



TAX

Chancellor's Budget 2009

KPMG full commentary

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April 2009

ADVISORY



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Our View



Sue Bonney
Head of Tax & People
Services

“Today’s budget was rather a mixed bag for big businesses. There was positive news on the key issue of the taxation of foreign profits and targeted practical measures for business. Unfortunately however, a raft of additional legislation (principally around anti-avoidance) has introduced yet more complexity.”

Welcome measures:

Foreign profits: News that the move to exempt foreign-sourced tax dividends will come in from July and that it will be decoupled from the controversial debt cap rules which limit the extent to which interest can be deducted from UK tax is good news for business. It shows that the authorities have listened to business and it should lead to repatriation of cash to the UK.

Capital allowances: The move to double capital allowances is good news. Business can deduct more spend against their taxable profits more quickly. It could encourage more investment sooner but only companies that are taxpaying (ie not making losses) will benefit

Extension to loss carry-backs for SMEs and more reliefs for tax payment dates: Both these moves are helpful as they give smaller business some more valuable breathing space but there was no extension to help larger businesses on this front.

Less welcome measures

Personal liability for senior accounting executives: Senior executives in large businesses face personal liabilities if their processes and controls are deemed less than ‘adequate’ whilst reasonable in concept, this could be tricky from a practical point of view and it is important to avoid this becoming a Sarbanes Oxley equivalent for UK tax.

Personal tax rate now the highest among large western European economies: with the introduction of the 50 percent band for those earnings over £150,000, the UK now has the highest personal tax rate in Western Europe. Business may be concerned that this may make it harder for them to recruit and retain talented personnel.

Targeted provisions on closing ‘loopholes’: Targeted provisions closing ‘loopholes’ coupled with the fiscal squeeze will inevitably lead to more complexity and uncertainty.

Economic Implications



Andrew Smith
Chief Economist

The Economy and the Public Finances

The Chancellor bowed to the inevitable after the dramatic fall in UK output over the last six months. Rather than the shallow recession forecast in November's Pre-Budget Report, he now expects output to drop by 3.5 percent this year. A recovery is still forecast in 2010 with growth of 1 percent, rising to over 3 percent in 2011.

Consequently, the public finances have deteriorated even further. Lower economic activity is resulting in collapsing tax revenues on the one hand and rising public spending, particularly on unemployment benefits, on the other - making huge budget deficits inevitable.

From 2-3 percent of GDP in recent years, government net borrowing reached 6 percent in 2008-09 and is projected to double to 12 percent this financial year, declining only slowly to 6 percent by 2013-14. Public debt will double to 80 percent of GDP over the period.

Against this background, the Chancellor found little room for any additional fiscal boost to support the economy this year. November's measures, principally the ongoing temporary VAT cut, represent a loosening of about £16 billion (1 percent of GDP) and the new measures add only a net £5 billion.

Looking further ahead, Mr Darling outlined plans for redressing the deficit once the economy is on a sounder footing. In addition to plans already in the pipeline to raise National Insurance contribution rates from 2011 and a squeeze on public spending, tax rates for the higher paid are increased further from 2010.

Much depends on the speed of economic recovery. If the Treasury's economic forecast again proves optimistic, the outturn for the public finances will be correspondingly worse.

Corporate Tax



Simon Palmer
Head of Corporate Tax

The 2009 Budget was a mixed bag on the corporate tax side. The surprise announcement of a temporary 40 percent First Year Allowance for expenditure on plant or machinery in the main capital allowances pool was welcome although it is far from certain that it will stimulate capital investment to the extent the Chancellor suggested. The extension for a further year of the loss carry back for SMEs is also good news but, as it is still limited to £50,000 of losses, its impact remains relatively small.

The decoupling of the introduction of the worldwide debt cap and the distribution exemption is very welcome and shows that HMRC has been listening to business. The broadening of the circumstances in which a chargeable gain or loss may be reallocated within a group is also a very sensible relaxation of the rules and should help companies obtain effective relief for losses suffered.

A concern for large companies will be the decision to introduce personal liability for senior accounting executives, announced without any prior consultation. This arises from a Budget measure that creates a legal requirement for the Senior Accounting Officers (likely to be the Group CFOs) to certify personally and annually that adequate controls are in place to prepare accurate tax computations. Many companies are likely to have difficulty in confirming that their systems are adequate for all tax computation purposes, particularly in relation non-system areas such as transfer pricing, and there is a real risk of a significant additional administrative burden for most businesses affected.

So overall, although there is a lot for companies to be happy about, for large companies at least, this is likely to be overshadowed by the announcement on personal liability and the concern that this could herald a Sarbanes Oxley equivalent for UK tax.

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Taxation of foreign profits

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The Government has confirmed the introduction of the package of reforms to the taxation of foreign profits announced in the Pre-Budget Report, although with some changes from the draft legislation that was published on 9 December 2008. The relevant legislation will be included in Finance Bill 2009.

The package will consist of the following four elements:

- 1. Dividend exemption – Foreign and UK dividends and other distributions will generally be exempt from corporation tax if they fall into an exempt class and anti-avoidance provisions do not apply. The exemption is now to be extended to distributions received by all companies, including small companies.**
- 2. Debt cap rules – The tax deduction for finance expense payable by UK members of a group of companies will be restricted to the consolidated gross finance expense of the group. The rules apply to groups other than those consisting entirely of companies that are small or medium sized. A number of changes are proposed to the draft legislation published last December following HMRC's consultation with business. Further details of the rules are included in a separate item in the commentary entitled Worldwide Debt Cap.**
- 3. Controlled foreign companies ('CFC's') – As a consequence of the introduction of the dividend exemption, the acceptable distribution policy exemption is to be abolished. In addition, the exemption for superior and international holding companies under the exempt activities test is to be removed, with a two-year transitional period in certain circumstances. The exemption for local holding companies is now to be retained.**
- 4. Post-transaction reporting requirement – The existing Treasury consent rules are to be repealed and replaced by a new reporting requirement that applies to transactions with a value of £100 million or more, subject to a number of exclusions. Companies will now have to report within 6 months of the relevant transaction.**

The original package included an extension to the 'unallowable purpose' rules for loan relationships and derivative contracts. It has been announced that the case for further legislation in this area will be kept under review, but that the measure will now not be included in Finance Bill 2009.

Who is affected

All UK companies.

Timing

The dividend exemption will apply to dividends and other distributions received on or after 1 July 2009.

The debt cap rules will apply to finance expenses payable in accounting periods beginning on or after 1 January 2010.

The CFC changes will apply to CFC accounting periods beginning on or after 1 July 2009 with provision made for periods that straddle this date. The exemption for superior and international holding companies will be available to qualifying holding companies in transitional form until 1 July 2011.

The post-transaction reporting requirement will apply to transactions undertaken on or after 1 July 2009.

Our view

The introduction of the foreign profits package has been confirmed by the Government, as expected, but it is encouraging that a number of changes have been made to the original proposals to take account of concerns raised by business during the consultation process. The benefits of the dividend exemption and repeal of the Treasury consent rules are countered by the introduction of the debt cap rules, which although substantially modified are still likely to have a significant impact on many groups in terms of extra tax cost and/or additional compliance burden.

However, it is helpful that the introduction of the debt cap rules is to be delayed until 1 January 2010, at the earliest, as this will allow time for groups to assess the impact of the rules and ensure that they are able to comply with them. It should also provide sufficient time to unwind upstream loans that will be caught by the rules by paying dividends to the UK within the dividend exemption.

Personal tax accountability of senior accounting officers of large companies

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Legislation is to be introduced in the Finance Bill to require senior accounting officers of large companies to take reasonable steps to establish and monitor adequate accounting systems for the purpose of accurate tax reporting. They will be required to certify annually that the systems are adequate, or alternatively specify the nature of any inadequacies and confirm that they have been notified to the company auditors.

Each company will have an obligation to notify HMRC of the identity of the senior accounting officer. Penalties will be chargeable both on the senior accounting officer personally and on the company for:

- Careless or deliberate failure to comply with these obligations
- Carelessly or deliberately giving an incorrect certificate or notification

HMRC are to consult with interested parties regarding operational issues.

Who is affected

Large companies and groups, i.e. companies that are not defined as 'small' or 'medium sized' under the Companies Act 2006, and their senior accounting officers.

Timing

The measure will apply to accounting reference periods beginning on or after Royal Assent. Transitional arrangements may be necessary.

Our view

HMRC are understandably concerned at the risks to tax revenue arising from inadequacies in corporate accounting systems. It is surprising, however, that these proposals have been brought forward without any prior consultation having taken place as part of HMRC's Review of Powers, Deterrents and Safeguards.

We will need to see the detail of the proposed legislation in order to evaluate it fully. Among other things it is unclear what steps would be regarded as reasonable and what level of monitoring would be required, and we would expect HMRC to produce further guidance on these points. Many companies are likely to have difficulty in confirming that their systems are adequate for all tax computation purposes, particularly in relation to complex areas such as transfer pricing. Companies will need to consider the implications of these new obligations carefully and assess how the risks can be mitigated.

In addition, it would be unfortunate if the legislation imposed a significant additional administrative burden on companies which already have adequate accounting systems in place.

Extension of trading loss carry back for business

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Under current rules, ongoing businesses have the ability to carry back trading losses without limit to relieve against profits of the previous accounting period.

Finance Bill 2009 will extend the period for which trading losses can be carried back against previous profits. This extension will apply to trading losses of £50,000 made by companies in accounting periods ending between 24 November 2008 and 23 November 2010.

This measure was introduced in the Pre-Budget Report in November 2008 but today's announcement extends the period that losses can be carried back by another year.

Who is affected

This measure applies to both companies and unincorporated businesses.

The new measure applies to companies of all sizes but is likely to be more valuable to smaller companies.

Timing

For companies, this measure applies to £50,000 of trading losses incurred in the accounting period which ends between 24 November 2008 and 23 November 2009 and a further £50,000 of trading losses incurred in the accounting period which ends between 24 November 2009 and 23 November 2010.

Disguised interest and transfers of income streams

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The Government has today announced that legislation to counter avoidance involving disguised interest and transfers of income streams will be included within Finance Bill 2009. This legislation follows extensive consultation and numerous workshops with stakeholders following proposals introduced in the 2007 Pre-Budget Report ('the principles based approach to financial products avoidance'). The principles-based approach is intended to tackle tax avoidance in a simpler and clearer way than through piecemeal legislative amendment. No legislation has been produced today.

Disguised interest

The rules relating to disguised interest operate primarily on the basis of a principle, with certain exclusions. The principle is that a time value of money return (a return 'economically equivalent to interest') is charged to corporation tax in all circumstances and these rules apply where an arrangement is structured with the intention that the return would arise in a form that is not charged to tax as income. The exclusions listed in the Budget Note are broadly:

- i. where it is not a main purpose of the arrangements to secure that the return is not charged to tax as income
(Note that the most recent draft of the legislation referred to an exclusion where the arrangement has no tax avoidance purpose)
- ii. where the return arises to a company purely from an increase in the value of shares where they are shares in a company with which the company is connected (which will include shares in certain joint venture companies)
(Note that the most recent draft of the legislation contained an exclusion where the arrangement involved only excluded shares (i.e. certain group companies and non-group CFCs or companies that would be CFCs but for an exemption). Separate legislation was separately issued to act as a partial replacement for sections

91B to 91E FA 1996, in particular section 91D dealing with preference share arrangements where such shares are accounted for as a financial liability)

Note also that the most recent draft of the legislation contained an exclusion where the return was taxable otherwise under the loan relationship rules (Part 5 Corporation Tax Act ('CTA') 2009), the derivative contracts rules (Part 7 CTA 2009), the intangible fixed asset rules (Part 8 CTA 2009) or as trading income (Part 3 CTA 2009). It was expected that this exclusion would be extended to cover all circumstances where the return was otherwise brought into account as income. However, the Budget Note does not refer to this exclusion at all.

Transfers of income streams

The Budget Note states that the legislation will ensure that receipts derived from a right to receive income (and which are an economic substitute for income) are taxed as income for the purposes of corporation tax and income tax.

In the most recent draft of the legislation, the rules were designed to operate in circumstances where the transfer of a right to 'relevant receipts' takes place without the transfer of the underlying asset from which the right to relevant receipts arises (i.e. receipts that would be income of the transferor but for the transfer). Broadly, the consideration provided for the right to the relevant receipts was to be brought into account as income of the transferor. The consideration would be deemed to be the market value of those receipts in circumstances where the consideration provided was less than market value. Provisions were also introduced such that where the transfer of the right was a consequence of the transfer to the transferee of an annuity from which the right to relevant receipts arises, the rules would automatically apply.

The rules have been introduced to deal with transactions that exploit the differences between the taxation of income and capital items. In the most recent draft of the legislation, provisions were included relating to the transferee of the right where that transferee is a company; the consideration provided for the transfer of the right to the relevant receipts to be treated for the purposes of the loan relationship rules (Chapter 5 CTA 2009) as if it were a money debt arising from a transaction for the lending of money. The Budget Note confirms that a grant or surrender of a lease and the disposal of any interest in an oil licence are to be excluded from these provisions (though the most recent draft of the legislation referred only to leases of land).

The Budget Note confirms that the legislation will not apply to sales of income that arise from loan relationships or derivative contracts where that income would have been subject to any exclusions under those rules. It also confirms that there will be provisions to exclude amounts

which are already taxed as income, or where the transfer of the income is by way of security.

Who is affected

Disguised interest

The legislation will affect large companies that enter into arrangements to avoid tax on returns from investments that are economically equivalent to interest.

Transfers of income streams

The legislation will apply to companies and individuals, including partnerships, that dispose of rights to receive future income streams without disposing of any underlying asset.

Timing

The timing of the rules is as follows:

Disguised interest

The Budget Note states that the legislation will generally apply to arrangements to which a company becomes party on or after 22 April 2009, but that it will also apply to certain arrangements in place before that date that are within the scope of the existing disguised interest legislation which is to be repealed. This reflects the commencement provisions contained within the most recent draft of the legislation. The legislation will be included within Finance Bill 2009.

Transfers of income streams

The Budget Note states that the legislation will have effect for transfers of income taking place on or after 22 April 2009. The legislation will be included within Finance Bill 2009.

Our view

For both measures, the most recent draft of the legislation demonstrates that HMRC have listened to stakeholders during the workshops and also implemented some of the recommendations made by stakeholders during those sessions.

We consider that guidance would be helpful but, at this stage, we do not know whether guidance will be published.

There are a few inconsistencies between the latest draft of the legislation released during the consultation period and the Budget Note (as outlined above), but subject to sight of the final legislation, the rules should be a workable legislative framework.

Groups: Reallocation of chargeable gains

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Where a UK group company disposes of a chargeable asset, it may (in certain circumstances) jointly elect with another UK group company for the asset to be treated as if it had been transferred to that group company before a disposal outside of the group. This allows gains and losses arising in different group companies to be set against each other.

However, the current legislation only permits such an election to be made if there is a disposal outside the group. In particular, this can prevent groups from obtaining effective tax relief for a loss arising on a disposal to an overseas group company (e.g. when restructuring) or on a deemed disposal (e.g. where an asset has become of negligible value).

The proposed revision to the legislation would transfer the gain/loss rather than deeming the asset sold to have been transferred intra-group prior to its ultimate disposal. This should enable groups to reallocate a gain or loss arising on a disposal to a non-UK group company or following a deemed disposal event.

Who is affected

Multinational groups where a chargeable asset is sold by a UK company to a non-UK group member. Groups where a chargeable disposal is deemed to arise, for example where an asset has become of negligible value.

Timing

The legislation will apply to losses or gains arising on or after the date that Finance Bill 2009 receives Royal Assent.

Our view

The broadening of the circumstances in which a chargeable gain or loss may be reallocated within a group should, in particular, help taxpayers obtain effective relief for losses suffered.

Review of HMRC powers, deterrents and safeguards

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

A further range of measures is to be introduced in the Finance Bill as a result of the review of HMRC's powers, deterrents and safeguards, which has been in operation since the formation of HMRC in 2005. The new measures are as follows:

Payments, repayments and debt

- Voluntary Managed Payment Plans ('MPPs') will be introduced to allow taxpayers to spread their income or corporation tax payments equally over a period straddling the normal due dates
- HMRC will be able to collect small debts through the PAYE system
- HMRC will have the power to require companies and businesses to provide contact details to enable it to trace tax debtors

Compliance checks

- The compliance checking framework which was introduced in Finance Act 2008 ('FA 2008') for direct taxes and VAT will be extended to environmental taxes, IPT, SDLT, SDRT, IHT and PRT. This includes provisions on record-keeping requirements, inspection and information powers and time limits for assessments and claims
- Various specialist information powers which are effectively replaced by the powers in Schedule 36 to FA 2008 will be repealed
- A penalty will be introduced for carelessly or deliberately providing inaccurate information or documents

Penalties for late filing and late payment

- A new harmonised penalty regime will be introduced for late filing of tax returns and late payment of tax, covering income tax, corporation tax, PAYE, NICs, Construction Industry Scheme, SDLT, SDRT and IHT

Interest harmonisation

- A single regime will be introduced covering interest on underpayments and repayments of income tax, corporation tax, PAYE, Class 4 NICs, Construction Industry Scheme liabilities, environmental taxes, excise duties, stamp duties, IHT, IPT, pension scheme liabilities and PRT

Who is affected

All taxpayers are potentially affected.

Timing

Payments, repayments and debt

The legislation on MPPs and tracing tax debtors will apply from Royal Assent. Because of the need for changes to HMRC's systems the MPPs will not be introduced before April 2011. Collection of small debts through PAYE is likely to begin from April 2012.

Compliance checks

The repeal of specialist information powers is likely to take place soon after Royal Assent. The extension of the compliance-checking framework is likely to take effect from 1 April 2010, apart from the amendments to time limits which are not likely to be fully effective until 1 April 2011.

Penalties for late filing and late payment

The changes will be phased in over a number of years, starting with penalties for late payment of in-year PAYE in April 2010.

Interest harmonisation

Interest on CT and PRT will not be included in this year's finance bill and will be introduced in Finance Bill 2010. Where HMRC currently charge and pay interest, rates will be aligned shortly after Royal Assent. Other changes will be implemented over a number of years beginning with interest on late payments of in-year PAYE from April 2010.

Our view

KPMG has taken part in the consultations leading up to these proposals and many of our suggestions have been taken into account in the latest documents. Overall the proposals represent a welcome modernisation and harmonisation of the administrative framework. We will be looking at them in detail to see whether they reflect sufficiently the comments that have been made and provide adequate safeguards, and will make further representations if necessary.

Double taxation relief avoidance: repayment of foreign tax

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Under certain foreign tax regimes, e.g. the Maltese tax system, the shareholder of a company with a permanent establishment (PE) in that territory is entitled to a refund of the tax paid by the PE when the company pays a dividend to the shareholder. Similarly, a refund of the foreign tax may be available to the shareholder of a company resident in that territory which pays a dividend.

There were arguments that a UK company with such a foreign PE could credit all of the foreign tax paid by the PE against the UK tax liability on the same profits. Existing legislation in section 806(3) ICTA 1988 required the UK company claiming double tax relief to notify HMRC if the amount of credit claimed was subsequently rendered excessive through a repayment of the foreign tax. However, this arguably did not apply if the repayment was made to a different entity from the one which paid the foreign tax.

In the case of a UK company receiving a dividend from a company resident in such a territory, it is understood HMRC took the view that the underlying tax should be reduced under section 799(2) ICTA 1988 if part of the underlying tax was repaid to the UK company. However, this was not free from doubt based on the wording of the legislation.

From a UK CFC perspective, it was argued by some taxpayers that the repayment of foreign tax to the shareholder did not reduce the effective credit due against the CFC tax on an apportionment. In addition, there were arguments that existing anti-avoidance rules contained in section 804ZA and Schedule 28AB of ICTA 1988 did not apply in the above situations.

The new rules are intended to make it clear that the credit for foreign tax is reduced in the above circumstances and that, additionally, expense relief will not be available for such tax.

Who is affected

The rules will apply to UK resident companies with a subsidiary or a PE in a relevant jurisdiction where dividends are paid out of the foreign profits to the shareholder. This appears to be the case even if the foreign entities have not been set up specifically to take advantage of the old rules.

Timing

The measure will take effect on or after 22 April 2009. It is not yet clear whether it will apply to claims made on or after this date or by reference to the date of the refund or when the foreign tax is paid but it appears that it may even affect existing claims if the foreign tax is subsequently repaid.

Our view

The changes are likely to affect a number of planning structures intended to take advantage of the Maltese imputation system of taxation (although companies are taxed at 35 percent in Malta, in many cases six sevenths of this tax is repaid to the shareholder on the payment of a dividend so that the effective tax rate on the Maltese profits is only 5 percent).

For dividends received on or after 1 July from Maltese companies, the new rules will not be relevant if the distribution exemption applies but structures involving PEs may still be affected along with certain CFC planning, subject to EU law considerations.

Group relief: Preference shares

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Legislation is to be introduced to ensure that companies issuing particular types of new preference share capital to external investors do not lose the ability to claim and surrender group relief with other members of the group. The changes will make it more difficult to inadvertently break a group structure or trigger an anti-avoidance provision when issuing such shares to non-group members.

Schedule 18 to the Income and Corporation Taxes Act 1988 identifies the 'equity holders' in a company, and the amount of their entitlement to the profits or assets available for distribution. These rules are used to determine whether related companies are able to claim or surrender group relief, as well as forming a group for chargeable gains purposes.

Currently 'equity holders' includes the holders of the company's ordinary shares, which are all of the company's shares except for fixed-rate preference shares. Thus, fixed rate preference shareholders are the only shareholders ignored when determining whether companies are part of a group and able to claim loss surrender and chargeable gains relief.

The changes now remove the reference to 'fixed rate preference shares' and instead replace it with 'relevant preference shares'. This can include preference share dividends at a rate linked to a variable published market interest rate, or a rate linked to the index of consumer prices. This may also include circumstances where the preference dividend is only partially paid or not paid at all. These circumstances can arise in the case of companies in severe financial difficulties and where dividend payments are restricted by regulatory capital considerations.

Who is affected

Groups of companies where one or more subsidiaries is funded in part by preference shares issued to external investors. This is most likely to be financial institutions.

Timing

The changes apply to all accounting periods that commenced after 1 January 2008. An election can be made to retain the existing treatment of shares issued before 18 December 2008 (or shortly after where a commitment to issue the shares was entered into before that date).

Our view

The changes should reduce the instances where tax groups are unintentionally broken as the result of raising finance through the issuing of preference shares and the associated claims to losses and reliefs are lost.

These changes are most likely to be relevant to financial institutions and may, for example, provide a benefit where preference shares are issued in order to raise cash in a time of financial difficulty.

