

Chantrey Vellacott DFK LLP

Budget Report

24 March 2010

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1. Introduction

Overview

This Budget will be welcomed by almost no-one. Like Roy Jenkins some 35 years ago, the Chancellor has avoided a large pre-election bribe to the voters – but may not have done enough to satisfy either the financial markets, or the public.

The level of borrowing currently outstanding and proposed for the future is staggering – already 54% of GDP and forecast to rise as high as 75% in three years. This is even more extraordinary when compared to the litany of complaints about the under-funding of public services.

The immediate market reaction to the announcements was supportive but a large element of support derives from the clear public commitment to halving the deficit in four years. Although some simple arithmetic in support of this pledge was produced, the largest single element is a major spending review – work on which will not start until after the election. There is considerable scope for financial markets to take a much more cynical view than they have so far.

Much will depend on the economy's financial performance over the next few months. Leading indicators suggest the trough of the recession is past and the Chancellor believes we shall see growth this year, albeit modest. Were these factors to reverse, albeit slightly, the second dip of the recession would be much more painful as the spending strategy so far adopted would not be sustainable.

Dogma and Ideology

Some 40 minutes into the last Budget presentation of this parliament, the Chancellor Alistair Darling commented that his tax-raising proposals did “not come out of dogma or ideology”. Members of the middle classes listening could be tempted to disagree.

For the middle class and those living in the South East, the Budget contained little but pain: -

- The previously-announced progressive withdrawal of personal allowances for those on incomes above £100,000 per year and the introduction of a 50% rate for incomes over £150,000 per year were confirmed
- The restriction of higher rate tax relief on pensions where the beneficiary earns £130,000 per year was confirmed
- Personal allowances and the starting point of the basic rate band were left unchanged
- The inheritance tax nil rate band was left unchanged and, worse, will remain unchanged for the life of the next parliament
- Stamp Duty Land Tax on residential property sold for £1 million or more rises to 5%, though not until 12 months hence
- For those who also drink, smoke or use petrol there are above inflation rises in excise duty and even an extra 50p levy for each telephone landline

Entrepreneurs fare a little better – the amount eligible for 10% tax rate qualifying for entrepreneurs relief is raised to £2 million (interestingly, this is about the inflation-adjusted value the old retirement relief would by now have reached, had it not been replaced by taper relief). Equally, the widely-expected rise in the overall rate of capital gains tax has not materialised - yet.

For the smaller business, the rise in the annual investment allowance to £100,000 will be welcome, as will be the exemption from business rates for properties with a rateable value of £6,000 or less.

Tax Planning

The differential between income and capital gains tax rates – and the rise in the effective rate of income taxation have breathed new life into the tax planning industry. Our detailed notes show which schemes have been stopped this time but there is some hint that a number of other widely canvassed schemes have not been attacked directly.

In some cases, HM Revenue & Customs are avowedly hostile so any taxpayer entering such arrangements must do so with acceptance of the risk they carry. Rising rates mean that many more will be tempted to try.

2. Income Tax – Personal and Trusts

2.1 Rates and Allowances

Finance Bill 2010 will confirm that, as previously announced, the additional rate of tax of 50% (or 42.5% for dividends) will apply from 6 April 2010 on taxable income above £150,000.

As announced in the 2009 Pre-Budget Report, for 2010/11 the Personal Allowance is frozen at £6,475. The Personal Allowance for those over 65 will remain at £9,490 and for those aged 75 and over at £9,640. However, these allowances will be reduced by £1 for every £2 of income above £100,000.

For details of allowance rates and thresholds applicable in 2010/11, please see tables.

2.2 Individual Savings Accounts Limits

Last year's Budget increased the amount an individual can invest in ISAs each tax year from £7,200 to £10,200 from 6 April 2010 (from 6 October 2009 for the over 50's).

From 6 April 2011 for the next Parliament, the annual ISA limits will be increased in line with the Retail Prices Index. The subsequent new limits will be rounded to the nearest multiple of 120 to enable individuals who save monthly the ability to calculate their monthly savings more easily. The resulting increases will be split to enable 50% to be invested in stocks and shares, and 50% in cash.

This indexation is to be implemented outside of the Finance Bill.

2.3 Venture Capital Schemes

It has been confirmed that four changes have been agreed with the European Commission to widen the scope of the Enterprise Investment Scheme ("EIS") and the Venture Capital Trust ("VCT") scheme. The effective date will be the date that the relevant Finance Act receives Royal Assent, except for the change relating to the definition of eligible shares for VCT's which will not affect monies raised prior to that date.

The changes affecting both EIS and VCT are:

- Shares in companies will NOT qualify under the relevant legislation if the company can be regarded as an "enterprise in difficulty" for the purposes of the European Commission's Rescue and Restructuring Guidelines.
- The requirement in the present legislation that there is a qualifying trade carried on wholly or mainly in the UK will be changed to requiring that the company issuing the shares must have a permanent establishment in the UK. Permanent Establishment will be defined based upon the OECD definition.

