These notes refer to the Finance Act 2009 (c.10)
which received Royal Assent on 21 July 2009

FINANCE ACT 2009

EXPLANATORY NOTES

INTRODUCTION

1. These notes relate to the Finance Act 2009 that received Royal Assent on 21st July 2009. They have been prepared by HM Revenue and Customs in partnership with HM Treasury in order to assist the reader in understanding the Act. They do not form part of the Act and have not been endorsed by Parliament.

2. The notes need to be read in conjunction with the Act. They are not, and are not meant to be, a comprehensive description of the Act. So, where a section or part of a section does not seem to require any explanation or comment, none is given.

3. The Act is divided into nine parts:

   (1) Charges, rates, allowances, etc

   (2) Income tax, corporation tax and capital gains tax

   (3) Pensions

   (4) Value Added Tax

   (5) Stamp taxes

   (6) Oil

   (7) Administration

   (8) Miscellaneous

   (9) Final Provisions

   The Schedules follow the sections on the Act.

4. Terms used in the Act are explained in these notes where they first appear. Hansard references are provided at the end of the notes.

SECTION 1: INCOME TAX: CHARGE AND MAIN RATES FOR 2009-10

SUMMARY

1. Section 1 imposes the income tax charge for 2009-10 and sets the basic rate of income tax at 20 per cent and the higher rate at 40 per cent.

DETAILS OF THE SECTION

2. Subsection (1) imposes the income tax charge for 2009-10.

3. Subsection (2)(a) sets the basic rate of income tax at 20 per cent.

4. Subsection (2)(b) sets the higher rate of income tax at 40 per cent.

BACKGROUND NOTE

5. Income tax is an annual tax re-imposed each year by Parliament (even if the proposed rates are the same as for the previous year). The table below sets out the main rates and income bands for 2008-09 and the proposed main rates and income bands for 2009-10:

	2008-09	2009-10
Basic rate	£0 - £34,800 at 20 per cent	£0 - £37,400 at 20 per cent
Higher rate	Over £34,800 at 40 per cent	Over £37,400 at 40 per cent

The basic rate limit of £37,400 as identified in the table above is set for 2009-10 by section 2 of this Act.

SECTION 2: INCOME TAX: BASIC RATE LIMIT FOR 2009-10

SUMMARY

1. Section 2 sets the basic rate limit for income tax at £37,400 for 2009-10.

DETAILS OF THE SECTION

2. Subsection (1) replaces the amount currently in section 10(5) of the Income Tax Act 2007 (ITA) to set the basic rate limit at £37,400.

3. Subsection (2) disapplies the requirement under section 21 of ITA to index the basic rate limit for the 2009-10 tax year only.

BACKGROUND NOTE

4. An individual's taxable income up to the basic rate limit is liable to income tax at the basic rate of income tax. An individual's taxable income above the basic rate limit is liable to income tax at the higher rate of income tax.

5. The provisions in ITA which provide for the basic rate of income tax also provide for the amount, unless Parliament determines otherwise, to be increased annually by indexation. HM Treasury order of 24 November 2008 (2008 N^{o}. 3023) which specified the indexed amount for the 2009-10 tax year, is overridden by this section.

6. The table below sets out the amounts of the basic rate limit for 2008-09, the amount specified by order for 2009-10 and the amount specified by this section for 2009-10:

2008-09	2009-10 by Treasury order	2009-10 by this section
£34,800	£36,600	£37,400

7. The effect of this section is to override the amount specified by order for the basic rate limit and to set it at an amount £800 greater than the indexed increase.

SECTION 3: INCOME TAX: PERSONAL ALLOWANCE FOR 2009-10 FOR THOSE AGED UNDER 65

SUMMARY

1. Section 3 sets the personal allowance for income tax at £6,475 for 2009-10.

DETAILS OF THE SECTION

2. Subsection (1)(a) replaces the amount currently in section 35 of the Income Tax Act 2007 (ITA) to set the personal allowance for those under 65 at £6,475.

3. Subsection (1)(b) replaces the amount in section 257 of the Income and Corporation Taxes Act 1988 (ICTA) to set the personal allowance for non-resident Commonwealth citizens aged under 65 at £6,475.

4. Subsection (2)(a) disapplies the requirement under section 57 of ITA to index the basic level of personal allowance in section 35 of ITA for the 2009-10 tax year only.

5. Subsection (2)(b) disapplies the requirement under section 257C of ICTA to index the basic level of personal allowance in section 257(1) of ICTA for the 2009-10 tax year only.

BACKGROUND NOTE

6. Individuals, who meet the conditions set out in section 35 of ITA, are entitled to a personal allowance to be set against their income.

7. The provisions in ITA which provide for a personal allowance also provide for the amount, unless Parliament determines otherwise, to be increased annually by indexation. The HM Treasury order of 24 November 2008 (2008 N^{o}. 3023) which specified the indexed amount for 2009-10 tax year, is overridden by this section.

8. The table below sets out the amounts of the personal allowance for those aged under 65 for 2008-09 and the amount specified by this section for 2009-10:

2008-09	2009-10 by this section
£6,035	£6,475

9. The effect of this section is to override the amount specified by order for the amount of the personal allowance for individuals aged under 65 and set it at an amount £130 greater than the indexed increase.

10. United Kingdom personal allowances are available for non-resident Commonwealth citizens. Section 5 of and Schedule 1 to this Act remove these allowances from 2010-11.

11. The provisions in ICTA which provide for a personal allowance for non-resident Commonwealth citizens also provide for the amount, unless Parliament determines otherwise, to be increased annually by indexation. The HM Treasury order of 24 November 2008 (2008 N^{o}. 3024) which specified the indexed amount for 2009-10 tax year, is overridden by this section.

12. The effect of this section is to override the amount specified by order for the amount of the personal allowance available to non-resident Commonwealth citizens aged under 65 and set it at an amount £130 greater than the indexed increase.

SECTION 4: INCOME TAX: REDUCTION OF PERSONAL ALLOWANCE FOR INDIVIDUALS WITH INCOME EXCEEDING £100,000

SUMMARY

1. Section 4 applies reductions from 2010-11 to the amount of an individual's personal allowance, where their income exceeds £100,000.

DETAILS OF THE SECTION

2. Subsection (1) renumbers the existing provisions in section 35 of the Income Tax Act 2007 (ITA) as new section 35(1) and provides the personal allowance for those aged under 65 including the amount, which remain unchanged.

3. New section 35(2) provides that where an individual's adjusted net income exceeds £100,000 their personal allowance is by reduced one-half of the excess.

4. New section 35(3) provides that where the result of the application of new section 35(2) is not a multiple of £1, then the amount of the personal allowance is rounded up to the nearest £1.

5. New section 35(4) provides a signpost to the meaning of adjusted net income in section 58 of ITA.

6. Subsection (2) inserts new provisions into section 36 and section 37 of ITA which provide the higher amounts of personal allowance for those aged 65 to 74 and aged 75 and over. The higher amounts of personal allowance are reduced where an individual's adjusted net income exceeds an income limit. Section 36(2)(b) and section 37(2)(b) of ITA currently provide for these higher levels of personal allowance to be reduced by one-half of the excess, but no lower than the basic level of personal allowance for someone under 65. The new provisions ensure an individual's personal allowance, where they have an adjusted net income over £100,000, will be linked to the level of the personal allowance they would be entitled to if they were aged under 65.

7. Subsection (3) amends section 57 of ITA, the provision for indexation of the personal allowances following the movement of current section 35 of ITA to become new section 35(1).

8. Subsection (4) provides that the amendments made by subsection (1) and subsection (2) of this section are effective from 2010-11.

9. Subsection (5) provides that the amendment made by subsection (3) of this section is effective from 2011-12.

BACKGROUND NOTE

10. Individuals, who meet the conditions set out in section 35 of ITA, are entitled to a personal allowance to be set against their income. In 2009-10, the personal allowance for individuals aged below 65 is £6,475, £9,490 for those aged 65 to 74 and £9,640 for those aged 75 and over.

11. From 2010-11, where an individual's adjusted net income exceeds £100,000 their personal allowance will be reduced by one-half of the excess. For example, in 2010-11 an individual with an adjusted net income of £100,002 will have their personal allowance reduced by £1.

12. The calculation of an individual's adjusted net income for the purposes of these new income-related reductions to personal allowances is provided for by section 58 of ITA; it is the same measure of income that is used for the calculation of existing income-related reductions to personal allowances for those aged between 65 and 74, and those aged 75 and over. Using adjusted net income as the measure of an individual's income will provide consistency across all the reductions that will apply to personal allowances from 2010-11.

SECTION 5 SCHEDULE 1: ABOLITION OF PERSONAL ALLOWANCES FOR NON-RESIDENTS

SUMMARY

1. Section 5 and Schedule 1 provide for the withdrawal of personal allowances and reliefs from income tax for individuals not resident in the UK who have entitlement to those allowances or reliefs solely because they are Commonwealth citizens.

DETAILS OF THE SCHEDULE

2. Paragraph 1 sets out the sections in the Income and Corporation Taxes Act 1988 (ICTA) which are to be repealed in full. These cover, respectively, general provisions relating to basic and age-related personal allowances, provisions on married couple's allowance and blind person's allowance, provisions on payments securing annuities and the provision of allowances for non-resident individuals. Paragraphs 1(a) to (h) currently only have relevance to what is left of section 278 of ICTA, which is to be repealed by paragraph 1(i). The qualifying conditions for UK personal allowances and reliefs from income tax for non-resident persons will continue to apply as set out in section 56(3) of the Income Tax Act 2007 (ITA). The provisions for payments securing annuities continue through section 459 of ITA.

3. Paragraph 2 provides for a number of consequential amendments required to section 266 of ICTA (life assurance premiums) as a result of the changes made in paragraph 1.

4. Sub-paragraph (3) introduces new section 266(1A), which defines an eligible individual as either being resident in the UK, or, if not resident, meeting the conditions set out in section 56(3) of ITA. These conditions are that, at any time in a tax year, an individual:

    a. is resident in the Isle of Man or the Channel Islands;
    b. has previously resided in the United Kingdom and is resident abroad for the sake of the health of:
        i. the individual; or
        ii. a member of the individual's family who is resident with the individual;
    c. is a person who is or has been employed in the service of the Crown;

    d. is employed in the service of any territory under Her Majesty's protection;
    e. is employed in the service of a missionary society; or
    f. is a person whose late spouse or late civil partner was employed in the service of the Crown.

5. Section 266 of ICTA will now no longer be available to any individual who does not also meet the conditions set out in section 266(1A).

6. Sub-paragraphs (4)-(6) remove references to section 266(7) of ICTA which relate to payments to a trade union or a police organisation. These provisions continue through sections 457 and 458 of ITA.

7. Sub-paragraph 7 removes the reference to section 278 (personal allowances for non-residents) and introduces a reference to new section 266(1A).

8. Paragraph 3 provides for a number of consequential amendments required to 274 of ICTA as a result of the changes made in paragraph 1 and for changes to section 266 of ICTA made in paragraph 2. Subparagraphs (2), (3)(b) and (5) each omit the wording of 'other sum' or 'sums' because section 274 will apply only to life assurance premiums and to no other payments (specifically, it will not apply to the sum currently referred to in section 266(7) of ICTA). Sub-paragraph 3(c) further sets out the current rate of relief on qualifying life assurance premiums at 12.5 per cent, previously set out in section 274(3)(a). Sub-paragraph 4 repeals section 274(3) which becomes otiose.

9. Sub-paragraphs 3(a) and 6 remove references to section 273 of ICTA (Payments securing widow's and children's annuities) which is to be repealed. The provisions continue through section 459 of ITA.

10. Paragraph 4 omits a reference to section 266(7) of ICTA in Schedule 14 of that Act as that subsection is itself now omitted by this section/Schedule.

11. Paragraph 5 provides for a number of amendments in various Taxes Acts needed as a result of repealing certain sections in ICTA provided for in paragraphs 1 to 3 of this Schedule.

12. Paragraph 6 sets out the effective commencement of the change.

BACKGROUND NOTE

13. Generally, individuals who are not resident in the UK have no entitlement to claim UK personal allowances or reliefs from income tax. However there are a number of conditions, either set out in the Taxes Acts or under Double Taxation Agreements (DTA) supported by Statutory Instrument, which allow people who are not resident and who are subject to income tax in the UK to claim personal allowances and reliefs.

14. Previously, there was an entitlement for some individuals to claim purely by virtue of being a Commonwealth citizen but by meeting no other condition. Commonwealth citizens will no longer qualify for personal allowances, married couple's allowance, blind person's allowance and relief for life assurance premiums by reference to their Commonwealth citizenship status alone. They may, of course, continue to qualify under the other conditions or through DTA provisions if appropriate.

15. This change will mainly affect 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.

SECTION 6 SCHEDULE 2: ADDITIONAL RATE, DIVIDEND ADDITIONAL RATE, TRUST RATES AND PENSION TAX RATES

SUMMARY

1. Section 6 and Schedule 2 include the provisions for an additional rate of income tax and an additional rate for dividends and consequential amendments including increases to the trust rate and dividend trust rate. There are other consequential amendments including changes to the income tax charges applying to registered pension schemes. From tax year 2010-11 there will be a new additional rate of income tax that will apply to taxable income in excess of £150,000. A new 42.5 per cent dividend additional rate will alternatively apply where dividends form part of an individual's taxable income in excess of £150,000. This will provide three main rates of income tax: the basic rate, the higher rate and the additional rate. There will be three rates of tax applying to dividends: the dividend ordinary rate for dividends otherwise taxable at the basic rate, the dividend upper rate for dividends otherwise taxable at the higher rate and the dividend additional rate for dividends otherwise taxable at the additional rate.

DETAILS OF THE SECTION

2. Subsections (1) and (2) amend section 6 of the Income Tax Act 2007 (ITA) (the basic and higher rate). They add the additional rate to the main rates at which income tax is charged.

3. Subsection (3) adds a reference to the dividend additional rate in section 6 of ITA.

4. Subsection (4) amends section 9 of ITA (the trust rate and dividend trust rate) which sets out the trust and dividend rates that apply to the income of certain trusts (see background note). The trust rate will be increased to 50 per cent from 40 per cent, and the dividend trust rate will be increased to 42.5 per cent from 32.5 per cent.

5. Subsection (5) introduces Schedule 2 to this Act.

6. Subsection (6) provides that the amendments made by this section are effective for 2010-11 and subsequent years.

DETAILS OF THE SCHEDULE

7. Paragraph 2 amends section 6 of ITA (the basic and higher rate) by adding the additional rate to the rates of income tax that are set by Parliament each year.

8. Paragraph 3 amends section 8 of ITA (the dividend ordinary rate and dividend upper rate). It adds the dividend additional rate to the rates of tax at which dividend income is charged.

9. Paragraph 4(2) amends section 10(3) of ITA, which provides that an individual's income is charged to tax at the higher rate where it exceeds the basic rate limit. The amendment provides that an individual's income is charged to tax at the higher rate up to the higher rate limit.

10. Paragraph 4(3) inserts a new section 10(3A) into ITA which provides that an individual's income is charged to tax at the additional rate where it exceeds the higher rate limit.

11. Paragraph 4(4) inserts a new section 10(5A) into ITA which provides the amount of the higher rate limit. It is £150,000.

12. Paragraph 4(5) inserts a signpost to the provisions to increase the higher rate limit by gift aid donations and pension contributions where basic rate income tax relief is provided at source.

13. Paragraph 5(2) inserts a new section 13(2A) into ITA which provides that an individual's dividend income is charged to tax at the dividend additional rate where it would otherwise be charged at the additional rate and is not relevant foreign income charged in accordance with section 832 of the Income Tax (Trading and Other Income) Act 2005.

14. Paragraphs 5(3) to 5(5) make amendments to section 13 of ITA consequential to the insertion of new section 13(2A).

15. Paragraph 6 amends section 414(2)(b) of ITA (relief for gifts to charity) to provide that an individual's higher rate limit is increased by the grossed up amount of their gift aid donation.

16. Paragraph 7 provides for a consequential amendment to section 515 of ITA. Section 515 provides for the rate of tax where a charge arises on heritage maintenance settlements under section 512 of ITA. Tax is charged on the difference between the higher rate of income tax for a year and the trust rate. The amendment ensures that the rate of charge will reflect the introduction of the additional rate of tax.

17. Paragraph 8 amends section 989 of ITA (the definitions) consequential to the creation of the additional rate, the dividend additional rate and the higher rate limit.

18. Paragraph 9 amends Schedule 4 to ITA (index of defined expressions) consequential to the creation of the additional rate, the dividend additional rate and the higher rate limit and the move of the basic rate limit from section 20(2) to section 10 of ITA by Finance Act (FA) 2008.

19. Paragraph 11 amends section 192(4) of FA 2004 (relief for pension contributions at source) to provide that an individual's basic rate limit and higher rate limit are increased by the amount of their pension contributions where they receive tax relief at source by making a claim.

20. Paragraph 12 amends section 208 of FA 2004 (unauthorised payments charge) to provide that HM Treasury may by order vary the rate of the unauthorised payments charge, and that different rates can apply in different circumstances. This charge applies to the recipient where a registered pension scheme makes an unauthorised payment. Section 208(6) already provides for the rate of the unauthorised payments charge to be increased or decreased by Treasury Order, but not that different rates can be applied. Section 208(5) provides that the rate of the unauthorised payments charge is 40 per cent of the unauthorised payment.

21. Paragraph 13 amends section 209 of FA 2004 (unauthorised payments surcharge) to provide that HM Treasury may by order vary the rate of the unauthorised payments surcharge and that different rates can apply in different circumstances. This surcharge applies to the recipient where a registered pension scheme makes an unauthorised payment or payments worth more than 25 per cent of the value of the member's rights under the arrangement. Section 209(7) already provides for the rate of the unauthorised payments surcharge to be increased or decreased by Treasury Order. Section 209(6) provides that the rate of the unauthorised payments surcharge is 15 per cent of the surchargable unauthorised payment.

22. Paragraph 14 amends section 215 of FA 2004 (amount of the lifetime allowance charge) to provide that HM Treasury may by order vary the rate of the lifetime allowance charge. This charge applies to the recipient of benefits from registered pension schemes that cause their lifetime allowance to be exceeded. Section 215(2) provides that the rate of the lifetime allowance charge is 55 per cent (in respect of lump sum benefits) or 25 per cent (in respect of pension benefits) of the chargeable amount above the lifetime allowance. The lifetime allowance for the 2009-10 tax year is £1.75 million.

23. Paragraph 15 amends section 227 of FA 2004 (annual allowance charge) to provide that HM Treasury may by order vary the rate of the annual allowance charge. This charge applies to an individual with annual contributions or benefit accruals under a registered pension scheme that exceed the annual allowance. Section 227(4) provides that the rate of the annual allowance charge is 40 per cent of the amount that exceeds the annual allowance. The annual allowance for the 2009-10 tax year is £245,000.

24. Paragraph 16 amends section 240 (amount of scheme sanction charge) to provide that HM Treasury may by order vary the rate and applicable percentage of the scheme sanction charge. This charge applies to the administrator of a registered pension scheme that makes unauthorised payments or transactions (these are known as "scheme chargeable payments"). Section 240(1) provides that the rate of scheme sanction charge is 40 per cent. Section 240(3) provides that there is a deduction from the scheme sanction charge, which is the lesser of 25 per cent of the scheme chargeable payments, or the amount of the unauthorised payment charge paid by the person liable to it under section 208 of FA 2004.

25. Paragraph 17 amends section 242 (de-registration charge) to provide that HM Treasury may by order vary the rate of the de-registration charge. This charge applies to a scheme administrator where the tax registration of a pension scheme is withdrawn. Section 242(4) provides that the rate of the de-registration charge is 40 per cent of the value of the sums and assets held by the pension scheme immediately before de-registration.

26. Paragraph 18 provides that the powers to make regulations varying rates etc in connection with the charges applying to registered pension schemes, which are provided in the amendments to FA 2004 made by paragraphs 12 to 17 of this Schedule, are to be exercised through affirmative resolution procedures before the House of Commons.

27. Paragraph 19 introduces amendments to the Income Tax (Trading and Other Income) Act 2005 (ITTOIA) consequential to the creation of the additional rate, the dividend additional rate and the higher rate limit.

28. Paragraph 20 provides for a consequential amendment to section 640(6) of ITTOIA. Section 640 of ITTOIA sets out the amount of notional tax credit attached to certain capital payments, made by trustees to settlors, that are deemed for tax purposes to be income. A charge to tax on the settlor arises when the capital payment can be matched with undistributed income in the trust. A payment is matched first with the earlier income of the trust. The notional credit is linked to the rate of tax that the trustees have paid on the income with which the capital payment is matched. As the trust rate will increase to 50 per cent for 2010-11 onwards the amendment ensures that the notional tax credit for capital payments matched with undistributed income of 2010-11 onwards is also increased to 50 per cent.

29. Paragraph 21 provides for a consequential amendment to section 685A(3) of ITTOIA (settlor-interested settlements), which provides a notional tax credit at the higher rate for payments made to a non-settlor beneficiary of a settlor interested trust. As the trust rate will increase to 50 per cent for 2010-11 the amendment ensures that such income will in the hands of the beneficiary be treated as having paid tax at this rate.

30. Paragraph 22 amends section 669(3) of ITTOIA (reduction in residuary income: inheritance tax on accrued income) to provide that the reduction in the residuary income can be calculated by reference to the additional rate or dividend additional rate.

31. Paragraph 23 amends Part 2 of Schedule 4 to ITTOIA (index of defined expressions) consequential to the creation of the additional rate and the dividend additional rate.

32. Paragraph 24 amends section 7(5) of F(No.2)A 2005 (charge to income tax on social security pension lump sum) by adding the additional rate to the rates of tax which apply to social security pension lump sum payments. A social security lump sum is taxed at the highest rate of tax that applies on the individual's total income (excluding the lump sum). Presently these rates of tax are the basic rate and higher rate. From 2010-11, these rates of tax will include the additional rate.

33. Paragraph 25(1) provides that the powers conferred by amendments made by this Schedule can be exercised from Royal Assent for the 2010-11 and subsequent tax years. Subject to that, paragraph 25(2) provides that the amendments made by this Schedule have effect for 2010-11 and subsequent tax years.

BACKGROUND NOTE

34. For 2009-10 there are two main rates of income tax: the basic rate and higher rate. The effect of this section and Schedule is to add a further main rate of income tax – the "additional rate". This will be introduced in 2010-11 at a rate of 50 per cent.

35. Separately section 1 to this Act introduces the charge to income tax for 2009-10 and sets the main rates of income tax at 20 per cent for the basic rate and 40 per cent for the higher rate. From 2010-11, the additional rate of income tax will be set along with the other main rates of income tax.

36. The rates of tax which apply to dividends are not set separately each year. Rather they are included in section 8 of ITA. From 2010-11 the new dividend additional rate introduced by the section will be 42.5 per cent and will apply where dividends form part of an individual's taxable income in excess of £150,000.

37. The trust rate of tax is the rate of tax paid by trustees that generally applies to the income of discretionary or accumulation trusts. Trustees are liable to tax on income received at the trust rate of tax, but dividends and other similar income are chargeable at the dividend trust rate.

38. All income paid to the beneficiaries of discretionary or accumulation trusts that are not settlor interested carries a credit at the trust rate, so the payment is treated as if it had been made after the deduction of tax at that rate. Beneficiaries will be able to reclaim tax where the trust rate exceeds the rate of tax at which their income is chargeable. Different rules apply where the trust is settlor interested. The payment is not grossed up but notional tax is provided to the beneficiary.

SECTION 7: CORPORATION TAX: CHARGE AND MAIN RATES FOR FINANCIAL YEAR 2010

SUMMARY

1. Section 7 charges corporation tax for the financial year beginning 1 April 2010 and sets the main rate of corporation tax at 30 per cent on ring fence profits of North Sea oil companies and 28 per cent on the profits of other companies.

DETAILS OF THE SECTION

2. Subsection (2) sets the charge and the main rates of corporation tax for the financial year 2010.

BACKGROUND NOTE

3. The main rate of corporation tax is paid by companies with profits of more than £1,500,000 (the upper profits limit).

4. Where two or more companies are associated with one another, the profits limit is reduced. This is done by dividing the limit by the number of associated companies.

5. Companies with profits from oil extraction and oil rights in the UK and the UK Continental Shelf ('ring fence profits') will continue to be subject to a separate main rate of corporation tax applicable to those ring fenced profits. Profits from activities which are not ring fenced will continue to be charged at the main rate of corporation tax applicable to all other profits.

SECTION 8: SMALL COMPANIES' RATES AND FRACTIONS FOR FINANCIAL YEAR 2009

SUMMARY

1. Section 8 sets the small companies' rate of corporation tax for the financial year beginning 1 April 2009 at 21 per cent for all profits apart from "ring fence profits" of North Sea oil companies and 19 per cent for "ring fence profits". Additionally, it sets the fraction used in calculating marginal small companies' relief from the main rate at 7/400 for all profits apart from "ring fence profits" and 11/400 for "ring fence profits".

DETAILS OF THE SECTION

2. Subsection (1) sets the small companies' rate of corporation tax for the financial year 2009.

3. Subsection (2) sets the fraction used to calculate marginal small companies' relief.

4. Subsection (3) provides that where a company makes a claim for marginal small companies' relief in respect of an accounting period, part of which falls in the financial year 2009, or any subsequent financial year and its profits for that accounting period consist of both ring fence and other profits, then its claim to marginal small companies relief under section 13(2) of the Income and Corporation Taxes Act 1988 (ICTA) is modified appropriately. The conditions for this modification are laid out in subsections (3) to (7) of Section 3 of Finance Act 2007.

BACKGROUND NOTE

5. Companies with profits up to £300,000 pay corporation tax at the small companies' rate.

6. Companies with profits between £300,000 and £1,500,000 (the lower and upper limits) benefit from small companies' marginal relief from the main rate.

7. Marginal relief has the effect of gradually increasing the rate of tax for a company as its profits move from the lower to the upper profits limit.

8. The example below illustrates the effect of marginal relief for a company with taxable non-ring fence profits of £500,000. Its tax liability is calculated as follows:

£500,000 @ 28 per cent	£140,000
minus 7/400 of £1,000,000*	£17,500
Tax payable:	£122,500

* £1,000,000 is the difference between the upper limit and the profit.

9. The example below illustrates the effect of marginal relief for a company with taxable ring fence profits of £500,000. Its tax liability is calculated as follows:

£500,000 @ 30 per cent	£150,000
minus 11/400 of £1,000,000*	£27,500
Tax payable:	£122,500

* £1,000,000 is the difference between the upper limit and the profit.

10. Where two or more companies are associated with one another, the profits limits are divided by the number of associated companies.

SECTION 9 SCHEDULE 3: VAT: EXTENSION OF REDUCED STANDARD RATE AND ANTI-AVOIDANCE PROVISION

SUMMARY

1. Section 9 provides for the standard rate of VAT to revert to 17.5 per cent on 1 January 2010. Section 9 and Schedule 3 introduce a supplementary charge to VAT of 2.5 per cent on certain supplies that span the date on which the standard rate of VAT changes from 15 per cent to 17.5 per cent. They also make minor amendments to the VAT Act 1994 (VATA) provisions about orders effecting a temporary change in the VAT rate.