Hedging proceeds from future share issues

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

In circumstances in which a company anticipates making a share issue in a currency other than its functional currency, it may enter into a derivative contract to hedge the value of the issue proceeds. Previously, any gain from the contract would be subject to tax on termination or ceasing to be a hedge. The Disregard regulations (SI 2004/3256) will be amended such that all exchange gains or losses which arise under such a currency contract will be excluded from tax, unless any part of such gain is distributed to shareholders. In such a case, the gain will be taxed in the period and to the extent that it is distributed.

Who is affected

Companies which make shares issues in a currency other than its functional currency and hedge the proceeds using a currency contract.

Timing

The rules apply to currency derivative contracts entered into on or after 10 March 2009 with the intention of hedging future share issues. The rules also apply to such contracts which were entered into on or after 1 January 2009 and were extant at 10 March 2009, in which case any exchange loss to 9 March will be deductible provided there is a loss when the contract is finally closed out. Where the final currency loss is less than the loss showing on the contract at 9 March, the tax deductible loss is restricted to the final loss.

Our view

The measure has been introduced to help corporates deal with volatility in foreign exchange rates in periods in which calls on capital are likely and represents a logical extension to the existing rules.

Tax relief for business expenditure on cars

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Tax relief for expenditure on business cars will be subject to new capital allowances rules.

Writing down allowance for business cars will be given as follows:

- CO₂ emissions not exceeding 160g/km will be eligible for the main pool and writing down allowances at 20 percent per annum on reducing balance
- CO₂ emissions in excess of 160g/km will be eligible for the special rate pool and writing down allowances at 10 percent per annum on a reducing balance

Existing rules for 100 percent First Year Allowance for cars with CO₂ emissions of 110g/km will remain in force until 31 March 2013.

Expenditure on cars incurred before 1 April 2009, costing less than £12,000 were eligible for writing down allowance of 20 percent per annum regardless of emissions. This expenditure will remain in the main pool.

Expenditure on cars in excess of £12,000 incurred before 1 April 2009 will be allocated to a single asset pool with writing down allowances at 20 percent per annum capped at £3,000. This treatment will remain in force for 5 years. At the end of the 5 year period if there is a balance of unrelieved expenditure these amounts will be taken to the main pool. These transitional rules will end on the 31 March 2014 (for corporation tax) and 5 April 2014 (for income tax).

Under the old rules, rental payments on car hire where the value is in excess of £12,000 were adjusted downwards taking into account the retail price of the car when new.

Under the new business car rules, the reduction in car rental lease payments will only apply to cars with CO₂ emissions in excess of 160g/km. A flat rate 15 percent reduction of the rental payment will be applied.

Who is affected

All businesses that incur capital expenditure on cars.

Timing

Capital expenditure on business cars incurred on or after 1 April 2009 (for corporation tax) and 6 April 2009 (for income tax).

Our view

The rule changes have been subject to a very long consultation and they are broadly to be welcomed. Expenditure will either be eligible for 100 percent, 20 percent or 10 percent writing down allowances and removes the need for a single asset pool for expensive cars. The removal of the administrative burden is long overdue and the alignment of the rates of relief depending on CO₂ emissions is in line with the Government's green agenda.

The rules as set out are simple and easy to manage. However, it is questionable whether the Government has achieved the right balance between reducing the administrative burden and encouraging green technologies, as there is no link between the tax relief and actual usage of the cars.

Given the rule changes, businesses may need to review their decision on whether to buy or lease business cars.

Double taxation relief on dividends

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The reduction in the UK corporation tax rate from 30 percent to 28 percent took effect from 1 April 2008. This caused a mismatch between the rate at which foreign dividends are taxed and the amount of double tax relief available. Retrospective legislation will be introduced to correct this mismatch.

Under existing legislation, corporation tax is charged on an overseas dividend based, in effect, on the average corporation tax rate in force over the period in which the dividend is paid. However, any underlying tax available can be restricted by the 'mixer cap' formula which uses the corporation tax rate in force on the date the dividend is paid.

For example, for a company with a 31 December year end which received an overseas dividend in, say, June 2008, the average corporation tax rate for the 2008-09 financial years was 28.5 percent. Assuming underlying tax relief was available, the 'mixer cap' formula would have been applied using the rate at the time the dividend was paid, being 28 percent.

Hence the existing rules meant that some overseas dividends were taxed at a higher rate than the rate at which relief for underlying tax was available.

The new rules will make it clear that the amount of double taxation relief available is limited by reference to the average corporation tax rate not the rate in force on the date the dividend is paid.

Who is affected

UK resident companies in receipt of dividends paid by foreign companies in the financial year 2008-09.

Timing

The measure will have retrospective effect from the financial year beginning 1 April 2008.

Our view

This is a positive measure for UK corporate taxpayers which should ensure that the rates applied to the amount of corporation tax paid and double taxation relief available for overseas dividends correctly match.

As a result of the dividend exemption introduced as part of the foreign profits package, and announced to take effect from 1 July 2009, this will not be relevant for many dividends received by UK companies after this date.

Reclaiming income tax, capital gains tax and corporation tax overpayments

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The error or mistake relief provisions in ss33 and 33A, Taxes Management Act 1970 and in Paragraph 51, Schedule 18, Finance Act 1998 enable taxpayers to reclaim tax where an assessment is excessive due to a mistake in a return. Relief, if due, is given on a 'just and reasonable' basis.

Legislation will be brought forward in Finance Bill 2009 to provide a means of reclaiming overpayments where there is no other statutory route. The measure will remove the requirement that the overpayment must be the result of a mistake in a return and that it must be made under an assessment. It will enable claimants to quantify the amount to be repaid, subject to HMRC's right to enquire into the claim.

The proposed legislation is also said to amend the error or mistake relief rules to provide additional taxpayer safeguards.

Who is affected

Income tax, capital gains tax and corporation taxpayers reclaiming overpayments of tax.

Timing

The measure will have effect for claims made on or after 1 April 2010.

Our view

The current rules governing the reclaiming of overpayments resulting from taxpayer mistakes have a number of limitations – for example, they are subject to HMRC's discretion, they provide only limited appeal rights and they only apply where tax has been paid in an assessment as a

result of a mistake in a return. The proposals are said to address these limitations, and this is a welcome reform. It is not clear whether they will also address other issues such as the difficulty in applying the mistake relief provisions within a group of companies.

The new measure will also make it explicit that HMRC are not able to repay an amount except as provided by the measure or another provision of the Taxes Acts. This appears to be an attempt to limit the taxpayer's right to claims for restitution, for example. This provision will need to be examined carefully to see whether it would unfairly limit the taxpayer's right to obtain redress from HMRC.

Foreign exchange losses: targeted anti-avoidance rule

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Anti-avoidance legislation is to be introduced to counter the effect of strategies which use the tax rules on net investment hedging to procure a tax deductible currency loss, in circumstances in which an equal and opposite currency gain is realised by the group but is not taxed as a consequence of being 'matched'.

The new legislation counters two strategies. The first provision identifies such structures by application of a 'one way bet' test, which establishes whether, in the event of an overall tax deductible loss, a taxable profit would have been recognised, had exchange rates moved in the opposite direction and to an equal extent. The test is applied to a company and all connected parties for an 'arrangement'. If the loss exceeds the profits that would have been taxable, foreign exchange matching under the disregard regulations is denied for the whole of the matched position.

A second strategy targeted by these rules is the use of matched positions which produce a tax deductible expense as a consequence of accounting for a derivative foreign exchange contract by reference to the 'forward points'. The 'forward points' is the difference between the spot and forward rate at the date the derivative contract is entered into and is usually amortised through the profit and loss over the life of the derivative contract.

Such structures produce a tax deduction for one party to the contract equal to the forward points. If the equal and opposite profit on the derivative contract had been matched by the counterparty the result would be a one-sided tax deduction for the group. The new rules provide that matching is to be permitted only by calculations of movements of spot rates of exchange. Thus any component of a 'forward points' amortisation is excluded from the matching treatment. The legislation will impact upon arrangements that have been structured

to secure a tax deduction for 'forward points' debits with no exposure to corresponding credits in respect of the same instrument.

Who is affected

Companies which have used the matching facility to secure asymmetric tax treatment on foreign currency movements through matching.

Timing

The new rules apply to accounting periods beginning on or after 22 April 2009. Where an accounting period straddles 22 April 2009, the rules apply to exchange gains and losses arising between 22 April 2009 and the end of the period. Therefore, there is no grandfathering for existing arrangements.

Our view

This targeted anti avoidance legislation was announced and anticipated ahead of today's announcements.

Corporate intangible asset regime

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The corporate intangible asset regime was introduced in 2002 to allow a relief for corporation tax purposes for expenditure on intangible assets to broadly match the accounting treatment as the expenditure was released to the profit and loss account. The relief applied to intangible assets and goodwill.

The relief was restricted to intangible assets which were created or acquired from third parties after 31 March 2002. The regime included rules to exclude assets created by the claimant before 1 April 2002 or acquired from a related party who had created them before 1 April 2002 ('existing assets'). There were also rules to clarify when assets such as goodwill should be treated as created.

Since the inception of the regime there have been arguments about whether internally generated goodwill should be treated as created when it is first recognised in the accounts. This might occur, for example, when a trade was transferred intra-group. In these circumstances, the acquiring company would recognise the goodwill in its solus company accounts.

There have been various anti-avoidance measures enacted by HMRC to challenge arrangements designed to secure relief on assets that are regarded by HMRC as existing assets. Debate has continued in this area, including an argument that some goodwill only comes into existence on the merger of two businesses by a process of synergy.

HMRC are seeking to put beyond doubt the timing of the creation of internally generated intangible assets such as goodwill. If the business was carried on by the company or a related party prior to 1 April 2002, the internally generated intangible assets are treated as excluded from the intangible assets regime by the existing rules.

The budget note also makes it clear that this provision will apply to other internally generated assets as referred to in section 885 Corporation Tax

Act 2009 (such as brand names etc.) which, like goodwill, would not have qualified as eligible for capital allowances prior to 1 April 2002.

Who is affected

Companies claiming intangible asset reliefs for periods ending after 21 April 2009, in respect of internally generated intangible assets which are deemed to have been created prior to 1 April 2002.

Timing

The legislation will apply from 22 April 2009 and will be deemed to have always been in place, so it will affect future claims for relief even if the transaction crystallising the original claim occurred before this date. For the purposes of this measure only, an accounting period will be deemed to end on 21 April 2009 and another one to start on 22 April 2009.

Our view

The date on which intangible assets are treated as created has been a frontier which HMRC have been anxious to protect. HMRC has long argued that the existing rules are adequate to resolve the issue, but its decision to legislate specifically suggests that either the position was not free from doubt in their mind, or that the amounts at stake were too large to take any risk over judicial interpretation.

Double taxation relief avoidance: Banks using manufactured overseas dividends

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Anti-avoidance legislation will be introduced in Finance Bill 2009 to counter arrangements where taxpayers had sought to obtain an entitlement to a foreign tax credit on a deemed manufactured overseas dividend without having suffered the economic cost of the tax, either on the deemed manufactured overseas dividend or on the real dividend. Generally the targeted arrangements were only profitable after taking into account the benefit of the foreign tax credit. The measures are intended to deny deduction (which we presume includes denial of credit relief) for the foreign tax in the prescribed circumstances.

Who is affected

Largely banks operating in the UK.

Timing

The measures will have effect from 22 April 2009.

Our view

The budget note suggests that the proposed changes should apply only to taxpayers that had entered into particular tax-driven arrangements. It will be important to review draft legislation when it is available to ensure that the proposed changes do not have a wider application than intended; for example, to catch transactions involving the lending of shares in cross-border situations.

Double taxation relief avoidance: Credit abuse

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Anti-avoidance legislation is to be introduced to clarify the operation of Sections 798A and 798B ICTA 1988 in two circumstances.

The first is where a bank seeks to restrict the limitation on double taxation relief that applies to trading income (Section 798A ICTA 1988) by entering into an arrangement where the income is received by a non-trading subsidiary that is not within the scope of Section 798A ICTA 1988 and argues that the anti-avoidance rule in Section 798B(4) does not apply because the income would not be trading income of the bank. Legislation will be introduced to clarify that it will generally be assumed for these purposes, unless this is not reasonable, that all income received by a member of a banking group is trading income.

The second is where a group seeks to increase the amount of corporation tax attributable to profits of a particular activity by arguing that the activity is funded by free capital. The effect would be to increase the capacity for claiming credit for foreign taxes under Section 798A ICTA 1988. The measure introduced is intended to ensure that the group always attributes an average cost of funds when determining the profits of the relevant activities for the purposes of Section 798A ICTA 1988.

Who is affected

Largely banks operating in the UK.

Timing

The measures will have effect from 22 April 2009.

Our view

The measures are intended to clarify how a bank should apply Section 798A ICTA 1988. The changes may limit the amount of credit available for foreign taxes for taxpayers who sought to mitigate the impact of Section 798A ICTA 1988 in the circumstances described but should not have wide application.

Financial arrangements avoidance

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Structures for avoidance of tax have been developed and disclosed to HMRC and these are countered under the following provisions.

The first relates to intra-group convertible loans where there is a very strong likelihood that conversion will occur. The debt is structured such that, for accounting purposes, the debits brought into account by the issuer are much higher than the credits recognised by the investor because of the accounting effect of the assumptions on conversion required by the two parties. The effect of the legislation is to require the creditor company to recognise credits equal to the debits claimed by the issuer.

The second structure concerns intra group share issues in which the share terms mirror those of a derivative contract held by the company. Credits on the derivative are not recognised for accounts purposes because there is an obligation to pay out this profit on the shares. The dividends however are exempt from tax and thus a derivative profit is completely derecognised. Full recognition of the profits and losses on the derivative contract will be required even if not recognised in the accounts.

Who is affected

Companies which have undertaken such structures.

Timing

The new rules apply to debits and credits arising after 22 April 2009.

Our view

This is targeted anti avoidance legislation in respect of disclosed structures.

Anti-avoidance: Plant and machinery leasing

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Sale and leaseback arrangements

HM Revenue and Customs ('HMRC') have announced amendments to sections 216 and 221 CAA 2001 to block sale and operating/finance leaseback tax planning opportunities between connected parties involving the refinancing of plant or machinery.

Minor amendments and clarifications

In the Pre-Budget Report ('PBR') issued on 13 November 2008, HMRC re-wrote, for grants of long funding finance leases, the definition of 'disposal value' in item 5A of section 61 CAA 2001. Since that date, the disposal value has been:

- The higher of market value on commencement of the lease
- The qualifying lease payments (including any initial payment)

However, no amendment was made to section 25A TCGA 1992, which deals with the chargeable gains implications of the grant of a long funding lease. HMRC have now dealt with this by aligning the section 25A TCGA 1992 language with the item 5A language.

In the PBR, amendments were also made to section 785C ICTA 1988 to ensure that amounts taken into account for capital allowances purposes under item 5A were not taken into account again under section 785C ICTA 1988. HMRC have now re-written section 785C ICTA 1988 to ensure that where any initial payment under a lease is not taken into account for capital allowances purposes then that part is taxed under section 785C ICTA 1988. Although HMRC have not provided an example, it appears that there was a potential loophole here. HMRC have now closed the gap by ensuring that the exemption from section 785C ICTA 1988 does not apply to that part of the initial payment which has not has been brought into account for capital allowances purposes.

Who is affected

Sale and leaseback arrangements

The seller of plant or machinery under a connected party sale and operating leaseback or connected party sale and finance leaseback.

Minor amendments and clarifications

The grantor of a long funding lease.

Timing

The measures will have effect for sales of and grants of long funding leases over plant or machinery on or after 22 April 2009.

Our view

Sale and leasebacks

Absent any draft legislation, it is unclear what precise tax planning HMRC are seeking to counteract and thus it is not possible to determine whether the measure could affect typical commercial transactions. It is important that draft legislation is made available soon so the taxpayers can assess their position.

Minor amendments and clarifications

The amendments, by filling in any perceived gap in section 785C ICTA 1988 for grants of long funding leases and by aligning section 61 and section 25A on grant of a long funding lease, constitute a tidying up exercise.

Sale of lessor companies etc: Reforms

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Schedule 10, Finance Act 2006 was introduced to counter avoidance involving the sale of companies carrying on a plant or machinery leasing business. The legislation operates by bringing into charge an amount of income, broadly equivalent to any deferred tax liability in respect of leased assets, for the leasing company that is taxable whilst the sold company is in the seller's group and allowing a corresponding expense for the sold company when it is within the buyer's group. The provisions prevent the corresponding expense being carried back but give a 12 month extension for utilisation of the expense by way of group relief.

In the 2008 Pre-Budget Report, a number of detailed amendments were made that were aimed mainly at intermediate lessors. HMRC have now introduced a number of relieving measures to ensure that the provisions operate fairly, including the removal of the charge for internal consortium reorganisations. In addition, the period over which a loss derived from the Schedule 10 expense can be utilised has been extended from 12 months to 5 years and the amount of the loss allowed is to be increased in line with the interest rate applicable to interest on tax overpaid. A point of detail has been changed in respect of companies carrying on leasing businesses in partnership to adjust the amount of expense attributable to the partner following an intra-day change in partnership interests in the leasing business.

Who is affected

Companies carrying on a trade of leasing plant or machinery.

Timing

The change allowing extended access to losses derived from the Schedule 10 expense will have effect for accounting periods ending on or after 22 April 2009. The other amendments will have effect where the relevant day is on or after 22 April 2009.

Our view

Following a Consultation on Schedule 10 last summer, HMRC have decided against ring-fencing a leasing trade post acquisition and other options. They have decided to extend the period over which a loss derived from the Schedule 10 expense can be utilised from 12 months to 5 years and have introduced an indexing which is intended to reflect the real cost of a delay in claiming any loss created by these provisions. HMRC have asked for comment on the draft legislation.

The extension and the indexation are welcome. However, the current economic climate may mean that purchasers may continue to significantly discount the benefit of the expense for the purchaser group. This may be exacerbated by the fact that indexation does not reflect the marginal cost of borrowing for companies (which may be high in the current environment) but instead the low rate for interest on overpaid tax. Therefore, sellers of leasing companies may see little pricing benefits whilst suffering the Schedule 10 charge upfront.

Stamp duty land tax: temporary increase in thresholds

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The Government has announced that it will extend to the end of 2009 the current exemption from SDLT that applies to residential property sold for £175,000 or less.

In September 2008, the Government raised the threshold beneath which no SDLT is payable on residential property, from £125,000 to £175,000. This was achieved by means of a statutory instrument that took effect from 3 September 2008 and exempted residential property sold for £175,000 or less. The measure was to cease to have effect on 3 September 2009. The Government has announced that primary legislation in this year's Finance Act will extend the period of the exemption to 31 December 2009 after which the threshold will revert to £125,000 (or £150,000 in the case of residential property in disadvantaged areas).

Who is affected

Any person purchasing a residential property and paying £175,000 or less for it.

Timing

The measure will be effective for land transactions with an effective date between 22 April 2009 and 31 December 2009, extending the existing provision effective from 3 September 2008.

Our view

The stamp duty 'holiday' has had little effect on the property market to date but KPMG welcomes any measure that might improve the property market.

Stock lending and repurchase arrangements: Stamp duty, stamp duty reserve tax and tax on chargeable gains

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Stamp Duty and Stamp Duty Reserve Tax (SDRT): Stock lending and repurchase ('repo') arrangements are exempt from stamp duty and SDRT where, amongst other things, securities of the same kind and amount are returned under the arrangements. When a stock lending or repo arrangement terminates unexpectedly because of the insolvency of one of the parties to the arrangement a SDRT charge can arise. Default by the borrower, or purchaser under repo arrangements, would reinstate the charge to SDRT that would have arisen in the absence of the relief.

The Finance Bill 2009 will contain provisions which remove this charge. The measure will disapply the stamp duty and SDRT rules that impose a charge upon the insolvency of the borrower or purchaser.

In addition, where the lender/seller buys securities to replace those lost owing to the insolvency of the borrower/purchaser, the purchase will be relieved from stamp duty or SDRT. Where the borrower under a stock loan arrangement needs to replace lost collateral securities, any replacement purchase will not incur a stamp duty or SDRT charge.

Capital Gains Tax: There is a parallel measure for Capital Gains Tax purposes. Transfers and re-transfers of securities under a stock lending arrangement are disregarded for capital gains purposes. However, where the borrower under a stock lending arrangement becomes insolvent and then defaults (i.e. the securities are not returned to the lender), the lender is treated as making a disposal of those securities for

capital gains purposes (s263B(4) TCGA 1992). Finance Bill 2009 will contain provisions whereby the lender will not be deemed to dispose of its securities in these circumstances provided it uses collateral posed by the defaulting borrower to buy replacement securities of the same kind. The effect will be to allow the normal stock lending rules to continue to apply so that no capital gains or losses will arise to the lender.

It was announced in the 2008 Pre-Budget Report that similar capital gains treatment would be considered for securities transferred under a repo arrangement. It has been decided that no such changes will be made in respect of repos.

Who is affected

Market makers, securities dealers and anyone who enters into stock lending or sale and repo arrangements with a financial institution which becomes insolvent and is unable to return securities borrowed under the arrangement.

Timing

The reliefs will apply where the insolvency of the borrower or lender occurs on or after 1 September 2008.

Our view

This is a welcome change, backdated to September 2008, which implements a measure announced in the 2008 Pre-Budget Report.

Stamp duty land tax: alternative finance investment bonds

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Certain types of Sharia compliant bonds are backed by a sale and leaseback of UK property. The proposal is to ensure that there are no SDLT costs, in these circumstances, that are associated with:

- The sale and leaseback of the UK property
- The transfer of the property back from the bond issuer to the property owner at the end of the bond term
- The transfer of the bonds themselves

Who is affected

This measure will benefit those who are seeking to raise capital by means of certain types of UK land-backed Sharia compliant bond finance.

Timing

The measure will take effect for land transactions with an effective date on or after Royal Assent to Finance Bill 2009.

Our view

KPMG welcomes any measures that remove tax barriers from Islamic financing structures. It is hoped such measures will contribute to the UK's development as a major centre for Islamic Finance.

Stamp duty land tax: treatment of shared ownership

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

A new type of shared ownership scheme, 'Rent to HomeBuy', helps individuals to purchase homes using shared ownership schemes by allowing them initially to occupy the property under an Assured Shorthold Tenancy while they save for a deposit to purchase the property. The current treatment of these schemes can be complex. The Stamp Duty Land Tax (SDLT) rules for these schemes will be simplified.

The favourable SDLT treatment to purchasers under shared ownership schemes operated by a Registered Social Landlord will be extended to purchasers under shared ownership schemes operated by Registered Providers of Social Housing where the scheme is assisted by public subsidy.

Who is affected

Individuals purchasing residential property under the new 'Rent to HomeBuy' scheme or buying property from a Registered Provider of Social Housing.