Changes affecting only VCTs are:

- Currently the ordinary share capital of a VCT must be included in the official UK list throughout the relevant accounting period. This is to be changed to a requirement that the shares are admitted for trading on any EU regulated market.
- Current legislation requires 30 per cent of a VCT's qualifying holdings to be in holdings of eligible shares throughout the relevant accounting period. This will be changed to 70 per cent, but the definition of eligible shares will be also be amended to include shares with certain preferential rights to dividends.

This will be legislated in a Finance Bill introduced in the next Parliament.

2.4 EMI Schemes

As previously announced, to comply with EU State-aid guidelines, a change is being made to the requirement that a company issuing qualifying Enterprise Management Incentives ("EMI") options must operate wholly or mainly in the UK.

All that will be required in future is that the company issuing EMI options has a "permanent establishment" in the UK. If the issuing company is a parent company of a group, at least one company carrying on a qualifying trade must have a permanent establishment in the UK. Permanent establishment is statutorily defined.

This change will be included in a Finance Bill to be introduced in the next Parliament and will apply to options granted after the legislation receives Royal assent.

2.5 Financial Services Compensation Scheme

The Financial Services Compensation Scheme (FSCS) can be required to take action to protect holders of insurance policies or annuity contracts and other insurers. Where the FSCS does intervene, it is not clear that the tax status of insurance or annuity products remains unchanged.

Parliament is to be asked to allow regulation-making powers with a view to ensure the tax treatment of such products will remain broadly the same as if the FSCS had not intervened.

This proposal is to be included in the Finance Bill so should take effect on 6 April.

2.6 Dividends from Real Estate Investment Trusts

REITs - which benefit from exemption from corporation tax on the profits and gains of their property rental business - are required to distribute 90 per cent of their property rental profits. Currently, stock dividends are not treated as part of the income distribution in calculating whether the 90% distribution test is met.

Stock dividends are to rank as income distributions with effect from the date the Finance Act 2010 receives Royal Assent.

2.7 Deficiency Relief

Deficiency relief may be available to an individual on the maturity of a life insurance policy, life annuity or capital redemption policy where no gain has accrued over the premiums paid, but taxable 'chargeable event gains' have arisen on earlier withdrawals.

It is intended that legislation will be introduced as soon as possible in the next Parliament to ensure that deficiency relief will be effective from 6 April 2010 at the new 50% additional rate of tax and the 42.5% additional rate for dividends.

Anti-avoidance rules will also be introduced to restrict relief where arrangements are made after 22 April 2009 with the main purpose of securing a tax reduction after 6 April 2010 greater than the income tax due on earlier chargeable events.

2.8 Share Incentives

Legislation is to be introduced to counter the use of Share Incentive Plans ("SIPs") for the purpose of tax avoidance. The legislation will affect payments made and alterations to share capital or rights attaching to shares occurring on or after 24 March 2010.

Companies obtain a corporation tax deduction for payments made to SIP trustees to buy shares from non-corporate shareholders for use in the SIP. This deduction may be withdrawn if insufficient shares are appropriated to employees within the set time limits, but there is no provision for the deduction to be withheld at the outset where the company had no intention that the shares would be passed to employees under the SIP.

This has apparently led to schemes where the company makes the payment with the corporation tax deduction being the main purpose. The share capital or the rights attaching to the shares are altered with the effect that the employees in the SIP receive few shares carrying any real value.

The legislation will be amended so that corporation tax deductions will not be given where the payment to the SIP is part of a tax avoidance scheme or where the obtaining of a corporation tax deduction is the main purpose.

Clarification of the legislation which allows HMRC to withdraw approval of a SIP where the value of shares is materially affected by alterations to the share capital or rights attaching to the shares is also to be made.

2.9 CSOP Plans

Legislation is to be introduced to counter avoidance using Company Share Option Plans ("CSOP"). The legislation will be effective in respect of CSOP options granted over shares in a company under the control of a listed company on or after 24 March 2010.

It is possible for shares in companies that are under the control of listed companies to be used for CSOP options, up to a maximum amount of £30,000 per employee. This is based on the market value of the shares at the date of grant.

HMRC believe arrangements known as "geared growth" deliver additional rewards to employees that were not intended by the legislation. The arrangements will be countered by changing the definition of shares that can be used for CSOP. In particular the legislation will be amended so that shares in a company under the control of a listed company can no longer be used for CSOP.

The measure will provide a transitional period of six months to allow affected companies to amend their scheme rules to enable them to conform.

2.10 Release of Directors' Loans

A tax scheme has been widely marketed encouraging companies to write off amounts owed to them by their directors.