DETAILS OF THE SECTION

2. Subsection (1) provides that the Value Added Tax (Change of Rate Order) 2008, which temporarily reduces the standard rate of VAT to 15 per cent, will cease to be in force on 1 January 2010.

3. Subsection (2)(a) introduces Parts 1 to 5 of Schedule 3, which provide for a supplementary charge to VAT and govern the circumstances to which it applies.

4. Subsection (2)(b) introduces Part 6 of Schedule 3, which provides for minor amendments to VATA provisions that allow a temporary adjustment to the standard rate of VAT.

DETAILS OF THE SCHEDULE

5. Paragraph 1 introduces a supplementary charge to VAT on supplies of goods and services, subject to the standard rate of VAT, which take place on or after 25 November 2008. The supplementary charge is payable where:

   - the supply spans the date on which the standard rate reverts to 17.5 per cent;
   - the customer is not entitled to recover all of the VAT on the supply; and
   - at least one of the relevant conditions laid down in paragraphs 2 or 3 is met.

6. Paragraph 2 provides that a supply of goods or services spans the date of the VAT rate change where the supplier raises a VAT invoice or receives payment (or both) prior to the VAT rate change and the basic time of supply takes place on or after the date of the change.

7. The supplementary charge will apply where at least one of the following relevant conditions is met:

   - condition A - the supplier and the customer are connected with each other at any time during the period from the date of the supply to the date of the VAT change;
   - condition B - the relevant consideration for the supply and any related supply of goods or services amounts to more than £100,000;

- condition C - the supplier or a person connected with him finances a prepayment by the customer; or

- condition D - the supplier raises a VAT invoice where payment is not due until at least 6 months from the date of the invoice (applies to the issue of a VAT invoice only).

8. Paragraph 3 applies to the supply of the grant of a right to receive goods or services at a discount or free of charge where the grant is supplied before the date of the VAT rate change but the basic time of supply of some or all of the goods or services takes place on or after that date. A right for this purpose includes an option or an interest deriving from a right (or option). The supplementary charge will apply where at least one of the following relevant conditions is met.

- condition A - the grantor and the customer are connected with each other at any time during the period from the date of the supply to the date of the VAT change;

- condition B - the relevant consideration for the grant of the right and any related supply of goods or services amounts to more than £100,000; and

- condition C - the supplier or a person connected with him finances the customer's payment for the grant of the right.

9. Paragraph 4 defines the basic time of supply by reference to section 6 of VATA, as the time that goods are delivered or made available, or that services are performed. This is subject to a special rule for listed supplies in paragraphs 18 and 19 of Schedule 3.

10. Paragraph 5 extends the connected persons condition in paragraphs 2 and 3. It applies where there is a series of supplies of, or a series of grants of, the right to receive, the same or substantially the same, goods or services. In these circumstances, if any supplier or grantor in the series is connected to the customer, the supplementary charge will apply to the supply to the customer.

11. Paragraph 6 defines "relevant consideration" and "related supply" for the purpose of condition B in paragraphs 2 and 3.

12. Relevant consideration in relation to the supply of goods or services consists of the amount shown on an invoice or the amount of payment received. Relevant consideration in relation to the grant of a right consists of the consideration for the grant of the right. In all cases it is net of VAT.

13. A supply of goods or services or a grant of a right is related to another such supply or grant where they are both made as part of the same scheme. "Scheme" includes any arrangements, transaction or series of transactions.

14. Paragraph 7 sets out the circumstances in which a supplier or a person connected with the supplier is treated as financing the payment for a supply of goods or services or the grant of a right to receive goods or services, for the purposes of condition C in paragraphs 2 and 3.

15. Paragraph 8 provides that section 839 of the Income and Corporation Taxes Act 1988 applies for the purpose of defining "connected persons". Individuals are connected to spouses or civil partners, certain relatives, persons with whom they are in partnership, and companies they control (on their own or in conjunction with other persons). Companies are connected to other companies under the same control. Trustees are connected with trust settlors (if individuals) and close companies controlled by the trust.

16. Paragraph 9 provides that receipt of payment by a supplier includes receipt of payment by a person to whom the right to receive that payment has been assigned.

17. Paragraph 10 provides powers for the Treasury to amend the relevant conditions and make other incidental or consequential amendments to the Schedule by order.

18. Paragraph 11 lists provisions that are excluded from having retrospective effect to 25 November 2008 as they were not included in the Financial Secretary to the Treasury's written Ministerial statement of that date on the scope of the legislation. These provisions have effect from the Financial Secretary to the Treasury's written Ministerial statement of 31 March 2009. They are:

- condition B in paragraphs 2 and 3;
- paragraph 6 which defines "relevant consideration" and "related supply" for the purpose of condition B; and
- references to persons connected to the supplier or grantor in condition C in paragraphs 2 and 3

19. Paragraph 12 provides for exceptions to the application of the supplementary charge. Where a supply consists of the lease, hire or rent of any asset, a supplementary charge will not apply if the VAT invoice or payment covers a period of up to one year and this accords with normal commercial practice, as defined in paragraph 14.

20. Paragraph 13 provides that the supplementary charge will not apply if a supply meets condition B in paragraph 2 or 3 and it is made in accordance with normal commercial practice.

21. Paragraph 14 defines 'normal commercial practice'.

22. Paragraph 15 provides powers for HM Treasury to introduce further exceptions to the application of the supplementary charge by order. Such exceptions may remove supplementary charges falling due on or after the order comes into effect, if the supplies concerned were made at any time from 25 November 2008 onwards.

23. Paragraph 16 provides that the supplier of, or the grantor of a right to receive, goods or services is liable to account for the supplementary charge. Where the supplier or grantor is a member of a VAT group, the representative member of that group is liable to account for it. In the case of goods and services, payment is due on the date that the standard rate of VAT reverts to 17.5 per cent. In the case of the grant of a right covered by paragraph 3, payment is due on the date that the right is first exercised on or after the date of the VAT change.

24. Paragraph 17 provides that the rate of the supplementary charge is the difference between the VAT charged on the supply of goods or services or of a grant (i.e. 15 per cent) and the rate in force when the supplementary charge becomes due (i.e. 17.5 per cent).

25. Paragraphs 17(3)-(4) provide that where, under the terms of a grant of a right, some goods or services are supplied before the rate change and some are supplied after it, the consideration should be apportioned to ascertain the amount that is properly subject to the supplementary charge.

26. Paragraph 18(1) defines a "listed supply", for the purposes of the schedule, as ones which are:

- listed in paragraph 18(2); and
- are supplies of goods or services where payment is made periodically or from time to time and which are treated as having taken place by virtue of either the issue of a VAT invoice by the supplier or receipt of payment.

27. Paragraph18(3) provides powers for HM Treasury to amend the list by order.

28. Paragraph 19 provides that, for the purposes of listed supplies in paragraph 18, the basic time of supply occurs at the end of the period for which a VAT invoice is raised or payment is received.

29. However, under paragraph 19(2), where a supplier has raised a VAT invoice or received payment in respect of a listed supply which is still continuing and issues an invoice for a "billing period" that ends before the end of the period covered by the VAT invoice or payment, the end of the billing period becomes the basic time of supply for that part of the supply. In such cases, paragraph 19(3) provides that the consideration for the listed supply must be apportioned between the periods on a just and reasonable basis.

30. Paragraph 19(4) provides that, where a listed supply arises in relation to a premium for the grant of a tenancy or a lease, the basic time of supply is the date of the grant.

31. Paragraph 20 provides that, where a person is required to account for a supplementary charge but deregisters for VAT before the supplementary charge becomes payable, he is required to account for it in his final return. However, any interest that arises on an assessment in relation to the supplementary charge will run from the date when the supplementary charge is due rather than the date when the final return is due.

32. Paragraph 21 provides for adjustment of contracts where a contract is made for the supply of goods or services before the rate change and a supplementary charge is due on the supply. In such cases, unless the contract provides otherwise, the consideration due under the contract will be increased by the amount of any supplementary charge.

33. Paragraph 22 permits HMRC to make regulations concerning the provision, replacement or correction of VAT invoices when a supplementary charge applies, to ensure that the supplier and customer correctly account for VAT.

34. Paragraph 23 provides that orders made under the provisions of the schedule are subject to the negative resolution procedure apart from those made (at least in part) under paragraph 10 which extend the scope of the supplementary charge, which require House of Commons approval within 28 days of being made.

35. Paragraph 25 provides for amendments to VATA:

- section 2(2) will be amended to clarify that an order varying the VAT rate can be made for a period of less than twelve months, and makes it explicit that any order introduced under section 2(2) may be revoked; and

- section 97(4A) will be introduced to clarify that, where an order temporarily reducing the VAT rate is revoked and the rate returns to that previously in force under the Act, the revocation is subject to negative procedure.

BACKGROUND NOTE

36. At the 2008 Pre-Budget Report the Chancellor announced a temporary reduction in the standard rate of VAT from 17.5 per cent to 15 per cent. On 25 November 2008 the Financial Secretary to the Treasury, in a written Ministerial statement, explained that the Government would introduce anti-forestalling legislation to prevent artificial avoidance seeking to exploit the change in VAT rate. On 31 March 2009 the Financial Secretary to the Treasury made a further statement concerning additional provisions aimed at blocking such avoidance. Both statements can be seen at www.hmrc.gov.uk

SECTION 10: STAMP DUTY LAND TAX: THRESHOLDS FOR RESIDENTIAL PROPERTY

SUMMARY

1. Section 10 amends the provisions in Finance Act 2003 in order to raise the starting threshold for stamp duty land tax (SDLT) on residential property from £125,000 to £175,000. The measure will be time-limited and will apply to transactions made between 22 April 2009 and 31 December 2009. After that date the SDLT threshold for residential property will revert to £125,000.

DETAILS OF THE SECTION

2. Subsection (1) provides that, in relation to transactions with an effective date on or after 22 April 2009 and before 1 January 2010, Part 4 of FA 2003 has effect as if references in the tables of that Part to £125,000 were replaced by £175,000. This means that the starting threshold for SDLT for transactions with an effective date within this period is £175,000.

3. Subsection (2) revokes two sets of regulations that were introduced in September 2008.

4. Subsection (2)(a) revokes the Stamp Duty Land Tax (Variation of Part 4 of the Finance Act 2003) Regulations 2008 (S.I. 2008/2338). These Regulations varied the requirements for notification of land transactions so that any transactions which are exempt from SDLT as a result of Regulations made under paragraph 5 of Schedule 3 to Finance Act 2003, have to be notified to HMRC.

5. Subsection (2)(b) revokes the Stamp Duty Land Tax (Exemption of certain Acquisitions of Residential Property) Regulations 2008 (S.I. 2008/2339). These Regulations exempted from SDLT acquisitions of residential property of not more than £175,000 between 3 September 2008 and 2 September 2009 inclusive.

6. Subsection (3) provides that the revocations made by subsection (2) have effect in relation to transactions with an effective date on or after 22 April 2009.

BACKGROUND NOTE

7. SDLT is a transaction tax, payable by the buyer, on the purchase of land and property. SDLT is charged at varying rates, depending on the consideration given for a land transaction. In September 2008 the Chancellor announced, using regulation–making powers, that residential property worth not more than £175,000 would be exempt from SDLT for acquisitions made between 3 September 2008 and 2 September 2009 inclusive. These regulations will now be revoked and this section will ensure that the increased threshold of £175,000 for residential property will continue to apply beyond 3 September 2009 and will now end on 31 December 2009.

8. The effective date for the purposes of SDLT is normally the date of completion, not the date of exchange of contracts. However, the effective date may be earlier than the date of completion if the contract is substantially performed, for example, if the purchaser takes possession or pays the purchase price in advance of completion. Most residential contracts will not be substantially performed in advance of completion.

SECTION 11: RATES OF DUTY ON ALCOHOLIC LIQUOR

SUMMARY

1. Section 11 provides for increases in the rates of excise duty charged on spirits, beer, wine and made-wine, and cider, to have effect from 23 April 2009.

DETAILS OF THE SECTION

2. Subsection (2) increases the rate of excise duty for spirits in section 5 of Alcoholic Liquor Duties Act 1979 (ALDA) from £21.35 to £22.64.

3. Subsection (3) increases the rate of excise duty for beer, other than small brewery beer, in section 36(1AA)(a) of ALDA from £14.96 to £16.47.

4. Subsection (4)(a) increases the rate of excise duty for sparkling cider of a strength exceeding 5.5 per cent in section 62(1A)(a) of ALDA from £188.10 to £207.20.

5. Subsection (4)(b) increases the rate of excise duty for still cider of a strength exceeding 7.5 per cent in section 62(1A) (b) of ALDA from £43.37 to £47.77.

6. Subsection (4)(c) increases the rate of excise duty for all other ciders in section 62(1A) (c) of ALDA from £28.90 to £31.83.

7. Subsection (5) provides for the replacement of Parts 1 and 2 of the Table of rates of duty on wine and made-wine in Schedule 1 to ALDA with new Parts 1 and 2, showing the following rates of duty per hectolitre:

   a. wine or made-wine of a strength not exceeding 4 per cent: £65.94.

   b. wine or made-wine of a strength exceeding 4 per cent but not exceeding 5.5 per cent: £90.68.

   c. wine or made-wine of a strength exceeding 5.5 per cent but not exceeding 15 per cent and not being sparkling: £214.02.

   d. sparkling wine or sparkling made-wine of a strength exceeding 5.5 per cent but less than 8.5 per cent: £207.20.

   e. sparkling wine or sparkling made-wine of a strength of 8.5 per cent or more, but not exceeding 15 per cent: £274.13.

   f. wine or made-wine of a strength exceeding 15 per cent but not exceeding 22 per cent: £285.33.

   g. wine or made-wine of a strength exceeding 22 per cent: £22.64 per litre.

8. Subsection (6) provides for The Alcoholic Liquor Duties (Surcharges) and Tobacco Products Duty Order 2008 as it relates to excise duty on alcoholic liquors and the Alcoholic Liquor (Surcharge on Spirits Duty) Order, to be revoked.

BACKGROUND NOTE.

9. This section increases the excise duty rates on all alcoholic liquor by a nominal 2 per cent, save for wine and made wine of a strength exceeding 22 per cent, where a new rate is substituted so as to ensure parity with the duty rate applied to spirits.

SECTION 12: RATES OF TOBACCO PRODUCTS DUTY

SUMMARY

1. Section 12 provides for an increase in the rates of excise duty on tobacco products (cigarettes, cigars, hand-rolling tobacco and other smoking tobacco and chewing tobacco) to have effect from 6pm on 22 April 2009.

DETAILS OF THE SECTION

2. Subsection (1) substitutes a new Table of rates of duty into Schedule 1 to the Tobacco Products Duty Act 1979.

3. The increases are based on the rates introduced by Treasury Order on 24 November 2008. Subsection (2) revokes those parts of that Order which introduced the increases. The changes represent an increase in excise duty of 2 per cent on current quantity-based rates. The value-based rate on cigarettes remains unchanged at 24 per cent.

4. Subsection (3) provides for the new Table of duty rates and the revocation to have effect from 6pm on 22 April 2009.

BACKGROUND NOTE

5. Smoking remains the greatest cause of preventable illness and premature death and the biggest cause of health inequality in the UK. Successive Governments have followed a policy of using tax to maintain the high price of tobacco and help reduce smoking, especially among the young.

6. Research has consistently shown that the price of cigarettes affects demand. Cigarette prices in the UK are at historically high levels.

7. This section increases quantity-based excise duty on all tobacco products at 2 per cent above current levels, thereby helping to maintain their real price, as well as maintaining their contribution to government revenues.

8. The section will increase the price of a packet of 20 cigarettes by 7p, a 25g pack of hand-rolling tobacco by 7p and a packet of small cigars by 3p.

9. The 2 per cent increase in tobacco duty is estimated to raise £60 million per year in duty and VAT revenues.

SECTION 13: VEHICLE EXCISE DUTY: RATES FOR 2009-10

SUMMARY

1. Section 13 provides for changes in the rates of vehicle excise duty (VED) in 2009-10 by amendment of the Vehicle Excise and Registration Act 1994 (VERA). Changes to the rates take effect in relation to vehicle licences taken out on or after 1 May 2009.

DETAILS OF THE SECTION

2. Subsection (2)(a) amends paragraph 1(2) of Schedule 1 to VERA to increase the general rate of VED by £5 to £190 save for vehicles with an engine size of 1549cc or less.

3. Subsection (2)(b) amends paragraph 1(2A) of Schedule 1 to VERA to increase the general rate of duty by £5 to £125 for vehicles with an engine size of 1549cc or less.

4. Subsection (3) amends paragraph 1B of Schedule 1 to VERA to change the graduated rates of duty which apply to cars first registered on or after 1 March 2001.

5. Under subsection (3), the rate payable depends on the amount of carbon dioxide emitted per kilometre. Cars which emit no more than 100 grammes of carbon dioxide per kilometre will still pay no duty. The rate for cars which emit more than 100 but not more than 120 grammes of carbon dioxide per kilometre remains unchanged at £35 (for petrol and diesel) and £15 (alternative fuel).

6. The rate for cars which emit more than 120 but not more than 140 grammes of carbon dioxide per kilometre also remains unchanged at £120 (petrol and diesel) and £100 (alternative fuel). All other rates increase by £5. The rates table operates so that cars emitting over 225 grammes of carbon dioxide per kilometre that were registered between 1 March 2001 and 23 March 2006 continue to pay a lower rate than those registered from 23 March 2006 onwards.

7. Subsection (4)(a) amends paragraph 1J(a) of Schedule 1 to VERA to increase by £5 to £185 the rate of duty for those Light Goods Vehicles which are not lower-emission vans. Lower-emissions vans are models which met the Euro 4 air quality pollutant emissions standard early and were registered on or after 1 March 2003 and before 1 January 2007, or that meet the Euro 5 pollutant emissions standard early and are registered on or after 1 January 2009 and before 1 January 2011.

8. Subsection(4)(b) amends paragraph 1J(b) of Schedule 1 to VERA to increase the rate of duty for lower-emission vans by £5 to £125.

9. Subsection (5) provides that all new rates under this section will take effect for licences taken out on or after 1 May 2009.

BACKGROUND NOTE

10. Vehicle Excise Duty (VED) was reformed in 2001 when a carbon dioxide (CO_2) emissions based system was introduced for cars registered from 1st March 2001 onwards. This is part of the Government's policy to use transport taxes to create incentives for the reduction of emissions.

11. Cars and vans registered before 1 March 2001 are treated for VED on the basis of engine size, and are charged the general rate of VED. Vans registered on or after 1 March 2001 are treated for VED according to whether they qualify for a reduced rate by having met reduced pollutant emissions standards early. These standards have been agreed at a European level and are intended to improve air quality.

12. The reduced rate of VED for post-2001 cars under subsection (3) applies to cars using alternative fuels or featuring a hybrid fuel-electric powertrain. Alternative fuels include Liquefied Petroleum Gas, Compressed Natural Gas and high blend (85 per cent content) bioethanol.

13. This year the Government intends to freeze rates for the lowest emissions post-2001 cars (emitting 140g/km of CO_2 or less), and increase rates for all other cars and vans by £5.

14. The Government intends to maintain the exemption from the top rate of VED for post-2001 cars that have a CO_2 emissions value which exceeds 225g/km but were first registered between 1 March 2001 and 23 March 2006, as provided for by Subsection (3).

15. The changes in rates apply to all vehicle licences taken out on or after 1 May 2009 regardless of the commencement date on the licence.

SECTION 14 SCHEDULE 4: VEHICLE EXCISE DUTY: RATES FROM APRIL 2010

SUMMARY

1. Section 14 provides for changes in the rates of vehicle excise duty (VED) in 2010-11 by amendment of the Vehicle Excise and Registration Act 1994 (VERA). Changes to the rates take effect in relation to vehicle licences taken out on or after 1 April 2010. Schedule 4 amends VERA to specify the scope of the application of rates of VED payable on a first vehicle licence on a car from 1 April 2010, and to specify the application of VED rates to vehicles registered in the United Kingdom subsequent to a period of registration overseas.

DETAILS OF THE SECTION

2. Subsection (2) amends paragraph 1(2) of Schedule 1 to VERA to increase the general rate of VED by £15 to £205 save for vehicles with an engine size of 1549cc or less.

3. Subsection (3) introduces the amendments made to paragraph 1B of Schedule 1 to VERA to bring into effect separate rates of duty payable on the first vehicle licence on a light passenger vehicle (a car), as well as to change rates of duty payable on other licences for cars first registered on or after 1 March 2001.

4. Subsection (4) amends paragraph 1B of Schedule 1 to VERA to specify that the annual rate of duty applicable to a car registered on or after 1 March 2001 shall be determined in accordance with the tables substituted for the existing table by subsection (7).

5. Subsections (5) and (6) inserts new sub-paragraph 1B(c) to Schedule 1 to VERA to add an additional factor to those determining the annual rate of vehicle excise duty applicable to a car registered on or after 1 March 2001. Reference is to be made to whether the duty is payable on the first vehicle licence for the vehicle.

6. Subsection (7) substitutes new rates Table 1 and Table 2 for the existing rates table, to provide rates payable on a first vehicle licence on a car, and on all other licences for cars registered on or after 1st March 2001. Table 2 operates so that cars emitting over 225 grammes of carbon dioxide per kilometre that were registered in the United Kingdom or overseas before 23 March 2006 pay a lower rate than those registered from 23 March 2006 onwards

7. Subsection (8) amends paragraph 1J(a) of Schedule 1 to VERA to increase by £15 to £200 the rate of duty for those Light Goods Vehicles which are not lower-emission vans. Lower-emissions vans are models which met the Euro 4 air quality pollutant emissions standard early and were registered on or after 1 March 2003 and before 1 January 2007, or that meet the Euro 5 pollutant emissions standard early and are registered on or after 1 January 2009 and before 1 January 2011.

8. Subsection (9) introduces the Schedule which contains further provisions about rates of duty including the application of rates of duty payable on a first vehicle licence for a car.

9. Subsection (10) provides that all new rates under this section will take effect for licences taken out on or after 1 April 2010.

DETAILS OF THE SCHEDULE

10. Paragraph 2(2) amends section 3(4)(b) of VERA to reflect the fact that the expression 'first vehicle licence' is to become a defined term in VERA.

11. Paragraph 2(3) inserts new section 3(7) into VERA to make an exception to the general rule that a licence may be taken out for a period of six months where the annual rate of duty exceeds £50. This exception applies in the case of a first vehicle licence, as defined by amendment to VERA under Paragraph 4 (2) of this Schedule, where allowing a six-month period of licensing would lead to a lower rate of VED being chargeable over the first year as a whole.

12. Paragraphs 3(2) and (3) amends sections 19(1) and (2) of VERA to provide that the person applying for a rebate on a licence that is currently in force for a vehicle may receive 'the relevant amount'. This amendment is consequential on the other amendments to section 19 of VERA made by paragraph 3 of the Schedule to the Act.

13. Paragraph 3(4) inserts new sections 19(3A) and (3B) into VERA, which relate to the method of calculation of the amount of a rebate on a licence. A reference to 'the relevant amount' is inserted by the amendment and it is specified that the method of calculation is subject to an exception. The exception is that, where the annual rate of VED on a vehicle's first vehicle licence was higher than it would have been if it had not been the first licence taken out on the vehicle, any rebate shall be calculated by reference to the lower rate of VED, rather than the rate of VED actually paid. The exception only applies where the application for a refund is made by virtue of section 19(3)(d), (e) or (f) of VERA.

14. Paragraph 4 (2) amends section 62(1) of VERA to define the expression 'first vehicle licence' for the purposes of the Act. A nil licence will not count as a first vehicle licence.

15. Paragraph 4 (3) inserts new sections 62(1B) and (1C) into VERA. Section 62(1B) specifies that where a vehicle has been registered on the issue of a temporary licence, the first vehicle licence is the licence issued following the temporary licence. Section 62(1C) provides that there is deemed to be no first vehicle licence in respect of a specified category of vehicle. This category consists of any vehicle which has previously been registered outside the United Kingdom, and, at its first registration in the United Kingdom, more than six months have passed since its first registration overseas, and it has been driven further than 6,000 kilometres.

16. Paragraph 5 (2)(a) amends paragraph 1A(1)(a) of Schedule 1 to VERA which specifies the circumstances in which the graduated rates of duty apply to cars registered after 1 March 2001. These circumstances are described by reference to first registration of the vehicle. The amendment provides that for these purposes it makes no difference whether the vehicle is first registered in the United Kingdom or overseas.

17. Paragraph 5 (2)(b) makes the same change to paragraph 1A(5) to Schedule 1 of VERA. The effect of paragraph 1A(5) is that the application of the graduated rates of duty is unaffected by modifications which take place after first registration of the vehicle.

18. Paragraph 5 (3)(a) and (b) make the same change to paragraphs 1C(3)(a) and 1C(3)(b) of Schedule 1 to VERA. These provisions of VERA apply a reduced rate of duty to a vehicle which is before first registration (or subsequently) fitted with equipment to meet prescribed emissions standards.

19. Paragraph 5 (3)(c) amends paragraph 1C(4) to Schedule 1 of VERA. This provision of VERA applies a reduced rate of duty to a vehicle which is certified by the Secretary of State before first registration as meeting prescribed emissions standards. The amendment provides that here it is first registration under VERA to which reference is being made.

20. Paragraph 5 (4)(a) amends paragraph 1H(1)(a) of Schedule 1 to VERA which specifies circumstances in which rates of duty other than the general rates apply to a light goods vehicle. These circumstances are described by reference to first registration of the vehicle. The amendment provides that for these purposes it makes no difference whether the vehicle is first registered in the United Kingdom or overseas.

21. Paragraph 5 (4)(b) makes the same change to paragraph 1H(3) of Schedule 1 to VERA. The effect of paragraph 1H(3) is that the application of rates of duty to a light goods vehicle is unaffected by modifications which take place after first registration of the vehicle.

22. Paragraph 5 (5) makes the same change to paragraph 1K(a) of Schedule 1 to VERA. The effect of paragraph 1K(a), when read with paragraph 1J, is to apply a particular rate of duty to a lower-emission van first registered on or after 1 March 2003 and before 1 January 2007.

23. Paragraph 5 (6) makes the same change to paragraph 1M(a) of Schedule 1 to VERA. The effect of paragraph 1M(a), when read with paragraph 1J, is to apply a particular rate of duty to certain types of lower-emission van first registered on or after 1 January 2009 and before 1 January 2011.

24. Paragraph 6 (2) inserts new paragraphs 25(2) and (3) into Schedule 2 to VERA to establish an exemption from duty for vehicles in the period of their first vehicle licence. This exemption applies to light passenger vehicles first registered in the UK or overseas on or after 1 March 2001 that have a CO_2 emission value which exceeds 100g/km but not exceeding 130g/km.

25. Paragraph 7 (1) provides that, subject to Paragraph 7(2) of this Schedule, the amendments made by this Schedule will take effect for licences taken out on or after 1 April 2010.

26. Paragraph 7 (2) provides that amendments made by Paragraph 5 of this Schedule do not apply to vehicles first registered under VERA before 1 April 2010.