Registered Providers of Social Housing purchasing property with the assistance of a public subsidy.

Timing

The provisions for rent to shared ownership schemes will have effect where the effective date of the grant of the shared ownership lease, or the declaration of the shared ownership trust, under the scheme is on or after 22 April 2009. The remaining provisions will have effect for land transactions where the effective date for SDLT purposes is on or after the date that Finance Bill 2009 receives Royal Assent.

Our view

The extension of the SDLT reliefs for shared ownership transactions and purchases by RSLs assisted by public subsidy to the new Registered Providers of Social Housing is a logical extension of the rules. It is a welcome measure that will ensure the relief is harmonised between both types of provider and their tenants.

Details of which entities will qualify as a Registered Providers of Social Housing are not yet clear because the provisions of the Housing and Regeneration Act 2008 have not yet come into force. The Act provides for the replacement of Registered Social Landlords by the new Registered Providers of Social Housing and the new regime will be open to profit making companies where the scheme is assisted by public subsidy.

Stamp duty land tax: leasehold enfranchisement

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Leaseholders of flats have statutory rights to acquire the freehold of their block collectively from the landlord, subject to specific rules about the process used to exercise the right.

There is a statutory relief within the Stamp Duty Land Tax ('SDLT') rules which means that such a purchase of a freehold by multiple leaseholders is not charged at a higher rate of SDLT than each leaseholder would pay if individually purchasing part of the freehold. But the conditions for the relief require the acquisition to be a purchase by a 'Right to Enfranchise' (RTE) company and the statutory provision for such companies has not yet come into effect. This means that the relief has not been available.

With effect from 22 April 2009 changes will be made to legislation enabling the SDLT relief for leasehold enfranchisement to operate as intended and it will now apply to leaseholders who exercise their current statutory rights.

Who is affected

Leaseholders who exercise their statutory rights of enfranchisement.

Timing

The provisions will apply to land transactions with effective dates on or after 22 April 2009.

Our view

This is a welcome change which puts into effect the original intention in the 2003 SDLT legislation.

Real Estate Investment Trusts ('REIT'): Artificial restructuring

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The REIT rules allow a corporate group with at least 75 percent of its income being rental income and 75 percent of its assets being rental property to elect for REIT status. This enables an exemption from corporation tax on rental income and gains on disposal of property.

Under current rules it is possible for corporate occupiers with a substantial property portfolio to restructure so that the operating business is not in the same capital gains group as the property holding company. This may allow the group to meet the conditions required for REIT status and obtain tax exemptions for the income received from the operating company.

The REIT rules exclude 'owner occupied' property from being qualifying rental income. A restructuring of this type would, under current rules, allow rental received from the operating business to qualify for exemption.

The Budget Note says that Treasury will take a regulation making power to allow them to prevent the use of 'artificial structures' to circumvent the REIT legislation and that the primary legislation will be amended to exclude owner occupied property from the regime.

At PBR, it was implied that this latter point would be achieved by ensuring that the legislation applied the test of whether property was owner occupied by looking at the economic grouping rather than the REIT grouping such that property would not escape categorisation as owner occupied by artificially removing it from the REIT group.

New rules have been announced today to extend REIT status to certain pub groups. Currently, tax legislation ensures that owners of 'tied' premises (such as tenanted pub estates) would be taxed as if their income was entirely derived from trading rather than rental activities. This prevented such groups from electing for REIT status as they would

not meet the requirement that 75 percent of income was treated as rental income for tax purposes.

This designation as trading income will not be taken into account for the purposes of the REIT legislation and therefore removes an artificial obstacle to REIT status.

This positive change for pub companies is newly announced whereas the general amendment to exclude owner occupied estates was announced at PBR.

Who is affected

Corporate groups that own a substantial property portfolio but are not mainly property investment businesses and who do not have significant third party rental income.

Certain pub groups with tenanted estates (as opposed to managed estates).

Timing

Accounting periods beginning on or after 22 April 2009.

Our view

The corporate occupier change had been expected following discussions with HM Treasury on the underlying policy of the REIT regime with respect to owner occupier businesses. The let out for tied premises is a response to lobbying by affected groups.

Real Estate Investment Trusts ('REIT'): Amendments

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

A number of minor changes have been announced to the REIT legislation. These have been requested by the property industry and are as follows:

- A REIT can currently issue only one class of ordinary share and non-voting fixed rate preference shares that are non convertible. The change allows the latter category to be convertible
- There is a minor change to provide the same definition of a tax exempt asset for both REITs which are single companies and REITs which are groups of companies
- A change has been made to clarify the circumstances where the funds from a disposal of property can be treated as a tax exempt asset for 24 months when that property had been only partially used for exempt rental purposes. This is clearing up a drafting anomaly
- Another drafting anomaly has been removed under which a REIT had to fail both the listing and close company conditions on joining the regime. This has been rectified such that either or both of them can be failed

Who is affected

Only groups of companies which have elected for tax status as a REIT will be affected.

Timing

The changes will take effect from 22 April 2009.

Our view

While these changes are welcome, they are relatively minor. The property industry had lobbied HMRC for more significant amendments to ease the burden that REITs are experiencing in the current economic climate in meeting their mandatory distribution requirement.

North Sea fiscal regime

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The changes are in eight main areas:

- Facilitating change of use.** The new rules will allow companies access to Ring Fence Corporate Tax ('RFCT') and Petroleum Revenue Tax ('PRT') relief for the decommissioning costs of those UK and UK Continental Shelf ('UKCS') assets that have been put to use in change of use projects. This mirrors the treatment where decommissioning takes place after relevant assets have ceased to be used for oil and gas production. The new rules will also remove the claw back of PRT relief where the assets have been wholly put to use for a qualifying change of use purpose and removes profit from change of use activities from the scope of PRT
- Chargeable gains.** On the swap of developed UK/UKCS licences, no chargeable gains will arise to the extent that the value of one licence matches the other, bringing the treatment of developed assets into line with undeveloped ones. Separately, where the proceeds from the disposal are reinvested in another chargeable ring fence asset, no chargeable gain will arise. In effect, the gain is rolled over. Previously, the gain could only have been held over for up to 10 years
- Field Allowance.** A new Field Allowance is to be introduced which will provide certain categories of new field with a fixed allowance which can, over time, be offset against the profits, subject to the supplementary charge to corporation tax, of the companies involved in the field. The Field Allowance will apply to small fields, ultra heavy oil fields ('UH') and ultra high temperature/high pressure fields ('HTHP') and will specify a maximum field allowance in total and per annum. The taxable profits offset by Field Allowance for small fields are £75million and £15million per annum respectively whilst those for UH and HTHP are £800m and £160m per annum respectively. Once the allowance is exhausted the field will, in effect, pay the full North Sea rate of tax
- Accelerated decommissioning relief.** New rules will be introduced which prevent a company entering into arrangements to incur

decommissioning expenditure in advance of the decommissioning process. To claim capital allowances the expenditure must have been incurred and paid out in respect of the decommissioning work carried out or undertaken in the accounting period

5. **Cushion gas storage.** Following calls for clarification on the tax treatment of cushion gas in gas storage facilities, the Government has confirmed that cushion gas is eligible for plant and machinery allowances
6. **PRT licence expiry.** The new rules allow companies decommissioning relief where they cease to be a participator in a field because a licence has expired and ensure that any income that may arise in respect of the assets in question will also be chargeable to PRT
7. **PRT simplification.** The current PRT law will be simplified and some other redundant rules repealed including changes where the statutory information requirement for commingled oil is to be replaced by a simpler 'just and reasonable' allocation methodology and provisional expenditure allowance. Transitional rules will apply
8. **Definition of a consortium within the ring fence.** The new rules will amend the definition of a consortium used for the current RFCT rules to bring it into line with the general corporation tax definition

Who is affected

Oil and gas companies that operate in the UK or on the UK Continental Shelf (UKCS).

Timing

The new rules will take effect from a range of dates:

1. **Facilitating change of use.** The new measures will have effect for RFCT in relation to expenditure incurred on or after 22 April 2009; and for PRT in relation to chargeable periods beginning after 30 June 2009
2. **Chargeable gains.** The changes to the chargeable gains rules will have effect in relation to disposals made on or after 22 April 2009
3. **Field Allowance.** The new Field Allowance will apply to fields given development consent on or after 22 April 2009
4. **Accelerated decommissioning relief.** The restrictions will have effect for expenditure incurred on and after 22 April 2009

5. Cushion gas storage. We understand that HMRC will issue a briefing shortly and will hold informal consultation on the suggested approach
6. PRT licence expiry. The changes to the PRT rules extending relief for decommissioning costs where the company is no longer a licensee will have effect for chargeable periods beginning after 30 June 2009
7. PRT simplification. The repeals and other changes to simplify the PRT regime will, where appropriate, have effect for chargeable periods beginning after 30 June 2009
8. Definition of a consortium within the ring fence. The change to the RFCT legislation to modify the definition of a consortium will have effect on or after 22 April 2009

Our view

The changes introduced are largely in line with the proposals announced in the consultation documents and Pre-Budget Report.

Although these changes are expected to be broadly welcomed by the Industry the package is expected to be more or less neutral for the Exchequer.

Certainty on trading and investment for authorised investment funds and investors in equivalent offshore funds

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

This measure provides certainty to AIFs and UK-resident investors in equivalent offshore funds that specific transactions will not be treated as 'trading' transactions for tax purposes.

Transactions undertaken by an AIF which are set out on the 'white list', when the AIF also meets a genuine diversity of ownership condition, will be treated as non-trading transactions and therefore not taxed in the AIF as any gain would be a capital gain and not trading income.

For an equivalent offshore fund which is also a 'reporting fund' under the new offshore fund rules, profits from transactions set out on the 'white list' will not be included in the 'reportable income' for UK-resident investors.

Rules will also be introduced so that financial traders cannot avoid tax by routing transactions through an AIF or equivalent offshore fund.

Who is affected

AIFs and UK-resident investors in equivalent offshore funds.

Timing

Legislation applying to AIFs will have effect on and after 1 September 2009. Legislation applying the equivalents will have effect on and after 1 December 2009.

Our view

This is a welcome move and is in response to extensive industry lobbying and consultation to improve the competitiveness of the UK tax regime for funds. AIFs will now have certainty in their tax treatment and equivalent offshore funds will not be put at a disadvantage as far as the tax rate borne by investors is concerned.

We expect ongoing discussion on which funds are regarded as equivalent e.g. whether or not this is a regulatory test.

In addition, it appears that offshore funds must still meet the conditions of the Investment Manager Exemption to avoid being subject to tax in the UK. Some may regard this as a clearer test than the genuine diversity of ownership test above; some may regard it as more onerous.

Tax elected funds

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Under current rules, UK Authorised Investment Funds (AIFs) are normally chargeable to corporation tax on income at a special rate of 20 percent. For tax exempt investors such as pension funds and Individual Savings Account (ISA) investors, any tax that sticks at the fund level is a real cost.

Under the new tax elected fund (TEF) regime, UK AIFs that meet certain conditions will be able to elect to be treated as a TEF. TEFs will be required to make two types of distribution of the income they receive - a dividend and a non dividend (interest) distribution. UK dividend income will remain non taxable in the fund and will be distributed as a dividend. For all other income that is distributed as a non-dividend (interest) distribution, the fund will receive a tax deduction up to the same amount. The new regime will be introduced by secondary legislation.

This measure will move the point of taxation from the AIF to the investor so that the investor is treated as though they had invested in the underlying assets directly.

UK investors are treated as receiving UK dividend income (including the non payable dividend tax credit) and a payment of yearly interest.

Who is affected

AIFs and their investors.

Timing

The new regime will have effect from 1 September 2009.

Our view

The introduction of UK non-taxable funds, in the form of TEFs, is welcome, as is the new TEF regime being elective.

The requirement for two streams of income (dividend and non-dividend (interest) distributions) is also welcome as this is in line with the current UK corporate streaming requirements for AIFs which should help encourage and alleviate concerns for TEF providers and third party

administrators around additional operational complexities and costs of additional streams that were previously proposed.

UK investors will now be treated as though they have invested in the underlying assets of a TEF directly. In this regard, it is welcome that UK dividends will continue to be non-taxable, non-dividend (interest) distribution will be tax deductible, and consultation around the taxation of foreign dividends should ensure non-UK dividends will follow the treatment of UK dividends, i.e. non-taxable.

However, there is still significant concern and uncertainty for investors around whether treaty relief will be available for TEFs under existing double tax agreements. There is also a concern from previous HM Treasury discussion papers that election into the new TEF regime will be irrevocable, and should treaty relief not be available, this may place TEF providers and investors at a disadvantage compared to non-TEFs.

It remains to be seen how many funds will elect into the new regime as it is only of real tax benefit to balanced funds. UK equity, bond, and going forward overseas equity funds, will not normally pay tax; and therefore from a tax perspective the new TEF regime may be of limited interest.

Chargeable gains and offshore funds

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Under current legislation, for the purpose of tax on chargeable gains, units in a unit trust are treated as if they were shares in a company. However rights in funds in foreign jurisdictions which are not companies, unit trusts or partnerships (mostly those constituted by contractual arrangements) are often treated differently depending on the structure. Where such a fund comes within the new 'characteristics-based' definition of an offshore fund, then a new section of the Taxation of Chargeable Gains Act 1992 (TCGA) will apply similar treatment to rights in such funds.

The effect of this change will be that an interest in a transparent offshore fund will be an asset for the purpose of calculating capital gains tax on chargeable gains, as is already the case for shares in a company or units in a unit trust. Investors will no longer be required to consider disposals of the underlying assets for calculating capital gains tax on chargeable gains.

There will be no effect on interests in tax transparent foreign partnerships which will continue to be treated as transparent for both income and gains in the same way as United Kingdom partnerships. These will be specifically excluded from the definition of offshore funds.

There will be transitional rules covering the timing and other aspects of the effect of this measure for existing investments in contract-based funds.

Investors subject to corporation tax will continue to treat their gains as transparent for the purposes of tax until discussions have taken place with industry about how to make similar changes to the tax treatment of chargeable gains for investors subject to corporation tax.

Who is affected

Investors in offshore funds such as Luxembourg Fonds Commun de Placement (FCPs) but not partnerships, that are transparent for the purposes of tax on income and gains.

Timing

The new treatment will apply to investments in contract-based offshore funds on and after 1 December 2009.

Elections into the new treatment can be made on and after 22 April 2009 and can be applied retrospectively back to the tax year 2003-04.

These will allow investors to elect to apply the new rules retrospectively, where such investors consider this will be an advantage. Elections can be made by capital gains taxpayers from the tax year 2003-04. Once made, an election will be irrevocable and will apply for all relevant tax years after the date of election. Investors making such an election will be treated as having been invested in an offshore fund that is certified by HMRC as a qualifying fund.

Our view

It will be welcome to a number of management groups that investors in offshore funds that are transparent for income and gains will no longer be required to consider disposals of such funds' underlying assets for calculating capital gains tax on chargeable gains. This will ensure that investors in unit trusts obtain parity in tax treatment as investors in other types of offshore funds which are not companies, unit trusts or partnerships.

It is a common problem that contractual funds such as Luxembourg FCPs are not attractive to UK retail investors because of their complexity.

The interaction with the offshore funds legislation will need to be monitored.

Some categories of investor, for example pension funds, rely on such funds being treated as transparent. This change of treatment by HMRC could adversely affect such investors.

Grandfathering provisions and transitional rules for existing investments in contract-based funds are welcome.

Offshore funds

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Legislation will be introduced in Finance Bill 2009 to change the definition of an offshore fund for UK tax purposes and amend the existing powers (in Finance Act (FA) 2008) to provide for the modernisation of the regime in regulations. Transitional rules will provide 'grandfathering' for investors in existing arrangements. Details of the transitional rules will be included in the primary legislation. Draft legislation was published following the 2008 Pre-Budget Report and changes have been made following comments received during the consultation. The detailed rules for the operation of the offshore funds tax regime will be in regulations, as announced in Budget 2008.

Under current legislation, the definition of an investment in an offshore fund is based on the regulatory definition of 'collective investment scheme' as set out in the Financial Services and Markets Act 2000, with modifications for tax purposes.

The new definition of an offshore fund uses a characteristics based approach which has been the subject of detailed consultation with the funds industry as set out in the relevant HM Treasury documents. There are also exceptions specified in the legislation to ensure that fixed share capital arrangements that do not mimic open-ended arrangements will remain outside the definition. This includes specific provisions for continuation votes and capital only arrangements.

Who is affected

Providers of offshore funds, and UK investors in certain offshore arrangements.

Timing

This measure will have effect on and after 1 December 2009.

Our view

Managers of closed-ended funds are concerned that the proposed changes will bring certain products, for example those with a fixed life, into the offshore funds regime for the first time. This would potentially

subject their investors to an income tax charge on disposal rather than a capital gains tax charge. We still await more detail on the proposed changes but the deferral to 1 December 2009 is welcome.

Transitional rules for the provision of 'grandfathering' regulations for investors in existing arrangements are also welcome.

More detail on the new definition and the modernised reporting regime is needed sooner rather than later.

New rules for investment trusts investing in interest-bearing assets

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

This measure will allow investment trusts to invest in interest bearing assets in a tax efficient manner. The new rules will be optional and will allow an investment trust to stream its distributions and benefit from a tax deduction in respect of the interest distributions it makes. The effect will be to remove any corporation tax liability on interest income which is distributed. The interest distributions will be received by shareholders as a payment of yearly interest.

This proposal has been the subject of consultation over the last few months. Draft regulations were issued in December 2008 on which KPMG and others commented. No further draft regulations have yet been released.

Who is affected

Investment trust companies and their shareholders.

Timing

The measure will take effect for any interest distributions made on or after 1 September 2009, if an election is made. This suggests that investment trusts may be able to elect into the new regime part way through an accounting period. The original draft regulations had suggested that the proposals would take effect in relation to a full accounting period and therefore it is not yet clear whether a distribution made on or after 1 September 2009 but out of profits accrued before that date will be included.

Our view

This proposal is a welcome measure. It will remove the significant disadvantage that UK investment trusts currently suffer when competing with authorised investment funds that are bond funds. It will benefit, in

particular, investors that are tax exempt such as pension funds and charities.

As is intended by the Government, the proposed new framework will provide a method for UK investment trusts to invest in bonds, and other assets producing an interest like return, without suffering tax on that income. For both existing investment trusts and new funds being launched it should allow greater flexibility with their investment strategies.

Currently investment trusts pay corporation tax on interest received, but tax-exempt shareholders have no way of recovering this tax. This is in contrast to open-ended bond funds, which currently can benefit from a tax deduction for interest distributions, and so no tax 'sticks' at fund level.

If investment trusts elect into the regime they will need to make administrative arrangements to stream their distributions. This could prove to be a significant operational burden but the benefits may outweigh the costs.

Our view is that in order for the regulations to be fully effective, there is also a need for an amendment to the tests (s842 of the Income and Corporation Taxes Act 1988) which a company is required to satisfy to be an investment trust. The definition of 'security' in this test is currently unclear. The proposal will encourage investment trusts to invest in a wider range of securities and they will therefore need certainty as to whether this could adversely impact their status as an investment trust.

Failure to amend s842 could mean that the perceived risks associated with the new framework will result in investment companies continuing to be established offshore, with the associated adverse effect on the UK's financial services infrastructure as administration and other services are also more likely to move abroad (see KPMG/IMA November 2007 paper 'The Value to the UK Economy of UK-Domiciled Authorised Investment Funds').

Manufactured interest

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

As announced on 27 January 2009 by the Financial Secretary to the Treasury, legislation will be introduced in Finance Bill 2009 to prevent a recent decision of the High Court from affecting the tax treatment of real payments of manufactured interest.

The issue has arisen following a High Court case (*DCC Holdings (UK) Ltd v HMRC* [2008] EWHC 2429) which cast doubt on the tax treatment of manufactured payments, both for payers and recipients. HMRC were concerned that the analysis leading to the taxpayer being entitled to a deduction for a deemed section 737A ICTA 1988 manufactured payment could lead to claims by companies for deductions of real payments of manufactured interest in excess of amounts appearing in accounts prepared in accordance with GAAP and in excess of any actual loss; conversely, recipients could be taxable on amounts in excess of their actual income.

Prior to the High Court decision HMRC considered that the tax treatment of real payments of manufactured interest had not been uncertain. This was on the basis that they had received no claims for deductions for real manufactured payments in excess of the amounts recognised in the accounts. On the other hand, the tax treatment of deemed manufactured payments had been in doubt. Accordingly, the new legislation will apply to real manufactured payments made both before and after the announcement, but to deemed manufactured payments after the announcement.

The provisions will ensure that the taxable amounts in respect of payments of manufactured payments are (subject to any express rule to the contrary) those that are recognised in accordance with GAAP.

Who is affected

Large companies that make payments of manufactured interest may be affected by these provisions. Companies that have entered into repo agreements after 1 October 2007 should not be affected by these provisions.

Timing

As announced on 27 January 2009, the legislation will apply to real manufactured payments made before that date, as well as to those made after, although for deemed manufactured interest payments, the legislation will apply only to payments made on or after 27 January 2009.

Our view

We consider that the provisions are helpful to taxpayers, to the extent they provide clarity and certainty on the tax treatment of manufactured interest.

Transfers of business between mutual societies

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Legislation is to be included in Finance Bill 2009 to make regulations in relation to the tax consequences of:

- Amalgamations of mutual societies
- Transfers of the whole or part of the business of a mutual society to another mutual society to a company or a subsidiary company of a mutual society

HMRC have been in discussion with industry and others, including KPMG, regarding business transfers and mergers between mutual societies. Different tax rules currently apply depending on the type of transfer or the type of mutual organisations that are merging. In addition, there are no tax rules specific to mergers between different types of mutual organisation since such a merger has not been possible until very recently.

Changes are to be made in regulations to provide clarity and certainty for the relevant business transfers and to ensure that the tax rules applying to mergers of mutuals are the same, regardless of the type of merger. In addition, measures will be included to counter potential future avoidance activity.

The regulations are expected to deal with capital gains, capital allowances and trading losses, loan relationships, intellectual property and stamp taxes.

Who is affected

Building societies, industrial and provident societies and friendly societies.

Timing

The changes will apply to transfers of businesses taking place on or after 22 April 2009.

Our view

Recent changes in the law mean that it is now possible for mergers between different types of mutual organisation such as industrial and provident societies and building societies (for example, the recently announced 'cross mutual' merger between the Co-op and the Britannia Building Society). At the moment the tax rules that apply to mergers between building societies are not always the same as those that apply to mergers between industrial and provident societies. It is presently unclear, therefore, what rules would apply to a 'cross mutual' merger.

We welcome the application of consistent tax rules for mergers of all types of mutual organisation. How the various differences in tax treatment for different mutuals will be resolved depends upon the detailed changes that will appear in regulations.