Finance Bill 2010 will introduce legislation to deny a corporation tax deduction where a close company releases or writes off a loan payable by a participator or their associates. This will have effect for any amounts written off on or after 24 March 2010.

The person benefiting from the write off will continue to be taxed as if they had received a distribution.

2.11 Earnings paid through Trusts

The Government has announced that it intends to introduce anti-avoidance legislation, effective from 6 April 2011, to prevent attempts to avoid tax and National Insurance contributions through the use of Employee Benefit Trusts and other arrangements to disguise payments of remuneration.

This is despite a recent HMRC comment (Spotlight series) to the effect they consider many of these arrangements ineffective.

“Other arrangements” may well include the use of Employer Funded Retirement Benefit Schemes (EFRBS), which have been a hot topic in tax circles for some time.

The publication of a date over twelve months in the future may encourage some taxpayers involved in such arrangements.

2.12 Benefits of “Green” Cars

A new relief will be introduced in the Finance Bill 2010 for the following types of vehicles provided by a company to an employee or director and which are available for private use;

- Cars that cannot produce CO² engine emissions under any circumstances when driven;
- Cars which have an approved CO² engine emission figure of 75g per kilometre or less; and
- Vans that cannot produce CO² engine emissions under any circumstances when driven.

Normally the benefit in kind charge for cars is dependent on the list price of the vehicle multiplied by the appropriate percentage.

For the above the appropriate percentage will be 0 per cent if the car cannot produce CO₂ emissions and 5 per cent for a car if the CO² emissions are 75g per kilometre or less.

For vans, the benefit in kind is set as a flat rate charge. For vans the flat rate charge will be £0 where the van cannot produce CO² emissions.

The above measure will have effect from 6 April 2010 until 5 April 2015.

2.13 Employer Childcare

Measures will be introduced to relax the conditions for exemption from the chargeable benefit rules for employer supported childcare, provided in the form of childcare vouchers or directly contracted childcare.

The relaxation will ensure that employees at or near the National Minimum Wage will now be able to take advantage of salary sacrifice arrangements even if the result would be to depress their earnings below that rate.

The change will have retrospective effect for the tax year 2005/06 and subsequent tax years.

The Government intends to include this measure in a Finance Bill to be introduced as soon as possible in the next Parliament.

2.14 Giving to Overseas Charities

Following a judgement in the European Court of Justice in January 2009, the tax reliefs available to UK charities and their donors are to be extended to similar organisations in the European Economic Area (EU countries as well as Norway and Iceland). To qualify, such organisations will have to be equivalent to UK charities or community amateur sports clubs (“CASC”).

This proposal would allow qualifying organisations in the EEA to claim UK charity tax reliefs and exemptions including exemption from income, capital gains, corporation and inheritance tax as well as VAT and stamp duty reliefs. A UK taxpayer would similarly be able to claim Gift Aid relief on gifts to such organisations.

A number of other changes are also being introduced at the same time. These will;

- Align the definition of charity across all charity tax reliefs and exemptions. To be accepted as charitable, an organisation will have to be set up for charitable purposes only, as set out in the Charities Acts;
- Limit the scope for fraudulent claims by applying a fit and proper person test to charity directors or trustees, CASC officials and also anyone who in practice controls the financial aspects of running the charity;
- Remove inconsistencies in the current rules and ensure the rules work for both UK and non-UK organisations, including:
 - Requiring Payroll Giving donations to be applied for charitable purposes;
 - Obliging UK charities that pay non-UK recipients to take reasonable steps to ensure that the monies are used for genuine charitable purposes; and
 - Applying the same rules on recovering tax from charities where the individual has not paid enough tax to cover the Gift Aid donation whether the donor is UK resident or not
- Ensure that HMRC can maintain a cost efficient service to charities by restricting the number of in-year repayments that may be claimed by a charity and the amount of each claim. Currently a charity may make an unlimited number of claims. New forms will be introduced for making a claim.

The new rules will have effect some time in 2010/11 subject to a commencement order, though a few changes take effect immediately. Although the new definition of charity will apply to Gift Aid donations from 6 April 2010, it would probably be prudent to await at least the publication of a Finance Bill containing this provision.

This will be legislated in a Finance Bill introduced in the next Parliament.

2.15 Guardianship of Children

With effect from 6 April 2010, individuals who care for one or more children placed with them under a special guardianship order or a residence order will be able to receive certain payments made to them exempt from income tax.

This will be the case where the child or children are not the biological children or step-children of the guardian. The new measures will be similar to the current tax exemptions in relation to payments made to adopters.

These new exemptions will only apply to qualifying payments made by the child's parents or on behalf of the local authority to qualifying carers.

2.16 Remittance Basis – subsidiaries of non resident companies

From 6 April 2008 individuals domiciled outside of the UK, or not ordinarily resident in the UK, have been subject to a significantly revised regime detailing when and how they can benefit from the remittance basis of taxation on their overseas income and gains.