BACKGROUND NOTE

27. VED was reformed in 2001 when a carbon dioxide (CO_2) emissions based system was introduced for cars registered from 1st March 2001 onwards. This is part of the Government's policy to use transport taxes to create incentives for the reduction of emissions. Cars and vans registered before 1 March 2001 are treated for VED on the basis of engine size, and are charged the general rate of VED. Vans registered on or after 1 March 2001 are treated for VED according to whether they qualify for a reduced rate by having met reduced pollutant emissions standards early. These standards have been agreed at a European level and are intended to improve air quality.

28. The reduced rate of VED for post-2001 cars under Subsection (3) applies to cars using alternative fuels or featuring a hybrid fuel-electric powertrain. Alternative fuels include Liquefied Petroleum Gas, Compressed Natural Gas and high blend (85 per cent content) bioethanol.

29. For 2010-11 the Government intends to introduce First-Year Rates of VED payable on a first vehicle licence for a new car. Cars emitting up to 130g/km of CO_2 will be exempt from VED on a first vehicle licence in 2010-11. Cars emitting between 131 and 165g/km will pay the same rate of VED on their first vehicle licence as on all subsequent licences. Cars emitting over 165g/km will pay a higher rate on the first vehicle licence than on subsequent licences, up to a top rate of £950. The intention is that first vehicle licence rates should apply only to brand new cars and almost new imported used cars.

30. For other cars already registered on or after 1 March 2001 to which first vehicle licence rates will not apply, the Government intends to apply increases and decreases of up to £30 depending on the CO_2 emissions of the car.

31. The Government intends to maintain the exemption from the top rate of VED for cars that have a CO_2 emissions value which exceeds 225g/km but were first registered before 23 March 2006, as provided for by Subsection (7).

32. In 2010-11, the Government intends to increase by £15 the rates for larger engine size (over 1549cc) pre-2001 cars and the standard rate for post-2001 vans (those that are not lower-emissions vans). The changes in rates apply to all vehicle licences taken out on or after 1 April 2010 regardless of the commencement date of the licence.

33. For 2010-11 the Government intends to introduce First-Year Rates of VED payable on a first vehicle licence for a new car. Cars emitting up to 130g/km of CO_2 will be exempt from VED on a first vehicle licence in 2010-11. Cars emitting between 131 and 165g/km will pay the same rate of VED on their first vehicle licence as on all subsequent licences. Cars emitting over 165 g/km will pay a higher rate on the first vehicle licence than on subsequent licences, up to a top rate of £950. The intention is that first vehicle licence rates should apply only to brand new cars and almost new imported used cars.

34. Six-month licence rates are generally available where an annual rate of duty on a vehicle licence exceeds £50, and are chargeable at 55 per cent of the annual rate. Paragraph 2(3) of this Schedule provides an exception in the case of certain first vehicle licence rates for cars. The exception is intended to remove the possibility of paying less than the full annual rate of duty on a car's first vehicle licence by taking out a six month licence as the first vehicle licence.

35. VED rebates are available to registered vehicle keepers on any unexpired complete months remaining on a vehicle licence, where the registered keeper's circumstance is one of those set out in section 19 of VERA. Paragraph 3 of this Schedule provides an alternative method of calculation for refunds, in the case of first vehicle licence rates for cars where the licence rate for a subsequent licence is lower than the first vehicle licence rate, and in the case where the refund is for a licence on a vehicle that has been sold, exported or has a Statutory Off-Road Notification in force. This method of calculating the level of refund has been adopted to remove the possibility of paying less than the full annual rate of duty on a car's first vehicle licence by taking a refund on the first vehicle licence which is at a higher rate than the rate that would apply in relation to a subsequent licence.

36. A first vehicle licence is the licence on the issue of which a vehicle is first registered in the UK, except for the exception inserted by paragraph 4(3) of this Schedule. This exception is intended to remove the possibility to pay less than the full annual rate of duty on a car's first vehicle licence over a twelve month period by importing an almost-new car into the UK. The intention is to use an existing definition of what constitutes a new vehicle, which has been translated from the Value Added Tax Act 1994 (section 95). This defines a car as new unless more than six months have elapsed since its first entry into service and it has travelled more than 6,000 kilometres under its own power. Imported cars not considered to be new according to this definition will not be issued with a first vehicle licence and will not be charged associated First-Year Rates of duty.

37. With effect from 1st April 2010, periods of registration outside of the UK will be taken into consideration for licensing purposes, for vehicles imported into the UK on or after 23 March 2006. This change is intended to ensure that vehicles pay similar rates of duty, whether or not they were first registered in the UK, subject to paragraph 4(3) of this Schedule.

38. Cars emitting below 130g/km of CO_2 will be exempt from VED for the period for which the first vehicle licence would otherwise apply. For subsequent licences the threshold for the exemption changes to 100g/km.

SECTION 15: FUEL DUTIES (RATES AND REBATES FROM SPRING 2009)

SUMMARY

1. Section 15 provides for changes in rates of duty and rates of rebate on products charged to duty under the Hydrocarbon Oil Duties Act 1979 (HODA).

2. Duty rates on the main road fuels are increased by 1.84 pence per litre (ppl), and effective rates of duty on non-road fuels are increased by the same proportion as main road fuels. Duty increases on biofuels and natural gas maintain the differential with the main road fuels, while the differential for road fuel gas other than natural gas is reduced by the equivalent of 1 penny per litre. These changes came into effect on 1 April 2009.

3. From 1 May 2009, duty on leaded petrol is increased by 1.84 pence per litre (ppl) and on aviation gasoline (avgas) by 2.31 ppl.

DETAILS OF THE SECTION

4. Subsection (2) amends the rates of duty on unleaded petrol, aviation gasoline, light oil other than unleaded petrol or aviation gasoline, and heavy oil in HODA.

5. Subsections (3)-(5) amend the rate of duty on biodiesel, bioethanol and road fuel gases.

6. Subsections (6)-(8) amend the effective rate of duty on fuel oil, gas oil, light oil for use as furnace fuel and biodiesel for off-road use.

7. Subsection (9) provides for the changes for aviation gasoline and light oil other than unleaded petrol or aviation gasoline to come into force on 1 May 2009.

8. Subsection (10) provides for the changes other than to aviation gasoline and light oil other than unleaded petrol or aviation gasoline to be treated as having come into force on 1 April 2009.

BACKGROUND NOTE

9. In the 2007 and 2008 Budgets and 2008 Pre-Budget Report, the Government announced that duty rates on the main road fuels would be increased by 1.84 ppl, and duty on non-road fuels would be increased by the same proportion, with effect from 1 April 2009. On 30 March 2009, HM Revenue and Customs issued a Business Brief 22/09 confirming that the pre-announced increases were going ahead.

10. Duty increases on biofuels and natural gas maintain the differential with the main road fuels, while the differential for road fuel gas other than natural gas is reduced by the equivalent of 1 penny per litre. These increases also took effect from 1 April 2009. With effect from 1 May 2009, duty on leaded petrol is increased by 1.84 ppl and on aviation gasoline by 2.31 ppl.

SECTION 16: FUEL DUTIES: RATES AND REBATES FROM SEPTEMBER 2009

SUMMARY

1. Section 16 provides for changes in the rates of duty and rates of rebate on hydrocarbon oils and biodiesel, and rates of duty on road fuel gases, bioethanol, and fuel substitutes, with effect from 1 September 2009.

DETAILS OF THE SECTION

2. Subsection (2) amends the rates of duty on unleaded petrol, aviation gasoline, light oil other than unleaded petrol or aviation gasoline, and heavy oil in HODA.

3. Subsections (3)-(5) amend the rate of duty on biodiesel, bioethanol and road fuel gases.

4. Subsections (6)-(8) amend the effective rate of duty on fuel oil, gas oil, light oil for use as furnace fuel and biodiesel for off-road use.

5. Subsection (9) provides for the changes to come into effect on 1 September 2009.

BACKGROUND NOTE

6. Budget 2009 announced that the duty on the main road fuels and leaded petrol would be increased by 2 pence per litre with effect from 1 September 2009. The duty rates for biodiesel, bioethanol, and road fuel gases (natural gas and liquefied petroleum gas) will also be increased to maintain the current differentials

7. Effective rates of duty for non-road fuels will be increased by the same percentage as main road fuels, as will the rate for aviation gasoline, from the same date.

SECTION 17 SCHEDULE 5: RATES OF AIR PASSENGER DUTY

SUMMARY

1. Section 17 and Schedule 5 provide for the air passenger duty (APD) destination bands to be restructured from two to four. It also simplifies the existing provisions of APD relating to special accounting schemes.

DETAILS OF THE SECTION

2. Section 1 replaces subsections (1) to (4) of Section 30 of Finance Act (FA) 1994 with new subsections (1) to (4A).

3. Subsection (1) determines that the rates in subsections (2) to (4A) are on a per-passenger basis.

4. Subsection (2) sets the APD rates to destinations within the United Kingdom and destinations listed in Part 1 of Schedule 5A

5. Subsections (3) to (4) set out the APD rates for destinations listed in Parts 2 and 3 of Schedule 5A.

6. Subsection (4A) sets out the rates for destinations (other than the United Kingdom) not listed in Schedule 5A.

DETAILS OF THE SCHEDULE

7. Paragraph 2 amends section 30 of FA 1994. Sub-paragraph (2) inserts new subsection (8A) to provide that HM Treasury may by order amend Schedule 5A, which provides the list of territories and parts under which they are listed. Sub-paragraph (3) repeals subsections (9) to (9B) removing the definitions of "EEA State" and "qualifying territory" as well as the power to amend subsection (9A).

8. Paragraph 3 replaces section 39 of FA 1994 with a new section 39 that relates to schemes for simplified operation of Chapter 4 of FA 1994 (which relates to APD). It allows for Chapter 4 to have effect in relation to a special accounting scheme where this has been agreed between the Commissioners for HM Revenue and Customs (HMRC) and the registered operator.

9. New sections 39(3)(a) and (b) provide that a special accounting scheme is a scheme which allows the registered operator to use a method of calculation (other than one based on actual passenger numbers), that enables it to arrive at figures that it may regard as being (a) the number of chargeable passengers and (b) the rate to be applied.

10. Subsection (4) of new section 39 provides that the Commissioners for HMRC may publish the terms and conditions of such schemes.

11. Subsection (5) of new section 39 provides that where a special accounting scheme has been agreed with an operator Chapter 4 of FA 1994 has effect in accordance with that scheme (and any general terms and conditions in a notice published under subsection (4)) for the agreed period.

12. New section 39(6) provides that special accounting schemes may be varied at any time only with the agreement of both the Commissioners for HMRC and the registered operator, but only for the future.

13. Paragraph 4 amends and extends section 42(4) of FA 1994 and provides that a draft order laid and approved by the House of Commons is also required before destination territories and associated banding as set out in Parts 1 to 3 of Schedule 5A may be moved from a lower rate to a higher rate destination band.

14. Paragraphs 8(1) and (2) provide that no agreement under the new section 39 may be made so as to have effect in respect of the carriage of passengers beginning before 1 November 2009. Existing special schemes are unaffected by the new special schemes arrangements and may continue to apply in respect of the carriage of passengers beginning before 1 November 2009.

BACKGROUND NOTE

15. In the 2008 Pre-Budget Report, the Government announced that it would reform APD from a two-distance band regime to a four-distance band regime, rather than proceed with a per plane tax.

16. The four distance bands will be set at 2,000 mile intervals from London, and destinations will be categorised based on the distance from London to the capital city of the destination country/ territory, with the exception of the Russian Federation, which will be split east and west of the Urals, as it is administratively simple to do so.

17. Each band will have two rates, one for the standard class of travel and one for other classes of travel. This section and Schedule provides for these changes to the destination bands and sets rates. In addition, it simplifies the current arrangements for special accounting schemes to reduce the burden on industry, and contains consequential repeals.

SECTION 18: STANDARD RATE OF LANDFILL TAX

SUMMARY

1. Section 18 increases the standard rate of landfill tax from £40 per tonne to £48 per tonne for disposals of waste made at authorised landfill sites on or after 1 April 2010.

DETAILS OF THE SECTION

2. Subsection (1) amends section 42 of the Finance Act 1996 to increase the standard rate of landfill tax to £48 per tonne.

3. Subsection (2) provides for the increase to apply to disposals of relevant waste made, or treated as made, on or after 1 April 2010.

BACKGROUND NOTE

4. Landfill tax was introduced on 1 October 1996 to encourage waste producers and the waste management industry to switch to more sustainable alternatives to landfilling waste. The tax applies to active and inactive waste, disposed of at authorised landfill sites. Active waste attracts the standard rate of tax, while inactive waste is subject to a lower rate.

5. The standard rate is currently £40 per tonne, which came into effect on 1 April 2009 as a result of a change made by Finance Act 2008. Budget 2007 announced that the rate would increase to £48 per tonne from 1 April 2010 – this section deals with that announcement. The Government announced on 22 April 2009 that the standard rate will continue to increase by £8 per tonne on 1 April each year from 2011 to 2013. These increases aim to encourage greater diversion of waste from landfill to more sustainable waste management options.

6. The lower rate, which applies to inert or inactive waste, is currently £2.50 per tonne. The Government announced on 22 April 2009 that the rate will not increase in 2010-11.

SECTION 19: RATES OF GAMING DUTY

SUMMARY

1. Section 19 will increase the gross gaming yield bands for gaming duty in line with inflation for accounting periods starting on or after 1 April 2009, preventing fiscal drag and benefiting the industry.

DETAILS OF THE SECTION

2. Subsection (1) substitutes a new table for the existing table in section 11(2) of the Finance Act 1997 which has the effect of increasing the gross gaming yield bands for gaming duty and subsection (2) provides for this change to have effect for accounting periods beginning on or after 1 April 2009.

BACKGROUND NOTE

3. Gaming duty is charged on any premises in the UK where dutiable gaming takes place. Dutiable gaming includes the playing of games such as roulette, baccarat, and blackjack. The amount of duty is calculated by reference to bands of gross gaming yields (GGY) (i.e. gross profits) for that accounting period. For example, duty will be paid at a rate of 15 per cent on the first £1,929,000 of GGY, then 20 per cent for the next £1,329,500 of GGY, and so on. Gaming duty is charged on premises in respect of accounting periods of six months, normally beginning 1 April and 1 September, with interim three monthly payments.

4. The change made by this measure increases the GGY bands but makes no change to the rates. The basis for revalorisation of the bands is the Retail Price Index (RPI) for the year ended 31 December 2008. In this case the RPI was calculated at 0.95 per cent.

5. The current and revalorised bandings are:

Tax Rate	15 per cent of first	20 per cent of next	30 per cent of next	40 per cent of next	50 per cent of
Current	£1,911,000	£1,317,000	£2,307,000	£4,869,500	Remainder
Revalorised	£1,929,000	£1,329,500	£2,329,000	£4,915,500	Remainder

6. This section is connected to section 114 which makes other changes to gaming duty and the administration of gaming duty.

SECTION 20: BINGO DUTY

SUMMARY

1. Section 20 provides for an increase in the rate of bingo duty and an increase in the money prize limit for exempt small-scale amusements provided commercially.

DETAILS OF THE SECTION

2. Subsection (2) increases the rate of bingo duty in section 17(1)(b) of the Betting and Gaming Duties Act 1981 (BGDA) from 15 per cent to 22 per cent.

3. Subsection (3) increases the money prize limit in paragraph 5(2)(c) of Schedule 3 to BGDA from £50 to £70.

4. Subsection (4) provides that the duty rate change has effect in relation to accounting periods commencing on or after 27 April 2009.

5. Subsection (5) provides that the increase to the money prize limit has effect in relation to bingo played on or after 1 June 2009.

BACKGROUND NOTE

6. There are two elements to this section; the first increases the rate of bingo duty, the second increases the money prize limit that may be distributed or offered in the course of small scale bingo conducted on certain premises without incurring a charge to bingo duty.

7. Bingo duty is calculated at the rate of 15 per cent of a person's bingo promotion profits for an accounting period. The rate was set when the current charging structure was introduced on 27 October 2003.

8. The rate increase is being made as part of a package of measures designed to simplify the tax treatment of fees charged in relation to equal chance gaming. These include the removal of VAT from bingo participation fees and the imposition of gaming duty to charges made in connection with card room gaming in casinos.

9. The second element of the section is concerned with the exemption from bingo duty provided for small-scale amusements provided commercially which are restricted to specified premises and operate within certain monetary limits. This includes small scale bingo played in venues such as family entertainment centres, adult gaming centres and pleasure fairs provided by travelling showmen in certain circumstances.

10. The increase in the money prize limit has been made to continue the alignment with the limit imposed for the purposes of the social regulation of prize gaming conducted in such premises. That increase, which will take place by Regulation, follows a review and consultation exercise undertaken by The Department for Culture, Media and Sport.

SECTION 21: AMOUNTS OF AMUSEMENT MACHINE LICENCES

SUMMARY

1. Section 21 will increase the amounts of amusement machine licence duty (AMLD) payable in respect of licence applications that are received by Her Majesty's Revenue and Customs after 4pm on 22 April 2009.

DETAILS OF THE SECTION

2. Section 21 substitutes a new table for the existing table of amounts of AMLD in section 23(2) of the Betting and Gaming Duties Act 1981. This will increase the amount of duty payable on licences and will have effect for any application for an amusement machine licence that is received by Her Majesty's Revenue and Customs after 4pm on 22 April 2009.

BACKGROUND NOTE

3. AMLD is a duty of excise that is charged on a licence that allows gaming machines to be provided for play in the United Kingdom. Other than specific classes of "excepted machines" all gaming machines fall within the scope of AMLD. The amount of duty that is payable is determined by the period that is covered, between one and twelve months, and the numbers and categories of machines. Machine categories are defined by reference to their maximum prize values and cost to play.

4. This section amends the amounts of duty that are payable in respect of amusement machine licences. The new duty amounts will apply to licence applications received after 4pm on 22 April 2009.

5. This section is connected to section 22 which introduces additional changes in relation to AMLD.

SECTION 22: PROVISIONS AFFECTING AMOUNT OF AMUSEMENT MACHINE LICENCE DUTY

SUMMARY

1. Section 22 provides for changes to the descriptions of excepted machines, small-prize machines and Category C gaming machines for the purposes of amusement machine licence duty (AMLD) in the Betting and Gaming Duties Act 1981 (BGDA). The amendments made by this section will have effect from 1 June 2009.

DETAILS OF THE SECTION

2. Subsection (4) amends paragraph (c) of section 21(5) of BGDA to increase the prize level for certain machines that are exempt from AMLD. The prize level will rise from £5 to £15, with a maximum cash amount of £8.

3. Subsection (5) introduces a new class of excepted machine to section 21(5). Gaming machines with a maximum stake of £1 and a maximum prize value of £50 will be exempt from AMLD so long as the prize is not money, or something that can be exchanged for money or anything else.

4. Subsection (6) inserts new sections 21(6) and (7) to determine how non-money prizes will be given a value for the purpose of determining their duty liability.

5. Subsection (7) provides for the prize level of a "small-prize machine" in section 22(2) to be increased from £8 to £10.

6. Subsection (9) provides for the stake and prize levels of a Category C gaming machine in section 23(3) of BGDA to be increased to £1 and £70 respectively.

7. Subsection (10) omits section 23(5) which provided valuation provisions in respect of other AMLD provisions. The provisions of that section are replaced by subsection (6) of this section.

8. Subsection (11) contains consequential repeals

BACKGROUND NOTE

9. Amusement machine licence duty (AMLD) is a duty of excise that is charged on a licence that authorises the provision of gaming machines for play in the United Kingdom. Other than specific classes of "excepted machines", all gaming machines fall within the scope of AMLD. The amount of duty that is payable is determined by the numbers and categories of machines. Machine categories are defined by reference to their maximum prize values and cost to play.

10. This section follows from the announcement by the Department for Culture, Media and Sport (DCMS) that permitted prize levels for Category C and Category D machines would be increased by Order in the summer. The definition of Category C gaming machines and "excepted machines" for the purposes of AMLD in the BGDA is in line with the definitions of Category C and D gaming machines used by DCMS. This section amends the definition of a Category C gaming machine and an "excepted machine" for AMLD purposes.

11. This section is connected to section 21, which makes changes to the amounts of AMLD.

SECTION 23 SCHEDULE 6: TEMPORARY EXTENSION OF LOSS CARRY BACK PROVISIONS

SUMMARY

1. Section 23 and Schedule 6 provide for a temporary extension to the income tax and corporation tax rules for carrying back trade losses.

DETAILS OF THE SECTION

2. Section 23 introduces Schedule 6. Paragraphs 1 and 2 of the Schedule refer to income tax. Paragraph 3 refers to corporation tax.

DETAILS OF THE SCHEDULE

3. Paragraph 1(1) provides that a person who has made a trade loss in the tax year 2008-09 or 2009-10 may make a claim under this paragraph if relief is available for an amount of the loss under section 64 of the Income Tax Act 2007 (ITA) and either of two conditions are met. For the purpose of this paragraph a loss in a profession or vocation is treated in the same way as a trade loss (see paragraph 2(2)).

4. Paragraph 1(2) sets out "condition A" which is that the person makes a claim under section 64 of ITA for the trade loss.

5. Paragraph 1(3) sets out "condition B" which is that the person's total income in both the year in which the loss is made and the preceding tax year is either nil, or does not include any income from which a deduction could be made under a section 64 claim.

6. Paragraph 1(4) sets out the amount of the loss that may be relieved ("the deductible amount"). The deductible amount that may be deducted from profits of the two tax years before the year immediately before the year of loss is subject to the £50,000 limit in paragraph 1(12).

7. Paragraph 1(5) provides that a claim for relief is for the deductible amount to be deducted in computing the person's total income (for 2005-06 and/or 2006-07) or in calculating the person's net income (for 2007-08 or 2007-08 and 2008-09, as relevant). The ways in which it may be deducted are set out in sub-paragraphs (6) to (10).

8. Paragraph 1(6) provides that a deduction is only to be made from profits of the trade.

9. Paragraph 1(7) explains how the deductions are to be made in the case of a loss made in tax year 2008-09 where the person makes a claim for relief under section 64 of ITA for tax year 2007-08 (whether a claim for 2007-08 alone or where relief is claimed under section 64 for both 2007-08 and 2008-09). The amount of the available loss for 2008-09 that is not relieved under a section 64 claim for 2007-08 (and 2008-09 if claimed) is deducted firstly from the profits of the trade for the tax year 2006-07 and, if any of the loss remains unrelieved, secondly from the profits of the trade for the tax year 2005-06. The total amount that may be deducted for 2005-06 and 2006-07 cannot exceed £50,000.

10. Paragraph 1(8) explains how deductions are to be made in any other case where the loss is made in tax year 2008-09. The amount of the available loss for 2008-09 that is not relieved under a section 64 claim is deducted firstly from the profits of the trade for 2007-08 and, if any of the loss remains unrelieved, secondly from the profits of the trade for the tax year 2006-07 and thirdly from the profits of the trade for the tax year 2005-06. The total amount that may be deducted for 2005-06 and 2006-07 cannot exceed £50,000.

11. Paragraph 1(9) explains how the deductions are to be made in the case of a loss made in tax year 2009-10 where the person makes a claim for relief under section 64 of ITA for tax year 2008-09 (whether a claim for 2008-09 alone or where relief is claimed under section 64 for both 2008-09 and 2009-10). The amount of the available loss for 2009-10 that is not relieved under a section 64 claim for 2008-09 (and 2009-10 if claimed) is deducted firstly from the profits of the trade for the tax year 2007-08 and, if any of the loss remains unrelieved, secondly from the profits of the trade for the tax year 2006-07. The total amount that may be deducted for 2006-07 and 2007-08 cannot exceed £50,000.

12. Paragraph 1(10) explains how deductions are to be made in any other case where the loss is made in tax year 2009-10. The amount of the available loss for 2009-10 that is not relieved under a section 64 claim is deducted firstly from the profits of the trade for 2008-09 and, if any of the loss remains unrelieved, secondly from the profits of the trade for the tax year 2007-08 and thirdly from the profits of the trade for the tax year 2006-07. The total amount that may be deducted for 2006-07 and 2007-08 cannot exceed £50,000.

13. Paragraph 1(11) confirms that the sections of ITA listed in this subsection which apply to section 64 of ITA also apply to the relief in this paragraph.

14. Paragraph 1(12) provides that the total amount that may be deducted from the profits of the trade for the tax years 2005-06 and 2006-07 (in the case of a loss made in tax year 2008-09) is £50,000; and that the total amount that may be deducted from the profits of the trade for the tax years 2006-07 and 2007-08 (in the case of a loss made in tax year 2009-10) is also £50,000.

15. Paragraph 2(1) sets out the time limits for making a claim under paragraph 1. For losses made in 2008-09 claims must be made by 31 January 2011 and for losses made in 2009-10 claims must be made by 31 January 2012.

16. Paragraph 2(3) provides that paragraph 1 is subject to paragraph 2 of Schedule 1B to the Taxes Management Act 1970 which sets out the rules that apply where loss relief is given for an earlier tax year to that in which the claim to the relief is made.

17. Paragraph 2(4) provides that sections 61 (Non-partners: losses of a tax year), 62 (Partners: losses of a tax year etc) and 63 (Prohibition against double counting) of ITA apply to paragraph 1 in the same way as they apply to trade loss reliefs in Chapter 2 of Part 4 of ITA.

18. Paragraph 2(6) provides that a reference to section 64 of ITA in paragraph 3(1) of the Social Security Contributions and Benefits Act 1992 (and paragraph 3(1) of the Social Security Contributions and Benefits (Northern Ireland) Act 1992 includes paragraph 1. This ensures that any deduction under paragraph 1 which reduces profits chargeable to income tax also reduces profits in respect of which Class 4 National Insurance Contributions are payable.

19. Paragraph 3 provides for a temporary extension of the corporation tax rules for carrying back trade losses in relation to a maximum £50,000 trading losses incurred in relevant accounting periods ending between 24 November 2008 and 23 November 2009 and a maximum £50,000 trading losses incurred in relevant accounting periods ending between 24 November 2009 and 23 November 2010. Section 393A of the Income and Corporation Taxes Act 1988 (ICTA) continues to allow a one year carry back for trading losses of a relevant accounting period which are not relievable under this paragraph.

20. Paragraph 3(1) provides that the extended three-year carry back of company trading losses applies by virtue of section 393A of ICTA.

21. Paragraph 3(2) provides that the extended corporate loss carry back applies solely to losses arising in a trade in accounting periods ending after 23 November 2008 and before 24 November 2010.

22. Paragraph 3(3) provides that the maximum amount of losses that may be carried back by a company by virtue of this paragraph is £50,000 for losses arising in accounting periods ending after 23 November 2008 and before 24 November 2009 and £50,000 for losses arising in accounting periods ending after 23 November 2009 and before 24 November 2010 (regardless of the number of accounting periods falling within the each of those periods).

23. Paragraph 3(4) provides that where a loss is made in an accounting period which is shorter than twelve months the amount of the loss that can be carried back from that period by a company is limited to a proportion of the £50,000 limit, determined in accordance with sub-paragraph (5).