Agreement to forgo tax reliefs for companies which are part of government asset protection scheme

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Legislation will be introduced to ensure that provisions of the Corporation Tax Acts do not override any undertakings by a company to surrender its rights to tax losses and other reliefs in connection with the Governments Asset Protection Scheme and other similar arrangements.

The Corporation Tax Acts provide that certain loss reliefs and other allowances are given automatically. For example, losses incurred in a trade in one accounting period are, in the absence of any other claim, automatically carried forward and reduce the amount of profit that is taxable in that later period.

The new legislation will ensure that these provisions can be switched off where a person has undertaken to forgo these tax reliefs in connection with schemes that provide taxpayer support.

Who is affected

Groups of companies that enter into arrangements to surrender rights to tax losses and other reliefs in connection with arrangements such as the asset protection scheme.

Timing

The legislation will apply to such arrangements entered into from 22 April 2009.

Our view

The measure should have very limited application and is merely designed to ensure that agreements to surrender tax attributes made in connection with certain arrangements with the Treasury (such as the Asset Protection Scheme) are not overridden by automatic statutory reliefs. Without reviewing the draft legislation it is not clear whether the commencement rule will apply to current participants in the Asset Protection Scheme.

Substantial donors regulations

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The substantial donor provisions were introduced in Finance Act 2006 as part of a package of anti-avoidance measures aimed at charities. These provisions potentially apply to all charities entering into transactions with their substantial donors (or persons connected with those donors) and can trigger a tax liability for the charity.

The threshold of relievably gifts which an individual or a company may make before becoming a substantial donor will be increased from £100,000 in a six year period to £150,000 in a six year period. The threshold for a 12 month period will remain at £25,000.

Who is affected

Individuals and companies that make tax relievably gifts to charities between £100,000 and £150,000 in a six year period.

Those charities that receive such donations.

Timing

The increased threshold will take effect from 23 April 2009.

Our view

Whilst the increase to the threshold to be used for defining substantial donors is welcomed, it is unlikely to have a significant impact in terms of reducing the number of donors that fall to be treated as substantial donors.

It is disappointing that there were no other specific changes to the legislation announced in the Budget in relation to the substantial donor provisions, particularly following the proposals in the Substantial Donor Consultation Document published in July 2008, and the summary of responses to this consultation published in late 2008. However, the Budget did announce further informal consultation to develop new rules based around an effective anti-avoidance purpose test. The Government aims to bring forward proposals at the 2009 Pre-Budget Report with a view to legislating in 2010.

Publishing the names of deliberate tax defaulters

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

HMRC has announced its intention to introduce legislation in Finance Bill 2009 enabling them to publish names and details of individuals and companies who are penalised for deliberate defaults leading to a loss of tax of more than £25,000. Names of those who make a full unprompted disclosure or a full prompted disclosure within the required time will not be published.

Currently only the names and details of those who are convicted of criminal offences are published. The proposed change is designed to apply consistent treatment for tax fraud whether investigated through civil or criminal proceedings.

Details will be published quarterly on HMRC's website within 12 months of the penalty becoming final and will be removed from publication after a year.

In addition, new reporting requirements for those who have incurred a penalty for the deliberate understatement of tax of at least £5,000 will be introduced requiring them to provide more information on their tax affairs for up to 5 years to ensure that they have proper systems to be able to make correct returns and allow HMRC to monitor their compliance.

Who is affected

- Taxpayers (individuals, businesses and companies) who are penalised for deliberately understating tax due or overstating claims or losses of more than £25,000
- Taxpayers who are penalised for deliberately failing to notify HMRC when required to do so resulting in a loss of tax of more than £25,000
- Taxpayers are penalised for deliberately committing certain VAT and Excise wrongdoings leading to a loss of tax of more than £25,000

The additional reporting requirements apply to similar categories of taxpayer but will be triggered by the size of the penalty imposed rather than the amount of the default.

Those who make an unprompted or a full prompted disclosure within the required time are unaffected by the proposed provisions.

Timing

The new provision will be effective from a date to be specified in secondary legislation. No details of deliberate defaults committed prior to the legislation becoming effective will be published.

Our view

HMRC promises that the criteria for publication will be tightly defined and that sufficient details will be published to ensure that the correct person is identified as a result of the default. And it promises that details will not be published until all appeal avenues against the additional tax and penalties are exhausted or expired.

Clearly such safeguards are an important prerequisite to the introduction of the proposals. However, this still represents a significant breach of taxpayer confidentiality without a clear case being made to support the move as a means of deterring evasion based on evidence from other jurisdictions or appropriate research.

Similar 'naming and shaming' provisions have existed in Ireland for more than 20 years which have no doubt influenced the Government's thinking. Nevertheless, when the possibility of introducing a similar policy in the UK was mentioned three years ago in a consultation document issued as part of HMRC's Review of Powers, Deterrents and Safeguards, it attracted generally unfavourable comments and was not pursued. It is surprising that it has been brought forward again at this stage with no further consultation.

The proposal provides further incentive to potentially affected taxpayers to take advantage of the New Disclosure Opportunity announced today planned to run from autumn 2009 to March 2010.

Worldwide debt cap

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The Worldwide Debt Cap proposals are an integral part of the Foreign Profits package and HMRC have been consulting widely on what form these new rules should take. Having announced an update on their current thinking on 7 April 2009 which addressed a significant number of the concerns taxpayers had raised with HMRC, no further details have been released today. However, there is now clarity on the commencement date.

Who is affected

All UK companies

Timing

Today's announcements have confirmed that the debt cap rules will apply to finance expenses payable in accounting periods beginning on or after 1 January 2010. Therefore whilst they remain part of the Foreign Profits package they will not come into force at the same date as the dividend exemption is introduced.

Our view

HMRC have confirmed that the policy behind the revised debt cap proposals issued with HMRC's Update Note on 7 April 2009 has not changed. The intention is that the Worldwide Debt Cap is an additional measure to restrict relief for interest costs in UK companies above and beyond existing rules. It will not become a UK thin capitalisation safe harbour nor a replacement for Advanced Thin Capitalisation Agreements ('ATCAs').

The Update Note contained a number of revised proposals and substantial changes to the calculation of the debt cap disallowance when compared to the proposals issued previously.

Key features of the proposals as they currently stand

- There are changes to the definitions of 'Available Amount', 'Tested Amount' and 'Ultimate Corporate Parent' which address a number of concerns raised with the original proposals

- The definition of 'Ultimate Corporate Parent' (which must be identified to establish the worldwide group) is to be amended to include additional entities and exclude others. For example, tax transparent bodies listed on a recognised stock exchange and dual listed structures are included. Collective Investment Schemes are excluded from the revised definition so that, for the Private Equity sector in particular, the debt cap should apply only at the level of each portfolio investment
- The disallowance of interest expense and the treatment of corresponding interest income as exempt will now be applied on a 'net' basis and by company, rather than on a 'gross' basis and by transaction. This should help reduce the compliance burden and remove certain anomalies
- Foreign exchange gains and losses, some hedging adjustments and some debt factoring charges are to be excluded from the definition of finance expense but all finance lease interest will be included. Amounts arising on 'short term' debt will also be excluded
- A single Gateway Test is introduced to apply to both inbound and outbound investors and, if the test is passed, will mean companies will not need to apply the detailed rules. It is most likely to be passed by inbound groups. Outbound groups are only likely to pass the test where they have significant external debt outside the UK and will therefore normally need to apply the detailed rules. It will not exempt purely UK groups although HMRC have indicated that Inspectors may have discretion to agree practical arrangements with groups on how this test will apply
- A Financial Services exemption is to be introduced which will mean Financial Services groups would not need to apply the detailed rules provided their income is derived substantially from qualifying activities
- There is a potential exemption for group treasury companies not in the Financial Services sector
- There is the introduction of a 'white list' of acceptable GAAP on which to base the debt cap calculations
- There are revisions to the mechanism of disallowing interest and making a corresponding adjustment in circumstances where there are non-trading deficits and surplus management expenses
- A target anti-avoidance rule (TAAR), is to be introduced to counter arrangements which have the purpose of decreasing the Tested Amount, increasing the Available Amount or increasing or decreasing debt taken into account in the Gateway Test
- There is the introduction of an EEA overlay to the rules aimed at creating parity between UK and EEA companies in scenarios in

which they suffer an interest disallowance and corresponding reduction in finance income

- In order to ease the compliance burden, the ability to self-certify that the debt cap does not apply is proposed

The interaction with transfer pricing, controlled foreign company rules, and the late paid interest rules is still to be confirmed but the Update Note states that this will be addressed.

These revisions reflect many of the representations made to HMRC in the course of the consultation exercise to date. However, in many cases the full impact of these changes can only be properly assessed once draft legislation is published. It is likely that due to the complexity and breadth of the provisions there will remain scenarios that will cause problems for some groups. Groups should therefore continue to contribute to HMRC discussions and provide feedback on the draft legislation when it is available.

Computations of profits in a non Sterling currency

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Amendments are to be made to the rules for the carry forward or back of losses where computations are prepared in a non Sterling currency.

Draft legislation has previously been published and the following comments are based on this.

The rules on the translation of profits and losses calculated for the purposes of corporation tax in a non Sterling currency are to be amended. In particular, the rules dealing with the carry forward and carry back of tax losses are being revised so that, effectively, the losses are offset against past or future profits in the non Sterling currency rather than in Sterling as is currently the case.

The changes relate to rules in FA 1993 which determine the currency in which computations are required to be prepared. Under these provisions, the starting point is that Sterling should be used. However, where taxable profits and losses are determined using generally accepted accounting practice (e.g. trading activities/loan relationships) and certain conditions are satisfied, the computations are required to be prepared in a non Sterling currency and then translated to Sterling for inclusion in the corporation tax return.

Where a company computes its taxable profits or losses in a non Sterling currency, the current rules require the company to carry forward or back any unused losses in Sterling, with the translation to Sterling being made using an exchange rate for the period in which the loss is incurred. It has now been recognised, as a result of recent fluctuations in exchange rates, that the current rules lead to exchange exposure for both taxpayers and the exchequer where the exchange rate moves significantly between the periods in which the profits and losses are recognised.

Following an announcement on 18 December 2008 that the rules would be revised, draft legislation has been published with the effect that losses will now be translated to Sterling at the same exchange rate as the profits against which they are offset. For example, suppose a company makes a Euro trading profit in 2010 and translates this to Sterling using an exchange rate for that period and has a trading loss brought forward from 2009. Following the changes, the loss will be translated to Sterling (prior to offset against the profit) at the same exchange rate for 2010 (rather than using rate for 2009 as would previously have been the case).

There are further rules to deal with the situation where the currency in which the computation for the period when the profits arose is prepared differs from the currency used when the losses arose e.g. a company has a Euro computational currency when the loss arises but this has changed to Sterling when the company becomes profitable.

One of the effects of the changes is that it may be preferable to delay the utilisation of a loss by carrying it forward rather than back if the exchange rates are such that overall taxable profits are lower.

Exchange rates to be used

Under current legislation in section 92D FA 1993, non Sterling taxable profits and losses are translated to Sterling using either the average rate of exchange for the period or an appropriate spot rate of exchange for the transaction in question. For accounting periods beginning on or after 29 December 2007, spot rates may be used, on a just and reasonable basis, where there is more than one transaction in the period although an average rate for the period may also be used. However, where the amount to be retranslated relates to a single transaction, the spot rate of exchange for the transaction must be used.

Election

An election can be made in respect of the commencement/transitional rule, with a time limit of 30 days from the start of the first accounting period beginning on or after Royal Assent. This has the following effect

- The new (permanent) rule on the translation of losses only applies to accounting periods beginning on or after Royal Assent (rather than from 29 December 2007)
- The transitional rules for the carry forward of losses from pre-commencement to post commencement periods are disapplied. Accordingly, the old rule will apply so that the loss arising in the pre-commencement period is translated to Sterling at an exchange rate for the period in which the loss arises

The election, which is irrevocable, must be made within 30 days of the start of the first accounting period beginning on or after Royal Assent

e.g. if Royal Assent is in July and the company has a 31 July year end, the election must be made by 30 August 2009.

The policy intent behind the election is to ensure that companies are not disadvantaged by the changes to the rules.

Who is affected

Timing

The changes apply to accounting periods beginning on or after 29 December 2007.

Transitional rule – carry back of losses to pre-commencement periods.

The rules on the carry back of losses are amended where a loss arising in a post commencement period is carried back to a pre-commencement period e.g. for a company with a 31 December year end, a trading loss is carried back from 2008 to 2007.

In these circumstances, the loss is translated to Sterling using 2008 exchange rates and the profit will be translated to Sterling using the 2007 rates i.e. as though the changes had not been made.

Transitional rule – carry forward of losses from pre-commencement to post commencement periods.

In these circumstances, there is a three step process as follows

- The loss is translated to Sterling using exchange rates for the period in which the loss arises.
- The Sterling loss is then translated to the original currency using the spot rate of exchange on the first day of the accounting period beginning on or after 29 December 2007
- This non Sterling loss is translated to Sterling at the same exchange rate used to translate the profits (possibly the average rate for the period)

Our view

It is understood that the changes made are as a result of the significant losses incurred by financial sector companies. However, they are potentially relevant for all companies that prepare their corporation tax computations in a non Sterling currency.

The time limit for the election is short (30 days from the start of the first period beginning after Royal Assent) but this is understandable because HMRC want to minimise the scope for companies using hindsight of exchange rates when determining whether or not to elect.

Stamp duty land tax: consultation document on disclosure of tax avoidance schemes

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The rules for disclosure of Stamp Duty Land Tax ('SDLT') avoidance schemes do not currently apply to schemes involving only residential property and do not require users of schemes, as opposed to promoters of schemes, to notify HMRC as they have to do for other taxes.

HMRC have issued a consultation document which proposes to change the rules to include schemes involving high value residential property (with a value of at least £1 million) and to introduce arrangements so that HMRC will be able to identify users of SDLT schemes. Draft regulations have been published.

This follows informal consultation on these issues carried out following an announcement in the Budget last year.

Who is affected

Promoters and users of SDLT schemes.

Timing

Comments are invited by 16 July 2009 and implementation is expected towards the end of 2009.

Our view

This is an expected proposal and the willingness to consult further on the basis of draft regulations is welcomed.

Furnished holiday lettings in the European economic area

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Landlords who earn income from furnished holiday accommodation in the UK are currently treated as if they are trading for tax purposes. This means that they are entitled to:

- Claim loss relief as if this part of the UK property rental business constituted a trade
- Treat the relevant assets as trading assets (relevant for certain purposes including roll-over relief, gift hold-over relief, taper relief and relief for loans to traders)
- Claim plant and machinery allowances on applicable capital expenditure, even though the properties are used for accommodation (which would normally be excluded)
- Include such profits as relevant earnings for calculating the maximum relief due for an individual's pension contributions

These rules currently only apply to landlords with income from furnished holiday accommodation in the UK, and not elsewhere in the European Economic Area (EEA). This address a concern of HMRC that this approach is not compliant with European law.

As such, it has been announced that the furnished holiday letting rules will be completely repealed from 2010-2011. Until such time, landlords with furnished holiday accommodation within the EEA (but outside the UK), will be taxed on the same basis as those with furnished holiday accommodation within the UK.

Who is affected

Immediately: Individuals, partnerships and companies who let furnished holiday accommodation within the EEA, but outside the UK, who are liable to UK tax on the income and capital gains from the property.

From 2010-2011: Owners of furnished holiday accommodation within the EEA including the UK.

It does not affect owners of furnished holiday accommodation outside the EEA.

Timing

The extension to accommodation within the EEA takes effect from 22 April 2009 until the start of the tax year 2010-11.

The furnished holiday letting rules will be repealed with effect from 6 April 2010 (for Income Tax) and 1 April 2010 (for Corporate Tax).

Our view

Whilst in the short term the change in treatment may be beneficial to owners of furnished holiday accommodation within the EEA, the decision to withdraw this favourable tax treatment altogether rather than extending it to all investors who invest in furnished holiday accommodation in the EEA is disappointing.

This change is only likely to affect a relatively small number of UK based investors but it may have potentially wide-ranging implications for them.

Structured foreign exchange arrangements

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

A technical note will be issued in the summer covering the treatment of certain structured foreign exchange arrangements.

The note will 'set out the issues and potential approached to certain structured financial arrangements (often described as over hedging or under hedging) that, although not undertaken for tax avoidance, seek to pass onto the Exchequer, through tax relief, commercial risk that would otherwise be borne by groups on such transactions'.

This refers to arrangements whereby a group's net external foreign currency exposure is hedged via cash tax receipts and payments.

It is also said that the Government believes that the economic risks should be shared between the Exchequer and business 'as Parliament intended'.

Who is affected

It is expected that this will affect companies that take account of cash tax receipts and payments in determining their foreign exchange hedging strategies.

Timing

The technical note will be issued in the summer.

Our view

We await publication of the technical note but it is helpful that consultations are being undertaken rather than HMRC rushing to legislate.

Temporary first year allowances: plant and machinery

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

In order to aid business investment the Government has introduced a temporary 40 percent First Year Allowance (FYA) for expenditure on plant or machinery that would normally be allocated to the main capital allowances pool. This FYA will not apply to assets that should be allocated to the special rate pool.

Who is affected

Any company, partnership or individual carrying on a qualifying activity.

Timing

The FYA will apply to capital expenditure incurred on qualifying expenditure from 1 April 2009 (corporation tax) and 6 April 2009 (income tax) for a period of 12 months.

Our view

This temporary measure provides a boost for businesses looking to invest and for a temporary period accelerates the tax relief for capital expenditure. The proposed change in law could be more generous by allowing the increased writing down allowance to apply to carried forward pool balances in addition to new expenditure in the period.

This measure will be of limited use to the struggling hotel, retail and real estate sectors as most of their capital expenditure will qualify for special rate pool writing down allowances of 10 percent per annum.

In addition this measure has less benefit for loss making businesses as many will be unable to take immediate advantage of the tax relief. An innovative approach by the Government could have been to allow any current year losses generated by the 40 percent FYA to be surrendered for a tax credit.

Timing of relief for financing costs

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Amendments are to be made to the timing of relief for financing costs so that, in most cases, where the lender is an overseas company, the cost of borrowing will be deductible on an accounts basis.

For company borrowers, there are rules which provide that interest relief for certain connected party loans is given on a paid basis and discount is deductible on redemption, rather than when the financing expense is recognised in the accounts. Currently, this 'paid basis' does not apply where the lender is a UK company and there have been challenges on the basis that the rules are not compliant with EU law.

In July 2008, Revenue & Customs Brief 33/08 was issued which provided for a temporary concessionary relief whilst consultations were undertaken which have led to the changes outlined above. The form of the concession was that the 'paid basis' did not apply where the lender and borrower companies were connected because of the 'control test', irrespective of where the lending company is resident (so tax havens, for example, were not excluded from the concessionary treatment). This has meant that interest arising on loans from overseas group companies could be deductible on an accounts basis irrespective of when payment is made. In subsequent discussions, HMRC have extended the concession to companies falling within the other tests of connection for interest and discounted loans.

The following comments are based on draft legislation which has been issued previously.

Legislation is to be amended so that it will only apply to a company lender which is either:

- Resident (by reference to domicile, residence or place of management) in a non qualifying territory
- Effectively managed in a non qualifying territory which does not tax companies by reference to domicile, residence or place of management

A territory is non qualifying if the UK does not have a double tax treaty with it which contains a non discrimination article. Qualifying territories are listed in the HM Revenue & Customs ('HMRC') manuals at INTM 432112. The list covers approximately 100 countries but does not include certain tax havens.

The reference to companies being effectively managed in non qualifying territories is directed at companies located in jurisdictions which tax on a source basis e.g. Hong Kong.

Following the proposed changes, financing costs will be deductible on an accounts basis unless an overseas company lender is present in a non qualifying or 'bad' territory.

There may be interest or discount which has been disallowed in periods beginning before 1 April 2009. The draft legislation does not include a transitional rule dealing with such interest. Draft guidance has been issued which says that 'where it is necessary for a company to keep track of brought forward interest, some of which has been deducted in computations for earlier periods and some of which has not, any reasonable method of apportionment will be accepted.' If a company has such interest, it would be advisable to put contemporaneous documentation in place at the time of payment as evidence as to what interest is being paid.

Who is affected

All companies who borrow from non UK resident companies are potentially affected. This will include borrowings from partnerships where the partners include non resident companies, which is potentially relevant to borrowing from private equity partnerships.

Timing

The changes apply to accounting periods beginning on or after 1 April 2009.

A company can elect that the current basis continues to apply for the first accounting period beginning on or after 1 April 2009. However, no election may be made for an accounting period ending after 31 March 2011. The election must be made in the corporation tax return for the accounting period to which it is to have effect.

It is understood that the Revenue & Customs Brief concession will not apply to periods beginning on or after 1 April 2009 even if the election to defer the application of the rules is made.

Our view

The changes made are good news for business because, in most cases, the financing cost of borrowing from overseas company lenders will be relieved on an accounts basis.

The scope of the legislation is slightly narrower than that provided in the temporary concessionary relief described above because, for example, the cost of borrowing from overseas group companies located in certain tax havens which are not qualifying territories will revert to being deductible on a paid basis.

There is some uncertainty regarding the application of the proposed changes where the borrower is a close company and the loan is from a partnership. A company is close if it is under the control of five or fewer persons and typically this includes many private equity backed groups.

For such groups, the application of the new rules is not clear where there are a large number of partners and it is difficult to identify the residence of all of them. In addition, a private equity partnership will, typically, have flexible allocations of profit shares between categories of partners so the allocation of the financing charge between the partners in a particular period is likely to be difficult.

HMRC are consulting on how best to deal with this and the outcome is expected to be dealt with in guidance.

Timing of relief for royalties

There is a similar provision (in section 851 CTA 2009 formerly section 94 Schedule 29 FA 2002) which provides that royalties due to certain connected parties will be deductible on a paid basis if they are paid more than twelve months after the period in which they are recognised in the accounts. However, and somewhat surprisingly, this rule has not been amended in a similar way to those for financing costs. It is difficult to see how the provision is EU compliant where royalties are due to an EU resident company.

Waiver of connected party trade debts

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The rules applying to the release of trade debts between connected companies are to be amended so that the company with the liability is not taxable on the release.

A change was previously made (for periods of account beginning on or after 1 January 2005) that had the effect of denying bad debt relief in respect of trade debts owed between connected companies. However, at this time, no corresponding change was made to the rules applying to the company which had purchased the goods/services and was subsequently released from the liability. Accordingly, if a debt which arose from trading between connected companies was released, bad debt relief was not available to the supplier, but the group customer was taxed on the amount of the release.

Who is affected

The changes apply to the release of trade debts owed between connected companies. Companies are connected where one controls the other or they are under common control.