The remittance basis rules ensure that an individual is taxed in the UK when their foreign income or gains are remitted to the UK by or for the benefit of any "relevant person".

Finance Bill 2010 will introduce a further minor amendment to the remittance basis, effective from 6 April 2010. This will make it clear that the definition of a relevant person includes subsidiaries of non-resident companies which would be defined as close companies if they were resident in the UK where other relevant persons (such as the taxpayer, their spouse or civil partner, children and minor grandchildren) are participators.

2.17 Trusts for Asbestos Victims

As a part of arrangements with creditors, certain companies set up trust funds specifically to provide compensation for the benefit of individuals with asbestos related conditions.

It is intended these trusts be exempted from the income, capital gains and inheritance tax normally paid by trustees. This is similar to the existing exemption for charitable trusts and more generous than the reliefs available to other disabled persons. If enacted, these exemptions would apply to all trusts set up on or before 23 March 2010 and offer retrospective relief from 6 April 2006.

This is to be included in a Finance Bill to be introduced in the next Parliament.

2.18 Settlor-Interested Trusts

The trustees of a settlor-interested discretionary trust pay tax at the highest trust rates.

This income is then taxable on the settlor, who receives a credit for the tax paid by the trustees. In some cases this can result in the settlor receiving a tax repayment, which will become more common with the introduction of the 50% rate for trusts from 6 April 2010.

Repayments of income tax to settlors which relate to tax charged after 5 April 2010 will have to be repaid to the trustees and not retained by the settlor. Legislation will also be amended to ensure these payments are disregarded for Inheritance Tax purposes.

This will be legislated in a Finance Bill introduced in the next Parliament.

2.19 Restrictions on Tax Relief for Pensions

As previously announced, Finance Bill 2010 will introduce legislation to recover tax relief above the basic rate on pension contributions for certain high earners.

From 6 April 2011 taxpayers with gross income above £180,000 will have to pay a new tax charge designed to restrict their tax relief on pension contributions (including those funded by an employer) to the basic rate of tax. For taxpayers with gross income above £150,000 but below £180,000 a taper will apply so that relief will be reduced by 1% for every £1,000 of gross income above the threshold. However relief will not be restricted where pre-tax income is below £130,000 (excluding employer contributions).

This high income excess relief charge will be collected through their Self Assessment Tax Return, with payment arising on the normal due dates of 31 January and possibly 31 July 2012.

For this purpose gross income includes the value of any pension contribution funded by an employer, and is calculated before the deduction of personal pension contributions or charitable donations.

Finance Act 2009 introduced anti-forestalling measures that imposed a similar special annual allowance charge for 2009/10 and 2010/11 where high earners increased their annual pension savings above £20,000 (or £30,000 in certain circumstances)

2.20 Levels of Pension Allowances

A Treasury Order was laid before Parliament on Budget Day to confirm that the following pension limits will continue to apply up to 5 April 2016:

- The Lifetime Allowance (to be applied to total pension savings on the crystallisation of benefits) of £1.8 million
- The Annual Allowance (to be applied to total pension contributions in a Pension Input Period) of £255,000.

Amounts over these limits may be subject to tax at 25% or 55% (for lump sums) for the Lifetime Allowance, or 40% or 50% for the Annual Allowance.

3. Capital Gains Tax

3.1 Entrepreneurs Relief

Legislation will be included in the Finance Bill 2010 to double the CGT Entrepreneurs' Relief lifetime limit to £2 million. This will affect individuals and trustees of settlements where the disposal takes place after 6 April 2010 and means that for qualifying gains of up to £2 million, the effective rate of CGT is 10%.

Individuals and trustees contemplating an exchange of contracts on a sale of their business or trading company before 6 April 2010 might want to reconsider the timing of their transaction and should take urgent advice in this regard.

This proposal is to be included in the Finance Bill so should take effect on 6 April.

3.2 Transactions in Securities

Perhaps the most venerable piece of anti-avoidance legislation in the tax code – S760 - is to be replaced with clearer legislation targeted at arrangements involving tax avoidance. Whilst being limited to transactions with a tax avoidance purpose it will additionally apply to certain transactions involving close companies. The legislation will apply to transactions where the tax advantage is obtained on or after 24 March 2010.

The current legislation provides for avoidance to be countered where a person receives an abnormal dividend with a view to obtaining a tax advantage. The legislation covered listed as well as non-listed companies, but the proposed legislation will only apply to close companies including overseas companies.

The new legislation will deal with avoidance in the same way as existing legislation, but will clarify how a tax advantage is to be quantified. The legislation will restructure the scope with a wider range of companies being covered, but the test of whether an income tax advantage has been obtained and a new exemption covering changes in ownership should result in fewer persons needing to consider whether the rules apply to them. Old rules regarding dividend stripping are to be scrapped as the avoidance opportunities have been removed.