24. Paragraph 3(5) provides a formula for calculating the proportion referred to in sub-paragraph (4).

25. Paragraph 3(6) provides that losses unrelated to decommissioning expenditure are relieved before those attributable to decommissioning expenditure. This ensures that where a company's loss making trade falls within the North Sea Oil & Gas tax regime, the company's ability to gain relief under section 164 of the Capital Allowances Act 2001 (decommissioning expenditure) is unaffected.

BACKGROUND NOTE

26. The section and Schedule extend the trade loss carry back rules for income tax and corporation tax. For income tax the rules are extended in relation to a trade loss (including a loss in a profession or vocation) made in tax year 2008-09 or 2009-10. For corporation tax the extension applies to trading losses arising in an accounting period ending after 23 November 2008 and before 24 November 2010. The extension has effect from 22 April 2009.

SECTION 24: FIRST-YEAR CAPITAL ALLOWANCES FOR EXPENDITURE IN 2009-2010

SUMMARY

1. Section 24 provides for a temporary first-year capital allowance at the rate of 40 per cent for a period of one year for spending by businesses on most plant and machinery that would normally qualify for a writing-down allowance at the 20 per cent rate. The provision applies to spending on or after 1 April 2009 for businesses within the charge to corporation tax and on or after 6 April 2009 for businesses within the charge to income tax.

DETAILS OF THE SECTION

2. Subsection (1) explains that Part 2 of the Capital Allowances Act 2001 (CAA) has effect as if mention of the section appeared in section 39 and mention of the section and the 40 per cent rate appeared in the Table in section 52(3). This is because Part 2 will not actually be amended as the section is only a temporary measure but all the provisions in Part 2 are to apply for the temporary period as if it was a new section in Part 2.

3. Subsection (2) provides the conditions that the expenditure must meet in order to be first-year qualifying expenditure under this section. The conditions are that the expenditure is:

- incurred in 2009-2010;
- not within any of the standard general exclusions in section 46(2) of CAA (these include spending on cars and on assets for leasing);
- not special rate expenditure (as defined in section 104A of CAA, which includes spending on long-life assets and integral features); and
- not first-rate qualifying expenditure under any other provision in Chapter 4 of Part 2 of CAA.

4. Subsection (3) explains what is meant by the incurring of expenditure in 2009-2010.

5. Subsection (4) ensures that property lessors are not prohibited by the general exclusion on leased assets from claiming the temporary first-year allowance in respect of expenditure on background plant or machinery for a building (as defined in section 70R of CAA) provided that the expenditure is not special rate expenditure.

6. Subsection (6) provides that, in determining whether expenditure is incurred in 2009-10, any effect of section 12 of CAA is to be disregarded. Section 12 normally deems pre-commencement business expenditure to have been incurred on the first day when the business starts. Thus, if the pre-commencement expenditure were incurred before 1 April 2009 (for corporation tax) or 6 April 2009 (for income tax), but the business commences after those dates, this subsection would stop the pre-commencement expenditure from qualifying for the temporary first-year allowance.

BACKGROUND NOTE

7. Capital allowances allow the cost of capital assets to be written off against a business's taxable profits. They take the place of commercial depreciation charged in commercial accounts. The main rate of capital allowances for general spending on plant and machinery is currently 20 per cent a year on the reducing balance basis. First-year allowances (FYAs) bring forward the time that tax relief is available for capital spending and allow a greater proportion of the cost of an investment to qualify for tax relief against a business's taxable profits of the period during which the investment is made.

8. For a period of one year all businesses can claim 40 per cent FYAs on their investments in most plant and machinery. The period will run from 1 April 2009 to 31 March 2010 for businesses within the charge to corporation tax and 6 April 2009 to 5 April 2010 for businesses within the charge to income tax.

9. There are some exceptions, including spending on special rate expenditure (including integral features & long-life assets), all expenditure on cars and expenditure on assets for leasing.

10. In conjunction with the Annual Investment Allowance, which effectively provides a 100 per cent first-year allowance for the first £50,000 investment in most plant and machinery (apart from cars) and which was introduced in Finance Act 2008, this new temporary 40 per cent first-year allowance will provide a valuable increased cash-flow benefit for businesses investing in plant and machinery in 2009-2010.

SECTION 25: AGREEMENTS TO FORGO TAX RELIEFS

SUMMARY

1. Section 25 ensures the Corporation Tax Acts do not override an undertaking by a person to surrender the right to benefit from tax losses and other reliefs. It will apply to undertakings given in connection with arrangements designated by HM Treasury.

DETAILS OF THE SECTION

2. Subsection (1) of the section ensures that where HM Treasury has designated an arrangement with a person as one to which the section applies, then any tax losses or other reliefs which that person has agreed to forgo under the terms of the arrangement will not be overridden by any statutory provision.

3. Whilst many reliefs provided under the Taxes Acts require a formal claim, some do not. For example, section 393(1) of the Income and Corporation Taxes Act 1988 provides that losses incurred in a trade in one accounting period are, in the absence of any other claim, automatically carried forwards to the next period, and reduce the amount of profit that is taxable in that later period

4. The effect of this subsection is switch off any rules that grant such reliefs automatically where a person has undertaken to forgo these tax reliefs in connection with schemes that provide taxpayer support.

5. Subsection (2) sets out the types of arrangement that HM Treasury may designate for the purposes of subsection (1). The section will apply where the agreement to forgo tax relief is made as part of arrangements whereby the Government, through HM Treasury, another Government Department or another public body, provides financial support of whatever kind, either directly to the person who has given the undertaking or to another person, as part of the designated arrangement.

6. Subsection (3) denies any further relief from tax that might otherwise arise as a consequence of a person forgoing a right to tax relief, either to that person or any other. This might arise, for example, where one company in a group receives financial support from a designated arrangement and another company surrenders losses, and there is a compensatory payment made to the second company. In these circumstances, the payer would not be able to claim any deduction from their profits or other form of tax relief in respect of the compensatory payment.

7. Subsections (4) and (5) provide definitions and the commencement rule respectively. The section applies to arrangements entered into on or after 22 April 2009, but it may have effect in respect of tax reliefs that arise or would otherwise be effective in respect of periods before that date.

BACKGROUND NOTE

8. On 19 January 2009 the Government announced its intention to offer an Asset Protection Scheme to restore confidence in the banks and get credit flowing again, by dealing with the losses associated with impaired assets.

9. The details of the Asset Protection Scheme were published on 26 February 2009. Under the scheme, the Government provides protection against future credit losses on certain assets in exchange for a fee. Arrangements under this section would include arrangements under the Asset Protection Scheme.

SECTION 26 AND SCHEDULE 7: CONTAMINATED AND DERELICT LAND

SUMMARY

1. Section 26 and Schedule 7 amend Part 14 of the Corporation Tax Act 2009 (CTA), commonly referred to as Land Remediation Relief. The amendments are to extend the scope of the relief to the bringing of long term derelict land back into productive use and to refocus the existing relief on bringing land contaminated by previous industrial use back into productive use.

DETAILS OF THE SCHEDULE:

2. Paragraphs 2 and 3 amend the heading of Part 14 of CTA and sections 1143(1) & (7) to reflect the extension of the relief to include derelict land.

3. Paragraph 4(2) amends the wording of section 1144(1) to reflect the inclusion of an additional condition for qualifying expenditure "Condition F".

4. Paragraphs 4(3) to (5) make necessary amendments to reflect the extension of the relief to include derelict land.

5. Paragraph 4(6) amends section 1144 (5), "Condition D", to reflect the changes to the rules on payments to sub-contractors. New section 1144(5)(c) applies to give relief for qualifying land remediation expenditure paid to unconnected sub-contractors. The new section 1144(5)(d) gives relief for qualifying land remediation expenditure paid to connected sub-contractors, as calculated in section 1175.

6. Paragraph 4(7) inserts a new section 1144(6A) with a new Condition F. This condition provides that qualifying expenditure does not include expenditure incurred on paying landfill tax.

7. Paragraph 5 replaces the existing section 1145 with a new section 1145, which defines land "in a contaminated state", section 1145A, which defines land "in a derelict state" and section 1145B, which excludes nuclear sites.

8. Paragraph 6(2)(a) amends section 1146(1) to reflect that section 1146 only applies to "relevant contaminated land remediation" and that a new section is being introduced for "relevant derelict land remediation."

9. Paragraph 6(2)(b) amends section 1146(1)(a) to reflect that a new condition C must also be met if works are to qualify as "relevant land remediation".

10. Paragraph 6(3) amends section 1146(3)(a) to reflect the concept of "relevant harm" as defined in new section 1145(4). As part of the changes the sub-paragraph also deletes section 1146(3)(b).

11. Paragraph 6(4) inserts a new section 1146(3A), "Condition C" which gives HM Treasury the power to exclude by order methods of remediation that are considered inappropriate.

12. Paragraph 6(5) amends section 1146(5) to reflect the changes in what constitutes contaminated land.

13. Paragraph 6(6) amends the heading of section 1146 to reflect that the section only applies to contaminated land.

14. Paragraph 7 adds a new section 1146A "Relevant derelict land remediation", which defines those activities that qualify as relevant derelict land remediation.

15. Paragraph 8 amends the heading of chapter 2 of Part 14, to reflect the extension of the relief to include derelict land.

16. Paragraph 9(2) amends section 1147(2), "Condition A". It reflects the introduction of the concept that to qualify a company must hold a major interest in the land.

17. Paragraph 9(3) amends section 1147(3), "Condition B", to reflect the extension of the relief to include derelict land.

18. Paragraph 10(2) amends section 1149(2), "Condition A". It reflects the introduction of the concept that to qualify a company must hold a major interest in the land.

19. Paragraph 10(3) introduces a replacement section 1149(3) that reflects the extension of the relief to include derelict land.

20. The new section 1149(3)(b) sets out that to qualify, derelict land has to have been derelict throughout the period from 1 April 1998, or acquisition (if earlier).

21. The new section 1149(3A)(a) allows HM Treasury to specify, by order, circumstances in which work may be qualifying expenditure for the purposes of Part 14 of CTA even though the contamination occurred during the period of ownership.

22. The new section 1149(3A)(b) allows HM Treasury to amend by order the date set out in section 1149(3)(b)(ii), currently 1 April 1998.

23. Paragraphs 11(3) and (5) amend section 1150 to reflect the extension of the relief to include derelict land and the exclusion of cases where the polluter may indirectly benefit from the relief.

24. Paragraph 11(4) introduces new sections 1150(2) and 1150(3).

25. Section 1150(2) denies relief if the person responsible, whether wholly or in part, for the land being in a contaminated or derelict state, or a person connected with that person has a "relevant interest in the land".

26. Section 1150(3) sets out what is a "relevant interest in the land". It means that relief is not available under Part 14 of CTA if the polluter, or a person connected to the polluter retains an interest in the land such as a licence to occupy. It excludes from the relief cases where the polluter sells the land with an option to re-acquire the land after it has been cleaned up. Section 1150 (3)(b) excludes cases where the consideration received by the polluter reflects the value of the land after

remediation. This is so that the polluter does not indirectly obtain the benefit of the relief.

27. Paragraph 12(2) amends section 1161(2), "Condition A". It reflects the introduction of the concept that to qualify a company must hold a major interest in the land.

28. Paragraph 12(3) amends section 1161 to reflect the extension of the relief to include derelict land and introduces new section 1161(3A).

29. New section 1161(3)(b) sets out that to qualify, derelict land has to have been derelict throughout the period from 1 April 1998, or acquisition (if earlier).

30. New section 1161(3A)(a) allows HM Treasury to specify, by order, circumstances in which work may be qualifying expenditure for the purposes of Part 14 of CTA even though the contamination occurred during the period of ownership.

31. New section 1161(3A)(b) allows HM Treasury to amend by order the date set out in section 1161 (3)(b)(ii), currently 1 April 1998.

32. Paragraph 13 introduces a replacement section 1162 that aligns the treatment of life insurance companies with that of other companies.

33. Paragraph 14 amends section 1163 to reflect the extension of the relief to include derelict land.

34. Paragraph 14(4) introduces new sections 1163(2) and (3). These mean that relief is not available under Part 14 of CTA if the polluter, or a person connected to the polluter retains an interest in the land, such as a licence to occupy. It excludes cases where the polluter sells the land, with an option to re-acquire the land after it has been cleaned up. It also excludes cases where the consideration received by the polluter reflects the value of the land after remediation. This is so that the polluter does not indirectly obtain the benefit of the relief.

35. Paragraph 17 amends section 1173 to reflect the extension of the relief to include derelict land.

36. Paragraph 18 deletes section 1174, the introductory section on subcontractor payments. This reflects that the rules on sub-contractor payments are being amended so that they no longer apply to payments to unconnected sub-contractors.

37. Paragraph 19 amends section 1175 so that the rules on sub-contractor payments no longer apply to unconnected sub-contractors.

38. Paragraph 19(2) inserts a new subsection (1A) into section 1175 which defines a "sub-contractor payment".

39. Paragraph 19(3) amends section 1175(2) so that the subsection defines the amount of "qualifying expenditure on connected sub-contracted land remediation".

40. Paragraph 19(4) amends sections 1175(3)(a)-(b) so that it includes both expenditure incurred by the sub-contractor and also expenditure incurred by another person to whom the sub-contractor further sub-contracts the work.

41. Paragraph 20 deletes section 1176, "qualifying expenditure on sub-contracted land remediation: other cases" so that there will be no special rules on payments to unconnected sub-contractors.

42. Paragraph 21 amends section 1178, ("persons having a "relevant connection" to a company) to reflect the extension of the relief to derelict land and the introduction of the concept that to qualify a company must hold a major interest in the land.

43. Paragraph 22 inserts a new section 1178A which introduces and defines a "major interest in land". This provides a clearer definition of the interest in land needed to qualify for relief under Part 14 of CTA.

44. Section 1178A(2) sets out the meaning "of a freehold interest in the land" under the land law in England and Wales, Scotland and Northern Ireland.

45. Section 1178A(3) sets out the meaning of "the acquisition of a relevant leasehold interest in land" under the land law in England and Wales, Scotland and Northern Ireland.

46. Section 1178A(4) sets out the minimum length of a lease qualifying as a major interest in land for the purposes of Part 14 of CTA.

47. Paragraph 23 amends section 1179, deleting the references to "harm", "Land" and "substance".

48. Paragraph 24 makes various amendments to section 76(7) of the Income and Corporation Taxes Act 1988, which are required as result of these legislative changes.

49. Paragraph 25 makes various amendments to Schedule 18 to Finance Act 1998, which are required as result of these legislative changes.

50. Paragraph 26 makes various amendments to Schedule 4 (index of expressions) to CTA which are required as result of these legislative changes.

51. Paragraph 27 sets out that orders made before 6 April 2010 under powers in the Schedule may have effect for expenditure incurred on or after 1 April 2009.

52. Paragraph 28 applies the amended Land Remediation Relief to expenditure incurred on or after 1 April 2009. It also excludes from the scope of the amended Land Remediation Relief, expenditure actually incurred before 1 April 2009, but deemed to have been incurred on or after 1 April 2009 under section 61 of CTA (pre-trading expenditure).

BACKGROUND NOTE

53. In 2004, the Barker Review of Housing Supply recommended that Land Remediation Relief should be extended to promote the remediation of long-term derelict sites.

54. The Government published its response to the consultation in "Tax incentives for development of brown-field land: a consultation response", in December 2007. In this the Government announced its intention to extend Land Remediation Relief to provide an incentive to bring long term derelict land back into productive use. The Government also announced its intention to extend Land Remediation Relief to include the cost of removing Japanese Knotweed. These changes are to take effect from 1 April 2009.

55. This legislation both extends relief to expenditure on long-term derelict land and refocuses the existing relief on the remediation of land contaminated by previous industrial activity or on the removal of Japanese Knotweed.

SECTION 27 AND SCHEDULE 8: VENTURE CAPITAL SCHEMES

SUMMARY

1. Section 27 introduces Schedule 8, which makes changes to the three venture capital schemes – the Enterprise Investment, Venture Capital Trust and Corporate Venturing Schemes (EIS, VCTs and CVS).

DETAILS OF THE SCHEDULE

Enterprise Investment Scheme

2. Paragraphs 1-5 of the Schedule make changes to Schedule 5B of the Taxation of Chargeable Gains Act 1992 (TCGA), which governs the deferral of capital gains under EIS

3. Paragraph 2 amends paragraph 1(2) of Schedule 5B. Currently 80 per cent of money raised by a share issue has to be employed by the company in a qualifying activity within 12 months of the issue of shares (or the time the trade commences, whichever is later) and the balance within a further 12 months. The paragraph replaces this rule with a condition that all the money must be employed within two years of the date of the issue (or commencement of trade if this is later).

4. In addition, the paragraph completely removes the conditions relating to employment of money raised from non-qualifying shares issued on the same day as qualifying shares.

5. Paragraph 3 makes changes to paragraph 1A of Schedule 5B (which deals with failures of the conditions), reflecting the new simplified conditions.

6. Paragraphs 4 corrects an anomaly concerning EIS reinvestment relief which can arise on the occasion of a share for share exchange.

7. Normally, share for share exchanges are not treated as a disposal of the old shares for taxation purposes. But where EIS deferral relief was attributable to the old shares, the rules in Schedule 5B prevent the share for share rules from applying, to ensure that the exchange is a chargeable event bringing the deferred gain back into charge.

8. However, this means that there is a disposal of the old shares for tax purposes, so that, in addition to the deferred gain being brought back into charge, a taxable gain can arise in relation to the old shares. As a result of the changes made by paragraph 4, on the occasion of a share for share exchange qualifying under sections 135 and 136 of TGCA, any deferred gain will be brought back into charge as before but no gain or loss will be brought into charge in respect of the disposal of the shares that form the subject of the exchange.

9. Sub-paragraph (2) amends paragraph 9(1) Schedule 5B to TGCA and inserts a new sub-paragraph (1A) in paragraph 9 of Schedule 5B to TGCA, so it can no longer disapply sections 135 and 136 of TGCA generally but can only disapply sections 135 and 136 for the purposes of the application of paragraphs 3 and 4 of Schedule 5B (which provide for the deferred gain under EIS to be brought back into charge).

10. Sub-paragraphs (3) and (4) make consequential amendments to other parts of paragraph 9 of Schedule 5B to TGCA to ensure that the existing provisions in paragraph 9 governing when sections 135 and 136 are disapplied operate in relation to the more limited scope of the effect of the disapplication provided for in new sub-paragraph (1A).

11. Paragraph 6 amends section 158 of the Income Tax Act 2007 (ITA) to remove the restrictions on investments in one year being relieved against income of the preceding earlier year ("carry-back").

12. In particular, paragraph 6(2) removes the limitation that only the costs of shares purchased before 6 October may be carried back, and paragraph 6(3) removes the £50,000 limit on the amount that may be carried back, and the rule restricting carry-back to half of shares issued. Thus the only remaining restriction on carrying back relief is the overriding investment limit for any year.

13. Paragraph 7 amends section 175 of ITA. Currently 80 per cent of money raised by a share issue has to be employed by the company in a qualifying activity within 12 months of the issue of shares (or the time the trade commences, whichever is later) and the balance within a further 12 months. The paragraph replaces this rule with a simple condition that all the money must be employed within two years of the date of the issue (or commencement of trade if this is later).

14. In addition, the paragraph completely removes the conditions relating to employment of money raised from non-qualifying shares issued on the same day as qualifying shares.

Corporate Venturing Scheme

15. Paragraph 8 amends paragraph 36 of Schedule 15 to the Finance Act (FA) 2000, removing the 80 per cent condition from the CVS and again replacing it with a rule that 100 per cent of the money raised be employed in the qualifying trade within two years.

Venture Capital Trusts

16. Paragraph 9 amends section 293 of ITA to replace the current use of money raised requirement. The new requirement will be that the money raised should be wholly employed within two years of the issue of the relevant holding or, if the issue takes place before the commencement of the intended trade, within two years of commencement.

BACKGROUND NOTE

17. The three venture capital schemes are designed to assist smaller higher risk trading companies to raise finance by offering a range of tax reliefs to investors.

18. A consultation on the EIS was held in 2008 (*The Enterprise Investment Scheme: A Consultation Document*). The Government's response was published in November 2008. The proposed changes to the EIS in the Finance Act were set out in that response document.

19. The changes to the CVS and VCTs parallel those made to EIS. The Government seeks to keep conditions aligned across the three Schemes where appropriate.

20. The schemes were approved as State Aid by the European Commission on 29 April 2009.

SECTION 28 SCHEDULE 9: PREFERENCE SHARES - GROUP RELIEF

SUMMARY

1. Section 28 and Schedule 9 provide that holders of certain preference shares, including those commonly issued by financial institutions as part of their regulatory Tier 1 capital base, are not treated as equity holders of a company. Previously only the holders of fixed-rate preference shares qualified for this exclusion. It is necessary to distinguish between equity holders and non-equity holders in order to identify companies that are sufficiently under common ownership so as to be regarded as belonging to the same group for tax purposes.

DETAILS OF THE SCHEDULE

2. Paragraph 1 introduces the amendments which follow. These amend Schedule 18 to the Income and Corporation Taxes Act 1988 (ICTA).

3. The rules in Schedule 18 to ICTA establish who are to be regarded as the equity holders in a company and to what extent, by reference to their shareholdings or entitlement to share in the company's distributable profits or assets. The rules are used primarily to determine a company's entitlement to surrender or claim group relief from related companies for trading losses and other amounts. A number of other tax provisions rely upon the rules in Schedule 18. Those provisions include chargeable gains, real estate investment trusts, venture capital relief and leasing rules.

4. Paragraph 2 details the amendments to paragraph 1 of Schedule 18 to ICTA. The previous exclusion from treatment as an equity holder for holders of 'fixed-rate preference shares' is replaced by a new exclusion for holders of 'relevant preference shares'. Relevant preference shares must be issued for new consideration, so cannot, for example, be a bonus issue. They may carry either no rights to dividends, or rights which fulfil the conditions set out in new paragraph 1A of Schedule 18 to ICTA. Shares which carry no rights to dividends are explicitly included as relevant rate preference shares.

5. Paragraph 3 inserts new paragraph 1A into Schedule 18 to ICTA. This sets out the rights to dividends carried by shares that are relevant preference shares. The holders of relevant preference shares are not treated as equity holders in a company. It is necessary to distinguish between equity holders and non-equity holders in order to identify companies that are sufficiently under common ownership so as to be regarded as belonging to the same group for tax purposes.

6. New paragraph 1A(1) determines that where preference shares carry a right to a dividend, they will be relevant preference shares if they fulfil the 'reasonable commercial return' condition and one of conditions A, B or C set out in the following sub-paragraphs. The reasonable commercial return condition is carried over from the definition of a fixed-rate preference share, so is unchanged.

7. New paragraph 1A(2) sets out condition A. This is met by shares that carry rights to a dividend and would previously have been regarded as fixed-rate preference shares.

8. New paragraph 1A(3) sets out condition B. This is met where the dividend payable on the shares is not fixed absolutely, but is fixed by reference to a published variable rate, either a market rate of interest such as a central bank base rate, or to an appropriate retail prices index.

9. Both conditions A and B are further qualified to ensure that the terms under which the shares are issued do not grant the issuer a right to pay dividends of less than the nominal rate. Where shares are issued under such terms, then condition C is relevant.

10. New paragraph 1A(4) sets out condition C. This is met in cases where condition A or B would have been met, but for the fact that the company has a right to reduce the dividends paid on the preference shares below the nominal rate in circumstances that are covered by the 'relevant circumstances' set out in new paragraph 1A(5).

11. If the terms under which the shares have been issued clearly permit the company to reduce or not to pay the dividends only in these relevant circumstances, and no other, then condition C will be met by virtue of new paragraph 1A(4)(a).

12. However, there will be some circumstances in which the terms on which shares are issued are not in fact explicit. For example, the terms of issue may grant the directors of the company a degree of discretion as to whether to pay a dividend, or to pay a reduced dividend. In such cases, new paragraph 1A(4)(b) allows wider factors to be taken into account so that condition C will be met where having regard to all the circumstances it is reasonable to assume that the company is likely to reduce or not to pay the dividends in the relevant circumstances, and no other.

13. New paragraph 1A(5) sets out the relevant circumstances for the purposes of the preceding sub-paragraph. The first circumstance is when the company is in severe financial difficulties at the time the dividend is or would be payable. The second circumstance covers the situation where the dividend is reduced or not paid in order to follow a recommendation of a relevant regulatory body.

14. New paragraph 1A(6) provides a power for the Treasury to make an order specifying what will be regarded as constituting 'severe financial difficulties' for these purposes.

15. New paragraph 1A(7) defines a "relevant regulatory body" in terms which cover the Financial Services Authority in the UK or an equivalent regulator in another State.

16. Paragraph 5 is the commencement rule. Shares can be relevant preference shares in relation to any accounting period that commences on or after 1 January 2008, irrespective of when the shares were issued.

17. Paragraph 6 permits a company to make an election to disregard the new rules for 'relevant preference shares' in respect of any shares that it had already issued, or was about to issue, when the changes were first announced by a Written Ministerial Statement on 18 December 2008. Apart from shares that were in the process of being issued, an election will not have any effect for shares issued after 18 December 2008, where the revised rules will apply.

18. Paragraph 7 sets out how make an election, and specifies that once made, it cannot be withdrawn.

19. Paragraph 8 ensures that the changes to Schedule 18 to ICTA do not change the meaning of a 'fixed-rate preference share' for the purposes of the controlled foreign company rules in paragraph 1(7) of Schedule 25 to ICTA.

BACKGROUND NOTE

20. The policy underlying these changes is that the holders of preference shares that provide the holder with no more than an interest like return should not be regarded as equity holders in the issuing company.

21. The central change introduced by this section and Schedule was announced by a Written Ministerial Statement on 18 December 2008. A copy of that statement is available on the HMRC website.

SECTION 29 SCHEDULE 10: SALE OF LESSOR COMPANIES ETC - REFORMS

SUMMARY

1. Section 29 and Schedule 10 make changes to Schedule 10 to the Finance Act (FA) 2006 to ensure that the Schedule operates fairly.

DETAILS OF THE SCHEDULE

2. Paragraph 2 makes changes to paragraph 7 of Schedule 10 by introducing in sub-paragraph (9) conditions to be satisfied before sub-paragraph (8)(b) applies. The conditions ensure that sub-paragraph (8)(b) only applies to plant or machinery acquired on or after 5 December 2005 or acquired at any time from a person connected to the company on 5 December.

3. Paragraph 3 inserts new paragraph 13A which sets out the circumstances where there is deemed to be no qualifying change in ownership. There is no qualifying change in ownership if the interest remains the same or the percentage of share capital held by the principal company remains unchanged.

4. Paragraph 4 amends paragraph 17 of Schedule 10 to FA 2006 by amending the condition in sub-paragraph (8) to be satisfied before sub-paragraph (7)(b) of paragraph 17 applies.

5. Paragraph 6 inserts new paragraph 23A so that in circumstances where all of the companies that carried on the business in partnership cease to have a share in the profits or losses of the business and as a consequence the plant or machinery is treated as disposed of for a value equal to its open market value then no amount of income will be treated as received for the purposes of paragraph 23.

6. Paragraph 7 changes the application of paragraph 32 so that it applies only when there is a percentage increase over the whole day and sets the calculation for determining the amount of the expense allocated to the other company as a consequence of a percentage increase.