This can apply to both intra-group trade debts and also to trade debts between non group companies where, for example, an individual controls both companies.

The change also applies to the release of debts incurred in a UK or overseas property business.

Timing

The change applies to releases of debts which take place on or after 22 April 2009.

Our view

This is a welcome change because it removes an asymmetrical treatment for the release of intra-group trade debts and will assist

business as they reconstruct the balance sheets of loss making subsidiaries.

When the change was announced at the time of the Pre-Budget Report, it was proposed that the change would apply to periods beginning on or after 1 April 2009 so, for example, December year end companies would have had to wait until 2010 to benefit. It is to be welcomed that the rules will now apply to releases made on or after 22 April 2009.

HMRC charter

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Legislation will be introduced in the 2009 Finance Bill which will require HMRC to have a Charter. The Charter will set standards of behaviour and values to which HMRC will aspire in their dealings with taxpayers and others. The legislation will require HMRC to report annually on their performance against the standards.

Who is affected

All taxpayers and anyone who has dealings with HMRC.

Timing

The Charter must be in place by 31 December 2009 and is currently in the second round of consultation. HMRC plans to launch the Charter by Autumn 2009.

Our view

While it is welcome that the Charter will be given legislative backing there is still much to discuss on what should be included to help HMRC rebuild trust with taxpayers. It may appear to be a relatively minor point but the choice of name is significant. The current title suggests that the Charter is intended to be of benefit to the staff of HMRC not the taxpayer. Some might regard this as a bad sign.

Employee Issues



Jill Storey
Head of People Services
Tax

Budget 2009 contained two key measures targeted at higher earning employees. These are:

- The introduction of a new higher rate of tax of 50% on incomes over £150,000 from 6th April 2010
- Restriction of the amount of tax relief available on pension contributions for employees with income over £150,000

Employees earning over £150,000 will now, therefore, face a combined highest rate of tax and National Insurance of 51%, with much restricted capacity to shelter income through tax relief on pension contributions.

The 50% income tax rate is now one of the highest headline rates in Europe and stands in stark contrast to the 18% capital gains tax rate. Indeed, this difference in rates means that HMRC approved share scheme arrangements (e.g. Company Share Option Plans, SAYE schemes etc) are likely to become much more attractive.

Other measures include:

- The removal of the £80,000 price cap that currently applies when calculating the benefit-in-kind for company cars;
- Various amendments to the significant Finance Act 2008 changes to the "remittance basis" of taxation, which are designed to make the now (very complex) rules simpler to operate;
- Anti-avoidance legislation directed at living accommodation which is provided to employees under short lease premium arrangements;
- The introduction of a new penalty and interest regime for the late payment of in-year taxes and deductions due under PAYE.

Although, higher earning employees will feel the pinch as a result of the various changes announced in the Budget, this will also translate into higher costs for employers where international assignees are posted to the UK under tax-equalisation arrangements. In turn, the danger is that this may lead international businesses to reflect on whether the UK is the right place to be investing capital and resources.

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Pensions: Limiting tax relief for high income individuals (anti-forestalling)

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Members of registered pension schemes currently benefit from tax relief on their pension contributions at their highest marginal rate. So, for example, a £100 contribution into a pension scheme will cost a 40 percent taxpayer £60. Maximum personal relief is limited to contributions up to 100 percent of earnings and is also controlled by an annual allowance (currently £245,000, increasing to £255,000 in 2010-11).

The Government has announced its intention to restrict income tax relief on pensions contributions for people with taxable incomes of £150,000 or more. Relief at higher rates will be tapered away from that level so that for those earning over £180,000, relief will be restricted to the basic rate. No further details are available at the moment – the Government is to consult on its implementation.

As this change will have effect from 6 April 2011 there will also be legislation introduced with effect from 22 April 2009 to prevent people attempting to manipulate their affairs to avoid the consequences of the new rules. These “anti-forestalling” rules will introduce a new special annual allowance and associated tax charge, the effect of which will be to restrict tax relief to basic rate for any pension savings (which are not “normal ongoing regular pension savings”) above £20,000 per tax year. The restriction will apply regardless of who makes the contributions (employee or employer), and regardless of whether the pensions arrangement is defined benefit or money-purchase. The special tax charge will be collected through self-assessment.

Who is affected

From 22 April 2009

The special annual allowance charge will apply to individuals who in a tax year:

- Have relevant income of £150,000 or more in that tax year or in either of the previous two years; and
- Who increase their level of annual pension savings on or after 22 April 2009 over and above their normal regular pension savings pattern or receive extra benefits in a defined benefit scheme; and
- Have total pension savings for the year above £20,000

If a one off payment was made between 6 and 21 April 2009 this will not in itself be subject to tax but will reduce the £20,000 annual allowance and therefore limit their ability to obtain full tax relief on further contributions.

From 6 April 2011:

Anyone with income above £150,000 per annum.

Timing

The measure applies from 6 April 2011. The anti-forestalling provisions take effect from today (22 April 2009).

Our view

“Normal ongoing regular pension savings” includes only those contributions that are made at least quarterly, and were agreed prior to 22 April 2009. Those individuals who have regularly made an annual contribution, or who wish to make an annual or new bonus sacrifice into their pension arrangement, will be caught by this restriction straight away.

When pension benefit is taken it will be taxed at the individual's marginal rate. If, therefore, the individual is a higher rate taxpayer they may well have been given relief at basic rate on contributions but suffer higher rate on the pension, this would not seem to be a great deal for them! It may therefore be that many high-earners decide that pensions saving in registered schemes will not be worthwhile.

It is disappointing that this comes so soon after the extensive changes to pensions tax brought in by Finance Act 2004, and is so radically different to what was then put forward as the long term solution for pensions. Changes such as this undermine confidence in the pensions system.

We have set out below an illustration.

Assumptions				
Single man usually makes a contribution of £2,000 per month				
Decides to make an additional annual contribution of £10,000				
His rate of income tax relief on the additional contribution is as follows:				
Income level	Tax year			
	2008/09	2009/10	2010/11	2011/12
75,000	40%	40%	40%	40%
100,000	40%	40%	40%	40%
125,000	40%	40%	40%	40%
150,000	40%	40%	40%	40%
175,000	40%	20%	20%	23.33
180,000	40%	20%	20%	20%
<i>Note: assumes straight line reduction in higher rate relief from £150,000 to £180,000</i>				

Relevant income includes most forms of income but is after certain deductions including pension contributions which will be restricted to a maximum of £20,000.

Changes to company car tax from 2011-12

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

HMRC have announced various changes with effect from April 2011 in respect of company cars:

- The lower threshold CO₂ emissions figure (130g/km for 2010-11) will be reduced by 5g/km to 125g/km
- The £80,000 price cap that currently applies when calculating the cash equivalent of the car benefit will be abolished – in effect the list price for tax purposes will now be unlimited, making very expensive company cars less tax and NIC efficient
- The 'appropriate percentage' applicable to electrically-propelled cars first registered from 1998 onwards will be reduced from 15 percent to 9 percent. This is a simplification measure: the rate is currently already 9 percent but this is achieved through a reduction of 6 percent given to such cars from the normal starting rate of 15 percent
- The provisions relating to electrically-powered cars first registered before 1998 will be removed as there are no cars to which they can apply
- The reductions currently given for electric/petrol hybrid cars and cars propelled by bi-fuels, road fuel gas and bio-ethanol will be abolished. The discount given for Euro IV standard diesel cars registered before 1 January 2006 will also be abolished.

Who is affected

Employees who pay income tax on a car that has been provided for their private use by their employer.

Employers who pay Class 1A NIC on the taxable benefit of a company provided car.

Timing

The new rules will have effect from 6 April 2011.

Our view

Abolition of the £80,000 cap means that in effect there is now no upper limit on company car taxes –this will only affect a minority of employees

The clarification of the rules for different fuel types is welcomed. In effect this changes the focus on how HMRC calculate the benefit percentage from the CO₂ emissions figure and fuel type to solely the CO₂ emissions figure.

The remittance basis: Minor amendments

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Last year's Finance Act introduced major changes to the remittance basis tax regime with effect from 6 April 2008. Major changes included:

- Individuals who claimed the remittance basis suffering a cost, namely the loss of their personal allowance and annual capital gains exemption, and additionally.
- Individuals who were resident for at least 7 out of the prior 9 tax years having to pay a Remittance Basis Charge of £30,000.

Implementation of these changes required extremely complicated legislation. As set out in Budget Note BN 55, further changes are being introduced with the intention of making the rules simpler to operate whilst ensuring the legislation effectively delivers its policy objectives.

See also the commentary in Personal Tax for the effect of the amendments on individuals other than employees.

Who is affected

Individuals who are resident in the UK and either not ordinarily resident and/or not UK domiciled.

Timing

Certain changes are backdated to the introduction of the new regime – 6 April 2008. Others will have effect on or after Budget day 22 April 2008.

Our view

This extremely complex legislation was introduced in a rush and the detail, necessary to implement the new policy, has undergone significant change since the draft legislation was first published. Given the complexity and the haste with which it was introduced, it is not surprising that minor amendments are still being made to make the legislation workable. These changes are welcome, though we consider that further amendments are required.

The situations where claiming the remittance basis is not required have been extended to cases where the individual has total UK income or gains of no more than £100 in the relevant tax year, which have been taxed in the UK. This is provided that no remittances are made to the UK in the tax year. This is a step in the right direction, though we feel that the £100 limit is set at too low a threshold.

Certain exemptions which prevent a remittance being treated as taxable have applied hitherto only to "relevant foreign income". We welcome the proposal to allow these exemptions to apply to property purchased out of foreign employment income and foreign chargeable gains, rather than just to relevant foreign income.

The Finance Act 2008 legislation was drafted in such away that many individuals arriving in or departing from the UK in a tax year would be required to file tax returns, even when there would be little or no UK tax to pay because tax had already been paid in the home country. This requirement has now been removed, with effect from 6 April 2008, where an individual has overseas employment income of less than £10,000 and overseas bank interest of less than £100 in any tax year, provided all this income is subject to foreign tax. This is a sensible relaxation of the rules which will remove an unnecessary compliance burden on taxpayers and HMRC.

Also, HMRC have decided to incorporate Statement of Practice (SP) 1/09 into legislation next year. SP1/09 was issued on 18 March 2009, and was effective from 6 April 2009, and relates to the employment-related income of those who are resident but not ordinarily resident in the UK. It deals, in particular, with how HMRC will treat transactions relating to an offshore bank account which contains only income relating to a single employment, and how earnings should be apportioned between UK and non-UK duties when the employee is taxed on the remittance basis. A difficulty with the SP is that it did not, in our view, allow employees time to arrange their affairs to meet the requisite conditions before the start of the 2009/10 tax year. Various points relating to SP1/09 are being discussed with HMRC, and it is welcome that HMRC have indicated that there will be due consultation with all stakeholders before the SP is legislated.

Living accommodation provided by reason of employment: payment of lease premiums

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Legislation will be introduced to amend the benefit-in-kind rules on living accommodation as they apply to the provision of accommodation through payments by an employer of a premium under a short term lease.

HMRC say this is to 'stop attempts to avoid tax on the benefit of the living accommodation' and add that 'some arrangements are being entered into that involve upfront payments, which are described as lease premium, and payment of a very small rent, in order to try to avoid paying tax'.

For lease premiums relating to leases of 10 years or less, the new rules will treat the premium as if it were actual rent paid. The taxable amount for each tax year will be the amount of lease premium spread over the length of the lease plus the amount of any rent paid, less any amount made good by the employee. The new rules will not apply to leases relating to property used mainly for a business purpose by the employer and partly for the domestic use of an employee.

Who is affected

Employees (typically short term assignees to the UK) and their employers.

Timing

The new legislation will apply to leases entered into or extended on or after 22 April 2009.

Our view

Lease premium planning has been relatively commonplace over the years and relies on the different benefit-in-kind tax treatment for payments of lease premiums as opposed to rent.

Whilst HMRC often raise enquiries into lease premiums arrangements it seems clear they have now concluded that the existing legislation does not adequately support their arguments and that new rules are therefore required. We will have to await publication of the Finance Bill for the detail. An intriguing point is what will constitute use 'mainly for a business purpose by the employer' as regards when the new rules will not apply.

Review of HMRC powers, deterrents and safeguards: penalties for late filing of returns and late payment of tax

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

A further range of measures is to be introduced in Finance Bill 2009 as a result of the review of HMRC's powers, deterrents and safeguards, which has been in operation since the formation of HMRC in 2005.

The new measures cover multiple taxes but include specific points in relation to Pay As You Earn (PAYE) and the Construction Industry Scheme (CIS). These specific measures include applying penalties for the first time to all employers who are late in making monthly PAYE and NICs payments.

We concentrate here on the position for employers. Please see the Corporate Tax section for more information.

PAYE

Penalties for the late payment of taxes and deductions collected through the PAYE system will depend on the number of defaults in any 12 month period, starting with no penalty for the first default. A second late payment and any subsequent failures in the default period will attract a penalty of two percent rising to five percent of the unpaid taxes.

Further penalties of five percent will be imposed for any amounts of tax still unpaid at six and 12 months.

The measures also provide for removing late payments penalties charged during an agreed time to pay arrangement with HMRC unless the taxpayer defaults or misuses the arrangement.

Interest on late payments of in-year PAYE is expected to be introduced from April 2010.

CIS

A fixed penalty of £100 will be introduced for a failure to submit any return by the filing date, with an additional fixed penalty of £200 if any return is outstanding more than three months after the filing date.

Further penalties will apply of five percent of the deductions due for the return period for prolonged failures over six months, and again at 12 months. Higher penalties of 70 percent of the deductions due will apply where a person fails to submit a return for over 12 months and has deliberately withheld information necessary for HMRC to assess the tax due. This will rise to 100 percent if the failure is deliberate with concealment.

Who is affected

All employers are potentially affected.

Timing

The changes will be phased in over a number of years, starting with penalties for late payment of in-year PAYE, and interest on in-year PAYE, in April 2010.

Our view

KPMG has taken part in the wider consultations leading up to these proposals. Clearly, a balance needs to be struck between the imposition of penalties against those who persistently pay taxes or file returns late and those who inadvertently miss a deadline. It will be important that the new regime relating to PAYE and the CIS is applied fairly and proportionately so that the sanctions are appropriately targeted. KPMG will be monitoring the position closely and will make further representations if this does not appear to be the case.

Save As You Earn process simplification

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

A SAYE plan is an HMRC approved employee share plan with a share option linked to a savings account with a bank or other financial institution. The employee makes a monthly savings contribution of between £5 and £250 to the savings account, which pays a tax free maturity bonus at a pre-set rate. When the savings account matures (after either 3 or 5 years), the employee can generally use the accumulated funds to exercise the share option but is not obliged to do so.

Following an informal HMRC consultation on the process for setting SAYE bonus rates last year, draft legislation published today, is intended to streamline the process for changing SAYE bonus rates.

Who is affected

Employers operating SAYE plans for employees.

Timing

The changes will have effect on and after 29 April 2009.

Our view

We do not expect the changes to SAYE plans to have a significant impact on employers operating such plans, as the changes are mainly aimed at banks and other financial institutions offering SAYE savings contracts. The most interesting point for employers relates to SAYE invitations that straddle a bonus rate change. Problems have previously arisen where employees are invited to participate in an SAYE plan and the SAYE bonus rate changes before the closing date for the return of applications. From 29 April 2009 employees will be able to enter into a savings contract at the bonus rates in force at the date of invitation in certain circumstances.

UK personal allowances and reliefs for non-resident individuals

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Personal allowances and reliefs are not given to individuals who are not resident in the UK unless such individuals fall into certain categories (set out in section 278, Income and Corporation Taxes Act 1988) or the allowances/reliefs are available under the terms of relevant tax treaties. These allowances and reliefs include basic and age-related personal allowances, married couples' allowances, blind person's allowances and relief for life assurance.

One category mentioned in s278 is Commonwealth citizens. From 6 April 2010, this category is to be withdrawn.

Who is affected

Commonwealth citizens who are not resident in the UK.

HMRC say that those mainly affected are citizens of the following countries:

- Bahamas; Cameroon; Cook Islands; Dominica; Maldives; Mozambique; Nauru; Niue; St Lucia; St Vincent & the Grenadines; Samoa; Tanzania; Tonga; and Vanuatu.

Timing

From 6 April 2010.

Our view

This proposal will have little impact for those able to claim the reliefs and allowances under relevant tax treaties. As a result, this is likely to have relatively little impact.

Avoiding unintended tax consequences in relation to pension savings

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Insurance companies can make pension provision which benefits from tax privileges, and that provision can be registered as a pension scheme for tax purposes. They can also transfer tax-relieved pension savings to other registered pension schemes and provide an annuity from those savings.

Unintended tax consequences may arise when the Financial Services Compensation Scheme (FSCS) provides assistance to an insurer as the FSCS is not a registered pension scheme for tax purposes.

Finance Bill 2009 will introduce a regulation-making power to allow changes to be made to the tax consequences of FSCS assistance for insurers who make pension provision. The regulations will be able to provide for individual members to have their payments after FSCS intervention to be treated for tax purposes in broadly the same way as if FSCS had not intervened.

Who is affected

Individuals who have tax-relieved pension savings with an insurance company in the possible circumstance where the insurer qualifies for assistance from the FSCS.

Timing

The measure will take effect from the date the Finance Bill 2009 receives Royal Assent. But any regulations made under the new power will be able to be backdated to payments made by the Financial Services Compensation Scheme on or after 6 October 2008 where they do not disadvantage the individual.

Our view

This is a sensible measure to ensure pension scheme members in this situation are not disadvantaged.

Taxation of payments from the financial assistance scheme

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The FAS is a Government-funded scheme. It provides financial help to members of defined benefit occupational pension schemes who have lost significant amounts of their accrued rights because their scheme was wound up when it had insufficient assets. It only applies to schemes wound up between 1 January 1997 and 5 April 2005; since then the Pension Protection Fund has been performing a similar function.

The FAS is not a pension scheme. It makes payments to the members of qualifying pension schemes to top up any pension payments made by the scheme, bringing the total paid up to 90 percent of the pension entitlement, subject to an overall cap.

The FAS is being extended so that it will, in the future, be responsible for making all of the payments due to qualifying members, including lump sums. This means that it will in future make payments similar to those made by a registered pension scheme.

As set out in Budget Note BN 48, legislation will be introduced in Finance Bill 2009 to allow payments made by the FAS to be given broadly the same tax treatment as if they had been made by a registered pension scheme. This means that the individual will not be disadvantaged by incurring charges to income tax that would otherwise arise because the payment is received from a body that is not a registered pension scheme.

Who is affected

Members of defined benefit occupational pension schemes where the pension scheme is no longer able to meet all its pension obligations and qualifies for assistance from the Financial Assistance Scheme (FAS).

Timing

The amendment will have effect for all payments made by the FAS, whenever made.

Our view

This is a sensible measure which ensures pension scheme members are not disadvantaged if their scheme falls into the FAS.

HMRC charter

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Legislation will be introduced in the 2009 Finance Bill which will require HMRC to have a Charter. The Charter will set standards of behaviour and values to which HMRC will aspire in their dealings with taxpayers and others. The legislation will require HMRC to report annually on their performance against the standards.

Who is affected

All taxpayers and anyone who has dealings with HMRC.

Timing

The Charter must be in place by 31 December 2009 and is currently in the second round of consultation. HMRC plans to launch the Charter by Autumn 2009.

Our view

While it is welcome that the Charter will be given legislative backing there is still much to discuss on what should be included to help HMRC rebuild trust with taxpayers. It may appear to be a relatively minor point but the choice of name is significant. The current title suggests that the Charter is intended to be of benefit to the staff of HMRC not the taxpayer. Some might regard this as a bad sign.

Indirect Tax



Gary Harley
Head of Indirect Tax

The 2009 Budget represents a housekeeping Budget with neither revenue generating measures nor tax give-aways.

Probably as a result of the delay in the Budget this year, a number of the indirect tax amendments we would normally have expected to see in the Budget had been preannounced.

Most specifically, the partial exemption simplification and the detail of the anti forestalling legislation pre-empting the reintroduction of 17.5 percent VAT on 1 January 2010 had already been announced.

HMRC are withdrawing a number of concessions including those that currently apply to the option to tax and the second hand car margin scheme; this represents a rationalisation of concessions.

Finance Bill 2009 will also include legislation implementing the changes to the taxation of cross border supplies of services. These will start to take effect from 1 January 2010.

The usual changes to registration limits, fuel scale charges increases in alcohol, oil and tobacco duty etc have also been made.

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VAT: Change of standard rate

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

As set out in HMRC Budget Note BN 71 the standard rate of VAT will revert to 17.5 percent from 1 January 2010. The temporary decrease to 15 percent which had effect from 1 December 2008 was announced as part of a group of measures in last November's Pre Budget aimed at stimulating the economy.

Who is affected

All businesses and individuals will be affected. Anyone that is unable to recover fully the VAT that they incur will see an increase in costs. Businesses or organisations in sectors such as financial services, charities, educational establishments and other public services will see an increase in costs, as the irrecoverable VAT they suffer on standard rated goods and services increases back to 17.5 percent. Assuming the rate increase is passed on (and of course that the decrease was also passed on,) this will also affect consumers who will see the prices of standard rated goods and services rise.

All businesses will be affected as any change in VAT rate creates numerous accounting and systems issues. Whilst businesses will have previously operated with a VAT rate of 17.5 percent, changes will need to be made to systems as well as coping with complex anti forestalling provisions that span the rate change. Retail businesses are likely to suffer significant administrative costs implementing price changes.

Timing

The new rate will take effect from 1 January 2010.

Our view

Whilst the rate increase was expected, it is disappointing that once again the change in VAT rate comes at a difficult time for business. Following the administrative burden caused by the short notice of the

rate decrease in the run up to Christmas the reversion to 17.5 percent is in the middle of many businesses' holiday period.

Furthermore there are complex anti-forestalling provisions which were announced under HMRC Budget Note BN 72 for supplies which span the change of rate which are an additional burden to business – more details can be found in summary of BN 72.

VAT: Change of standard rate: Anti-forestalling legislation

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

This measure as set out in HMRC Budget Note BN 72 is described as aiming to counter schemes that seek to apply the 15 percent VAT rate to goods and services which are supplied after the VAT rate returns to 17.5 percent. A ministerial statement was issued with the announcement of the VAT rate increase in November. This stated the importance of protecting public finances from artificial avoidance seeking to exploit the change in VAT rates. The Ministerial statement at the end of March sets out the details of the anti-forestalling legislation. Of particular concern is the complexity and wide scope of the provisions which may inadvertently catch legitimate business transactions.