4. Corporation and Business Tax

4.1 Rates

The main rate of Corporation Tax will remain at the current rate of 28%.

The Small Companies Rate will remain at 21% for 2010/11. The planned rise to 22%, which was previously expected to have effect from 1 April 2010, was not mentioned in this year's Budget.

The thresholds for the small companies' rate and the main rate remain at £300,000 and £1,500,000 respectively.

The marginal rate of corporation tax applying to profits between £300,000 and £1,500,000 will continue to be 29.75%.

There are separate rules governing "ring fence profits", which primarily relate to companies in the oil industry.

For details of rates and thresholds applicable in 2010/11, please see tables.

4.2 Annual Investment Allowance

The Annual Investment Allowance (AIA) provides for expenditure by a business on certain plant and machinery capital equipment to be written off in full as a tax deductible expense.

The current maximum of £50,000 will be doubled to £100,000 with effect from 1 April 2010 (where businesses are chargeable to corporation tax) and 6 April 2010 (where businesses are chargeable to income tax).

The qualifying taxpayers are:

- Any individuals carrying on a qualifying activity (which includes trades, professions, vocations, ordinary property businesses and individuals having an employment or office);
- Any partnership consisting only of individuals; and
- Any company, subject to the fact that groups will only be entitled to a single allowance per group.

The AIA will be pro-rated if the chargeable period is more or less than a year; similarly, proportionate allowances are available where the accounting period that spans the financial year end.

New anti-tax avoidance provisions are being introduced as of 24 March 2010 restricting property loss relief against general income to the extent that the loss is attributable to the AIA.

Where a business spends more than £100,000 in any chargeable period any additional expenditure will be dealt within the normal capital allowances regime.

This proposal is to be included in the Finance Bill.

4.3 Capital Allowances for Eco-Technology

The Enhanced Capital Allowance regime provides for expenditure by a business on certain qualifying plant and machinery capital equipment to be written off in full as a tax deductible expense.

The plant and machinery has to be energy saving and/or water efficient (environmentally beneficial) that either reduce energy consumption, save water or improve water quality.

The effective date will be announced later in the year by a Treasury Order.

New qualifying technologies include permanent magnet synchronous motors and biomass fired warm air heaters; but compact heat exchangers and liquid pressure amplification will be removed and the criteria for taps and showers will be tightened.

4.4 Zero-emission Goods Vehicles

Expenditure by a business on new and unused zero-emission goods vehicles will attract 100% first year allowance if the vehicle is acquired after 1 April 2010 by a company (6 April 2010 for unincorporated businesses). This incentive is expected to remain available for five years.

The vehicles must not produce any carbon emissions and be designed primarily to convey goods. There are restrictions covering vehicles acquired for subsequent leasing.

As this incentive represents State Aid under EU rules, there would be further EU-imposed restrictions relating to the solvency of the taxpayer, their industry sector and capping the maximum allowance over the five-year period at €85 million.

4.5 Sale of Lessor Companies

The sale of lessor company legislation introduces taxation symmetry between buying and selling groups so that timing benefits are recouped.

Draft legislation published with the Pre-Budget report and effective from 9 December 2009 will be amended to include elections covering technical aspects where the lessor company is owned by a controlled foreign company or "leases ships into tonnage tax".

Other changes cover lessor companies owned by consortia. These changes would be effective from 24 March 2010.

4.6 Video Games

It was announced that tax relief, similar to that available to the film industry, will be introduced for the UK video games industry, subject to consultation and state aid approval from the European Commission.

4.7 Impact of Accounting Standards

Generally, all accounting standards are now driven by the International Accounting Standards Board (IASB) and then adopted by the UK Accounting Standards Board.

The IASB are currently working towards new financial reporting standards for financial instruments – IAS39. Normally, it would be expected that UK tax legislation caters for these new standards by updating its loan relationship rules that cover the taxation of financial instruments on companies. These changes will be implemented by Regulation, rather than by primary legislation.

The revisions would amend UK tax law so that Companies implementing changes in accounting standards whether introduced at UK or International level are subject to UK corporation tax rules. Whenever revisions come into effect, they would apply to an earlier accounting period should the change in accounting treatment affect that earlier period.

4.8 Consortium Relief

It was announced that the consortium relief rules are to be amended so that EU and EEA resident companies that form part of UK consortia will be permitted to pass the losses of those consortia to their UK resident subsidiaries. At the same time, the rules are to be tightened to ensure that consortium relief is only given in the correct proportion of the member company's involvement.

4.9 Distributions

HMRC have had a longstanding practice of treating all UK distributions as being of an income nature subject to some specific exceptions. Changes in 2005 have made this policy impossible to continue. Although most income distributions received by companies were exempted from corporation tax in Budget 2009, current legislation excludes from exempt distributions those that are capital in nature.