7. Paragraph 8 makes changes to paragraph 39 of Schedule 10. The changes extend the period over which a loss derived from the expense can be utilised and provide for an increase in the amount of any loss not utilised.

8. Paragraph 9 sets out when the legislation will have effect. Changes made by paragraph 8 allowing extended access to losses derived from the 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.

BACKGROUND NOTE

9. This Schedule makes changes to Schedule 10 to FA 2006 to ensure that it operates fairly, particularly in the context of a leasing business carried on by a company owned by a consortium or carried on by companies in partnership. In addition it extends the period over which the buying group can access losses derived from the expense and maintains the value of any unutilised loss over a similar period.

10. Schedule 10 was introduced in response to a well-established pattern of avoidance involving the sale of a lessor company with deferred tax profits. Groups sought to turn the temporary tax timing advantage gleaned from a claim to capital allowances into a permanent deferral by selling lessor companies with deferred tax profits to structural loss-makers who were then able to utilise losses to reduce the taxable profits of the lessor company.

11. The legislation is triggered when a lessor company changes hands. A charge and matching relief are calculated to reflect the tax timing advantage gained by a claim to capital allowances. The charge affects the selling group and the relief benefits the buying group.

12. The legislation has operated successfully but it has become clear that where there have been more complex transactions involving businesses carried on by companies in partnership and businesses carried on by companies owned by consortia it has had unexpected results.

13. The changes introduced here ensure that no Schedule 10 charge arises when a partnership is dissolved or a consortium company is transferred intra-group and that a company carrying on a leasing business in partnership that increases its interest in the business is allocated an appropriate amount of relief.

14. Changes to extend the period over which a loss derived from the expense is available to set against profits of the purchaser's wider group along with measures to ensure it retains its value over this period have been introduced in response to discussions with the leasing industry. These changes will benefit buying groups that are temporarily loss-making in the current economic downturn.

SECTION 30 AND SCHEDULE 11: TAX RELIEF FOR BUSINESS EXPENDITURE ON CARS AND MOTOR CYCLES

SUMMARY

1. Section 30 and Schedule 11 make provision for the reform of the rules for tax relief for business expenditure on the purchase and hire of cars and motor cycles. The rate at which capital allowances can be claimed and the proportion of rental payments that may be deducted for tax will be determined by the carbon dioxide emissions of the car, rather than its cost as under the current rules. Motor cycles are taken out of the definition of a car for capital allowances and for the purposes of restricting the tax deduction for lease rental payments.

DETAILS OF THE SCHEDULE

2. This Schedule is in two parts; the first part details the amendments that are made to the Capital Allowances Act 2001 (CAA) in respect of the changes to the capital allowances rules. The second part details amendments to other Acts to effect the changes to rules restricting deductions for car hire expenses.

Part 1 - Capital Allowances

Plant and machinery allowances for cars and motor cycles

3. Paragraph 2 amends general exclusion 2 in section 38B of CAA, which states that expenditure on cars cannot qualify for annual investment allowance, by substituting the new definition of a car in section 268A of CAA for the old definition in section 81 of CAA. Section 81 of CAA (extended meaning of "car") is repealed by paragraph 5 below.

4. Paragraph 3 substitutes the new definition of a car in section 268A of CAA for the old definition in section 81 of CAA in the second exclusion in section 46(2) of CAA which provides that expenditure on cars cannot be first-year qualifying expenditure.

5. Paragraph 4 repeals sections 74 to 79 of CAA (cars above the cost threshold). Sections 74 and 75 of CAA require that, if expenditure on a car exceeds £12,000, the expenditure be pooled in a single asset pool. Writing down allowances (WDA) are restricted to a maximum of £3,000 per annum.

Section 76 of CAA deals with contributions. It provides that where a person makes a contribution towards another party's expenditure on a car costing more than £12,000, the person making the contribution can claim the WDAs. However, the available WDAs are restricted to a total of £3,000.

Sections 77 to 78 of CAA require that when a car is used for a non-qualifying purpose (e.g. private use) that the WDA is further restricted on a just and reasonable basis to reflect business use. On disposal of the vehicle any balancing charges/allowances are restricted in the same way.

Section 79 of CAA is an anti-avoidance measure that may apply in certain circumstances when cars (in single asset pools) are sold to connected parties.

6. Paragraph 6 substitutes the new definition of a car in the table in section 84 of CAA, which lists expenditure that cannot be treated as short-life asset expenditure.

7. Paragraph 7 amends section 104A (special rate expenditure) of CAA. Expenditure on cars which are not main rate cars, i.e. those with tail pipe emissions exceeding 160 grams of CO_2 per kilometre driven, qualifies for writing down allowances at the special rate of 10 per cent.

8. Sub-paragraph (2) amends subsection (1) of section 104A of CAA so that expenditure on or after the second relevant date on a car that is not a main rate car is treated as special rate expenditure.

9. Sub-paragraph (3) amends subsection (2) of section 104A of CAA for the introduction of a second relevant date.

10. Paragraph 8 inserts new section 104AA of CAA (meaning of "main rate car"). Generally it is a car with CO_2 emissions of 160 grams per kilometre driven or less, although all cars that were first registered before 1 March 2001 are main rate cars.

11. Paragraph 9 inserts new section 104F into CAA. This is to prevent the artificial generation of balancing allowances by groups of companies who engineer the cessation of a group company's business of providing cars, only for another company in the group to continue a similar activity. It applies if conditions A, B and C are met.

12. New subsection (4) explains that condition C is that the company would otherwise be entitled to a balancing allowance in the special rate pool and that this balancing allowance would be greater than the total of any balancing charges less any balancing allowances in any other pools.

13. New subsection (5) explains that the balancing allowance that the company is entitled to in respect of the special rate pool, is limited to the balancing charges less balancing allowances arising on the other pools. This is so that a company will not be denied a balancing allowance on the special rate pool while at the same time bringing a balancing charge into account in another pool.

14. New subsections (6) and (7) explain that an amount equal to the balancing allowance, that the ceasing company would otherwise have been entitled to, will be treated as expenditure incurred by another company in the same group relief group, provided it carries on a qualifying activity of making cars available to other persons. This is the relevant company.

15. New subsection (9) explains that when the ceasing company's penultimate chargeable period and the period in which the relevant company is treated as acquiring the expenditure overlap, the expenditure acquired is apportioned so that writing down allowances cannot be claimed by the relevant company for the overlapping period. This is to prevent writing down allowances on the expenditure being claimed by both companies for the same period.

16. Paragraph 10 inserts new section 208A into CAA. This is an anti-avoidance rule to prevent persons selling a car in a section 206 pool at undervalue in order to generate a balancing allowance.

17. New subsection (2) explains that a section 206 car is one that is allocated to a single asset pool because it is used partly for a purpose other than a qualifying activity.

18. Paragraph 11 inserts new sections 268A, 268B and 268C (*Cars etc*) into CAA. New section 268A defines the terms "car" and "motor cycle". New section 268B defines an electrically-propelled vehicle. New section 268C defines various terms relating to emissions.

Consequential amendments of CAA 2001

19. Paragraph 13 omits subsection (7) from section 33. This subsection explained that the extended meaning of "car" in section 81 of CAA did not apply to section 33, but section 81 is deleted by paragraph 3 above.

20. Paragraph 14 makes amendments to section 45D of CAA, which provides that expenditure on electric cars or those with CO_2 emissions of 110g/km or less qualifies for a first-year allowance. These cars still qualify for first-year allowance but the wording of the section has been changed to be consistent with new sections 268A and 268B of CAA.

21. Paragraph 16 amends section 55(6) of CAA (determination of entitlement or liability) so that a company is not entitled to a balancing allowance when the conditions in the anti-avoidance provision in the new section 104F of CAA are met.

22. Paragraph 18 amends section 66 of CAA (list of provisions about disposal values) to omit the reference to section 79 as it is being repealed; new section 208A of CAA is included.

23. Paragraph 19 sets out the consequential changes that are needed to the table in section 84 of CAA (which describes the circumstances where short-life asset treatment is ruled out) to reflect the new definition of hire cars for disabled people. Expenditure on hire cars for disabled people will still qualify for short-life asset treatment.

24. Paragraph 20 makes amendments to section 86 (short-life assets) of CAA. If the final chargeable period for a short life asset pool has not occurred before the four year cut-off, the balance of unrelieved expenditure on a car in a short life asset pool will be taken to either the main pool or special rate pool, depending on its CO_2 emissions.

25. Sub-paragraph (2) amends "main pool" in subsection (2)(b) to "appropriate pool" as some special rate cars may be short life assets.

26. Paragraph 22 inserts new section 268D into CAA. New subsections (1) and (2) define the meaning of a hire car for a disabled person and a disabled person. A

disabled person is a person in receipt of the listed allowances or supplements (the list is unchanged from that in section 82(4) of CAA).

27. Paragraph 23 amends the defined expressions in Part 2 of Schedule 1 (defined expressions) to reflect the new definitions that are being introduced.

28. Sub-paragraph (3) adds a number of new definitions for the purposes of Part 2 of CAA .

29. Paragraph 25 repeals paragraph 6 in Schedule 19 to Finance Act 2002, that refers to cars in a single asset pool because of their cost, as a consequence of the changes being made by this Schedule.

Commencement and transitionals: introduction

30. Paragraphs 26 to 33 set out the dates and events from which the new legislation has effect by reference to "relevant dates". They also provide transitional rules for expenditure incurred on cars and motor cycles before 1 April 2009 (for corporation tax) and 6 April 2009 (for income tax).

31. Paragraph 26 defines the "relevant dates" for income tax and corporation tax purposes.

32. Paragraph 27 explains the difference between "new expenditure" and "old expenditure" by reference to the relevant dates in paragraph 26. The amendments made by this Part of this Schedule (the new rules) have effect from different dates for old and new expenditure.

Commencement

33. Paragraph 28(1) explains that the amendments made by this Part of the Schedule apply only to new expenditure (as defined in paragraph 27 of the legislation). Sub-paragraph (2) provides that the new section 208A of CAA (disposal value in avoidance cases) will only apply where a person disposes of a car, the expenditure on which was new expenditure. Section 79 of CAA, which is repealed, will not apply to new expenditure.

34. Paragraph 29 explains that although sections 74 to 79 are repealed, the repeal is only effective for "old" expenditure for chargeable periods beginning on or after 1 (for persons within the charge to corporation tax) or 6 (for persons within the charge to income tax) April 2014.

35. Sub-paragraph (1) provides that the new rules do not apply to old expenditure until the first chargeable period beginning on or after the third relevant date (see paragraph 26); sections 74 to 78 of CAA will continue to apply to old expenditure until then.

36. Sub-paragraph (2) provides that section 79 of CAA does not apply to old expenditure for chargeable periods beginning on or after the third relevant date, but will apply to old expenditure until then.

Transitionals

37. Paragraph 30(1) applies where expenditure is incurred on a car and some of it is old expenditure and some is new.

Sub-paragraph (2) provides that in these circumstances the expenditure must be treated as if it was on the provision of separate but identical cars or motor cycles so that the new expenditure is treated under the new (amended) rules and the old expenditure is treated under the old rules.

Sub-paragraph (3) explains that when a person disposes of a car, in respect of which both new and old expenditure was incurred, the disposal proceeds must be apportioned between new rules pools and old rules pools on a just and reasonable basis.

38. Paragraph 31(1) explains how old expenditure, in a single asset pool by virtue of section 74 of CAA, is to be treated at the end of the transitional period, that is, in the first chargeable period beginning on or after 1 or 6 April 2014. Sub-paragraphs (2) and (3) provide that any unrelieved old expenditure is carried forward to the main pool and that this must be done in the first chargeable period beginning on or after 1 or 6 April 2014.

39. Paragraph 32 provides that any orders that may be made by the Treasury under section 82(4)(d) of CAA (in connection with payments to disabled persons) before the first relevant date and which are still in effect, have effect on and after that date as if they had been made under new section 268D(2)(d).

Part 2 - Restrictions on Deductions for Hire Expenses

40. The following paragraphs make a number of amendments to the Income Tax (Trading and Other Income) Act 2005 (ITTOIA), Corporation Taxes Act 2009 (CTA) and Income and Corporation Taxes Act 1988 (ICTA).

41. Paragraph 35 amends section 31(1)(b) to reflect the fact that motor cycles are no longer to be treated as cars.

42. Paragraph 36 makes amendments to section 48 of ITTOIA which restricts the deductions from profits that may be made in respect of the costs of hiring certain cars.

43. Paragraph 36(2) deletes "or motor cycle" where it first occurs in section 48(1) of ITTOIA, so that motor cycle hire expenses are no longer restricted. It replaces sub-paragraphs (2)(a) and (2)(b) with new sub-paragraphs (2)(a), (b), (c) and (d) which describe the different types of cars to which the restriction does not apply under the new rules.

44. Sub-paragraphs (3) and (4) amend sections 48(2) and (4) of ITTOIA by deleting the existing formula used to calculate the reduction that is applied to the deduction for rental costs of leased cars that cost more than £12,000 when new, and replacing it with a flat rate 15 per cent reduction, that will apply in respect of cars that emit more than 160 grams of CO_2 per kilometre driven.

45. Sub–paragraph (6) deletes section 48(5) of ITTOIA (which gives the Treasury a power to amend by Order the calculation at section 48(3) of ITTOIA); this is no longer required as the old calculation has been replaced with a flat rate reduction.

46. Paragraph 37 makes various amendments to section 49 of ITTOIA, which defines the terms used in section 48, and inserts an additional definition.

47. Sub-paragraph (2)(c) inserts a new sub-paragraph 49(1)(za) before section 49(1)(a) of ITTOIA. This provides that a motor cycle, as defined by section 185(1) of the Road Traffic Act 1988, is not a car for the purposes of section 48 of ITTOIA. The effect of this is that expenses incurred on hiring a motor cycle do not fall within section 48.

48. Sub-paragraph (5) amends section 49(6) of ITTOIA which defines the word "new", by deleting the words "and section 48". This is because section 48, as amended, no longer uses the word "new".

49. Paragraph 38 deletes section 50 (hiring cars with low carbon dioxide emissions) of ITTOIA. That section provides that cars with low CO_2 emissions are not subject to the lease rental restriction, but it is now incorporated into section 48(1) of ITTOIA.

50. Paragraph 39 inserts new section 50A into ITTOIA and new section 50B ITTOIA.

51. New section 50A provides that there is no restriction of allowable car hire expenses under section 48 of ITTOIA if the taxpayer meets one of two conditions, A or B

52. New section 50A(2) explains that condition A is met when the car is made available to the taxpayer for a period of 45 consecutive days or less. Hire periods of the same car may be aggregated for the purposes of determining the number of consecutive days.

53. New section 50A(3) explains that condition B is met when the taxpayer makes the car available to another person for more than 45 consecutive days. Hire periods of the same car may be aggregated for the purposes of determining the number of consecutive days.

54. New section 50A(4) provides that condition B is not met when the car is being provided to an employee of the taxpayer or of a person connected with the taxpayer.

55. New section 50A(5) is an anti-avoidance provision.

56. New section 50A(6) provides that where condition B is met for only part of a chargeable period, the taxpayer, when bringing the expenses to account, must apportion them between the parts of that period where the conditions are and are not met according to the respective lengths of those parts of the period.

57. New section 50A(7) provides that periods of consecutive days are amalgamated if the intervening period between them is not more than 14 days.

58. New section 50B provides that where two or more connected persons in a chain of leases would otherwise be required to apply the restriction to expenditure incurred on the hiring of the same car for the same period the restriction will apply to the superior lease in the chain provided it is on arm's length terms.

59. New section 50B(1) provides that section 50B applies to connected persons who incur expenses on the hiring of the same car for the same period who but for section 50B (or section 58B of CTA 2009) would have to apply a reduction to the expenses of car hire.

60. New section 50B(2) provides that this section does not apply if none of the persons in subsection (1) hire the car on commercial terms.

61. New section 50B(3) provides that where, but for this section, the reduction would apply to more than one connected person in respect of expenses incurred on the hiring of the same car for the same period, then the reduction will only apply once, and sets out how the reduction is to be applied.

62. New section 50B(4) provides that the reduction applies to all expenses incurred on the hiring of the same car by the same person; and "commercial arrangements" are such as would reasonably have been expected if the parties to the arrangements had been dealing at arm's length.

Corporation Tax

63. Paragraph 47 makes various amendments to section 56 of CTA 2009 (rules restricting deductions from profits: car or motor cycle hire) to mirror the amendments made to section 48 of ITTOIA detailed in paragraphs 42-45 of this note. Under the current rules there is a restriction in the amount of the expenditure incurred, in the hire of cars that cost over £12,000 when new, that a person can claim against their taxable profits. This system is to be replaced with a system based on the carbon dioxide (CO_2) emissions of cars, which applies a 15 per cent disallowance on expenses incurred on the hire/ lease of cars that emit more than 160 grams of CO_2 per kilometre driven.

64. Paragraph 48 makes various amendments to section 57 of CTA (car or motor cycle hire: supplementary). It also provides a number of supplementary definitions to section 57 CTA. These amendments mirror the amendments made to section 49 of ITTOIA by paragraph 37 as detailed in paragraphs 46-48 of this note.

65. Sub-paragraph (2)(c) inserts a new subparagraph 57(1)(za) before section 57(1)(a), making clear that a motor cycle, as defined by section 185(1) of the Road Traffic Act 1988, is excluded from the 15 per cent leasing reduction.

66. Paragraph 49 deletes section 58 (hiring cars with low CO_2 emissions before 1 April 2013) of CTA. That section provides that cars with low CO_2 emissions are not subject to the lease rental restriction, but is now no longer required as it has been incorporated into section 48(1) of CTA.

67. Paragraph 50 adds new sections 58A and 58B into CTA. The effect of sections 58A and 58B is to insert the same rules that are introduced in sections 50A and 50B of

ITTOIA by paragraph 39 above into CTA. The purpose of section 58A is to provide that the restriction in section 56 does not apply to persons who enter into short term hire (for not more than 45 consecutive days) agreements, or to businesses that provide cars on longer term (more than 45 consecutive days) hire. Section 58B ensures that the restriction of allowable car hire expenses imposed by section 56 does not apply to more than one lessee in a chain of leases.

68. Paragraph 57 makes various amendments to section 1251 of CTA (car or motor cycle hire: companies with investment business). The effect of these amendments is that the rules for restricting the car hire expenses that may be deducted by companies with investment business mirror those for other companies in sections 56 to 58B of CTA.

69. Paragraphs 60 and 61 amends sections 76ZN and 76ZO of ICTA so that the rules restricting the car hire expenses that may be deducted by insurance companies are the same as those for other companies, as detailed in paragraphs 63 to 67 of this note.

70. Paragraphs 62 and 63 amend the rules restricting deductions for car hire expenses in sections 578A and 578B of ICTA to mirror those in sections 56 to 58B of CTA.

Consequential repeals

71. Paragraph 64 sets out consequential amendments to FA 2008 and CTA 2009

Commencement

72. Paragraphs 65 and 66 set out the dates and events from which the new legislation takes effect by reference to relevant dates.

73. Sub-paragraph(1) of paragraph 66 provides that the new rules apply to deductions for expenditure incurred on the hiring of a car or motor cycle under an agreement under which the hire period begins on or after the first relevant date (but see paragraph 67). The first relevant date is 1 April 2009 (for corporation tax) or 6 April 2009 (for income tax).

74. Sub-paragraph (2) provides that for the purposes of this paragraph and paragraph 67, the hire period, in relation to an agreement, begins on the first day on which the car or motor cycle is required to be made available for use under the agreement.

Election for new regime not to apply in certain cases

75. Paragraph 67 provides for an election for the new regime not to apply in certain cases. Where a person entered into an agreement before 8 December 2008 for the hire of a car or motor cycle, but the hire period did not begin until after 1 or 6 April 2009, then the person may elect that the old rules restricting the deduction for the hire expenses under the contract will apply rather than the new. The hire period must, however, begin before 1 or 6 April 2010 for the election to apply. Sub-paragraphs (3) to (6) describe the procedure for the election.

BACKGROUND NOTE

76. Depreciation of fixed assets charged in the commercial accounts of a business is not allowed as a deduction in computing the taxable profits. Instead capital allowances may be given at prescribed rates on certain assets, including plant and machinery. The annual investment allowance provides an annual 100 per cent allowance for the first £50,000 of investment in plant and machinery to all businesses. There are also certain 100 per cent first-year allowances available for certain types of expenditure (such as expenditure on qualifying energy-saving plant or machinery). Otherwise expenditure on plant and machinery assets attracts a writing down allowance (WDA) calculated on a reducing balance basis. Qualifying expenditure has to be pooled for the purpose of determining entitlement to writing down allowances**.** WDA for assets in the main pool is 20 per cent (of unrelieved expenditure in the pool) per annum. The special rate pool was introduced from April 2008 with a WDA rate of 10 per cent.

77. Cars are plant and machinery, but there are special capital allowances rules that apply only to cars. The existing rules are based on the cost of the car:

- expenditure on cars with very low carbon dioxide emissions (up to110g/km) can qualify for 100 per cent first-year allowances, so that the full cost of the car is written off against profits in the period that it is incurred;

- expenditure on cars costing £12,000 or less is allocated to the main pool and WDAs are given at 20 per cent per annum on the reducing balance of expenditure; and

- expenditure on cars costing over £12,000 must be dealt with separately from expenditure on other assets with expenditure on each car being allocated to a single asset pool. The WDAs are calculated in the normal way (at 20 per cent) and then restricted to an annual amount of £3,000. However, when the car is sold any unrelieved depreciation is allowed through a balancing allowance, while any excess allowances over economic depreciation are recovered through a balancing charge.

78. Expenditure on cars that are partly used for non-business purposes is also allocated to a single asset pool to enable an adjustment to be made to restrict the WDA for the proportion of business use of the car (the "private use" adjustment).

79. Certain cars (qualifying hire cars- including cars used as taxis, daily hire cars and cars leased to the disabled) are exempt from the current rules for cars costing over £12,000. Expenditure on such cars is dealt with in accordance with the capital allowances rules for other plant and machinery. Motor cycles are within the capital allowances definition of a car and are therefore subject to the rules for cars.

80. Not all businesses buy their cars but instead hire (lease) them. There are rules that restrict the tax deduction for hire expenses where the car cost more than £12,000. The amount of the lease rental payments that would otherwise be allowed is reduced using a formula or fraction which is based on the retail price of the car when new. This is commonly known as the lease rental restriction (LRR). Every business lessee in a chain of leases is potentially subject to the LRR.

81. The capital allowances rules for cars were originally introduced as a surrogate benefits charge on luxury cars, but the rules are now seen by business as outdated (in today's market more than half of business cars cost more than £12,000) and onerous to comply with. Maintaining separate capital allowance pools for each expensive car is considered to impose a disproportionate compliance burden. This Schedule provides for the reform of these rules that business has pressed for, as announced at Budget 2008. The new rules are designed to fit with the Government's environmental objectives in that they aim to encourage businesses to use cars with lower carbon dioxide emissions. The allowances to which a business is entitled will now be governed by the car's carbon dioxide emissions rather than its cost.

82. The new capital allowances rules for cars generally apply to qualifying expenditure incurred on or after 1 April 2009 for businesses within the charge to corporation tax or 6 April 2009 for businesses within the charge to income tax. 100 per cent first-year allowances continue to be available on cars with very low carbon dioxide emissions (until 31 March 2013) but expenditure on other cars will be allocated to one of the two plant and machinery pools.

83. The appropriate pool is determined by the car's carbon dioxide emissions. Expenditure on cars with carbon dioxide emissions exceeding 160g/km will be allocated to the special rate pool while expenditure on cars with emissions of 160g/km or less will be allocated to the main rate pool. Cars that are partly used for non-business purposes will continue to be allocated to a single asset pool to enable a private use adjustment to be made, but the rate of WDA will depend on the car's carbon dioxide emissions.

84. Expenditure incurred before April 2009 will continue to be subject to the old rules for a transitional period of around five years. Any expenditure remaining in a single asset pool (unless there is any non-business use of the car) will be transferred to the main capital allowances pool at the beginning of the first chargeable period to commence on or after 1 or 6 April 2014.

85. For leases that commenced on or after 1 or 6 April 2009, the special rules that restrict the amount of lease rental payments that can be deducted for tax purposes for a car costing over £12,000 will be similarly reformed. The restriction will be changed to a flat rate disallowance of 15 per cent of relevant payments and will apply only in respect of cars with CO_2 emissions above 160g/km.

86. From April 2009 the LRR will apply to only one lessee in any chain of leases. Broadly, businesses will not be subject to a restriction of their allowable lease rental payments where the car is made available to them for a period of no more than 45 consecutive days. Also a business will not be subject to LRR in respect of expenses it incurs in hiring a car where it makes the car available to a customer for a sub-hire period of more than 45 consecutive days (this exclusion does not apply, however, where a business makes cars available to its employees or the employees of a connected person).

87. Leases that commenced before 1 or 6 April 2009 will continue to be subject to the old rules for the duration of the lease.

88. Hire cars (cars used as taxis, daily hire cars and cars leased to the disabled) that are exempt from the current rules will be fully included in the new rules. However, motor cycles will be excluded from the definition of cars and will not, therefore, be subject to these rules. Expenditure incurred on motor cycles on or after 1 or 6 April 2009 will qualify, where appropriate, for Annual Investment Allowance, first year allowances and to be treated as short life asset expenditure.

89. The changes made by this Schedule represent a simplification of the rules for most businesses (by a reduction in both the numbers of cars in single asset pools and the number of leases that are subject to LRR) and will therefore reduce compliance costs. The changes are part of a package of measures to encourage businesses to choose cars that emit lower levels of carbon dioxide.

SECTION 31 SCHEDULE 12: NOTIONAL TRANSFERS WITHIN A GROUP

SUMMARY

1. Section 31 and Schedule 12 provide groups of companies with a simpler procedure to match the chargeable gains or allowable losses that arise on the disposal of chargeable assets when an election is made, removing the need to actually transfer ownership of assets within a group. Currently when an election is made, an asset is deemed to have been transferred from one group company to another before a disposal outside the group. However, an election cannot currently be made in all the circumstances in which gains or losses can arise; for example where there is no disposal to a third party.

DETAILS OF THE SCHEDULE

2. Paragraph 1 provides that section 171A of the Taxation of Chargeable Gains Act 1992 (TCGA) is replaced with new sections 171A – 171C.

3. New section 171A(1) sets out the three requirements for an election to transfer a chargeable gain or allowable loss between two group companies. The first two requirements are met where a gain or loss accrues to a company at a time when both it and the other company are members of the same group. The third requirement is met if section 171(1) of TCGA would have applied to a disposal of the asset from one to the other immediately prior to the gain or loss accruing. Section 171 of TCGA provides for tax neutrality on the disposal of a chargeable asset from one group company to another. It sets the consideration given for the asset for tax purposes at the amount which would give rise to neither a chargeable gain nor an allowable loss.

4. New section 171A(2) modifies the application of section 171(1A)(b) TCGA in its application for the purposes of the new section 171A (1)(c).