Who is affected

This may affect any business that makes supplies which span the change of rate. These supplies are those where the basic tax point for supply i.e. delivery of the goods or performances of the services, is after the change but the actual tax point i.e. invoice or payment is before the rate change. Businesses which make these supplies will need to determine firstly whether their customer can recover the VAT and then whether any one of the following conditions are met.

- The supplier and customer are connected parties; or
- The supplier funds the purchase of the goods or services (or grant of right); or
- A VAT invoice is issued by the supplier where payment is not due for at least six months; or
- A prepayment of £100k or more is made except where this is made in accordance with normal commercial practice when no rate increase is expected.

Where these conditions are met an additional supplementary charge to VAT of 2.5 percent will be due on 1 January 2010.

Timing

The first three conditions have effect from 25 November 2008 and the £100k provision has effect from 31 March 2008 with the additional VAT charge falling due on the VAT return covering 1 January 2010.

Our view

A draft copy of the proposed anti-forestalling legislation in the Finance Bill was recently released for consultation. From the wording in the Budget Notice it does not appear that the numerous submissions made on consultation have been adopted but the detailed post consultation legislation is not yet available. The complex anti-forestalling provisions could represent a significant additional burden to business on managing the VAT rate change. Whilst we understand HMRC's concerns that businesses should not take artificial advantage of the lower rate these rules are both overly complex and too widely drawn. We wait to see the detail of the legislation in the Finance Bill.

VAT package – Place of supply, time of supply, EC sales lists

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

HMRC have confirmed the changes already announced to implement the VAT package. The changes include changes to the place of supply of services - the basic rule will be that services are supplied where the customer is established so that the VAT reverse charge applies. These changes are to be phased in from 2010 to 2013.

There are corresponding changes to the time of supply rules for services purchased by UK businesses from overseas suppliers from 2010.

Quarterly EC Sales Lists will be introduced from 2010 for services supplied to businesses in other EU countries where the customer is required to account for VAT under the reverse charge procedure and monthly EC sales lists for goods. The time available to submit the ESLs will be reduced from six weeks to 14 or 21 days.

Who is affected

Businesses that supply and/or receive supplies of services cross border.

Timing

The new rules will be phased in to have effect on 1 January 2010 (when the majority of changes to the place of supply will be introduced), 1 January 2011, and 1 January 2013.

Our view

There will be winners and losers in the changes to the place of supply. Whilst the place of supply changes will reduce many businesses need to reclaim non-UK VAT or register elsewhere in the EU, businesses that are unable to recover all VAT on purchases such as those in the financial sector could see an increase to their cost base as services

which are currently not subject to UK VAT are required to be reverse charged.

Changes to the time of supply for purchases of cross border services will require businesses to set up procedures to establish when VAT needs to be accounted for. The EC Sales lists for goods and services will require systems and process changes to enable businesses to comply with reduced timescales.

Many businesses are already considering the requirements and planning for the changes although some points of detail remain to be resolved. There could be a significant administrative burden in complying with the new rules. Also, there are significant issues of interpretation which are currently unclear.

Refunds of VAT across EU member states

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

UK businesses will be able to submit claims to HMRC where VAT has been incurred in other EU member states. Currently claims have to be made to the tax authorities of the relevant member states.

The current paper-based system is to be replaced with an electronic procedure using a standardised form and the time limits for making a claim is to be extended from six to nine months. HMRC will have to make a refund within four months (rather than the current six months). Interest will be paid by the member state of refund where refunds are not paid within the relevant deadlines.

Who is affected

UK businesses who wish to obtain a refund of VAT incurred in other EU member states.

Timing

The new rules will take effect from 1 January 2010.

Our view

This forms part of a package of measures designed to simplify and modernise the VAT system for cross border trading. The measure is to be welcomed as it simplifies the reclaim procedure and should improve cash flows.

VAT exemption for gaming participation fees and other miscellaneous amendments

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

BN73 sets out the measures taken in relation to the indirect taxation of gaming machines, bingo and games of chance.

Of particular note is:

- The extension of the exemption to VAT of participation fees to all forms of bingo and other games of chance
- The increase in rate of bingo duty from 15% to 22%
- The increase in the money prize limit for bingo duty from £50 to £70 for small scale amusements
- The extension of bingo duty to remote bingo operators.

Who is affected

Anyone making gaming machines available for play.

Any business, club or institution offering bingo (remote and non-remote).

Any business, club or institution offering games of chance.

Timing

Various.

Our view

The increase in the rate of bingo duty is significant but may to some extent be compensated for by the extension to the exemption to VAT. HMRC are also seeking to establish a clearer basis for the taxation of remote bingo operators.

Changes to opting to tax land and buildings

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Changes are to be made to simplify the procedure for opting to tax supplies of land and buildings. In some cases, a business is required to obtain prior written consent from HMRC before it can opt to tax. This simplification should result in fewer cases where prior permission is required.

Separately, HMRC are to withdraw two informal concessions relating to the option to tax that HMRC consider allow businesses to reclaim more VAT than the law allows.

Who is affected

Businesses that have previously let land or buildings prior to opting to tax.

Timing

The measure to simplify the option to tax has effect from 1 May 2009.

Whilst there is no detail given on the exact nature of the two informal concessions, HMRC have stated that they will continue until 30 April 2010 after which one will be withdrawn and the other will continue but only in part.

Our view

Reducing the circumstances where a business is required to seek HMRC permission before it is able to opt to tax is to be welcomed.

The withdrawal of the informal concessions could potentially result in an increase in VAT costs for some businesses than is currently the case and so an early evaluation of factors affecting the decision to opt to tax is essential.

VAT reduced rate for children's car seat bases

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The 5 percent rate of VAT for children's car seats will be extended to include bases for such seats. The reduced rate of VAT applies to children's car seats. The relief includes the combination of a safety seat and a related wheeled framework, booster seats and booster cushions.

Who is affected

Suppliers and consumers of children's car seat bases.

Timing

The reduced rate will take effect on and after 1 July 2009.

Our view

The measure will bring down the cost of this essential safety equipment.

Withdrawal of ESC in relation to margin scheme for cars

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

As set out in the Technical Note on Withdrawal of Extra Statutory Concessions, an ESC which permitted second hand car dealers to account for VAT on either the purchase price or half the selling price of a vehicle for which they do not hold the necessary margin scheme records will be withdrawn with effect from 1 April 2010. From this date dealers who fail to keep evidence of the purchase and selling price will have to account for VAT on the full selling price.

Who is affected

Second hand car dealers.

Timing

The new rules will take effect from 1 April 2010.

Our view

The concession favoured car dealers over dealers in other second hand goods. As it has no basis in EU law and fails to ensure that VAT is accounted for on the profit margin, HMRC have decided to withdraw it. Failure to maintain proper records under the margin scheme rules will potentially have a severe financial impact.

VAT: changes in fuel scale charges

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

VAT scale charges will be amended for taxing private use of road fuel to reflect changes in fuel prices. It will also amend the table of CO₂ bands to maintain alignment with those used for direct tax purposes

A scale charge is a way of accounting for output tax on road fuel bought by a business that is then put to private use. If you use the scale charge, you can recover all the VAT charged on road fuel without having to split your mileage between business and private use. The scale charge for a particular vehicle is determined by carbon dioxide emissions. Where the carbon dioxide emissions figure of a vehicle is not a multiple of five, the figure is rounded down to the next multiple of five to determine the level of the charge. For a bi-fuel vehicle which has two carbon dioxide emissions figures, the lower of the two figures should be used. For cars which are too old to have a carbon dioxide emissions figure, HMRC have prescribed a level of emissions by reference to the vehicle's engine capacity (cc).

Who is affected

Businesses which recover input tax on fuel used for private motoring.

Timing

Businesses must use the new scale charges from the start of their next prescribed accounting period beginning on or after 1 May 2009

HMRC Notice 700/64 VAT: Motoring Expenses will be updated in due course.

Our view

This is an expected change and reflects the continued importance of reducing the UK's CO₂ emissions.

Increased VAT turnover thresholds for registration and deregistration

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The annual taxable turnover threshold which determines whether a person must be registered for VAT will increase from £67,000 to £68,000. The annual taxable turnover threshold which determines whether a person may apply for deregistration will be increased from £65,000 to £66,000. The existing conditions for determining registration and deregistration remain unchanged.

The registration and deregistration threshold for relevant acquisitions from other European Union Member States will also be increased from £67,000 to £68,000.

Schedules 1 and 3 to the Value Added Tax Act 1994 will be amended by statutory instrument to give effect to these changes.

Who is affected

Businesses whose taxable turnover is close to the current VAT thresholds for registration and deregistration.

Timing

The new registration and deregistration thresholds will have effect from 1 May 2009.

Our view

Whilst inflation is currently low any increase in the VAT thresholds is welcomed. This eases the burden and potential cost on some small businesses of being VAT registered. Those below the threshold can still apply for voluntary registration if applicable.

Increase in duty rates on hydrocarbon oils

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Legislation will be introduced in Finance Bills 2009 to 2013 to provide for the setting of fuel duty rates.

Road Fuels - On 1 April 2009, road fuels (unleaded petrol and diesel) were subject to an increase of 1.84 pence per litre (ppl). This rate will further increase by 2 ppl on 1 September 2009 with a 1 ppl rise above indexation on the 1 April from 2010 to 2013.

Light Oil - On 1 May 2009, light oil (other than unleaded petrol and aviation gasoline) will be subject to a rise of 1.84 ppl with a further increase of 2 ppl on 1 September 2009.

Aviation Gasoline - On 1 May 2009, aviation gasoline (avgas) will increase by 2.31 ppl. This rate will further increase by same percentage as the rates for main road fuels on 1 September 2009.

Non-road fuels – On 1 April 2009, non-road fuels (light oil burnt in a furnace, marked gas oil, fuel oil, gas oil and kerosene used as fuel, bio-diesel for non road use and biodiesel blended with gas oil) were increased by the same percentage as road fuels, and these rates will increase similarly on 1 September 2009 and on 1 April 2010 to 2013.

Biodiesel and Bioethanol – On 1 April, bio-diesel/bioethanol were subject to an increase of 1.84 ppl. This rate will further increase on September 2009 to maintain the current 20ppl differential. From 2010 the reduced rate for bio fuels will cease and they will be subject to duty at the same rate as main road fuels.

Natural gas and Liquid Petroleum Gas – On 1 April 2009, the duty rate for natural gas was increased to £0.1926 per kg to maintain the differential with road fuels while the rate for liquid petroleum gas was increased to 0.2482 per kg to reduce the differential with main road fuels by the equivalent of 1 ppl of petrol. These rates will increase on 1 September 2009 to maintain the differential with main road fuels. From 2010 to 2013 the difference in duty rate between liquid petroleum gas

and petrol will be reduced by the equivalent of 1 ppl on a litre of petrol each year.

Who is affected

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

Timing

The 2009 increases in duty rates have effect on and after 1 April 2009 or 1 May 2009 and 1 September 2009. Changes in future years will have effect on and after 1 April in that year.

Our view

An increase was widely anticipated but the return to the commitment to increase rates annually by a rate greater than inflation (i.e. the re-introduction of the fuel duty escalator) may catch some by surprise.

Tobacco products duty rate increase

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Legislation will be introduced in the Finance Bill 2009 to increase the rates of duty by 2 percent on tobacco products imported into, or manufactured in, the UK.

Who is affected

Manufacturers, importers and consumers of tobacco products.

Timing

The rate changes will have effect from 6pm on 22 April 2009.

Our view

Increases were widely anticipated.

Increase in duty rates on alcohol

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Legislation will be introduced in Finance Bill 2009 to provide for the setting of duty rates for alcohol. Duty rates will increase by 2 percent in real terms for all alcoholic drinks. The impact of the changes on retail prices is equivalent to:

- 13 pence on a typical bottle of spirits (70cl)
- 1 pence on a pint of beer
- 1 pence on a litre of still cider
- 4 pence on a typical bottle of sparkling cider (75cl)
- 4 pence on a typical bottle of wine or made-wine (75cl)
- 4 pence on a typical bottle of sparkling wine (75cl)

Who is affected

Manufacturers, importers, distributors, retailers and consumers of alcohol products.

Timing

The increases in duty rates will take effect on and after 23 April 2009.

Our view

There are rate changes each budget and these were expected increases.

Withdrawal of the warehousing for export drawback scheme for alcoholic liquors

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Companies will not be able to claim repayment of excise duty on 'duty paid' alcoholic goods that are warehoused for export from 1 June 2009. Amendments to the Excise Goods (Drawback) Regulations 1995 will be made today to withdraw this drawback scheme. All other drawback schemes, including warehouse drawback for other excise products, remain in place.

Manufacturers and exporters of alcoholic liquors, other than spoilt liquors, who claim drawback when alcohol is warehoused will no longer be able to claim such drawback. Drawback will now be limited to the actual export of the goods or situations where they are sourced whilst in duty suspension. The amended legislation introduces assessment provisions rather than recovery by HMRC being by way of demand. Such assessments can be appealed.

Who is affected

Manufacturers and exporters of excise goods, particularly in the alcoholic beverage sector, who use the warehouse for export scheme.

Timing

The new rules will take effect from 1 June 2009 when alcoholic goods warehoused for export after this date will be ineligible for repayment of excise duty.

Our view

The proposed amendments are limited to alcoholic liquors but amend provisions of legislation which include other excise product. The amendments do not however, affect the drawback for spoilt cider, wine or beer.

The provisions have been introduced in consequence of alcohol fraud which has abused the warehouse drawback system.

Landfill tax – standard rate to rise as expected

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

As previously announced, the standard rate of landfill tax will rise by £8 per tonne to £48 per tonne with effect from 1 April 2010. The Finance Bill 2009 will include legislation which will amend s 42 Finance Act 1996 which specifies the rates at which landfill tax are charged. There will be no increase in the lower rate of tax that applies to inert materials, which is £2.50 per tonne.

At present, the standard rate of landfill tax is £40 per tonne. It was also announced in the Treasury document 'Building Britain's Future', published today, that the £8 per annum increase in landfill tax rates would continue in 2011, 2012 and 2013. By 2013, therefore, landfill tax will rise to £72 per tonne.

The lower rate of tax is frozen until 2010/2011.

Who is affected

Landfill site operators.

Timing

The rise to £48 per tonne will take effect from 1 April 2010.

Our view

This increase to their cost base will have a significant impact on landfill site operators, and on the overall price of disposing material to landfill.

Landfill tax – taxable disposals of waste at landfill sites

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Landfill tax legislation is to be amended by the Finance Bill 2009 so as to bring within the scope of landfill tax certain uses of material at landfill sites. This change has been prompted by the recent Court of Appeal judgment in a case involving a major landfill site operator, where that operator successfully argued that materials used on site are not waste and are therefore not subject to landfill tax.

In addition, the legislation relating to tax free areas and to the exemption for site restoration materials will be withdrawn by the Finance Bill 2009, and an administrative change will be made to the landfill tax return.

Who is affected

Landfill site operators.

Timing

The new arrangements will come into effect on 1 September 2009.

Our view

Given that landfill tax has always been regarded as a tax on waste and not on recycled materials, this is a significant change of approach. It would seem that landfill tax revenues have been affected by the Court of Appeal case to such an extent that the Government is seeking to claw back some of the tax which it has lost.

It will be interesting to see the draft legislation which will provide clearer guidance on what uses of material at landfill will now be chargeable to landfill tax.

Landfill tax – a consultation exercise on modernising landfill tax

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

HM Treasury and HM Revenue and Customs today announced a consultation exercise entitled 'Modernising Landfill Tax'. Like the changes to be introduced to the landfill tax legislation in September 2009, this consultation exercise seems to have been prompted by the recent Court of Appeal judgment in a case involving a major landfill site operator, where that operator successfully argued that materials used on site are not waste and are therefore not subject to landfill tax.

The consultation considers the definitions of:

- Taxable disposal of waste at a landfill site
- Wastes that qualify for the lower rate of tax

It is timely to review the legislation governing these aspects and the way in which it reflects environmental protection regulation and waste industry practice.

Who is affected

Landfill site operators and their customers.

Timing

The closing date for responses is 24 July 2009. The intention is to introduce new legislation in the Finance Bill 2010.

Our view

This is a major consultation exercise and could result in significant and potentially costly changes for landfill site operators. Given that landfill tax does not have its roots in European law, it is interesting to note that the Government wishes to align the tax with European legislation.

We will be following the consultation exercise very closely and would advise landfill site operators and other interested parties to consider how any changes could impact upon their business and profitability.

Climate change levy: Restricted entitlement to levy relief for plastics sector

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Relief is to be extended to supplies of electricity and liquefied petroleum gas to certain plastics manufacturers.

It was announced in the Treasury document 'Building Britain's Future', published today, that a mechanism will be introduced to enable recovery of climate change levy from facilities that fail to meet their target under the climate change agreement scheme.

Who is affected

Manufacturers of certain plastic products.

Timing

The new rules will take effect on or after the date Finance Bill 2009 receives Royal Assent.

Our view

This is an opportunity for some in the plastics sector to reduce their energy costs in return for entering into a Climate Change Agreement.

Climate change levy: Recovery of relief claimed where a facility is in a sector which has not met its targets

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Where a facility benefits from up to 80 percent relief from climate change levy but is in an energy intensive sector which has failed to meet its targets, HMRC will be able to recover that relief in proportion to the extent by which the facility has failed to reach its target.

Who is affected

Energy intensive businesses who have signed up to a climate change agreement and are in a sector which has failed to reach its target for emission reductions.

Timing

The recovery mechanism will take effect from Climate Change Agreement certification periods starting from 1 April 2009.

Our view

This could substantially increase costs for businesses which fail to meet their CCA targets and will undoubtedly increase pressure to meet those targets in future.

Climate change levy: Relief withdrawn on low value solid fuel

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Changes are to be made to applicability of the Climate Change Levy to low value solid fuel.

Low value solid fuel valued at no more than £15 per tonne, on which the Climate Change Levy was previously not due, will become subject to the Climate Change Levy.

Who is affected

Suppliers and consumers of low value solid fuel.

Timing

The new rules will take effect on or after 1 January 2010.

Our view

This will substantially increase the costs of low value solid fuel to consumers and is likely to have a significant impact on supplies of these products.

Amusement machine licence duty: Changes to rates and machine categories

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

A number of changes to the level of Amusement Machine Licence Duty (AMLD) have been announced as follows:

AMLD will be increased for all categories of gaming machines.

Further changes include:

- An increase in the stake and prize levels of Category C Machines from 50p and £35 to £1 and £70
- New additions to the definition of section 21 'excepted machines' for licence purposes by reference to the size of stake and prize
- An increase in the prize limits from £8 to £10, for section 22 small-prize category machines

Who is affected

Providers of gaming machines for play in the UK.

Timing

The new duty amount for gaming machines will apply for all licence applications filed from 22 April 2009. The other changes will take effect from 1 June 2009.

Changes to customs powers

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Currently HMRC must have reasonable grounds for believing that a movement is not between member states before stopping and checking any particular movement. The new power allows them to check all movements and undertake selective and proportionate checks to collect or enforce customs duties or enforce any import prohibition or restriction.

Who is affected

All movements of goods and individuals between member states.

Timing

The new powers take effect from on or after Royal assent.

Our view

The powers are expressly limited by a requirement to act selectively and proportionately. Although additional checks are likely to be made, these should not adversely affect the business community.

Review of HMRC powers, deterrents and safeguards

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

A further range of measures is to be introduced in the Finance Bill as a result of the review of HMRC's powers, deterrents and safeguards, which has been in operation since the formation of HMRC in 2005. The new measures are as follows:

Payments, repayments and debt

- Voluntary Managed Payment Plans ('MPPs') will be introduced to allow taxpayers to spread their income or corporation tax payments equally over a period straddling the normal due dates
- HMRC will be able to collect small debts through the PAYE system
- HMRC will have the power to require companies and businesses to provide contact details to enable it to trace tax debtors

Compliance checks

- The compliance checking framework which was introduced in Finance Act 2008 ('FA 2008') for direct taxes and VAT will be extended to environmental taxes, IPT, SDLT, SDRT, IHT and PRT. This includes provisions on record-keeping requirements, inspection and information powers and time limits for assessments and claims
- Various specialist information powers which are effectively replaced by the powers in Schedule 36 to FA 2008 will be repealed
- A penalty will be introduced for carelessly or deliberately providing inaccurate information or documents

Penalties for late filing and late payment

- A new harmonised penalty regime will be introduced for late filing of tax returns and late payment of tax, covering income tax, corporation tax, PAYE, NICs, Construction Industry Scheme, SDLT, SDRT and IHT

Interest harmonisation

- A single regime will be introduced covering interest on underpayments and repayments of income tax, corporation tax, PAYE, Class 4 NICs, Construction Industry Scheme liabilities, environmental taxes, excise duties, stamp duties, IHT, IPT, pension scheme liabilities and PRT

Who is affected

All taxpayers are potentially affected.

Timing

Payments, repayments and debt

The legislation on MPPs and tracing tax debtors will apply from Royal Assent. Because of the need for changes to HMRC's systems the MPPs will not be introduced before April 2011. Collection of small debts through PAYE is likely to begin from April 2012.

Compliance checks

The repeal of specialist information powers is likely to take place soon after Royal Assent. The extension of the compliance-checking framework is likely to take effect from 1 April 2010, apart from the amendments to time limits which are not likely to be fully effective until 1 April 2011.

Penalties for late filing and late payment

The changes will be phased in over a number of years, starting with penalties for late payment of in-year PAYE in April 2010.

Interest harmonisation

Interest on CT and PRT will not be included in this year's finance bill and will be introduced in Finance Bill 2010. Where HMRC currently charge and pay interest, rates will be aligned shortly after Royal Assent. Other changes will be implemented over a number of years beginning with interest on late payments of in-year PAYE from April 2010.

Our view

KPMG has taken part in the consultations leading up to these proposals and many of our suggestions have been taken into account in the latest documents. Overall the proposals represent a welcome modernisation and harmonisation of the administrative framework. We will be looking at them in detail to see whether they reflect sufficiently the comments that have been made and provide adequate safeguards, and will make further representations if necessary.

HMRC charter

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Legislation will be introduced in the 2009 Finance Bill which will require HMRC to have a Charter. The Charter will set standards of behaviour and values to which HMRC will aspire in their dealings with taxpayers and others. The legislation will require HMRC to report annually on their performance against the standards.

Who is affected

All taxpayers and anyone who has dealings with HMRC.

Timing

The Charter must be in place by 31 December 2009 and is currently in the second round of consultation. HMRC plans to launch the Charter by Autumn 2009.

Our view

While it is welcome that the Charter will be given legislative backing there is still much to discuss on what should be included to help HMRC rebuild trust with taxpayers. It may appear to be a relatively minor point but the choice of name is significant. The current title suggests that the Charter is intended to be of benefit to the staff of HMRC not the taxpayer. Some might regard this as a bad sign.