The treatment of capital distributions will therefore be clarified to enable HMRC to revert to its previous policy where only specified distributions will be regarded as capital. This change will have retrospective effect unless companies elect for this not to apply.

This will be legislated in a Finance Bill introduced in the next Parliament.

4.10 Worldwide Debt Cap

Following consultation, some changes will be made to the "worldwide debt" cap legislation. Draft legislation was published at the time of the Pre-Budget Report last year.

The worldwide debt cap was intended to prevent excessive debt funding of UK companies. The changes will apply to periods of account for the worldwide group beginning on or after 1 January 2010.

The proposed changes are:

- Where a group includes securitisation companies then the financing costs of the group as a whole are calculated excluding the securitisation companies.
- Companies involved in capital market arrangements that incur an additional corporation tax liability as a result of these rules will be able to transfer the tax liability to another group company
- Long-term arrangements which give rise to an interest-like return are to be taken into account when calculating the cap even if they do not have the legal form of loans
- An LLP cannot be the ultimate parent of a group of companies for debt cap purposes

This will be legislated in a Finance Bill introduced in the next Parliament.

4.11 Double Tax Relief

Three areas have been identified where relief for foreign tax paid may be given under the double tax relief (DTR) or manufactured overseas dividend (MOD) rules when the taxpayer has not suffered the foreign tax cost.

The three areas are:

- Deduction of the foreign tax from taxable income when no tax credit is claimed for the foreign tax paid and only the net income is brought into the tax computation in the first place.

- The targeted DTR anti-avoidance rule, where the foreign tax is not paid by the taxpayer claiming credit, or where steps are taken to increase a claim before or after a prescribed scheme has been implemented.
- Financial traders using the MOD rules to offset the foreign tax against the tax due on an MOD and not including the gross amount of foreign income as taxable income.

The 2010 Finance Bill will include legislation to amend the first two points above so that DTR for foreign tax paid is only given when the foreign tax cost has been borne. Assuming that the Finance Bill is passed, this legislation will have effect for foreign tax paid on or after 1 April 2010 and 6 April 2010, for corporation tax and income tax & capital gains tax respectively.

The third point above is being amended by regulations laid today (24 March 2010) and will have effect for MODs paid 21 days after 24 March 2010.

4.12 Interest on Late Payment

Interest on the late payment of, and on repayment of, corporation tax and petroleum revenue tax will be brought within the harmonised interest regime.

The harmonised interest regime will ensure that a single set of rules will apply to all taxes administered by HM Revenue & Customs. Interest on quarterly instalment payments of corporation tax remains unchanged and is not part of the harmonised interest regime.

This will be legislated in a Finance Bill introduced in the next Parliament but the effective dates will be included in Treasury Orders which will specify commencement dates.

4.13 Bank Payroll Tax

As announced in the 2009 Pre-Budget Report, Finance Bill 2010 will introduce a new tax (BPT), payable by banks and certain financial businesses that pay bonuses in excess of £25,000 to relevant employees between 9 December 2009 and 5 April 2010. The rate of BPT is set at 50% and will be payable on or before 31 August 2010.

The BPT does not affect the employees' personal tax or NIC liabilities, and is not an allowable deduction for tax purposes for the employer.

A number of technical changes have been made to the draft legislation previously published, including:

- Clarification of when a bonus is taken as being awarded
- Narrowing the scope of the definition of a UK resident bank and relevant foreign bank and expanding the list of specific exclusions.
- Confirmation that the BPT will not be payable on bonuses paid to employees who were in the UK for less than 60 days in the 2009/10 tax year.
- Provisions for the charging of penalties and interest on late filing of returns (after 31 August 2010) or payment of the tax.

It is noteworthy that even though this tax has raised £2 billion - substantially more revenue than originally anticipated - no proposals to enhance or extend the scope of this levy have yet been proposed.

4.14 Risk Transfer Arrangements

There is to be consultation on the introduction of a generic, principle-based rule to counter schemes which result in a mismatch between the tax treatment of a loss recognised by one group company and a profit recognised by another group company.

These schemes involve two group companies entering into a loan relationship or derivative contract where one company recognises a tax loss without the other company recognising a taxable profit, and are often referred to as “group mismatch schemes”.

4.15 Hedging

The 2009 Pre Budget Report announced that legislation would be introduced in Finance Bill 2010 to restrict losses arising from over- and under-hedging structures using loan relationships and derivative contracts, so that the risks involved in these structures cannot effectively be transferred to the Exchequer. Subject to the Finance Bill being passed, these provisions will affect accounting periods beginning on or after 1 April 2010.