5. Section 171(1A)(b) sets out the condition to be fulfilled by the recipient of an asset on transfer from another company in the same group if no-gain, no-loss treatment is to apply to that transfer. Where the recipient is not resident in the United Kingdom, the condition is that the asset is a chargeable asset in relation to that company. A chargeable asset is one on which any gain from a disposal would be a chargeable gain, and form part of the company's chargeable profits. This requirement cross-refers to section 10B TCGA, which, without the modification provided by new section 171A(2), limits the chargeable profits to gains on assets that are situated in the United Kingdom and used for the purposes of the trade of a permanent establishment.

6. The only condition that is required to be fulfilled by a recipient of the gain or loss to be reallocated to a non-resident group company making an election under new section 171A TCGA is that they are carrying on a trade in the United Kingdom through a permanent establishment.

7. New sections 171A(4) and (5) set out the form of the election, which may be in relation to only part of the gain or loss. Subsection (4) also sets out the time limit for making the election, which is the second anniversary of the end of the accounting period of the company in which the gain or loss accrued.

8. New section 171A(6) ensures that one or more elections will not be valid if, taking into consideration any earlier elections in respect of the same gain or loss, they seek to reallocate more than the total amount of that gain or loss.

9. New section 171A(7) disapplies new section 171A for chargeable gains or allowable losses deemed to accrue to a company under section 179 of TCGA 1992 when it leaves a group (degrouping charges). This is because section 179A continues to apply to these gains and losses.

10. New section 171B sets out the consequences of the making of an election under new section 171A.

11. New section 171B(2) provides that the gain or loss (or any part of it) is treated as having accrued not to the company making the disposal, but to the other company that is party to the election.

12. New section 171B(3) provides that the reallocated gain or loss is treated as accruing at the time that the gain or loss originally accrued.

13. New sections 171B(4) and (5) apply where the company to which the gain or loss is reallocated is not resident in the UK, but trades in the UK through a permanent establishment. Subsection (4) treats any gain or loss reallocated to that company as accruing in respect of a 'chargeable asset' held by the company. Subsection (5) defines a chargeable asset for these purposes as an asset on which any chargeable gain arising on the disposal of the asset would form part of its chargeable profits for UK corporation tax purposes by virtue of section 10B of TCGA. Together these subsections ensure that any gain or loss remains within the scope of UK corporation tax on chargeable gains.

14. New section 171B(6) provides for any payment made between companies that are party to an election under new section 171A, that is made in connection with the election, to be disregarded for corporation tax purposes, to the extent that the payment does not exceed the amount of the reallocated chargeable gain or loss.

15. New section 171C makes particular provision for elections under new section 171A where a company that is party to such an election is an insurance company.

16. New section 171C(2) relaxes the requirement in new section 171A(1)(c) where the company to which any gain or loss is reallocated is an insurance company. This allows such a company to make an election under new section 171A by disapplying section 440(3) of the Income and Corporation Taxes Act 1988. Section 440(3) provides that section 171 of TCGA does not apply to a transfer of an asset held in a company's long-term insurance fund (L-TIF), or to a company's L-TIF.

17. New section 171C(3) disapplies new section 171C(2) where the company in which the gain originally accrues is an insurance company and where the asset is part of its L-TIF prior to the disposal.

18. New section 171C(4) provides that the effect of the election in cases where a gain or loss is reallocated to a company which is an insurance company is that the gain or loss is treated as arising on an asset that is not part of the company's L-TIF.

19. New subsection 171C(5) ensures that the terms 'insurance company' and 'long-term insurance fund' have the same meaning as in section 431(2) ICTA

20. Paragraph 2 provides the consequential amendment to section 179A(5) of TCGA, using the same approach to limit the amount that can be reallocated by an election under that section as in new section 171A(5).

21. Paragraph 5 of Schedule 12 provides that changes made by Schedule 12 will have effect in relation to gains or losses accruing on or after the date of Royal Assent.

BACKGROUND NOTE

22. The new provisions are intended to reduce compliance costs for groups of companies by providing a simpler and comprehensive means of transferring gains and losses so as to allow full matching of gains and losses that arise within different companies in a group.

23. The existing section 171A of TCGA is less comprehensive. It allows group companies to make an election only where there is a disposal of an asset outside the group. The effect of an election under the current provision is to treat that asset as having been transferred between the companies immediately before the disposal outside the group.

SECTION 32 AND SCHEDULE 13: STOCK LENDING: INSOLVENCY ETC OF BORROWER: CHARGEABLE GAINS

SUMMARY

1. Section 32 and Schedule 13 apply for the purposes of tax on chargeable gains where the borrower under a stock lending agreement becomes insolvent and unable to return borrowed stock. They prevent capital gains or losses arising to the extent that collateral is used to replace the borrowed stock with identical stock. The section can have effect where the insolvency occurs on or after 1 September 2008.

DETAILS OF THE SCHEDULE

2. Paragraph 2 amends section 263B (stock lending arrangements) of the Taxation of Chargeable Gains Act 1992 (TCGA). Sub-paragraph (2) of paragraph 2 inserts into section 263B(2) a reference to section 263CA, which is introduced into the TCGA by paragraph 3 of the Schedule. This ensures that section 263B interacts correctly with the new section 263CA.

3. Sub-paragraph (3) makes three amendments to section 263B(4) of TCGA. The first two make explicit that, where there is a deemed disposal by a stock lender of securities that have been lent and will not be returned, the consideration for that deemed disposal is the market value of those securities at the time it becomes clear that they will not be returned to the borrower. It has always been accepted that this is the case, but the opportunity has been taken to make it explicit.

4. The third amendment to section 263B(4) provides that that subsection will not apply if the new section 263CA has effect. This prevents any confusion as to which provisions apply.

5. Sub-paragraph (4) of paragraph 2 removes from section 263B(7) a definition of "interest" that does not apply within section 263B and so is not needed.

6. Paragraph 3 of the Schedule inserts the new section 263CA into the TCGA.

Section 263CA TCGA

7. Subsection (1) of new section 263CA provides the conditions for the section to apply. These are that there is a stock lending arrangement whereby securities are loaned by a lender to a borrower and:

- the borrower becomes insolvent and therefore cannot return the securities to the lender;
- collateral is used to enable the lender to acquire "replacement securities" (securities identical to those loaned to the borrower); and
- the replacement securities are acquired within 30 days of the borrower becoming insolvent.

8. Subsection (2) provides that section 263B(2) applies so that the transfer of the loaned securities from the lender to the borrower under the stock lending arrangement is not treated as disposal of those securities by the lender. The effect is that no chargeable gain or loss arises to the lender as a result of that transfer. This treatment is modified where subsection (5) applies (see paragraphs 11 to 15 below).

9. Subsection (3) provides that when the borrower becomes insolvent he is treated as having acquired the loaned securities which he cannot return to the lender. The borrower is treated as having acquired those securities for consideration equal to their market value at the date the borrower becomes insolvent.

10. Subsection (4) provides that the acquisition of the replacement securities by the lender is treated as though those securities were returned to the lender in accordance with the terms of the stock lending arrangement. This has the effect that the lender is not treated at acquiring those securities at that time, but as though he had held them continuously since he acquired the loaned securities originally.

11. Subsections (5) to (7) address the possibilities that:

- there is sufficient collateral to replace all the loaned securities but the lender decides to replace only some of them;
- all available collateral is used but it is insufficient to enable all the loaned securities to be replaced;
- there is insufficient collateral to enable all the loaned securities to be replaced, but the lender chooses only to use some of the available collateral rather than replacing the maximum number available by use of the whole of the collateral.

12. In each of these cases, the lender is treated as having disposed of the number of securities that are not replaced by utilisation of collateral. This deemed disposal takes place at the date of the borrower's insolvency.

13. Subsection (6)(a) provides that, where the whole of the collateral is used to acquire replacement securities (but it is not enough to replace all the securities), the consideration for the deemed disposal provided for in subsection (5) is nil, so that a loss arises to the lender at that time, based on the lender's cost of acquiring the securities that are not replaced.

14. Subsection (6)(b) has effect if only some of the available collateral is used to acquire some replacement securities. In that case, the consideration received for the deemed disposal under subsection (5) is the difference between:

- the value (at the time of the insolvency) of the replacement securities that could have been acquired by using the whole of the collateral; and
- the value (at that time) of the replacement securities that are in fact acquired by use of the collateral.

The difference will be broadly equal to the value at the time of the insolvency of the amount of collateral not used to acquire replacement securities.

15. Subsection (7) addresses the possibility that the lender may receive a payment in respect of the amount that the borrower owes to the lender, under the terms of the stock lending arrangement, in relation to the securities that could not be replaced because the amount of collateral was insufficient. On receipt of any such payment, a chargeable gain equal to the amount of the payment is treated as arising to the lender at the time the payment is received.

16. Subsection (8) provides that the borrower's liability to the lender resulting from the insufficiency of collateral is not to be treated as a relevant non-lending relationship within Part 6 of the Corporation Tax Act 2009 (CTA). This prevents any of the corporation tax loan relationship rules from applying in a transaction that is within section 263CA of TCGA.

17. Subsection (9) explains what is meant by references in the section to the borrower becoming insolvent.

18. Subsection (10) provides the definition of "collateral" for the purposes of the section, and ensures that terms used in both section 263B and section 263CA have the same meaning in both sections.

19. Paragraph 4(1) of the Schedule provides the commencement for section 263CA and for the changes made by paragraph 2(2) and (3)(c) which import reference to that section into section 263B. They have effect in all cases where the borrower becomes insolvent on or after 24 November 2008. Additionally, where the borrower became insolvent between 1 September 2008 and 23 November 2008 (inclusive), the lender may elect for the changes to apply.

20. The changes to section 263B made by sub-paragraphs (3)(a), (3)(b) and (4) of paragraph 2 are clarificatory, and do not affect the operation of that section. They have effect on and after the date of Royal Assent.

21. Paragraph 4(2) provides rules relating to an election under paragraph 4(1) for the new rules to have effect in relation to an insolvency falling between 1 September 2008 and 23 November 2008 inclusive. These are the normal time limits for amendments of Self Assessment tax returns for the accounting period or tax year in which 24 November 2008 falls.

22. Paragraph 4(3) provides for references in section 263CA(8) to provisions of the CTA to be taken as references to the corresponding provisions that applied for periods before the CTA came into force on 1 April 2009. This ensures that section 263CA operates in the same way in relation to times before and after the CTA has effect.

BACKGROUND NOTE

23. A stock lending arrangement involves the transfer of securities from a "lender" to a "borrower", under an agreement that provides for equivalent securities (identical in nature and number to those transferred) to be returned to the lender at a prescribed date. Although described as a "loan", the transactions involve the transfer of full title to the securities.

24. Because of the temporary nature of the change of ownership, the TCGA includes special rules to ignore the transfer from lender to borrower and the return of the equivalent securities from borrower to lender.

25. However, it is possible that during the currency of a stock lending arrangement, it may become apparent that the equivalent securities will not be returned to the lender. In that case, to recognise that there has been a permanent transfer of the securities, the lender is deemed to have disposed of the securities at the time it becomes apparent that they will not be returned, and the borrower is deemed to acquire them at that time. The consideration for this deemed disposal and acquisition is the market value of the securities at that time. (This is not specifically stated in the legislation as it currently stands, but changes made by this Schedule will make it explicit.)

26. There is one particular circumstance where the rule that the lender is deemed to have disposed of the loaned securities can give an unwanted result. This is where the failure to return the securities results from the borrower's becoming insolvent, and the arrangements include the lodging of collateral or the offering of indemnities by a third party to protect the borrower.

27. In such a case it is possible, by utilising the collateral or calling on the indemnity, to provide the lender with replacement securities exactly as would be the case if the borrower had returned securities under the agreement. Where this occurs, the rule that treats the lender as disposing of loaned securities could result in a chargeable gain arising to a lender, with an associated liability to tax, even though the lender's situation is the same as if the securities had been returned under the stock lending arrangements.

28. This section and Schedule prevent that outcome, treating the provision of replacement securities by use of collateral or indemnity as though they had been replaced under the agreement.

29. It should be noted that the Schedule refers only to "collateral", while this background note talks of both "collateral" and "indemnity". The definition of "collateral" in the section is framed to include indemnity, and the term is used below to describe both collateral and indemnity.

30. The Schedule also covers the situation where collateral is sufficient to replace only some of the borrowed securities, or where the lender chooses not to use available collateral to replace as many of the loaned securities as possible. In such circumstances the lender has effectively disposed of the securities that were not replaced by the collateral.

31. In the case where the lender chooses not to replace as many of the loaned securities as possible, the lender will retain some of the collateral. In that case, the lender is treated as having disposed of the number of loaned securities that were not replaced, and the consideration for that disposal is effectively the value of the collateral that was retained by the lender rather than being used to acquire replacement securities.

32. Where the value of the collateral was insufficient to replace all the loaned securities, under a standard stock lending agreement the borrower would owe the lender an amount equal to the value of the securities that could not be replaced.

33. Where the borrower has become insolvent, it is likely to be some time before it becomes clear whether the lender will receive anything in respect of this debt owed by the borrower. The section therefore provides for immediate relief to the lender by prescribing that, where the whole of the available collateral is used to acquire replacement securities, the lender is treated as receiving no consideration for the deemed disposal resulting from the inadequacy of the collateral. This should result in a loss being treated as arising to the lender on the deemed disposal, and the lender can deduct this loss from chargeable gains arising to him.

34. If, at a later date, the lender does receive any payment in respect of the debt, the whole amount received is treated as a chargeable gain arising at the time of receipt. The broad effect of this arrangement is that the lender's net gain or loss reflects his actual gain or loss on the securities that were not returned (taking account of the amount actually received in respect of the debt owing by the borrower), but at the time of the insolvency of the borrower the lender can claim a loss of the whole of his allowable expenditure on the securities in question, reflecting that there is no immediate receipt and that it may be some time (if ever) before the lender receives anything in respect of the debt.

35. Section 83 and Schedule 37 complement this section and Schedule, giving relief from charges to stamp duty or stamp duty reserve tax in circumstances where a party to a stock lending arrangement becomes insolvent.

SECTION 33: FSCS PAYMENTS REPRESENTING INTEREST

SUMMARY

1. Section 33 ensures that people who have or will receive compensation from the Financial Services Compensation Scheme (FSCS) that includes a payment representing interest are taxed in the same way as if the payment were interest paid by the financial institution that went into default. Where the FSCS has calculated a payment as if it were interest (accrued but unpaid by the financial institution) from which tax had been deducted then the section enables the recipient to treat the amount deducted by the FSCS in the same way as if it were tax deducted from interest.

DETAILS OF THE SECTION

2. Subsection (2) includes new section 380A Income Tax (Trading and Other Income) Act 2005 (ITTOIA) on the list of payments treated as interest in section 369 of that act.

3. New section 380A introduces provisions to ensure payments representing interest made under the FSCS are treated as if they were interest chargeable to income tax.

4. New section 380A(1) provides that any payment made under the FSCS representing interest is treated as interest in the hands of the recipient.

5. New subsection (3) provides for the amount treated as interest to include any amount equivalent to income tax deducted from the payment representing interest under the FSCS.

6. New section 979A of the Income Tax Act 2007 (ITA) ensures that where the FSCS has calculated compensation as if a sum of tax had been deducted then the recipient can bring that sum into account when calculating their tax liability.

7. New section 979A(1) provides that the new section applies if a payment is made under the FSCS which has been calculated as if the payment were interest from which tax would have been deducted.

8. New subsection (2) ensures that the recipient is treated as if they had been paid the relevant gross amount from which a sum representing income tax had been deducted at source.

9. New subsection (3) allows the sum treated as income tax to be repaid to the recipient or set off against their income tax liability.

10. New subsection (4) defines the "relevant gross amount" as the total of the sum representing income tax deducted by the FSCS and the payment representing interest.

11. New subsection (5) provides an obligation on the scheme manager of the FSCS to supply certain information to the recipient if requested to do so in writing. And new subsection (6) provides that the recipient can enforce such a request.

12. Subsection (5) of the section provides that the section applies to payments made by the FSCS on or after 6 October 2008.

BACKGROUND NOTE

13. The FSCS is the UK's statutory fund of last resort for customers of authorised financial services firms. The FSCS can pay compensation if a firm is unable, or likely to be unable, to pay protected claims against it. Since the beginning of October 2008 a number of banks have ceased trading in the UK. Some of the deposits held by these banks have been transferred to other solvent banks. Where the deposits could not be transferred, the FSCS has paid or may pay compensation to eligible depositors.

14. The FSCS includes in the compensation it pays a sum equivalent to accrued interest on the deposit from the last date interest was paid by the financial institution to the date of default of the financial institution. If the deposit was a fixed term deposit and the claimant opted to hold their deposit until maturity then the FSCS will pay a sum equivalent to interest that has accrued up to and including the maturity date of the deposit. When calculating the sum equivalent to interest the FSCS also takes into account whether or not the financial institution in default would have deducted tax from interest on that deposit. If the financial institution in default would have deducted tax then the FSCS deducts the same amount from the compensation – so the sum equivalent to interest is 'net of tax'.

15. Even though the sum equivalent to interest paid under the FSCS is the same amount that would have been paid as interest (either net or gross) by the financial institution if it had not been declared in default, the taxation of the sum is unclear. This section ensures that the recipients of the compensation are in the same position that they would have been had the financial institution not been declared in default and so the sums equivalent to interest are treated as interest in the hands of the recipient.

16. This means that the sums equivalent to accrued interest are chargeable to income tax in the same way as any bank interest. The amount that the FSCS has deducted to represent 'tax deducted' is included in the calculation of the income tax liability as tax paid. Therefore basic rate taxpayers will not have to pay anything more, starting rate and non-taxpayers can make repayment claims in the normal way, and higher rate taxpayers will be liable for an extra 20 per cent.

17. This section only applies for income tax purposes because for companies the taxation of deposits with financial institutions is within the loan relationship provisions in Parts 5 and 6 of the Corporation Tax Act 2009.

18. The following is a simplified example of how the FSCS calculates compensation. In the example the bank customer has deposited £10,000 in an interest bearing account and the interest is credited monthly. The bank went into default on the 15 November 2008 and FSCS compensation is calculated to this date.

Principal deposited on 1/7/08	£10,000
Interest paid monthly by the bank (£60 per month gross less tax deducted £12) July 2008 August 2008 September 2008 October 2008	 £48 £48 £48 £48
Depositor's Balance as at 15/11/08	£10,192.
Payment representing interest paid by the FSCS from 1/11/08 to 15/11/08 calculated as if tax of £6 were deducted from £30 gross.	£24
Total compensation paid by FSCS	£10,216

19. In the example above, it is the £24 paid by the FSCS that is the subject of this section. New section 380A of ITTOIA charges to income tax as interest the payment representing interest of £24 plus the amount representing tax that has been deducted by the FSCS - £6. The total charge to income tax under this section would be £30 and this is also the relevant gross amount for new section 979A of ITA.

20. If in the example the bank customer were a non-taxpayer then the £6 that represents tax that has been "deducted" by the FSCS can be included in a repayment claim. If the customer is a basic rate or higher rate taxpayer then the £6 will be included as a credit in the calculation of their tax liability for the 2008-09 tax year. This is exactly the same income tax treatment as if the interest were paid by the bank.

SECTION 34 SCHEDULE 14: CORPORATION TAX TREATMENT OF COMPANY DISTRIBUTIONS

SUMMARY

1. Section 34 and Schedule 14 determine the scope of the corporation tax charge on income on both UK and foreign company distributions. The rules for distributions received by small companies are distinct from the rules for medium and large companies, but in each case the result is that the great majority of distributions will be exempt from corporation tax. The Schedule contains anti-avoidance rules to prevent abuse of distribution exemption.

2. The changes introduced by this section are part of the package of measures being introduced as a result of the Government's review of the taxation of foreign profits.

DETAILS OF THE SECTION

3. The section introduces Schedule 14.

DETAILS OF THE SCHEDULE

4. Schedule 14 is divided into three Parts. Part 1 introduces a new Part 9A to the Corporation Act 2009 (CTA) to deal with company distributions. Part 2 makes other amendments to CTA, the Income and Corporation Taxes Act 1988 (ICTA) and other legislation. Part 3 gives the commencement and transitional rules for the Schedule.

Part 1 – Insertion of new Part 9A of CTA 2009

5. This Part of the Schedule includes only one paragraph, which introduces a new Part 9A to CTA. Part 9A replaces the existing rules that tax foreign dividends and that give exemption for UK distributions. Part 9A is divided into four Chapters. The first Chapter establishes a charge to corporation tax on income distributions received from UK or foreign companies. Chapter 2 sets out the conditions for a distribution received by a small company to be exempt from corporation tax and Chapter 3 does the same for large or medium-sized companies. Chapter 4 includes interpretation provisions.

Chapter 1 of Part 9A of CTA

6. Section 931A establishes that in principle UK and foreign distributions are subject to corporation tax on income, unless they are exempt according to the rules given later in the Part.

7. Subsection (2) limits the scope of the Part by excluding distributions of a capital nature. Capital distributions will continue to be taxed or exempt according to the rules applying to chargeable gains and are unaffected by this legislation.

Chapter 2 of Part 9A of CTA

8. Chapter 2 gives the conditions for a distribution received by a small company to be exempt. The definition of a small company for this purpose is given in Chapter 4 of Part 9A (section 931S).

9. Section 931B makes a distribution received by a small company exempt subject to the following conditions:

- the company paying the distribution must be resident of the UK or a "qualifying territory", which is a term defined in section 931C. The company must not be resident in more than one jurisdiction;

- the distribution must not be an amount of interest that is treated as a distribution in accordance with section 209(2)(d) or (e) of ICTA. In practice this will mainly refer to interest paid at more than a commercial rate (section 209(2)(d)). Paragraph 14 of the Schedule ensures that wherever possible excessive rates of interest will be dealt with by transfer pricing rules;

- the distribution must not be a dividend that qualifies for a foreign tax deduction; and

- the distribution must not be made as part of a tax advantage scheme, as defined in section 931U.

10. Section 931C(1) defines a qualifying territory for the purpose of section 931B as a territory with which the UK has a double taxation treaty that includes a non-discrimination provision in a standard form.

11. 'Non-discrimination provision' is defined in subsections (4) and (5) in terms that follow Articles 24 and 3 of the OECD Model Convention on Income and on Capital. Subsection (3) gives conditions about the meaning of the term "resident" for the purpose of section 931B in terms that follow Article 4(1) of the Model Convention, which defines what is meant by "resident of a Contracting State".

12. Subsection (2) allows HM Treasury by regulations to provide that a territory is a qualifying territory even if it does not satisfy subsection (1), or that it is not a qualifying territory even if it does satisfy that subsection. Subsection (6) provides amongst other things that the regulations may make different provision for different types of company. Any such regulations will be subject to affirmative resolution procedure (see paragraph 28 of the Schedule).

Chapter 3 of Part 9A of CTA

13. Chapter 3 gives the conditions for a distribution received by a large or medium-sized company to be exempt.

14. Section 931D makes a distribution exempt from corporation tax provided:

- it falls into one or more of the exempt classes; and
- it is not one of two types of distribution that do not qualify for exemption.

15. The first non-qualifying type relates to interest that is treated as a distribution, and to certain other distributions in respect of securities. The second non-qualifying type refers to distributions that qualify for a tax deduction in a foreign jurisdiction. These exclusions are identical to the second and third conditions that apply to small companies in section 931B.

Exempt classes

16. There are five exempt classes set out in sections 931E to 931I. Distributions will frequently fall into more than one of these classes, but it is sufficient to fall into any one of them for a distribution to be exempt, provided the anti-avoidance rules in sections 931J to 931Q do not apply.

17. Section 931E provides exemption for distributions paid to a parent company that controls the company making the distribution. Control for this purpose is defined by reference to the controlled foreign company (CFC) control rules, including the extension to joint ventures that have a 40 per cent interest combined with another 40 per cent to 55 per cent interest. The definition of control for CFC purposes was extended in Finance Act 2008 by reference to entitlement to the majority of income or capital rights. There is an anti-avoidance rule specific to this section in section 931J.

18. Section 931F provides exemption for all distributions paid in respect of non-redeemable ordinary shares. The terms "ordinary share" and "redeemable" are defined in section 931U. A share is an ordinary share provided it carries no preferential rights to income or capital. There is an anti-avoidance rule specific to this section in section 931K

19. Section 931G provides exemption for distributions in respect of portfolio holdings. Portfolio holdings are holdings of less than 10 per cent of shares of the same class as those in respect of which the relevant distribution is made. The 10 per cent limit must be met by reference to share capital, income rights and capital rights. Shares are not of the same class if different proportions of their nominal share capital are paid up (for this purpose any amount paid in respect of share premium is disregarded). There is an anti-avoidance rule specific to this section in section 931L.

20. Section 931H provides exemption for any dividends paid out of profits that are not derived from transactions that achieve (and that have as a main purpose to achieve) a UK tax advantage of more than a negligible amount. Profits not derived from such transactions are referred to as "relevant profits".

21. If a company has any profits that are not relevant profits, which are therefore derived from avoidance transactions, this exempt class will not be available and will remain unavailable until all those profits have been paid out as taxable dividends. However, once those "avoidance" profits have been fully paid out in taxable form, this exempt class will become available for any subsequent dividends paid from relevant profits, including the remaining part of a dividend that is paid partly but not wholly out of profits other than relevant profits.

22. There is a transitional rule in Part 3 of this Schedule that treats all profits earned from transactions that took place more than 12 months before the commencement date for the Schedule (that is, before 1 July 2008) as relevant profits. Any dividend paid out of such profits will therefore qualify for this exempt class.

23. If a dividend is paid partly out of relevant profits and partly out of other profits, it is treated as two separate dividends for the purposes of this Part and also for the purposes of Part 18 of ICTA, which allows double taxation relief to be given in respect of a non-exempt part of a dividend.

24. Paragraph 8 of the Schedule amends section 799 ICTA to ensure that section 931H and the double taxation relief rules in Part 18 ICTA are consistent with one another in the way that profits are specified in relation to a taxable dividend.

25. Section 931I provides exemption for distributions paid in respect of shares that would be taxed as loan relationships except that they are not held for an unallowable purpose and are consequently exempt from taxation under loan relationship rules. The loan relationship exemption would not in itself give exemption from taxation under Part 9A, which is instead provided by this section.

26. Section 931I refers to section 521C of CTA, which is itself being introduced by Schedule 24 of this Act (section 48). The term "unallowable purpose" will be defined by section 521E.

Exempt classes: anti-avoidance

27. Sections 931J to 931Q contain anti-avoidance rules. Sections 931J to 931L contain rules that can prevent distributions from falling within specific exempt classes. Where sections 931M to 931Q apply they prevent distributions from being exempt at all.

28. The terms "scheme" and "tax advantage scheme" that are used in these sections are defined in section 931V. A tax advantage scheme is a scheme that has as its main purpose, or one of its main purposes, to obtain a tax advantage of more than a negligible amount.

29. Section 931J is an anti-avoidance rule that applies to dividends that fall into the section 931E exempt class (distributions from controlled companies). Section 931E mirrors the CFC control rules and so in general the protection afforded by the CFC rules minimises the risk of avoidance schemes that use distributions exempt under this class. Section 931J blocks avoidance schemes that seek to obtain exemption despite the fact that the CFC control rules did not apply at the time when the profits included in the dividend were earned.