Personal Tax



David Kilshaw
Head of Private Client

In our Budget predictions we suggested that, given the current state of the economy, the Chancellor would be best advised to leave individuals and companies alone. It is disappointing, therefore, that there are 220 pages of Budget Notes which introduce yet more complex provisions to already over-burdened taxpayers. It is comforting to note that unincorporated businesses have been largely left alone; the same however cannot be said for individuals.

The main feature today is the increase of the income tax rate for those earning over £150,000 to 50 percent. This represents a change to the previously announced rate of 45 percent and has been brought forward a year to apply from 6 April 2010. The gradual withdrawal of the personal allowance for incomes over £100,000 does nothing to address the anomaly present in the rules as originally announced in the Pre-Budget Report which results in the first £12,950 of such income being taxed at an effective rate of 60 percent.

The withdrawal of higher rate relief for pension contributions made by those earning over £150,000 is wrong in principle and will not encourage contributions.

The Government have introduced a number of measures to correct areas where UK tax law is inconsistent with EU law. However, there does not seem to have been a consistent approach taken, with inheritance tax reliefs and tax credits on dividends being extended while the favourable tax treatment currently available for furnished holiday lettings is to be withdrawn for everyone.

On the changes to residence and domicile it is disappointing that the Government have not responded to comments that the legislation introduced in 2008 is overly complex and, therefore, difficult if not impossible to comply with. The minor amendments made in the Budget, while welcome, are likely to have little practical impact on non-domiciled taxpayers and on the attractiveness of the UK as a location of choice.

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Additional rate of income tax and income related reduction of the personal allowance from 2010-11

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

There have been the following changes announced to income tax rates and allowances:

- There will be a new additional higher rate of 50 percent for taxable income above £150,000
- The basic personal allowance for income tax will be gradually reduced to nil for individuals with taxable incomes above £100,000
- The trust rate will be increased to 50 percent and dividend rate to 42.5 percent to match those for income tax
- Powers will be introduced to vary the income tax rate for the charges that apply to registered pension schemes

These measures replace the proposals to introduce a 45 percent tax rate announced in the last Pre-Budget Report and also bring forward the proposals by one tax year.

The gradual reduction to the personal allowances will effectively work by a £1 reduction for every £2 of taxable income above £100,000. This replaces the two stage reduction announced at the Pre-Budget Report.

Who is affected

The reduction of personal allowances affects those with incomes over £100,000 and the new tax rate affects those with incomes over £150,000.

Timing

The additional rate of income tax, reduction to the personal allowance and the increases to the trust rate and dividend trust rate will apply from 6 April 2010.

Our view

The changes announced today do nothing to correct the anomaly present in the rules as originally announced in the Pre-Budget Report which effectively means that the rate of tax moves up to 60 percent as a result of the changes to the personal allowance before moving down to 40 percent and then finally up to 50 percent. This is set out below:

- Taxable income of £100,000 to £112,950 - effective marginal rate of tax 60 percent
- Taxable income of £112,951 to £149,999 - marginal rate of tax is 40 percent
- Taxable income of £150,000 onwards - marginal rate is 50 percent

These figures assume the personal allowance for 2010-11 remains the same as that for 2009-10 at £6,475.

Pensions: Limiting tax relief for high income individuals (anti-forestalling)

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Members of registered pension schemes currently benefit from tax relief on their pension contributions at their highest marginal rate. So, for example, a £100 contribution into a pension scheme will cost a 40 percent taxpayer £60. Maximum personal relief is limited to contributions up to 100 percent of earnings and is also controlled by an annual allowance (currently £245,000, increasing to £255,000 in 2010-11).

The Government has announced its intention to restrict income tax relief on pensions contributions for people with taxable incomes of £150,000 or more. Relief at higher rates will be tapered away from that level so that for those earning over £180,000, relief will be restricted to the basic rate. No further details are available at the moment – the Government is to consult on its implementation.

As this change will have effect from 6 April 2011 there will also be legislation introduced with effect from 22 April 2009 to prevent people attempting to manipulate their affairs to avoid the consequences of the new rules. These “anti-forestalling” rules will introduce a new special annual allowance and associated tax charge, the effect of which will be to restrict tax relief to basic rate for any pension savings (which are not “normal ongoing regular pension savings”) above £20,000 per tax year. The restriction will apply regardless of who makes the contributions (employee or employer), and regardless of whether the pensions arrangement is defined benefit or money-purchase. The special tax charge will be collected through self-assessment.

Who is affected

From 22 April 2009

The special annual allowance charge will apply to individuals who in a tax year:

- Have relevant income of £150,000 or more in that tax year or in either of the previous two years; and
- Who increase their level of annual pension savings on or after 22 April 2009 over and above their normal regular pension savings pattern or receive extra benefits in a defined benefit scheme; and
- Have total pension savings for the year above £20,000

If a one off payment was made between 6 and 21 April 2009 this will not in itself be subject to tax but will reduce the £20,000 annual allowance and therefore limit their ability to obtain full tax relief on further contributions.

From 6 April 2011:

Anyone with income above £150,000 per annum.

Timing

The measure applies from 6 April 2011. The anti-forestalling provisions take effect from today (22 April 2009).

Our view

“Normal ongoing regular pension savings” includes only those contributions that are made at least quarterly, and were agreed prior to 22 April 2009. Those individuals who have regularly made an annual contribution, or who wish to make an annual or new bonus sacrifice into their pension arrangement, will be caught by this restriction straight away.

When pension benefit is taken it will be taxed at the individual's marginal rate. If, therefore, the individual is a higher rate taxpayer they may well have been given relief at basic rate on contributions but suffer higher rate on the pension, this would not seem to be a great deal for them! It may therefore be that many high-earners decide that pensions saving in registered schemes will not be worthwhile.

It is disappointing that this comes so soon after the extensive changes to pensions tax brought in by Finance Act 2004, and is so radically different to what was then put forward as the long term solution for pensions. Changes such as this undermine confidence in the pensions system.

We have set out below an illustration.

Assumptions

Single man usually makes a contribution of £2,000 per month

Decides to make an additional annual contribution of £10,000

His rate of income tax relief on the additional contribution is as follows:

Income level	Tax year			
	2008/09	2009/10	2010/11	2011/12
75,000	40%	40%	40%	40%
100,000	40%	40%	40%	40%
125,000	40%	40%	40%	40%
150,000	40%	40%	40%	40%
175,000	40%	20%	20%	23.33
180,000	40%	20%	20%	20%

Note: assumes straight line reduction in higher rate relief from £150,000 to £180,000

Relevant income includes most forms of income but is after certain deductions including pension contributions which will be restricted to a maximum of £20,000.

Taxation of personal dividends

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Individuals who receive dividends from non-resident companies have been entitled to claim a non-repayable tax credit since 6 April 2008, where their shareholding in that company is less than 10 percent. This has been extended in the Budget such that individuals will still be able to claim a tax credit if their shareholding exceeds the 10 percent, but only if the company is resident in a territory which has an appropriately worded double tax agreement. The treatment now mirrors the non-repayable tax credits that are available in respect of dividends received from UK companies.

Anti-avoidance measures will be introduced to prevent the use of structures designed to secure the tax credit for dividend income originating other than in a qualifying territory. It is not yet known which countries will be regarded as qualifying territory.

Who is affected

This will affect those with large shareholdings (over 10 percent) in non-resident companies.

Timing

The extension of the relief will be effective from 22 April 2009.

Our view

The extension of the relief is welcome and the new rules appear to be more consistent with EU law.

Furnished holiday accommodation

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Individuals, partnerships and companies who let furnished holiday (FHL) accommodation in the UK are currently treated as trading for certain tax purposes, allowing claims to be made for loss relief, capital allowances on expenditure, certain capital gain tax reliefs (including business asset rollover relief, entrepreneur's relief and relief for gifts of business assets).

The Government have announced that the FHL rules will be repealed from 6 April 2010.

Until now, the FHL rules have only applied to furnished holiday accommodation situated in the UK. The Government now accepts that this treatment will also apply to furnished holiday accommodation situated in the European Economic Area (EEA). Therefore, if an EEA property satisfies all the other qualifying conditions, it will be a qualifying FHL property for FHL purposes.

Who is affected

Individuals, partnerships and companies who let furnished holiday property situated within the EEA, and who are liable to pay UK tax on the income and capital gains from the property.

Timing

In some cases, claims can now be made for relief on properties situated in EEA countries back to 2003/04.

The FHL treatment will be withdrawn from 6 April 2010.

Our view

"Whilst it must be welcomed that the Government now accept that they cannot discriminate between furnished holiday accommodation situated in the UK and in other EEA countries, it is disappointing that the tax relief will be withdrawn."

Please see further comments in the Corporate Tax Commentary

Extension of agricultural property and woodlands reliefs to land in the European Economic Area

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Agricultural Property Relief (APR) is available to reduce the value of agricultural property chargeable to inheritance tax. Previously, it was restricted to property in the United Kingdom, the Channel Islands or the Isle of Man, while Woodlands Relief only allowed inheritance tax to be deferred on the value of timber or underwood until sale where the land was located in the United Kingdom.

New legislation will extend the availability of agricultural property relief and woodlands relief to property located in other EEA states

The availability of capital gains tax holdover relief – deferring a capital gains tax charge on gift or sale at under value – has also been extended to cover agricultural property in EEA states where that land has been farmed by a person other than the owner.

Who is affected

Individuals, trustees, personal representatives and executors of estates with agricultural property and/or woodlands property.

It affects those who have paid IHT on such property located in another EEA state on or after 23 April 2003 in relation to agricultural property. The relief for woodlands property will apply to deaths after 22 April 2009, but will also be backdated to cover earlier deaths.

Timing

The extension of agricultural property relief and woodlands relief against inheritance tax and capital gains tax holdover relief will have effect from 22 April 2009 and contains an element of retrospection as it impacts on chargeable events involving these reliefs in earlier years.

The earliest deadline for claiming overpayments on agricultural property will be 21 April 2010. In the future, the statutory time limit for making a claim for repayment of overpaid IHT will reduce from six to four years. This will apply to repayment claims for overpayments where IHT has been paid and APR is now available. However, the new time limits will not apply to claims made before 1 April 2011.

The time limits for obtaining woodlands relief is usually within two years of death. Finance Bill 2009 will provide that the earliest deadline for reclaiming overpayments on such property will be 21 April 2010.

The time limit for claiming hold over relief is five years from the 31 January following the tax year to which the claim relates and therefore claims to holdover relief in respect of the tax year can be made until 31 January 2010. As the time limit for holdover relief will be reduced to four years from 1 April 2010, claims in respect of 2004/05 and 2005/06 will need to be made by that date.

Our view

This is a welcome development for UK domiciled holders of land and woodlands property elsewhere in the European Economic Area.

Residence and domicile

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

There will be some minor amendments to the new remittance basis introduced in Finance Act 2008. This made wholesale changes to the way that individuals who are not domiciled in the UK or not ordinarily resident in the UK are taxed. There are 70 pages of very complex provisions which introduce many new concepts and overturn existing case law.

The measures announced in the Budget make only minor changes to this complex legislation, and include:

- The minor exemptions, for example for personal effects, jewellery and watches, which currently only apply to relevant foreign income (broadly, investment income) will be extended to apply to employment income and capital gains. This will be backdated to have effect from 6 April 2008
- There is currently an exemption, which allows the remittance basis to apply without claim to those who have no UK income and who have been resident in the UK in not more than 6 of the 9 previous tax years. This exemption will be extended to include those with UK income of less than £100, provided they do not make any remittances. This will also be backdated to have effect from 6 April 2008
- There will be clarification of the current rules that provide for the remittance basis to apply without claim to those with unremitted foreign income and gains of less than £2,000 in any tax year. The amended legislation will make clear that the remittance basis will automatically apply in these circumstances unless the individual notifies HMRC that they do not wish to use it. Again, this will be backdated to 6 April 2008
- There will be amendments to ensure that the £30,000 Remittance Basis Charge will be available to cover income tax due on gift-aid payments in the same way as other income and capital gains tax. Again, this will be backdated to 6 April 2008
- There will be amendments to ensure that income arising in settlor interested trusts, that are treated by anti-avoidance legislation as the income of the settlor, will benefit from the same transitional

provisions as other income. Again, this will be backdated to 6 April 2008

- In addition, HMRC have announced that there will be amendments to the legislation to clarify the interaction between the remittance basis and the rules applying to settlor interested trusts. It is not clear precisely what is intended in this respect
- There are some amendments to the definition of relevant person as it applies to close companies, although these appear simply to clarify the law as it stands
- There will be minor amendments to deal with the remittance of property which is part of a set to ensure that in all circumstances such a remittance will be treated as a proportion of the entire value of the set (as opposed to simply the value of the part remitted)

Also see the commentary in employment taxes for the effect of the amendments on employees and their employers

Prior to the Budget, on 31 March 2009, HMRC published nearly 500 pages of guidance on the new rules and have withdrawn most of their earlier guidance which was provided in the form of Frequently Asked Questions. Despite its length, the new guidance does not cover all circumstances and there remains significant uncertainty regarding the eventual HMRC interpretation of parts of the legislation. We note that HMRC state that they 'are continuing to develop and add to this guidance' and indeed additional guidance on capital gains and the remittance basis has been issued subsequently.

Who is affected

The amendments will impact on all those who are not domiciled or not ordinarily resident in the UK.

Timing

The changes to the remittance basis will take effect from 22 April 2009, except where they will be backdated to 6 April 2008 as noted above.

Our view

It is disappointing that the Government have not responded to comments that the legislation introduced in Finance Act 2008 is overly complex and therefore difficult, if not impossible, to comply with. The minor amendments made in the budget, while welcomed, are minor and are likely to have little practical impact on non-domiciled taxpayers and on the attractiveness of the UK as a location of choice.

Individual savings accounts

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The ISA limit will be raised to £10,200, up to £5,100 of which can be saved in cash. The timing will depend on the age of the investor.

Who is affected

Primarily those over 50, but all savers from 2010/11.

Timing

The new limits will apply from 6 October 2009 for those over 50 and from 6 April 2010 to all other investors.

Our view

While any incentive to save is welcome, the raised ISA limits will not create any overnight millionaires! An extra £1,500 allowance from 6 October on a cash ISA paying 3 percent will give extra income of £22.50 over the rest of the tax year, meaning a tax saving of just £9 for a 40 percent taxpayer.

Extension of trading loss carry back for business – Unincorporated businesses and partnerships

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Trade loss carry back will be extended from the current one year entitlement to a period of three years, with losses being carried against later years first.

The amount of trading losses that can be carried back to the preceding year remains unlimited. However, after carry back to the preceding year, a maximum further £50,000 of unused trading losses will be available to the earlier two years.

Who is affected

Unincorporated businesses and partnerships making losses from trades, professions or vocations. Start up businesses have separate and more favourable rules on the set off of their losses and these remain unchanged.

Timing

For sole traders and partners, a separate £50,000 cap will apply to the extended carry-back of losses made in each of the tax years 2008/09 and 2009/10.

Our view

While the further extension of loss relief is welcome, it is disappointing that it was limited to only £50,000 and to losses of the same trade rather than against general income and potentially capital gains.

Changes to EIS/VCT

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

There are a number of changes to the rules governing the Enterprise Investment Scheme and Venture Capital Trust scheme.

Previously the rules for the Enterprise Investment Scheme limited the amount of relief that could be carried back, in certain circumstances, to the previous tax year to £50,000. The Chancellor has announced that going forward the amount of relief that can be carried back will be the normal annual investment limit.

The previously existing requirement that at least 80 percent of the money raised by the share issue must be employed within twelve months, with the remaining 20 percent employed within the following twelve months has been replaced with a requirement that simply 100 percent must be employed within two years. A similar rule existed for money received by Venture Capital Trust investee companies and similarly this has been replaced by the requirement that 100 percent must be employed within two years.

New legislation also addresses an anomaly caused by the interaction of the EIS and capital gains tax rules which can arise when a share-for-share exchange takes place, resulting in a shareholder being liable to capital gains tax in respect of both a deferred gain brought back into charge and the gain on the 'disposal' of the shares in the share exchange. The new legislation will only result in the deferred gain being brought back into charge in certain defined circumstances.

Who is affected

Investors receiving tax relief under the Enterprise Investment Scheme (EIS) and the Venture Capital Trust (VCT) scheme.

Timing

The carry back of EIS relief will apply to the tax year 2009/10 and subsequent years.

The measure in respect of the employment of money has effect for EIS and VCT investments made on or after 22 April 2009.

The removal of the link to other shares issued at the same time will apply to shares EIS issued on or after 22 April 2009. Similarly the correction of the capital gains anomaly will apply to new EIS share holdings issued on or after 22 April 2009.

Our view

These changes follow the outcome of a consultation exercise published at the time of Pre-Budget Report in November 2008.

The changes are welcome, especially the extension of relief that can be carried back, and should encourage further investment into smaller, high risk enterprises, while the simplification of the rules concerning expenditure give such enterprises more flexibility and lend more weight to commercial considerations rather than simply protecting investors' tax reliefs.

Regrettably, since 6 April 2006, the size of companies qualifying for the EIS scheme has been restricted to companies with gross assets before investment to £15 million to gross assets £7 million and the Chancellor has retained these restricted limits.

Charities: Substantial donor regulations

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The substantial donor regime covers charities which carry out certain transactions with their substantial donors, defined as making tax relievable donations of £25,000 or more in 12 months or £100,000 or more in a period of six years.

Such individuals are treated as a substantial donor of the charity for all chargeable periods falling wholly or partly within that 12 month or six year period and for a further five chargeable periods. If a charity enters into a specified transaction with a substantial donor or someone connected to the donor the transaction will be treated as non-charitable expenditure which is subject to tax.

The new measure in HMRC Budget Note BN 53 increases the threshold of relievable gifts which a person may make before becoming a substantial donor to £150,000 in a period of six years. The annual threshold of £25,000 remains unchanged.

Who is affected

Charities which receive donations between £100,000 and £150,000 from a particular donor in a six year period and the individuals and companies who make those donations.

Timing

The measure will have effect on and after 23 April 2009.

Our view

In implementing this measure it will be important to ensure that it does not create significant burdens for either charities or donors.

Gift aid

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

In the Budget Report HM Treasury makes reference to the government commissioning research into the effect of redirecting higher rate relief for Gift Aid payments from donors to the donee charity. This is part of its ongoing exploration into improving Gift Aid.

Who is affected

If introduced, higher rate tax payers who make donations to charities which they currently claim higher rate relief on.

Timing

As this is research being commissioned there is no indication of when or indeed if it will be implemented.

Our view

This may be an unpopular move for some wealthy individuals who make substantial donations to charity and could reduce the amounts they donate accordingly. In reality it may have little impact on the amounts charities actually receive and it will be interesting to see the results of the research.

HMRC charter

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Legislation will be introduced in the 2009 Finance Bill which will require HMRC to have a Charter. The Charter will set standards of behaviour and values to which HMRC will aspire in their dealings with taxpayers and others. The legislation will require HMRC to report annually on their performance against the standards.

Who is affected

All taxpayers and anyone who has dealings with HMRC.

Timing

The Charter must be in place by 31 December 2009 and is currently in the second round of consultation. HMRC plans to launch the Charter by Autumn 2009.

Our view

While it is welcome that the Charter will be given legislative backing there is still much to discuss on what should be included to help HMRC rebuild trust with taxpayers. It may appear to be a relatively minor point but the choice of name is significant. The current title suggests that the Charter is intended to be of benefit to the staff of HMRC not the taxpayer. Some might regard this as a bad sign.

Avoidance using life insurance policies

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Income Tax loss relief will be blocked for losses on offshore life insurance policies.

HMRC have decided to legislate to stop tax avoidance schemes which involved generating a loss on an offshore life insurance policy, which could be set off against gains on other such policies which would otherwise be liable to Income Tax.

HMRC did not consider that this scheme had the effect that the taxpayer intended under the existing legislation, but have decided to put the matter beyond doubt.

The measure was previously announced on 1 April 2009.

Who is affected

Individuals realising losses on offshore life insurance policies.

Timing

The new legislation will come into effect for losses relating to the tax years from 2009/10 onwards.

It will also apply to new policies made on or after 1 April 2009, or to existing policies varied on or after that date.

Our view

This is targeted at tax avoidance schemes, and is unlikely to have a significant general effect.

Anti avoidance – Interest relief

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

There will be no tax relief for certain interest payments made on or after 19 March 2009 if the interest is paid as part of arrangements where the deductibility of the interest means that the investor is guaranteed to make a profit.

Who is affected

These rules are aimed at schemes being promoted by a number of UK promoters.

Timing

The legislation will apply to interest payments made on or after 19 March 2009.

Our view

These anti-avoidance rules were announced by HM Treasury on 19 March 2009.

It will be important to ensure that the draft legislation does not inappropriately deny relief for interest paid where it should be genuinely deductible.

UK personal allowances and reliefs for non-resident individuals

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Personal allowances and reliefs are not given to individuals who are not resident in the UK unless such individuals fall into certain categories (set out in section 278, Income and Corporation Taxes Act 1988) or the allowances/reliefs are available under the terms of relevant tax treaties. These allowances and reliefs include basic and age-related personal allowances, married couples' allowances, blind person's allowances and relief for life assurance.

One category mentioned in s278 is Commonwealth citizens. From 6 April 2010, this category is to be withdrawn.

Who is affected

Commonwealth citizens who are not resident in the UK.

HMRC say that those mainly affected are citizens of the following countries:

- Bahamas; Cameroon; Cook Islands; Dominica; Maldives; Mozambique; Nauru; Niue; St Lucia; St Vincent & the Grenadines; Samoa; Tanzania; Tonga; and Vanuatu

Timing

From 6 April 2010.

Our view

This proposal will have little impact for those able to claim the reliefs and allowances under relevant tax treaties. As a result, this is likely to have relatively little impact.

Transfers of income streams

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The Government has today announced in HMRC Budget Note Budget Note 36 that legislation to counter avoidance involving transfers of income streams will be included within Finance Bill 2009. This legislation follows extensive consultation and numerous workshops with stakeholders following proposals introduced in the 2007 Pre-Budget Report (“the principles based approach to financial products avoidance”). The principles-based approach is intended to tackle tax avoidance in a simpler and clearer way than through piecemeal legislative amendment. No legislation has been produced today.

Legislation will ensure that receipts derived from a right to receive income (and which are an economic substitute for income) are taxed as income for the purposes of corporation tax and income tax. In many cases this is already the case under existing provisions or case law. However as these statutory rules are not comprehensive the proposed new rules will introduce a comprehensive principles-based code to ensure receipts of this type are dealt with appropriately.

There will be provisions to prevent income from being taxed twice and to prevent taxation when the transfer is by way of providing security.

Who is affected

The legislation will apply to companies and individuals, including partnerships, that dispose of rights to receive future income streams without disposing of any underlying asset.