The Budget announced that the Finance Bill 2010 will additionally include a regulation making power that will enable regulations to be laid to include financial instruments other than loan relationships and derivative contracts within the scope of the risk transfer provisions.

5. Indirect Taxes

5.1 VAT Registration Thresholds

The VAT registration threshold will rise by £2,000 to £70,000 from 1 April 2010. The de-registration limit rises similarly to £68,000.

The registration and de-registration limits for acquisitions from other EU member states will also be increased from £68,000 to £70,000.

5.2 Private Use of Business Assets

In January 2010 HMRC abolished the "Lennartz" method of accounting for VAT on the non-business use of a goods or services but allowed it to continue for private use. The Budget change legislates for this change and sets out measures to prevent taxpayers obtaining an advantage by attempting to unravel existing Lennartz schemes. The new rules will introduce an adjustment similar to the Capital Goods Scheme for changes in between business and non business use.

5.3 Fuel Scale

Whenever a business funds private motoring by subsidising fuel, it must account for VAT fuel scale charges, that is, output tax.

The revised scale charges are based on the level of CO² emissions, and range from a quarterly charge of £141 (VAT inclusive) on a car with CO² emissions of 120gms/km or below to £496 (VAT inclusive) for a car with emissions of 230gms/km or above.

HMRC have published tables showing the revised scale charges for a 12 month, three month and one month accounting period.

Businesses must use the new scales from the start of their first accounting period beginning on or after 1 May 2010. For details of the scales please see tables.

5.4 Emissions Allowances

With effect from 1 November 2010, the zero VAT rate for supplies of emissions allowances will be withdrawn. It will be replaced by a reverse charge treatment. This will require any VAT registered business purchasing emissions allowances to account for and pay the VAT chargeable instead of the supplier.

5.5 Power

There is to be an extension of the rules concerning the application of the reverse charge by UK VAT registered customers on supplies of natural gas they receive from suppliers established abroad.

With effect from 1 January 2011, the scope of the existing rules will be extended to cover all supplies made through a natural gas pipeline particularly heat and cooling supplied through networks.

Additionally, the relief from VAT at importation is to be extended to all natural gas imported via a network (including liquefied natural gas by tanker).

5.6 Aircraft

The definition of aircraft that can be supplied at the zero rate of VAT is to change from being based on weight and usage to being based on the status of the customer.

With effect from 1 September 2010, supplies of aircraft will be zero-rated only where used by airlines operating for reward chiefly on international routes.

5.7 Postal Services

With effect from 31 January 2011 some supplies made by the Royal Mail will become subject to VAT at 17.5%, a change from the current VAT exemption. The supplies on which VAT will be chargeable are those which are not subject to price and regulatory control and where the price has been individually negotiated. Examples include business collection charges, unaddressed mail, parcel force and some special delivery services. Excluded from the change and still VAT exempt will be normal first and second class mail, including metered mail.

6. Stamp Duties

6.1 SDLT on Larger Homes

Legislation will be included in the Finance Bill 2010 to increase the rate of Stamp Duty Land Tax to 5% on residential properties where the consideration exceeds £1 million. This increased rate will apply to sales where completion takes place on or after 6 April 2011.

6.2 SDLT for First Time Buyers

Legislation will be included in the Finance Bill 2010 to provide relief from SDLT on residential properties where the consideration is between £125,000 and £250,000. This increased limit applies to completions taking place between 25 March 2010 and 25 March 2012 where the purchasers are first time buyers and will be occupying the property as their only or main home.

There is concern that the definition of "first time buyer" may be extremely restrictive however.

6.3 SDLT Avoidance

Amongst the schemes marketed to reduce the cost of SDLT is one involving partnerships. This is to be stopped by Finance Bill 2010 which will extend the existing rules to prevent their exploitation through artificially reducing the amount of chargeable consideration on which SDLT is due.

The measures apply to "notional land transactions" with an effective date on or after 24 March 2010 and disapply the special partnership rules. There are transitional rules which mean any scheme transactions entered into before 24 March 2010 will come under the old rules.

6.4 Overpayments of Tax

The procedure for error or mistake claims for income, capital gains and corporation tax was amended in the last Budget so that overpayments can be claimed where there is no other statutory route. This is now to be extended to SDLT and PRT; draft legislation for the SDLT element has already been published.

It is expected the measure will come into effect for claims on or after 1 April 2011 when the time limit for making a claim will also reduce to four years. However, repayments will not be made where the SDLT return followed the general practice at the time it was made.

7. Compliance

7.1 Time to Pay

It was confirmed that HMRC will continue to offer time to pay to all viable businesses that are struggling to meet their tax payment obligations. Since November 2008 when it was introduced, some 200,000 businesses have received more time to pay tax liabilities of some £5.2 billion.