30. Section 931J applies only where there is a scheme or arrangement that has as a main purpose to obtain exemption under section 931E. For example, it would apply to the following type of scheme:

- a group company that is outside the scope of the CFC rules receives income that is diverted from the UK under an avoidance scheme or arrangement;
- the company is then brought under the control of a UK member of the group in order to allow subsequent dividends to fall within the section 931E exempt class; and
- a dividend is paid out of the company's distributable profits, which include those diverted from the UK during the pre-control period.

31. Where it applies, this section prevents a distribution from being exempt by virtue of the controlled companies exempt class. It will not prevent a distribution from being exempt by virtue of any other class.

32. If a dividend is paid as part of a scheme that falls within this section and the company has any pre-control profits, this anti-avoidance rule will apply. However, once those pre-control profits have been fully paid out in the form of taxable dividends, the anti-avoidance rule will cease to apply to any subsequent dividend (or part dividend).

33. As with section 931H, if the section applies to part but not all of a dividend, it is treated for the purposes of both Part 9A and Part 18 of ICTA as if it were two dividends.

34. There is a transitional rule in Part 3 of this Schedule that prevents any profits earned more than 12 months before the commencement date for the Schedule (that is, before 1 July 2008) from being treated as pre-control profits. Any dividend paid out of such profits will therefore not fall within this anti-avoidance rule.

35. Section 931K is an anti-avoidance rule that applies to dividends that fall within the section 931F exempt class (distributions in respect of non-redeemable ordinary shares). It applies only where there is a scheme or arrangement that has as a main purpose to obtain exemption under section 931F.

36. The anti-avoidance rule in this section will apply if rights are obtained under an avoidance scheme that are equivalent to the rights of either a preferential shareholder or a holder of a redeemable share.

37. Where it applies, this section prevents a distribution from being exempt by virtue of the non-redeemable ordinary shares exempt class. It will not prevent a distribution from being exempt by virtue of any other class.

38. Section 931L is an anti-avoidance rule that applies to dividends that fall within the section 931G exempt class (distributions in respect of portfolio holdings). It applies only where there is a scheme or arrangement that has as a main purpose to obtain exemption under section 931G.

39. The anti-avoidance rule in this section will apply if a shareholding that would be too large to qualify for the portfolio holdings exempt class is split between a number of connected companies in order that each company's holding falls below the 10 per cent threshold given in section 931G.

40. Where it applies, this section prevents a distribution from being exempt by virtue of the portfolio holdings exempt class. It will not prevent a distribution from being exempt by virtue of any other class.

41. Section 931M is an anti-avoidance rule that applies to distributions that arise from a tax advantage scheme (see section 931V) and that are part of an arrangement that yields a return economically equivalent to interest.

42. Subsection (1) excludes from the anti-avoidance rule any distribution that is exempt by reason of section 931E (distributions from controlled companies). Subsection (6) restricts the section to cases where there is a connection between the recipient and payer.

43. Subsection (7) defines the meaning of "connection" in subsection (6) by reference to an amended loan relationship definition of "connected company" in section 466. The reason for using the loan relationship definition is to ensure that section 931M has sufficient scope to cover all those cases where loan relationships legislation is disapplied by reason of a connected person rule, but there is a risk that the CFC rules may not apply because of an absence of control of the payer by the recipient.

44. The definition of "economically equivalent to interest" in this section is aligned with that given in section 486B of CTA, which is being introduced by Schedule 24 of this Act (section 48).

45. Section 931N is an anti-avoidance rule that applies to tax advantage schemes (see section 931V) that include a deduction given under any foreign tax law in respect of an amount calculated by reference to a distribution.

46. There are rules in sections 931B(c) and 931D(c) that deny exemption for any distribution that itself qualifies for a foreign tax deduction. This section prevents those rules being sidestepped through avoidance schemes that arrange for tax deductions to be given indirectly.

47. Section 931O is an anti-avoidance rule that applies to tax advantage schemes (see section 931V) involving payments for distributions. The language of this section is similar to that used in section 125 of ICTA, which was amended in 2005 in response to avoidance schemes involving annual payments. This section introduces a rule that will deny exemption in any case where the recipient or a person connected to the recipient makes a payment or gives up income in return for a distribution.

48. Section 931P is an anti-avoidance rule that guards against the risk that the terms on which goods or services are provided might be varied in a way that reduces taxable profits in return for a right or expectation that a distribution will be paid to compensate for the lost profits. It applies where there is a tax advantage scheme (see section 931V) that involves the payment of a distribution, but does not apply in any case where the transfer pricing rules in Schedule 28AA to ICTA cancel the tax advantage arising from the variation in terms.

49. Section 931Q is an anti-avoidance rule that denies exemption to distributions that have been artificially diverted from a company (referred to as "C" in the section) for which the distribution would have been a trade receipt. Part 9A does not apply to distributions that are trade receipts (although there is a special rule for insurance companies in paragraph 22 of this Schedule that has an equivalent effect), which are instead taxable as part of trade profits. This might create an incentive for a trading company to divert distributions that are trade receipts to a different company in order to obtain exemption under Part 9A.

50. The section applies only where there is a scheme or arrangement that has as a main purpose to obtain Part 9A exemption and where it is reasonable to assume that the distribution would have represented a trade receipt of C. Subsections (3) and (4) require that in considering whether it is reasonable to make this assumption, it must be assumed that C was a party to any transactions giving rise to the distribution.

Chapter 4 of Part 9A CTA 2009

51. Chapter 4 interprets terms used in Part 9A and also establishes how Part 9A interacts with certain other parts of CTA.

52. Section 931R allows a company to make an election that a particular distribution that would otherwise be an exempt distribution shall instead be taxable. Two reasons why a company might wish to make such an election are as follows:

- dividends can only be taken into account for the purposes of the CFC acceptable distribution policy (ADP) exemption if they are subject to tax; and
- it is possible that exemption could lead to an increased rate of withholding tax.

53. A company may elect for one or more dividends paid in an accounting period not to be exempt. If part but not all of a dividend is an ADP dividend, the company may elect for only the ADP part to be taxable, while retaining exemption for the other part. Any such election must be made within two years of the end of the accounting period in which the distribution is received.

54. Section 931S gives the definition of "small company", thereby establishing the scope of Chapter 2. The definition follows the 2003 European Commission recommendation except that certain financial companies listed in subsection (2) are not treated as small companies.

55. Section 931T defines the terms "payer" and "recipient" in relation to a distribution. These terms are used throughout Part 9A. It also defines the term "relevant person", which is used in several of the anti-avoidance sections as a means of referring to any company connected with the recipient of a distribution.

56. Section 931U defines "ordinary share" and "redeemable" for the purposes of sections 931F and 931K. An ordinary share carries no preferential rights and a share is redeemable if as a result of its terms of issue or any collateral arrangements either the holder or the issuer is entitled to redeem the share.

57. Section 931V defines "scheme" and "tax advantage scheme". The term "scheme" is broadly defined. A scheme is a tax advantage scheme if one of its main purposes is to obtain a tax advantage, as that term is defined in ICTA.

58. Section 931W gives priority to other Parts of CTA that in some cases include distributions under alternative heads of charge (trade profits, property income and life insurance taxation). Hence Part 9A will apply only where distributions are not taxed under these alternative heads of charge.

Part 2 – Other amendments

59. Paragraph 3 includes exempt foreign distributions within franked investment income (FII) for the purpose of calculating entitlement to small companies' relief. This treatment is consistent with that of UK distributions.

60. Paragraph 4 replaces the current exemption from corporation tax for foreign distributions received by charities and extends it to include all company distributions within Part 9A (i.e. all company distributions that are not of a capital nature). This replaces the exemption previously provided by section 1285 of CTA for UK distributions and by section 505(1)(iib) of ICTA for foreign distributions, which is repealed under sub-paragraph (3).

61. Paragraph 5 makes minor consequential amendments to some insurance anti-avoidance legislation.

62. Paragraph 6 has the effect that entitlement to a tax credit for the purposes of section 231 of ICTA applies whether or not the company making the qualifying distribution is resident in the United Kingdom.

63. Paragraphs 7 to 10 make changes to the rules giving underlying tax credit in respect of foreign dividend income. These rules are not necessary for any exempt foreign dividend and so are being simplified by the removal of the onshore pooling rules (sections 806A to 806K of ICTA).

64. Section 799 ICTA is amended in a way that affects the specification of profits for the purpose of calculating credit for underlying tax. In a case where a dividend is taxable because it is paid in respect of profits that are not "relevant profits" for the purposes of section 931H (dividends derived from profits not designed to reduce tax), those same profits are specified as the profits that form the basis of the underlying tax credit calculation.

65. Paragraphs 11 to 12 amend Schedule 23A to ICTA, which deals with manufactured dividends. Paragraph 11 amends paragraph 2 of Schedule 23A, which deals with manufactured UK dividends. Paragraph 12 amends paragraph 4 of Schedule 23A, which deals with manufactured overseas dividends.

66. The broad aim of the amendments is to align the tax treatment of manufactured dividends (whether payable in respect of UK or overseas equities) with their real equivalents. Similarly, the amendments aim to ensure that the payment of a manufactured dividend is deductible if and to the extent that the equivalent receipt is taxable.

67. In some cases exemption for the real dividend depends on the nature of the shares in respect of which it is payable. Paragraph 2 of Schedule 23A ensures that where a manufactured dividend is paid in respect of UK shares the payment is treated as made in respect of the shares in question. Paragraph 12 introduces new sub-paragraph (4A) of paragraph 4, which ensures that Part 9A will also apply to a manufactured overseas dividend as if it were paid in respect of the shares in question.

68. Paragraph 11 also introduces new subparagraph (3B) of paragraph 2 of Schedule 23A, to ensure that where exemption under Part 9A depends upon identity of the payer of the dividend, then the payer of a manufactured UK dividend shall be treated as the payer of the real dividend of which the manufactured payment is representative.

69. Paragraph 12 also introduces new subparagraph (4B) of paragraph 4 of Schedule 23A for the same purpose in relation to manufactured overseas dividends.

70. Paragraph 13 makes a consequential change to the offshore funds legislation to reflect the repeal of section 1285 (see paragraph 27) and its replacement by the rules in Chapters 2 and 3 of Part 9A.

71. Paragraph 14 makes the amendment necessary to ensure that transfer pricing rules take priority over section 209(2)(d), thereby limiting the scope of the denial of Part 9A exemption given in sections 931B and 931D.

72. Paragraphs 15 to 17 make consequential amendments to sections 85A and 89 of the Finance Act 1989. These sections contain detailed rules for the taxation of the profits of life assurance business on the I-E basis.

73. Paragraphs 18 and 22 extend the benefit of exemption under Part 9A rules to general insurance companies, including corporate members of Lloyd's. In each case, distributions will be excluded from the calculation of insurance trade profits to the same extent as is provided for by the Part 9A rules.

74. Paragraph 19 makes a consequential change to Real Estate Investment Trust (REIT) rules.

75. Paragraphs 20, 21, 23, 24, 26, 29 and 30 make minor consequential changes to CTA.

76. Paragraph 25 extends exemption to receipts from the sale of foreign dividend coupons to the same extent as the dividend would itself be exempt according to the rules given in Part 9A.

77. Paragraph 27 removes the general exemption for UK distributions by omitting section 1285. UK distributions instead qualify for exemption under the rules in Part 9A unless they are taxed elsewhere.

78. Paragraph 28 provides that regulations made under section 931C are subject to affirmative resolution procedure.

Part 3 – Commencement etc.

79. Paragraph 31 gives the commencement rule for the Schedule, which applies to all distributions paid on or after 1 July 2009.

80. Paragraph 32 sets out transitional provisions applying to sections 931H and 931J. In each case the purpose of the transitional rule is to prevent the need to consider transactions (or series of transactions) that were completed before 1 July 2008. To the extent that it is necessary to consider whether a distribution would have fallen into an exempt class before 1 July 2009, it is to be assumed that Part 9A was in force at that time.

BACKGROUND NOTE

81. Part 9A aligns the treatment of UK and foreign distributions and provides that the great majority will not be taxable.

82. Exemption is available to all sizes of company and for distributions arising from any size of shareholding.

83. In recognition of the fiscal risks associated with distribution exemption there are anti-avoidance rules to prevent abuse whereby profits that would otherwise have been subject to tax are returned as a tax exempt distribution.

SECTION 35 SCHEDULE 15: TAX TREATMENT OF FINANCING COSTS AND INCOME

SUMMARY

1. Section 35 and Schedule 15 make provision for the restriction of the tax deduction available for finance expenses of groups of companies. The effect of the new measure is to limit the aggregate UK tax deduction for the UK members of a group of companies that have net finance expenses to the consolidated gross finance expense of that group. The Schedule applies to a group that has either a UK or foreign parent. Finance expenses and finance income are payments of interest and interest like amounts.

2. Any restriction is calculated by comparing the UK measure of net finance expenses, calculated by reference to the UK group members that have net finance expenses, with the worldwide measure of the group's consolidated finance expense. Any restriction is then allocated to one or more of the UK group companies, leading to a disallowance of part or all of their finance expenses. To the extent that other UK members of the group have net finance income, the finance income of the UK group companies can be reduced in computing their corporation tax profits, but only to the limit of the restriction of finance expenses. The measure has effect for accounting periods beginning on or after 1 January 2010.

3. The changes introduced by this section are part of the package of measures being introduced as a result of the Government's review of the taxation of foreign profits.

DETAILS OF THE SECTION

4. The section introduces Schedule 15.

DETAILS OF THE SCHEDULE

Part 1 - Overview

5. Schedule 15 is divided into eleven parts. Part 1 provides an overview of the Schedule. Part 2 sets out the circumstances in which the Schedule applies to a worldwide group of companies for any particular period of account. Part 3 provides the basic rules where an amount of financing expense of UK group companies falls to be disallowed. Part 4 provides for certain financing income of UK group companies to be exempted from corporation tax but only to the extent that financing expense has been disallowed under Part 3. Part 5 allows certain intra-group financing income to be exempted from corporation tax where the paying company is resident in the European Economic Area (EEA) unless the paying company is resident in the UK and, the effect of Part 3 aside, is denied a deduction for the payment for tax purposes. Part 6 provides for anti-avoidance measures to counter the effect of schemes designed to avoid provisions of the Schedule. Part 7 and Part 8 define the amounts and types of intra-group financing income and financing expense that are used in Part 3 to calculate any disallowance, and are used in Part 4 to determine the amount of financing income to be disregarded. Part 9 sets out how the external gross finance expense of the worldwide group is to be computed for the purposes of the Schedule. Part 10 contains further definitions and other interpretative

provisions. Part 11 deals with commencement and consequential amendments to other legislation.

Part 2 – Application of this Schedule

6. This Part of the Schedule sets out gateway conditions to be applied by reference to a comparison of the consolidated gross debt of the worldwide group with the aggregate figure of net debt of the UK group companies. It also sets out rules for excluding groups engaged in particular financial services business. If these conditions for either test are met for any given period of account of the worldwide group then the UK members of the group are not subject to the remaining Parts of the Schedule.

7. Paragraph 2 sets a condition for application of the Schedule based on the amount of the worldwide group's debt. The term 'worldwide group' is defined in Part 10. The Schedule applies if the 'UK net debt' of the group exceeds 75 per cent of the 'worldwide gross debt' of the group.

8. Sub-paragraph (2) provides that the Schedule will not apply to a period in which the worldwide group is a "qualifying financial services group", which is defined by paragraph 7.

9. Sub-paragraphs (3)-(5) provide for the 75 per cent figure in sub-paragraph (1) to be increased or decreased prospectively by Treasury order, subject to affirmative resolution.

10. Paragraph 3 defines 'UK net debt' for the purpose of paragraph 2 as the average of the opening and closing net debt (the net debt amount) of each relevant group company. The term 'relevant group company' is defined in paragraph 86. Sub-paragraph (3) and (4) provide for a 'net debt' amount of less than £3 million, and for the net debt amount of a dormant company, to be treated as nil for this purpose respectively. Sub-paragraphs (5)-(7) allow the de minimis limit of £3 million to be increased or decreased prospectively by Treasury order.

11. Sub-paragraph (8) takes the opening and closing dates as the beginning and end of the period of account of the 'worldwide group', unless the company is only a 'relevant group company' for part of that period in which case the opening and closing dates are set by reference to when the company became or stopped being a 'relevant group company'.

12. Paragraph 4 explains that the 'net debt' of a 'relevant group company' at any particular time is the company's debt liabilities less its liquid assets such as cash and loans receivables, taken from the company's balance sheet. The class of both relevant liabilities and relevant assets are defined by sub-paragraphs (3) and (4), interpreted by reference to generally accepted accounting practice applicable to UK companies (see sub-paragraph (5)) and can be added to by regulations.

13. Paragraph 5 defines 'worldwide gross debt'. Sub-paragraph (1) explains that the figure is the average of the amounts taken at the end of the current and preceding periods of account of the worldwide group. Sub-paragraph (2) defines the term by reference to particular amounts of information disclosed in the group's balance sheet. The paragraph lists the amounts to be taken into account and sub-paragraph (3) provides that expressions used in the list are to be interpreted in accordance with the accounting standards used to draw up the financial statements. The class of liabilities can be added to by regulations. Sub-paragraph (4) provides that rules which apply to a group's consolidated financial statements within paragraphs 87 to 90 apply to this paragraph.

14. Paragraph 6 explains what is meant by references to amounts disclosed in the balance sheet of a 'relevant group company'. This includes provision (in sub-paragraphs (2)-(4)) to deal with a foreign company that has a UK permanent establishment and to deal with cases where either a UK company has not drawn up financial statements or there are no separate financial statements for a UK permanent establishment of a foreign company. In all cases references are to amounts that would be disclosed if financial statements were drawn up.

15. Paragraph 7 defines 'qualifying financial services groups'.

16. Sub-paragraph (1) provides that a worldwide group is a 'qualifying financial services group' in a period of account where it either meets the 'trading income condition' or would have met it had it not been for losses incurred by the group as a result of trading or investing in financial instruments.

17. Sub-paragraph (2) explains that the 'trading income condition' is met for a period of account where either substantially all of the 'UK trading income' of the worldwide group for that period, or substantially all of the 'worldwide trading income' of the group is derived from 'qualifying activities'. 'Qualifying activities' are defined in paragraph 8.

18. Sub-paragraph (3) defines 'UK trading income' and 'worldwide trading income' for the purposes of Part 2. 'UK trading income' for a period of account of the group is defined as the sum of the trading income of all companies that were "relevant group companies" at any time during that period of account. 'Relevant group company' is defined in paragraph 86. 'Worldwide trading income' for a period is defined as the trading income for that period of the 'worldwide group'. 'Worldwide group' is defined in paragraph 78.

19. Paragraph 8 provides the list of activities that are to be regarded as 'qualifying activities' for the purposes of Part 2. These are lending activities and activities that are ancillary to lending activities, insurance activities and insurance-related activities and relevant dealing in financial instruments.

20. Paragraph 9 defines 'lending activities and activities ancillary to lending activities'. Sub-paragraph (1) provides the list of activities that are lending activities for the purposes of Part 2. The list includes 'alternative finance arrangements' which has the same meaning as in Chapter 6 of Part 6 of the Corporation Tax Act 2009. This broadly applies to arrangements that have the same effect as lending arrangements without involving the payment of interest and relates primarily to Islamic finance products.

21. Sub-paragraph (2) excludes from the definition of a 'qualifying activity' activities ancillary to lending activities where the income derived from the ancillary activity is significant when compared to the income derived from lending activities by the worldwide group.

22. Sub-paragraph (3) provides that the income to be taken into account for the purposes of the test in sub-paragraph (2) is the same income that is taken into account for the purposes of the trading income condition in paragraph 7.

23. Sub-paragraph (4) provides a regulation making power to allow the Commissioners to make changes to the list of lending activities in sub-paragraph (1).

24. Sub-paragraph (5) provides that activities carried out in connection with lending activities and activities ancillary to lending activities include the buying, holding, managing and selling of assets.

25. Paragraph 10 defines 'insurance activities' and 'insurance related activities' for the purposes of Part 2. Sub-paragraph (1) defines 'insurance activities' as effecting or carrying out 'contracts of insurance' by a 'regulated insurer' and investment business arising directly from that activity. Sub-paragraph (6) defines the terms used elsewhere in the paragraph. 'Contract of insurance' has the same meaning as in Chapter 1 of Part 12 of ICTA 1988. In that Chapter, 'contract of insurance' has the meaning given by Article 3(1) of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001. 'Insurance business' has the same meaning as in the Financial Services Authority Handbook. A 'regulated insurer' is defined as any member of the worldwide group that is authorised to carry on an insurance business under the laws of any state or territory, or is a member of a body or organisation that is so authorised.

26. Sub-paragraph (2) explains what is meant by 'insurance-related activities'. Sub-paragraph (2)(a) covers activities that are ancillary to insurance activities defined in sub-paragraph (1). Sub-paragraph (2)(b) covers activities that are the same kind of activities carried out for the purposes of the insurance activity, but which are not actually carried out those purposes and would not be carried out but for insurance activities being carried out. An example would be the management of assets for a third party by an institution that also manages assets as part of its own insurance business.

27. Sub-paragraph (4) explains that activities within sub-paragraphs (2)(a) and (b) are not to be regarded as related to insurance activity if the income from those activities is significant when compared to the income derived by the worldwide group from insurance activities.

28. Sub-paragraph (5) provides that the income to be taken into account for the purposes of the test in sub-paragraph (4) is the same income that is taken into account for the purposes of the trading income condition in paragraph 7.

29. Paragraph 11 gives the meaning of the phrase 'relevant dealing in financial instruments' in paragraph 8. It provides that dealing in financial instruments is a qualifying activity where the profits or losses from that dealing, excluding those profits made in the capacity of a broker, are included in the trading profits of the business.

30. Paragraph 12 explains how UK trading income of the worldwide group is calculated for the purposes of paragraph 7. The trading income of a relevant group company will normally be the gross income arising from its activities without taking account of any deductions. However, where the income in respect of an activity is normally reported on a net basis in accordance with generally accepted accounting practice, then the trading income from that activity will be the net income.

31. Sub-paragraph (6) provides that where a proportion of an accounting period in which a relevant group company reports its trading income does not fall within a period of account of the worldwide group, then its income will be reduced on a time-apportioned basis.

32. Sub-paragraph (7) provides that gross or net income received from other UK members of the worldwide group is disregarded in calculating the amount of the UK trading income for the purposes of paragraph 7.

33. Paragraph 13 explains how the worldwide trading income of the worldwide group is calculated for the purposes of paragraph 7. As for the trading income of a relevant group company, the trading income of the worldwide group will normally be the gross income arising from its activities without taking account of any deductions. However, where the income in respect of an activity is normally reported on a net basis in accordance with international accounting standards, then the trading income from that activity will be the net income.

34. Paragraph 14 provides that if an amount disclosed in balance sheets at any given date is expressed in a currency other than sterling, then the amount must be translated into sterling by reference to the spot rate at that date. Sub-paragraphs (2) - (3) provide that where the group's and relevant group companies' balance sheets are all expressed in the same foreign currency:

    a. the calculation performed for Part 2 can be made by reference to the functional currency of the group; and

    b. the de minimis figure of £3 million in paragraph 3(3) can be translated into the functional currency of the group.

Part 3 – Disallowance of Deductions

35. Part 3 applies if the 'tested expense amount' exceeds 'the available amount'. In broad terms, the 'tested expense amount' is the aggregate of the net amount of financing expense payable by each of the relevant group companies that have net financing expense, while the available amount is the external gross finance expense of the worldwide group of companies. In calculating the 'tested expense amount', net amounts falling below a de minimis limit are excluded.

36. The excess is the amount of financing expense that must be disallowed in computing the corporation tax profits of the relevant group companies. Part 3 sets out how the group should notify HM Revenue & Customs (HMRC) of the allocation of the disallowance between the relevant group companies by submitting an allocation statement, and provides for an alternative procedure if the group fails to do so.

37. Paragraph 15 applies this Part of the Schedule if for any period of account ('the relevant period of account') of the 'worldwide group', the 'tested expense amount' exceeds the 'available amount'. The 'tested expense amount' is defined in Part 8 and the 'available amount' in Part 9. Under sub-paragraph (2), the excess is called the 'total disallowed amount'.

38. Paragraph 16 provides that Part 3 applies to a company that is a relevant group company at any time during the relevant period of account of the group.

39. Paragraph 17 provides that the companies to which Part 3 applies may appoint one of them to act on their behalf for the relevant period of account in respect of matters governed by Part 3. The appointment must be made by all the relevant group companies together, but once made does not have to be renewed for each subsequent period of account.

40. Sub-paragraph (3) provides a regulation-making power to allow the Commissioners for HM Revenue & Customs to introduce rules governing an appointment within this paragraph, and mentions matters that may be covered in particular in regulations.

41. Paragraph 18 defines the term 'the reporting body' for the purposes of Part 3 as the company appointed under paragraph 17 for the relevant period of account, or the companies to which Part 3 applies (acting jointly) if no such appointment has effect.

42. Paragraph 19 requires the reporting body to send a 'statement of allocated disallowances' for the relevant period of account to HMRC. Sub-paragraph (2) requires the statement to be received by HMRC within 12 months of the end of the period of account, and, by virtue of sub-paragraph (3), it must comply with the requirements of paragraph 21.

43. Paragraph 20 allows the reporting body to submit a revised statement to HMRC, with subsequent revisions also being allowed. Any revised statement must be received by HMRC within 36 months of the end of the period of account. It must also comply with the requirements of paragraph 21 and must indicate where it differs from the previous statement. The revised statement supersedes the previous statement.

44. Paragraph 21 sets out the requirements of a statement of allocated disallowances. Sub-paragraph (3) provides for the statement to show the 'tested expense amount', 'available amount' and 'total disallowed amount'. Under sub-paragraph (4) the statement must list the companies that are allocated a disallowance, and identify the particular financing expense amount(s) that are to be disallowed for each such company, as defined by sub-paragraph (5). Sub-paragraph (6) requires that the total of the amounts specified must equal the total disallowed amount.

45. Paragraph 22 gives the effect of the statement of allocated disallowances. It is that a financing expense amount of a company specified in a statement is not to be brought into account by the company for corporation tax purposes.

46. Paragraph 23 provides that where a company has delivered a company tax return for the relevant period, and as a result of a revised statement either the amount of profits on which corporation tax is chargeable for a relevant accounting period of a company changes, or any other information contained in the return is rendered incorrect, then the company is treated as having amended its return for the accounting period so as to reflect the change or correct the information.

47. Paragraph 24 provides a regulation-making power to allow the Commissioners to introduce rules governing a statement of allocated disallowances, and mentions matters that may be covered in particular.

48. Paragraph 25 sets out the consequences of a failure by a reporting body to submit a statement of allocated disallowances that complies with the requirements of paragraph 21. Sub-paragraph (2) explains that company to which Part 3 applies that has a net financing deduction must reduce the deductions brought into account in respect of financing expense amounts. The term net financing deduction is defined in paragraph 70(2).