Timing

The legislation will have effect for transfers of income taking place on or after 22 April 2009. The legislation will be included within Finance Bill 2009.

Our view

The most recent draft of the legislation demonstrates that HMRC have listened to stakeholders during the workshops, undertaking considerable revisions to the rules since publication in the 2007 Pre-Budget Report. At this stage, we do not know whether guidance will be published. Again, there are a few inconsistencies between the latest draft of the legislation released during the consultation process and the Budget Note (as outlined above), but subject to sight of the final legislation, the rules should be a workable legislative framework.

Financial services compensation scheme: payments representing interest

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Compensation paid by the Financial Services Compensation Scheme to customers of defaulting financial institutions may include an amount representing accrued interest from the last date interest was paid to the customer to the date that the institution defaulted.

Legislation is being introduced to ensure any such payment is treated as interest for income tax purposes and therefore subject to income tax.

Who is affected

Individuals who have received or will receive compensation from the Financial Services Compensation Scheme because of the default of a financial institution where the compensation includes payment in respect of accrued interest.

Timing

The new measure applies to payments made by the Financial Services Compensation Scheme on or after 6 October 2008.

Our view

This is a minor housekeeping measure to clarify the treatment of such payments for income tax purposes.

Child trust fund: payments for disabled children

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

In addition to the existing contributions into Child Trust Funds, the Government will contribute £100 per year to the Child Trust Fund accounts of disabled children; £200 per years for the severely disabled.

Who is affected

Children in receipt of Disability Living Allowance in 2009-10.

Timing

The payments will start in April 2010.

Our view

Extra support for disabled children is to be welcomed.

Reclaiming income tax, capital gains tax and corporation tax overpayments

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The error or mistake relief provisions in ss33 and 33A, Taxes Management Act 1970 and in Paragraph 51, Schedule 18, Finance Act 1998 enable taxpayers to reclaim tax where an assessment is excessive due to a mistake in a return. Relief, if due, is given on a 'just and reasonable' basis.

Legislation will be brought forward in Finance Bill 2009 to provide a means of reclaiming overpayments where there is no other statutory route. The measure will remove the requirement that the overpayment must be the result of a mistake in a return and that it must be made under an assessment. It will enable claimants to quantify the amount to be repaid, subject to HMRC's right to enquire into the claim.

The proposed legislation is also said to amend the error or mistake relief rules to provide additional taxpayer safeguards.

Who is affected

Income tax, capital gains tax and corporation taxpayers reclaiming overpayments of tax.

Timing

The measure will have effect for claims made on or after 1 April 2010.

Our view

The current rules governing the reclaiming of overpayments resulting from taxpayer mistakes have a number of limitations – for example, they are subject to HMRC's discretion, they provide only limited appeal rights

and they only apply where tax has been paid in an assessment as a result of a mistake in a return. The proposals are said to address these limitations, and this is a welcome reform. It is not clear whether they will also address other issues such as the difficulty in applying the mistake relief provisions within a group of companies.

The new measure will also make it explicit that HMRC are not able to repay an amount except as provided by the measure or another provision of the Taxes Acts. This appears to be an attempt to limit the taxpayer's right to claims for restitution, for example. This provision will need to be examined carefully to see whether it would unfairly limit the taxpayer's right to obtain redress from HMRC.

Publishing the names of deliberate tax defaulters

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

HMRC has announced its intention to introduce legislation in Finance Bill 2009 enabling them to publish names and details of individuals and companies who are penalised for deliberate defaults leading to a loss of tax of more than £25,000. Names of those who make a full unprompted disclosure or a full prompted disclosure within the required time will not be published.

Currently only the names and details of those who are convicted of criminal offences are published. The proposed change is designed to apply consistent treatment for tax fraud whether investigated through civil or criminal proceedings.

Details will be published quarterly on HMRC's website within 12 months of the penalty becoming final and will be removed from publication after a year.

In addition, new reporting requirements for those who have incurred a penalty for the deliberate understatement of tax of at least £5,000 will be introduced requiring them to provide more information on their tax affairs for up to 5 years to ensure that they have proper systems to be able to make correct returns and allow HMRC to monitor their compliance.

Who is affected

- Taxpayers (individuals, businesses and companies) who are penalised for deliberately understating tax due or overstating claims or losses of more than £25,000
- Taxpayers who are penalised for deliberately failing to notify HMRC when required to do so resulting in a loss of tax of more than £25,000
- Taxpayers are penalised for deliberately committing certain VAT and Excise wrongdoings leading to a loss of tax of more than £25,000

The additional reporting requirements apply to similar categories of taxpayer but will be triggered by the size of the penalty imposed rather than the amount of the default.

Those who make an unprompted or a full prompted disclosure within the required time are unaffected by the proposed provisions.

Timing

The new provision will be effective from a date to be specified in secondary legislation. No details of deliberate defaults committed prior to the legislation becoming effective will be published.

Our view

HMRC promises that the criteria for publication will be tightly defined and that sufficient details will be published to ensure that the correct person is identified as a result of the default. And it promises that details will not be published until all appeal avenues against the additional tax and penalties are exhausted or expired.

Clearly such safeguards are an important prerequisite to the introduction of the proposals. However, this still represents a significant breach of taxpayer confidentiality without a clear case being made to support the move as a means of deterring evasion based on evidence from other jurisdictions or appropriate research.

Similar 'naming and shaming' provisions have existed in Ireland for more than 20 years which have no doubt influenced the Government's thinking. Nevertheless, when the possibility of introducing a similar policy in the UK was mentioned three years ago in a consultation document issued as part of HMRC's Review of Powers, Deterrents and Safeguards, it attracted generally unfavourable comments and was not pursued. It is surprising that it has been brought forward again at this stage with no further consultation.

The proposal provides further incentive to potentially affected taxpayers to take advantage of the New Disclosure Opportunity announced today planned to run from autumn 2009 to March 2010.

Review of HMRC powers, deterrents and safeguards

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

A further range of measures is to be introduced in the Finance Bill as a result of the review of HMRC's powers, deterrents and safeguards, which has been in operation since the formation of HMRC in 2005. The new measures are as follows:

Payments, repayments and debt

- Voluntary Managed Payment Plans ('MPPs') will be introduced to allow taxpayers to spread their income or corporation tax payments equally over a period straddling the normal due dates
- HMRC will be able to collect small debts through the PAYE system
- HMRC will have the power to require companies and businesses to provide contact details to enable it to trace tax debtors

Compliance checks

- The compliance checking framework which was introduced in Finance Act 2008 ('FA 2008') for direct taxes and VAT will be extended to environmental taxes, IPT, SDLT, SDRT, IHT and PRT. This includes provisions on record-keeping requirements, inspection and information powers and time limits for assessments and claims
- Various specialist information powers which are effectively replaced by the powers in Schedule 36 to FA 2008 will be repealed
- A penalty will be introduced for carelessly or deliberately providing inaccurate information or documents

Penalties for late filing and late payment

- A new harmonised penalty regime will be introduced for late filing of tax returns and late payment of tax, covering income tax, corporation tax, PAYE, NICs, Construction Industry Scheme, SDLT, SDRT and IHT

Interest harmonisation

- A single regime will be introduced covering interest on underpayments and repayments of income tax, corporation tax, PAYE, Class 4 NICs, Construction Industry Scheme liabilities, environmental taxes, excise duties, stamp duties, IHT, IPT, pension scheme liabilities and PRT

Who is affected

All taxpayers are potentially affected.

Timing

Payments, repayments and debt

The legislation on MPPs and tracing tax debtors will apply from Royal Assent. Because of the need for changes to HMRC's systems the MPPs will not be introduced before April 2011. Collection of small debts through PAYE is likely to begin from April 2012.

Compliance checks

The repeal of specialist information powers is likely to take place soon after Royal Assent. The extension of the compliance-checking framework is likely to take effect from 1 April 2010, apart from the amendments to time limits which are not likely to be fully effective until 1 April 2011.

Penalties for late filing and late payment

The changes will be phased in over a number of years, starting with penalties for late payment of in-year PAYE in April 2010.

Interest harmonisation

Interest on CT and PRT will not be included in this year's finance bill and will be introduced in Finance Bill 2010. Where HMRC currently charge and pay interest, rates will be aligned shortly after Royal Assent. Other changes will be implemented over a number of years beginning with interest on late payments of in-year PAYE from April 2010.

Our view

KPMG has taken part in the consultations leading up to these proposals and many of our suggestions have been taken into account in the latest documents. Overall the proposals represent a welcome modernisation and harmonisation of the administrative framework. We will be looking at them in detail to see whether they reflect sufficiently the comments that have been made and provide adequate safeguards, and will make further representations if necessary.

New rules for investment trusts investing in interest-bearing assets

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

This measure will allow investment trusts to invest in interest bearing assets in a tax efficient manner. The new rules will be optional and will allow an investment trust to stream its distributions and benefit from a tax deduction in respect of the interest distributions it makes. The effect will be to remove any corporation tax liability on interest income which is distributed. The interest distributions will be received by shareholders as a payment of yearly interest.

This proposal has been the subject of consultation over the last few months. Draft regulations were issued in December 2008 on which KPMG and others commented. No further draft regulations have yet been released.

Who is affected

Investment trust companies and their shareholders.

Timing

The measure will take effect for any interest distributions made on or after 1 September 2009, if an election is made. This suggests that investment trusts may be able to elect into the new regime part way through an accounting period. The original draft regulations had suggested that the proposals would take effect in relation to a full accounting period and therefore it is not yet clear whether a distribution made on or after 1 September 2009 but out of profits accrued before that date will be included.

Our view

This proposal is a welcome measure. It will remove the significant disadvantage that UK investment trusts currently suffer when competing with authorised investment funds that are bond funds. It will benefit, in

particular, investors that are tax exempt such as pension funds and charities.

As is intended by the Government, the proposed new framework will provide a method for UK investment trusts to invest in bonds, and other assets producing an interest like return, without suffering tax on that income. For both existing investment trusts and new funds being launched it should allow greater flexibility with their investment strategies.

Currently investment trusts pay corporation tax on interest received, but tax-exempt shareholders have no way of recovering this tax. This is in contrast to open-ended bond funds, which currently can benefit from a tax deduction for interest distributions, and so no tax 'sticks' at fund level.

If investment trusts elect into the regime they will need to make administrative arrangements to stream their distributions. This could prove to be a significant operational burden but the benefits may outweigh the costs.

Our view is that in order for the regulations to be fully effective, there is also a need for an amendment to the tests (s842 of the Income and Corporation Taxes Act 1988) which a company is required to satisfy to be an investment trust. The definition of 'security' in this test is currently unclear. The proposal will encourage investment trusts to invest in a wider range of securities and they will therefore need certainty as to whether this could adversely impact their status as an investment trust.

Failure to amend s842 could mean that the perceived risks associated with the new framework will result in investment companies continuing to be established offshore, with the associated adverse effect on the UK's financial services infrastructure as administration and other services are also more likely to move abroad (see KPMG/IMA November 2007 paper 'The Value to the UK Economy of UK-Domiciled Authorised Investment Funds').

Offshore funds

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Legislation will be introduced in Finance Bill 2009 to change the definition of an offshore fund for UK tax purposes and amend the existing powers (in Finance Act (FA) 2008) to provide for the modernisation of the regime in regulations. Transitional rules will provide 'grandfathering' for investors in existing arrangements. Details of the transitional rules will be included in the primary legislation. Draft legislation was published following the 2008 Pre-Budget Report and changes have been made following comments received during the consultation. The detailed rules for the operation of the offshore funds tax regime will be in regulations, as announced in Budget 2008.

Under current legislation, the definition of an investment in an offshore fund is based on the regulatory definition of 'collective investment scheme' as set out in the Financial Services and Markets Act 2000, with modifications for tax purposes.

The new definition of an offshore fund uses a characteristics based approach which has been the subject of detailed consultation with the funds industry as set out in the relevant HM Treasury documents. There are also exceptions specified in the legislation to ensure that fixed share capital arrangements that do not mimic open-ended arrangements will remain outside the definition. This includes specific provisions for continuation votes and capital only arrangements.

Who is affected

Providers of offshore funds, and UK investors in certain offshore arrangements.

Timing

This measure will have effect on and after 1 December 2009.

Our view

Managers of closed-ended funds are concerned that the proposed changes will bring certain products, for example those with a fixed life, into the offshore funds regime for the first time. This would potentially

subject their investors to an income tax charge on disposal rather than a capital gains tax charge. We still await more detail on the proposed changes but the deferral to 1 December 2009 is welcome.

Transitional rules for the provision of 'grandfathering' regulations for investors in existing arrangements are also welcome.

More detail on the new definition and the modernised reporting regime is needed sooner rather than later.

Chargeable gains and offshore funds

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Under current legislation, for the purpose of tax on chargeable gains, units in a unit trust are treated as if they were shares in a company. However rights in funds in foreign jurisdictions which are not companies, unit trusts or partnerships (mostly those constituted by contractual arrangements) are often treated differently depending on the structure. Where such a fund comes within the new 'characteristics-based' definition of an offshore fund, then a new section of the Taxation of Chargeable Gains Act 1992 (TCGA) will apply similar treatment to rights in such funds.

The effect of this change will be that an interest in a transparent offshore fund will be an asset for the purpose of calculating capital gains tax on chargeable gains, as is already the case for shares in a company or units in a unit trust. Investors will no longer be required to consider disposals of the underlying assets for calculating capital gains tax on chargeable gains.

There will be no effect on interests in tax transparent foreign partnerships which will continue to be treated as transparent for both income and gains in the same way as United Kingdom partnerships. These will be specifically excluded from the definition of offshore funds

There will be transitional rules covering the timing and other aspects of the effect of this measure for existing investments in contract-based funds.

Investors subject to corporation tax will continue to treat their gains as transparent for the purposes of tax until discussions have taken place with industry about how to make similar changes to the tax treatment of chargeable gains for investors subject to corporation tax.

Who is affected

Investors in offshore funds such as Luxembourg Fonds Commun de Placement (FCPs) but not partnerships, that are transparent for the purposes of tax on income and gains.

Timing

The new treatment will apply to investments in contract-based offshore funds on and after 1 December 2009.

Elections into the new treatment can be made on and after 22 April 2009 and can be applied retrospectively back to the tax year 2003-04.

These will allow investors to elect to apply the new rules retrospectively, where such investors consider this will be an advantage. Elections can be made by capital gains taxpayers from the tax year 2003-04. Once made, an election will be irrevocable and will apply for all relevant tax years after the date of election. Investors making such an election will be treated as having been invested in an offshore fund that is certified by HMRC as a qualifying fund.

Our view

It will be welcome to a number of management groups that investors in offshore funds that are transparent for income and gains will no longer be required to consider disposals of such funds' underlying assets for calculating capital gains tax on chargeable gains. This will ensure that investors in unit trusts obtain parity in tax treatment as investors in other types of offshore funds which are not companies, unit trusts or partnerships.

It is a common problem that contractual funds such as Luxembourg FCPs are not attractive to UK retail investors because of their complexity.

The interaction with the offshore funds legislation will need to be monitored.

Some categories of investor, for example pension funds, rely on such funds being treated as transparent. This change of treatment by HMRC could adversely affect such investors.

Grandfathering provisions and transitional rules for existing investments in contract-based funds are welcome.

Tax elected funds

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Under current rules, UK Authorised Investment Funds (AIFs) are normally chargeable to corporation tax on income at a special rate of 20 percent. For tax exempt investors such as pension funds and Individual Savings Account (ISA) investors, any tax that sticks at the fund level is a real cost.

Under the new tax elected fund (TEF) regime, UK AIFs that meet certain conditions will be able to elect to be treated as a TEF. TEFs will be required to make two types of distribution of the income they receive - a dividend and a non dividend (interest) distribution. UK dividend income will remain non taxable in the fund and will be distributed as a dividend. For all other income that is distributed as a non-dividend (interest) distribution, the fund will receive a tax deduction up to the same amount. The new regime will be introduced by secondary legislation.

This measure will move the point of taxation from the AIF to the investor so that the investor is treated as though they had invested in the underlying assets directly.

UK investors are treated as receiving UK dividend income (including the non payable dividend tax credit) and a payment of yearly interest.

Who is affected

AIFs and their investors.

Timing

The new regime will have effect from 1 September 2009.

Our view

The introduction of UK non-taxable funds, in the form of TEFs, is welcome, as is the new TEF regime being elective.

The requirement for two streams of income (dividend and non-dividend (interest) distributions) is also welcome as this is in line with the current UK corporate streaming requirements for AIFs which should help encourage and alleviate concerns for TEF providers and third party

administrators around additional operational complexities and costs of additional streams that were previously proposed.

UK investors will now be treated as though they have invested in the underlying assets of a TEF directly. In this regard, it is welcome that UK dividends will continue to be non-taxable, non-dividend (interest) distribution will be tax deductible, and consultation around the taxation of foreign dividends should ensure non-UK dividends will follow the treatment of UK dividends, i.e. non-taxable.

However, there is still significant concern and uncertainty for investors around whether treaty relief will be available for TEFs under existing double tax agreements. There is also a concern from previous HM Treasury discussion papers that election into the new TEF regime will be irrevocable, and should treaty relief not be available, this may place TEF providers and investors at a disadvantage compared to non-TEFs.

It remains to be seen how many funds will elect into the new regime as it is only of real tax benefit to balanced funds. UK equity, bond, and going forward overseas equity funds, will not normally pay tax; and therefore from a tax perspective the new TEF regime may be of limited interest.

Certainty on trading and investment for authorised investment funds and investors in equivalent offshore funds

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

This measure provides certainty to AIFs and UK-resident investors in equivalent offshore funds that specific transactions will not be treated as 'trading' transactions for tax purposes.

Transactions undertaken by an AIF which are set out on the 'white list', when the AIF also meets a genuine diversity of ownership condition, will be treated as non-trading transactions and therefore not taxed in the AIF as any gain would be a capital gain and not trading income.

For an equivalent offshore fund which is also a 'reporting fund' under the new offshore fund rules, profits from transactions set out on the 'white list' will not be included in the 'reportable income' for UK-resident investors.

Rules will also be introduced so that financial traders cannot avoid tax by routing transactions through an AIF or equivalent offshore fund.

Who is affected

AIFs and UK-resident investors in equivalent offshore funds.

Timing

Legislation applying to AIFs will have effect on and after 1 September 2009. Legislation applying the equivalents will have effect on and after 1 December 2009.

Our view

This is a welcome move and is in response to extensive industry lobbying and consultation to improve the competitiveness of the UK tax regime for funds. AIFs will now have certainty in their tax treatment and equivalent offshore funds will not be put at a disadvantage as far as the tax rate borne by investors is concerned.

We expect ongoing discussion on which funds are regarded as equivalent e.g. whether or not this is a regulatory test.

In addition, it appears that offshore funds must still meet the conditions of the Investment Manager Exemption to avoid being subject to tax in the UK. Some may regard this as a clearer test than the genuine diversity of ownership test above; some may regard it as more onerous.

Taxation of personal dividends – distributions from offshore funds

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

These measures provide that:

- Individual shareholders of offshore funds largely invested in equities will be entitled to a non-repayable dividend tax credit
- Where an offshore fund invests predominantly (more than 60 percent) in interest bearing assets, the distributions received will be treated as 'interest' (with no tax credit available and tax at rates applicable to interest) and not a dividend or any other type of distribution.

The above measures do not affect the taxation of investors in offshore funds that are transparent for tax purposes.

Who is affected

Individuals receiving distributions from offshore funds.

Timing

These changes will have effect on and after 22 April 2009.

Our view

This is a welcome move to provide parity between the tax treatment of distributions received from UK funds (and non-UK companies for dividends) and offshore funds investing in equities and bonds. Questions remain as to how the 60 percent test will apply in practice. Will the onus be on the non-bond fund to demonstrate that they have not breached the limit at any point in an accounting period? Compliance with the test could be onerous.

Taxation of payments from the financial assistance scheme

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

The FAS is a Government-funded scheme. It provides financial help to members of defined benefit occupational pension schemes who have lost significant amounts of their accrued rights because their scheme was wound up when it had insufficient assets. It only applies to schemes wound up between 1 January 1997 and 5 April 2005; since then the Pension Protection Fund has been performing a similar function.

The FAS is not a pension scheme. It makes payments to the members of qualifying pension schemes to top up any pension payments made by the scheme, bringing the total paid up to 90 percent of the pension entitlement, subject to an overall cap.

The FAS is being extended so that it will, in the future, be responsible for making all of the payments due to qualifying members, including lump sums. This means that it will in future make payments similar to those made by a registered pension scheme.

As set out in Budget Note BN 48, legislation will be introduced in Finance Bill 2009 to allow payments made by the FAS to be given broadly the same tax treatment as if they had been made by a registered pension scheme. This means that the individual will not be disadvantaged by incurring charges to income tax that would otherwise arise because the payment is received from a body that is not a registered pension scheme.

Who is affected

Members of defined benefit occupational pension schemes where the pension scheme is no longer able to meet all its pension obligations and qualifies for assistance from the Financial Assistance Scheme (FAS).

Timing

The amendment will have effect for all payments made by the FAS, whenever made.

Our view

This is a sensible measure which ensures pension scheme members are not disadvantaged if their scheme falls into the FAS.

Avoiding unintended tax consequences in relation to pension savings

Impact on tax year			
Positive	Neutral	Negative	Both winners and losers

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The issue

Insurance companies can make pension provision which benefits from tax privileges, and that provision can be registered as a pension scheme for tax purposes. They can also transfer tax-relieved pension savings to other registered pension schemes and provide an annuity from those savings.

Unintended tax consequences may arise when the Financial Services Compensation Scheme (FSCS) provides assistance to an insurer as the FSCS is not a registered pension scheme for tax purposes.

Finance Bill 2009 will introduce a regulation-making power to allow changes to be made to the tax consequences of FSCS assistance for insurers who make pension provision. The regulations will be able to provide for individual members to have their payments after FSCS intervention to be treated for tax purposes in broadly the same way as if FSCS had not intervened.

Who is affected

Individuals who have tax-relieved pension savings with an insurance company in the possible circumstance where the insurer qualifies for assistance from the FSCS.

Timing

The measure will take effect from the date the Finance Bill 2009 receives Royal Assent. But any regulations made under the new power will be able to be backdated to payments made by the Financial Services Compensation Scheme on or after 6 October 2008 where they do not disadvantage the individual.

Our view

This is a sensible measure to ensure pension scheme members in this situation are not disadvantaged.

The Budget proposals and other tax changes are summarised on these pages. The Budget proposals may, however, be amended significantly before enactment. The content of this presentation is intended to provide a general guide to the subject matter and should not be regarded as a basis for ascertaining liability to tax or determining investment strategy in specific circumstances. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act upon such information without appropriate professional advice after a thorough examination of the particular situation.

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