Where the arrears of tax amount to £1 million or more, HMRC will in future require a business review to support the application

7.2 Disclosure of Tax Schemes (DOTAS)

Measures will be introduced in the Finance Bill 2010 and also through regulations to tighten DOTAS and provide for increased penalties for non-compliance.

The new and amended provisions will include:

- Introduce a new “trigger” point for the disclosure of actively marketed tax schemes;
- Introduce a requirement for a person who introduces a client to a notifiable scheme to provide HMRC with the name and address of the promoter of the scheme;
- Increase in the penalties for failure to comply with a disclosure obligation; and
- Introduce a new requirement for promoters to provide periodic information about clients who implement a notifiable scheme.

It is expected that the above will come into force sometime in the autumn of 2010.

7.3 Hidden Economy

It was announced that the initial findings of the Hidden Economy Advisory Group are that there is currently no clear route for those with undeclared tax to disclose their liabilities and establish their position. In view of this, HMRC are to build upon the success of the current and past disclosure opportunities to enable those concerned to leave the hidden economy.

7.4 Penalties for Late Returns

Measures will be introduced to complete the reform of the penalty regime for late filing of tax returns and late payment of tax. Reform has already happened for income, corporation, inheritance and other direct taxes. The latest reform is for other taxes, the most important of which is VAT.

In order to encourage timely filing and payment of tax the measures will introduce an escalating series of penalties depending on the number of failures within a set penalty period. Further penalties will arise if there is a prolonged delay in filing returns or paying the tax due.

The Government aims to include the required legislation in a Finance Bill to be introduced as soon as possible in the next Parliament.

7.5 Penalties for Undeclared Offshore Items

The amount of tax-geared penalties for undisclosed income or capital gains that are linked to offshore items are to be increased. The level of penalty is normally determined by the taxpayer's "culpability" and the quality of disclosure. Whilst the mechanism of the penalty framework will remain the same the maximum level of the percentage used to determine the tax-geared penalty will be determined with reference to the jurisdiction in which the non-compliance arises.

The maximum tax geared penalty will be 200% of the tax in the case where the jurisdiction has not concluded an Exchange of Information Agreement with the UK.

It is expected that the new penalty framework will apply to tax periods commencing on or after 1 April 2011.

7.6 Security for PAYE

Legislation will be introduced in Finance Act 2010 to allow HMRC to require financial security from employers where amounts due under PAYE or NIC obligations are seriously at risk. HMRC are to have discretion over the amount of the security.

There are already similar provisions in existence where HMRC believe that VAT revenue is at risk.

The measure will require regulations to be made and the intention is that the operative date will be 6 April 2011.

8. Miscellaneous

8.1 Inheritance Tax

In the 2009 Pre-Budget Report, it was announced that the nil rate band for 2010/11 would not increase as advised in FA2007 and would instead be frozen at the 2009/10 level of £325,000.

Legislation will now be introduced into the Finance Bill 2010 to extend this 'frozen' nil rate band for the next five years, setting the threshold at £325,000 from 6 April 2010 until the end of the tax year 2014/15.

The rate of Inheritance Tax remains at 40% on death estates and 20% for chargeable lifetime transfers.

HM Revenue & Customs have also announced that over the summer of 2010 they will examine the possibility of bringing inheritance tax into the Disclosure of Tax Avoidance Schemes (DOTAS) regime.

8.2 Landline Duty

With effect from 1 October 2010, owners of local loops are to pay a fixed duty of 50p per month for each telephone landline.

Local loops are the physical circuits that connect a network termination point to a public electronic communications network.

It is anticipated that the cost will be passed on to wholesalers and end-users.

8.3 Insurance Premium Tax

The changes to the legislation announced in the 2009 Pre-Budget Report to counteract the splitting of premiums into a taxable insurance contract and a separate contract for fees or commission (the relevant contract) are to be refined following further consultation with industry representatives.

Relevant contracts entered into on or after 24 March 2010 will be treated as subject to Insurance Premium Tax where the following conditions are met:

- The insured is an individual and enters into the taxable insurance contract in a personal capacity.
- The insured is required to enter into the relevant contract by, or would be unlikely to enter into it without also entering into, the taxable insurance contract.
- The amount charged, or the other terms on which services are to be provided to the insured, under the relevant contract are not open to negotiation by the insured.
- The amount charged to the insured under the taxable insurance contract is arrived at without a comprehensive risk assessment of the insured and his personal circumstances.

This legislation will not apply to insurance provided to businesses at the current time, but the legislation will include powers to enable the application to be extended by secondary legislation.

8.4 Business Rates Relief

The Chancellor announced that small businesses in England whose premises have a rateable value of up to £6,000 will pay no business rates for one year from October 2010, and that those whose premises have a rateable value of up to £12,000 will receive significant reductions.

This will be achieved by a temporary increase in small business rate relief and the rate relief taper respectively, and will need to be ratified by the new Parliament later in the year.