reduce from £1.8 million to £1.5 million on 6 April 2012.

Individuals will be able to apply for protection from the reduced LTA. They will be able to have an underpinned lifetime allowance of £1.8 million as long as they opt-out of all further pension accrual, ie pay no further contributions to money purchase arrangements and have no accrual in defined benefits arrangements other than deferred revaluation in line with existing scheme rules, or the consumer prices index. Individuals will have to opt-out by 6 April 2012. Those who already have existing protection from the current LTA will be unaffected by the reduction.

### **Who is affected**

The reduction in the AA affects those with annual pension savings exceeding £50,000. The reduction in the LTA affects individuals whose total pension savings either exceed £1.5 million at 6 April 2012, or are expected to exceed £1.5 million at some point in the future.

### **Timing**

The AA reduces to £50,000 from 6 April 2011. The LTA reduces to £1.5 million on 6 April 2012.

### **Our view**

We welcome the Government's decision to implement an alternative to the previous Government's tax relief measures, which were widely seen as inequitable, burdensome on employers and pension schemes, and likely to be highly damaging to UK pension provision.

The Government has developed an approach which is much fairer and sustainable. The highest earners will still feel a significant impact (though not as bad as under the previous proposals) but lower and middle earners should remain largely unscathed. However, more and more will be affected over time as the AA is frozen until at least 2015/16.

The real business issue now is how can employers respond, communicate the changes to their employees, and adapt their pension schemes to mitigate the impact of the reduced AA.

# Finance Bill 2011: Minor amendments to previously announced measures

Draft clauses for the 2011 Finance Bill were published in advance of the 2011 Budget on 9 December 2010. Any substantial changes to these draft clauses announced in this Budget have been detailed above. Budget 2011 has announced changes to some other clauses which, because of their minor nature, are not covered in detail in this commentary. The personal tax measures to be included in Finance Bill 2011 where such minor changes have been made are as follows:

- Allowances and thresholds;
- Furnished Holiday Lettings.

A copy of our commentary on the draft Finance Bill (including these measures) can be found [here](#).



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