49. Sub-paragraph (3) provides, by way of a formula, that a company's share of the total disallowed amount (the reduction) is in the same proportion as its net financing deduction bears to the tested expense amount.

50. Sub-paragraph (4) provides that the particular financing expense amounts that must be reduced, and the amounts of the reductions, must be determined in accordance with regulations. Sub-paragraph (5) lists the areas that the regulations may cover, but is not exhaustive.

51. Paragraph 26 provides a regulation-making power to allow the Commissioners to introduce rules to ensure that a company in relation to which a financing expense amount is reduced under paragraph 25 has sufficient information to determine its amount of disallowance and describes matters that may be covered in particular.

Part 4 – Exemption of financing income

52. Part 4 applies where there has been a disallowance under Part 3. The effect of Part 4 is to allow for an amount of financing income received by one or more UK members of a worldwide group to be exempted from corporation tax. The total amount of financing income that can be disregarded in this way is limited by reference to the 'total disallowed amount' (see paragraph 15), and by the aggregate amount of net financing income of the UK group companies, which is referred to as the 'tested income amount' and is defined in Part 8 as the sum of the net financing incomes of each UK group company.

53. Part 4 sets out how the group should notify HMRC of the allocation of the exemption between the group companies by submitting an allocation statement, and provides for an alternative procedure if the group fails to do so.

54. Paragraph 27 applies this Part of the Schedule to deal with the exemption of financing income for a period of account of the worldwide group where the tested expense amount exceeds the available amount. That is, in the same circumstances in which a disallowance arises under Part 3. Sub-paragraph (2) calls the excess the 'total disallowed amount'.

55. Paragraph 28 provides that Part 4 applies to a company that is a UK group company at any time during the period of account of the worldwide group. A 'UK group company' to which Part 4 applies is defined in paragraph 86 and is a wider class of companies within the worldwide group than 'relevant group companies' to which Part 3 applies.

56. Paragraph 29 provides that the companies to which Part 4 applies may appoint one of them to act on their behalf for the relevant period of account in respect of matters governed by Part 4.

57. Sub-paragraph (2) requires the appointment to be signed on behalf of each company by the 'appropriate person' for that company. The 'appropriate person' is defined by sub-paragraphs (4) and (5) as the proper officer of the company (usually the company secretary) or as such other person as has been authorised to act on its behalf for the purposes of the Schedule.

58. Sub-paragraph (3) provides a regulation-making power to allow the Commissioners to introduce rules governing an appointment within this paragraph, and mentions matters that may be covered in particular.

59. Paragraph 30 defines the term 'the reporting body' for the purposes of Part 4 as the company appointed under paragraph 29 for the relevant period of account, or the companies to which Part 4 applies (acting jointly) if no such appointment has effect.

60. Paragraph 31 requires the reporting body to send a 'statement of allocated exemptions' for the relevant period of account to HMRC. The statement must be received by HMRC within 12 months of the end of the period of account, and must comply with the requirements of paragraph 33.

61. Paragraph 32 allows the reporting body to submit a revised statement to HMRC, with subsequent revisions also being allowed. Any revised statement must be received by HMRC within 36 months of the end of the period of account, again must comply with the requirements of paragraph 33 and must indicate where it differs from the previous statement. The revised statement supersedes the previous statement.

62. Paragraph 33 sets out the requirements of a statement of allocated exemptions in terms of the information it must contain and sub-paragraph (2) requires it to be signed by the appropriate person or persons.

63. Sub-paragraph (3) provides for the statement to show the 'tested expense amount', 'available amount' and 'total disallowed amount'. Under sub-paragraph (4) the statement must list the companies that are allocated an exemption, and identify the particular financing income amount(s) that are to be exempted for each, as defined by sub-paragraph (5). Sub-paragraph (6) requires that the total of the amounts specified must not exceed the lower of

- total disallowed amount, (see paragraph 15), and
- the tested income amount (see Part 8).

64. Paragraph 34 gives the effect of the statement of allocated exemptions. It is that a financing income amount of a company specified in a statement is not to be brought into account by the company for corporation tax purposes.

65. Paragraph 35 provides that where a company has delivered a company tax return for the relevant period, and as a result of a revised statement either the amount of profits on which corporation tax is chargeable for a relevant accounting period of a company changes, or any other information contained in the return is rendered incorrect, then the company is treated as having amended its return for the accounting period so as to reflect the change or correct the information..

66. Paragraph 36 provides a regulation-making power to allow the Commissioners to introduce rules governing a statement of allocated exemption and mentions matters that may be covered in particular.

67. Paragraph 37 sets out the consequences of a failure by a reporting body to submit a statement of allocated exemptions that complies with the requirements of paragraph 33.

68. Sub-paragraph (2) provides that subject to the provisions of the paragraph, each financing income amount for the relevant period of account of each company to which Part 4 applies is to be reduced to nil.

69. Sub-paragraphs (4) and (5) provide, by way of a formula, that if the result of reducing each financing income to nil is that the total reductions for the relevant period exceed the total disallowed amount, then the reduction for each company is reduced by that part of the excess that its reduction bears to the total reduction.

70. Paragraph 38 provides a regulation-making power to allow the Commissioners to introduce rules to ensure that a company to which a financing income amount is reduced under paragraph 30 has sufficient information to determine its amount and mentions matters that may be covered in particular.

71. Sub-paragraph (2) provides for the regulations to require relevant information to be sent from one group company to another.

72. Sub-paragraphs (3) and (4) allow the regulations to make provision for circumstances where insufficient information is held by a company for the purpose of determining its appropriate financing income reduction.

73. Sub-paragraph (5) provides for the regulations to extend the time limits for amending a corporation tax return in certain specified circumstances so as to reflect a reduction under paragraph 37.

74. Paragraph 39 provides that where in certain defined circumstances one company makes a payment to another company as result of an adjustment to taxable income or expenses made under Schedule 15, then those amounts are not to be taken into account in computing the taxable profits of either company.

75. Sub-paragraphs (1)(a) to (d) define the conditions which are necessary for the paragraph to apply. Firstly, the financing income amounts of a company ("company A") and the financing expense amounts of another company ("company B") must both have either not been brought into account or reduced by the provisions of Schedule 15. If, solely or mainly because of those circumstances, company A makes one or more payments "the balancing payments" to company B, then under sub-paragraph (2) those balancing payments are neither taken into account for the purposes of corporation tax nor treated as distributions.

76. Sub-paragraph (3) provides that the amount not taken into account by virtue of sub-paragraph (2) must not exceed the amount of either the financing income amounts or financing expense amounts not brought into account or reduced by the provisions of Schedule 15.

Part 5 – Intra group financing income where payer denied deduction

77. Subject to conditions, Part 5 allows intra-group financing income received from a company resident in the EEA, excluding the UK, to be exempt from corporation tax. To the extent that tax relief is not available for finance costs within the EEA excluding the UK, like consequences follow for the recipient of the income to provide equivalence with an outcome arising from the other Parts of this Schedule.

78. Paragraph 40 gives exemption for an amount of financing income received from a group company that is resident in the EEA excluding the UK. Exemption is subject to meeting all the conditions A to C, which are defined in the following paragraphs.

79. Paragraph 41 defines 'relevant associate' for the purposes of this Part. Condition A of paragraph 40 requires the payer to be a relevant associate of the recipient of the financing income.

80. The payer is a relevant associate if it is a parent company or subsidiary of the recipient or a 75% subsidiary of the parent of the recipient. The term 'parent company' is defined in paragraph 92 by reference to International Accounting Standards (IAS) and the terms '75% subsidiary' is defined in section 838(1)(b) of the Income and Corporation Taxes Acts (ICTA) by reference to the proportion of ordinary share capital held.

81. Paragraph 42 defines 'tax resident' and 'EEA territory' for the purposes of Part 5. Condition B of paragraph 40 requires the payer to be a tax resident of an EEA territory.

82. Paragraphs 43 and 44 define the two elements of condition C of Paragraph 40. Both parts of condition C must be met to fulfil the condition that no relief is available in respect of the financing income.

83. Paragraph 43 defines the requirement set out in the first part of condition C of paragraph 40, which is the requirement that qualifying EEA relief is not available to the payer of the financing income in the current period or any preceding period by reason of the payment. There are two conditions A and B in this paragraph that must both be met in order for this requirement to be satisfied.

84. Sub-paragraph (2) explains that condition A is that no deduction in respect of the payment can be taken into account for the purposes of calculating the taxable profits of the payer in the current period or any preceding period. The current period is the period in which the payment is made (paragraph 40(4)(a)) and taxable profits means the profits taken into account for the taxation purposes of any EEA territory including the UK.

85. Sub-paragraph (3) explains that condition B is that no tax credit or other form of tax relief whatsoever is given to the payer or any other person that is determined by reference to the payment, in the current period or any previous period.

86. Sub-paragraph (4) explains that conditions A and B are not met if there was any step that the payer or any other person could have taken that would have caused the payment to be taken into account as described above.

87. Conditions A and B are also not met if, in certain circumstances, the payment was not taken into account as described above because of this Schedule.

88. Sub-paragraph (5)(b) explains that the Conditions are not met if the payer was denied a deduction or relief in respect of the payment due to provisions in a double taxation treaty. This could be where either the denial of the deduction in the EEA territory is sanctioned by the associated enterprises article of a DTA between that territory and the UK; or where a DTA between the EEA territory and another territory applies to determine which territory has taxing rights in respect of the profits, income or gains whose calculation takes into account the payment in question.

89. Sub-paragraph (6) explains what is meant by double taxation agreements and articles contained in those agreements.

90. Paragraph 44 sets out the second requirement of condition C in paragraph 40. It is very similar to the first requirement described in paragraph 43 above, except that it refers in each case to any future period.

91. Condition A therefore refers to no deduction being given in respect of the payment being taken into account in the computation of any profits that might arise and be chargeable in the EEA territory in any future period. Condition B asks whether any form of relief will become available in any future period, but in answering this question it is sufficient to consider only the position at the end of the current period.

92. As with paragraph 43, this Schedule and the provisions of double taxation agreements are both disregarded when considering conditions A and B.

93. Paragraph 45 defines the term 'tax' for the purposes of the Schedule. UK tax refers to corporation tax or income tax and tax of any other territory refers to taxes that are equivalent to either of these two taxes. A tax is not disqualified solely because it is charged by any regional tax authority, such as the German Länder.

94. Paragraph 46 defines the term 'financing income amount', which is the term used in paragraph 40 to describe the amount that is exempt from tax in the hands of a company subject to conditions A to C of that paragraph. A financing income amount is an amount that falls within any of conditions A to C in this paragraph.

- condition A refers to any amount taxed under loan relationships legislation except the matters described in sub-paragraph (3)
- condition B refers to a receipt corresponding to the finance element of a finance lease; and
- condition C refers to a receipt corresponding to the finance element of a debt factoring arrangement.

95. For this purpose sub-paragraph (6) provides for the provisions of Part 7 to apply in relation to an amount which is a financing income amount by virtue of meeting condition A, B or C in this paragraph in the same way as they do for a financing income amount that meets condition A, B or C in paragraph 48.

Part 6 – Anti-avoidance

96. Part 6 contains three sets of ant-avoidance rules targeted at schemes designed to circumvent provisions in the Schedule. The first rule is targeted at avoidance schemes that manipulate the rules in Part 2 of Schedule 15 in order to avoid the application of the Schedule to a group of companies that would not otherwise have met the 'gateway' conditions in paragraph 2. The second targets schemes to reduce the amount of a disallowance under the debt cap, whether by decreasing the tested expense amount or by increasing the available amount or the tested income amount, or any combination of these. The third rule counters manipulation of the Part 5 rules which disregard certain intra-group financing income.

97. Paragraph 47 counters schemes that attempt to manipulate the 'gateway' and 'financial services exclusion' rules. For example, a group that would otherwise fail the test in paragraph 2 (so that the debt cap rules applied) might borrow from a bank at the end of its period of account to boost the 'worldwide gross debt' amount defined at paragraph 3, repaying the loan the next day. A period of account of the worldwide group falls within paragraph 47 if three conditions are met.

98. Sub-paragraph (1) provides that, where the conditions are met, the 'gateway' result is ignored and the full rules of Schedule 15 apply to that period of account. This may (or may not) lead to a disallowance of financing costs of UK companies.

99. The first condition, at sub-paragraph (2), is met if a scheme has been entered into at any time before the end of the period, and the period would have been within paragraph 2(1) if the scheme had not been entered into. It is therefore capable of applying to schemes that have been entered into before the start of the period of account, as well as those put in place during the period. 'Scheme' is defined in wide terms at paragraph 53(1) and may involve a single transaction, or more than one.

100. Sub-paragraph (3) gives the second condition. It must be the main purpose, or one of the main purposes, of any party to the scheme to ensure that a group passes the gateway test. The party must have that purpose when it enters into the scheme. So, in the example above of a group company undertaking overnight borrowing at the end of the group's period of account, it would be necessary to examine that company's purpose when it borrowed. If the borrowing was for a genuine commercial purpose, and any consideration of its effect on the 'gateway' condition was no more than incidental, paragraph 47 would not apply.

101. The third condition, in sub-paragraph (4), is that the scheme is not an excluded scheme. 'Excluded scheme' is defined in paragraph 53(2) as one answering to a description specified in regulations made by the HMRC Commissioners (under negative procedure). This power to exclude particular schemes or arrangements applies to all three rules in Part 6, and provides a safeguard against the possibility that some normal tax planning arrangements, which would not be seen as abusive, might nevertheless be caught by the anti-avoidance rule.

102. Paragraph 48 is directed at schemes manipulating the tested expense amount, the tested income amount or the available amount, or any combination of these three. It looks at the aggregate effect of these three amounts – the 'relevant net deduction' - defined in paragraph 49. This is so much of the total disallowed amount (the tested expense amount less the available amount) as cannot be covered by a disregard of financing income of UK group companies. The relevant net deduction may be nil.

103. Sub-paragraph (1) provides that this rule applies where three conditions are met. Both the application of the rule, and the conditions, require a comparison to be made between the effect of the actual scheme, and the effect of an alternative scenario, based on assumptions set out in paragraph 50. Where the conditions are met, the tested expense amount, the tested income amount and the available amount must all be calculated on the basis of the alternative scenario. It is these amounts that group companies must take account of for the purposes of Part 3 or Part 4 of the Schedule.

104. Paragraph 50 provides that assumptions must be made in calculating amounts or sums in accordance with this paragraph, and sets out those assumptions. The first is that the scheme in question had not been entered into. The second is that, if the effect of the debt cap had not been a factor, anything which is more likely than not to have been done or not done would have been done or not done, as the case may be. For example, if there were three courses which the group might have followed with 60%, 35% and 5% probability respectively, only the one which the group had a 60% chance of following would be 'more likely than not'.

105. Paragraph 48(2) sets out the first condition. It must be the main purpose, or one of the main purposes, of any party to a scheme, on entering into it, to reduce the amount of the relevant net deduction, compared with what it would have been under the alternative scenario based on the assumptions in paragraph 50.

106. A UK member of the group, which had an outstanding loan from its overseas parent, might for example seek to reduce its financing expense amount by paying a lump sum to a bank in return for the bank taking on the obligation to pay interest. Had the debt cap not been a consideration, it would have carried on paying the interest to its parent in the normal way. Since the debits representing the amortisation of the lump sum arise from a related transaction (see paragraph 54(3)(c) of the Schedule), that company's financing expense amount is less than it would have been under the alternative scenario. This in turn means that the tested expense amount, and hence the 'net relevant deduction' are reduced. Provided that it is a main purpose of the UK company (or any other party to the scheme) to achieve this result, the paragraph 48(2) condition will be satisfied.

107. The further condition in paragraph 48(3) means that this anti-avoidance rule will bite only if the scheme also reduces the overall corporation tax profits (or increases the losses) of UK group companies, compared to the alternative scenario. In the example above, the debits from amortisation of the lump sum remain allowable loan relationships debits; the group may incur additional fees and hedging costs; and (absent the anti-avoidance rule) the debt cap restriction on relevant group companies would be reduced. All of this means that the effect of the scheme would almost certainly be a reduction in corporation tax profits.

108. This is not necessarily so, however. For example, the financing expenses of the company would similarly be reduced if the parent company were to replace the loan by equity. Such an arrangement might be a direct response to the introduction of the debt cap, so the group could not argue that reduction or elimination of a debt cap disallowance was not a main purpose. But such action would also increase (or, at any rate, not decrease) the corporation tax profits of the UK group. It would not be caught by the anti-avoidance rule.

109. The words 'profits …chargeable to corporation tax' in paragraph 48(3)(a) take their normal meaning. It is the totality of profits on which corporation tax is paid, after reduction by losses or reliefs brought forward, or group relief surrendered either by another UK company or a subsidiary in the European Economic Area. The alternative test, in paragraph 48(3)(b), is whether the losses of UK group companies, that are capable of being a carried-back or carried-forward amount, are increased. Paragraph 51 gives an exhaustive listing of 'carried-back amounts' or 'carried-forward amounts'. The latter includes capital losses.

110. A loss that has been offset against profits of the period, either in the same company or in another group company, is excluded from being a carried-back or carried-forward amount. For example, suppose that the sole effect of a scheme is to increase the corporation tax profits of UK group company X by £1 million, but also to increase the losses of company Y by £1 million. Y surrenders £1 million to X as group relief. Y's loss is therefore taken into account under paragraph 48(3)(a), and cannot be counted again under paragraph (b). This means that neither leg of paragraph 48(3) is satisfied: the aggregate corporation tax profits of the group are not decreased, nor is there an increase in the losses capable of being carried forward or back. Even if the remaining paragraph 48 conditions are satisfied, the scheme will not be within the anti-avoidance rule. If, however, Y chooses not to surrender its loss, but instead carries it forward (or back), the condition at paragraph 48(3)(b) will be met, and the anti-avoidance rule is not prevented from applying.

111. Where the accounting period of a UK group company does not coincide with the period of account of the worldwide group, paragraph 48(5) provides for time-apportionment of those profits or losses of accounting periods which fall wholly or partly within the relevant period of account.

112. The rule that losses taken into account in determining corporation tax profits cannot also contribute to carried-back or carried-forward amounts also applies to such time-apportionments. Suppose, for example, the worldwide group has a 12-month period of account ending on 31 December. A UK member of the group prepares accounts to 31 March, so that two of its accounting periods fall partly within the relevant period. This UK company has trading losses arising in the first period, which are carried forward and relieved in the second. In applying paragraph 48(5), losses that are taken into account under paragraph 48(3)(a) because they have reduced the corporation tax profits of the second period are not also treated as 'carried-forward amounts' of the first period.

113. Paragraph 48(4) provides that any 'excluded scheme' is not caught by this anti-avoidance rule.

114. Paragraph 52 deals with schemes that manipulate the rules in Part 5 of the Schedule. Under paragraph 40, financing income received by a UK company is disregarded for corporation tax purposes where three conditions are met. Sub-paragraph (2) requires that the scheme has the effect of securing that any of these three paragraph 40 conditions are met in relation to a particular financing income amount.

115. As with the previous two anti-avoidance rules, it must be the main purpose or one of the main purposes of any party to the scheme on entering into to it to achieve this effect (sub-paragraph (3)) and the scheme must not be an excluded one (sub-paragraph (4)).

116. Sub-paragraph (5) sets out the consequence of meeting these conditions – the "manipulated" condition of paragraph 40 is treated as if had not been met, and so the financing income amount is not disregarded.

Part 7 – Financing expense amounts and financing income amounts

117. Part 7 provides what is meant by the 'financing expense amount' and 'financing income amount' of a company. These amounts are used in Part 8 to compute the 'tested expense amount' and 'tested income amount', which in turn are used, together with the 'available amount' (defined in Part 9) to calculate the amounts, if any, of the financing expense incurred by 'relevant group companies' to be disallowed and of the financing income receivable by UK group companies to be exempted. In setting the basic rules for the 'financing expense amount' and the financing income amount', Part 7 includes specific rules for finance amounts arising in relation to certain activities or certain types of finance amount.

118. Paragraph 54(1) provides that a 'financing expense amount' of a worldwide group company for a period of account is an amount which meets one of three conditions set out in sub-paragraphs (2) to (5).

119. Sub-paragraphs (2) and (3) set condition A. Condition A is that the amount is a debit (broadly an expense) which, in the absence of the Schedule, would be brought into account for corporation tax purposes under the trade loan relationship rules in Corporation Tax Act 2009 (CTA) and which are not one of the specified excluded debits.

120. Sub-paragraph (4) deals with condition B. Condition B is that the debit is an amount which, in the absence of the Schedule, would be brought into account as a financing cost under a finance lease.

121. Sub-paragraph (5) describes condition C. This condition is that the debit is an amount which, in the absence of the Schedule, would be brought into account as a financing cost of debt factoring or a similar transaction.

122. Sub-paragraph (6) ensures that the debit or amount is reduced proportionately where the period in which it would, apart from this Schedule, be taken account of is not the same length as that of the worldwide group. Where the relevant accounting periods of the company straddle the period of account of the worldwide group, then the amounts in question are reduced proportionately.

123. Sub-paragraph (7) makes this paragraph subject to the specific rules provided by the rest of Part 7.

124. Paragraph 55 provides that, other than for the purposes of Part 5, the 'financing income amount' of a worldwide group company for a period of account is an amount which meets one of three conditions set out in sub-paragraphs (2) to (5). The three conditions essentially mirror the conditions for 'financing expense amount in the previous paragraph.

125. Sub-paragraphs (2) and (3) set condition A. Condition A is that the amount is a credit (broadly income or a receipt) which would be brought into account for corporation tax purposes under the loan relationship rules in CTA and which is not one of the specified excluded credits.

126. Sub-paragraph (4) sets condition B. An amount must be an amount which would be brought into account as finance income received under a finance lease.

127. Sub-paragraph (5) sets condition C. The condition is that the amount must be an amount would be brought into account as finance income from debt factoring or a similar transaction.

128. Sub-paragraph (6) ensures that the credit or amount is reduced proportionately where the period in which it would, apart from this schedule, be taken account of is not the same length as that of the worldwide group. Where the relevant accounting periods of the company straddle the period of account of the worldwide group, then the amounts in question are reduced proportionately.

129. Sub-paragraph (7) makes the paragraph subject to the specific rules of the remainder of Part 7.

130. Paragraph 56 sets out that various terms used in paragraph 54 and 55 have the same meaning as they do in the loan relationships rules in CTA.

131. Paragraphs 57 to 69 are intended to remove particular financing expense or income amounts, referred to as the 'relevant amounts' within the meaning of paragraphs 54 and 55 from the calculation of a company's net financing deduction (or in some cases net financing income) where certain conditions are met.

132. Paragraph 57 excludes the financing expense or income amounts where the company is a group treasury company during the worldwide group's period of account, and the company so elects within three years of the end of that period

133. Sub-paragraph (4) provides where in a period the worldwide group contains more than one group treasury company, an election for the group treasury exclusion will not be valid unless each of those companies makes an election.

134. Sub-paragraphs (5) to (8) establish that a series of conditions must be met before a company can qualify as a group treasury company. Broadly, the company must;

- be a member of the worldwide group
- undertake treasury activities for that group
- where the company is the only UK group company to be a group treasury company during that period 90 per cent of the gross income from its activities (its relevant income) must be group treasury revenue, and
- where the company is not the only UK group company to be a group treasury company during the period the 90 per cent test must be applied to the aggregate gross income of the treasury companies.

135. Sub-paragraph (9) identifies the activities that must be undertaken during a period in order that a company can qualify as a group treasury company.

136. Sub-paragraphs (10) and (11) define 'group treasury revenue', while sub-paragraph (12) defines, amongst other things, 'relevant income'. The amounts are those that are accounted for using general accepted accounting practice (which is defined in section 50 FA 2004). Dividends or other distributions are not treated as group treasury revenue unless they are received from another UK group treasury company.

137. Paragraph 58 excludes financing expense amounts and financing income amounts where they are taken into account in computing profits exempted from tax by virtue of the special rules applying to Real Estate Investment Trusts. The condition for exclusion is that the financing expense amounts and financing income amounts are brought into account in computing the profits of a tax-exempt business by virtue of section 120(3)(a) Finance Act 2006.

138. Paragraph 59 excludes the financing expense or income amounts where the company is engaged in oil extraction activities within the meaning of section 502, ICTA and where the amounts in question are taken into account in calculating the company's trading profits.

139. Paragraph 60 deals with intra-group short-term financing expense. It only applies to an amount which is a finance expense of a company meeting condition A in paragraph 54. In such cases sub-paragraph (2)-(5) provide for an election for the amount not to be included as a finance expense, provided that:

- company A and the other party to the loan relationship (company B) are both members of the worldwide group, and
- the expense relates to a short-term loan relationship as defined in paragraph 62.

140. Sub-paragraph (6) requires the election to be made jointly by companies A and B within 36 months of the end of the accounting period to which the relevant amount relates. Sub-paragraph (7) provides for the election to be irrevocable.

141. Paragraph 61 deals with intra-group short-term financing income. It only applies where a finance expense amount is not treated as such by company A in accordance with paragraph 44. It is a reciprocal provision which ensures that the finance income amount of the other party to the loan ('company B') is not treated as a finance income amount.

142. Paragraph 62 provides what finance arrangements can be treated as short-term loan relationships for the purposes of this Schedule.

143. Sub-paragraph (1) defines a finance arrangement to be a short-term loan relationship if it meets either conditions set out in regulations, or meets one of the conditions provided by sub-paragraphs (2) to (3). The broad effect of these sub-paragraphs is to include loan relationships that are either required from the outset to last for less than twelve months, or where there is no fixed term, are considered to no longer exist within 12 months. A loan relationship with no fixed term can only be treated as a short-term loan relationship once it has been repaid and its character as short-term determined.

144. Sub-paragraphs (4) to (6) provide a Treasury power to make regulations, subject to affirmative resolution, about the circumstances in which finance arrangements will not be considered short-term loan relationships.

145. Sub-paragraph (7) provides a regulating power to allow the Commissioners to introduce rules that will enable minor breaches of the regulations introduced under sub-paragraph (4) to be disregarded.

146. Paragraph 63 deals with stranded deficits in non-trading loan relationships from the perspective of the company incurring the financing expense. It only applies to an amount which is a financing expense of a company meeting condition A in paragraph 54. In such cases sub-paragraph (2) provides for an election for the amount not to be included as a finance expense amount if the following conditions, set by sub-paragraphs (4)-(7) are met;

- the other party to the loan relationship ('company B') is in the same worldwide group as company A;
- company B is either resident in the United Kingdom (UK) or trading in the UK through a branch;
- company B is carrying forward an amount of non-trading deficit and sets it off against the non-trading profits of a period which overlaps with the worldwide group's period of account, and;
- The amount set off is equal to or greater than the amount excluded under this paragraph.

147. Sub-paragraph (8) provides that the election is to be made jointly by companies A and B within 36 months of the end of the accounting period to which the relevant amount relates.

148. Paragraph 64 is a reciprocal provision to paragraph 63 dealing with stranded deficits in non-trading loan relationships from the perspective of the company receiving financing income. It ensures that relevant financing income of Company B which meets Condition A in paragraph 55 is not treated as an amount of finance income where Company A elects to exclude the expense.

149. Paragraph 65 makes provision for stranded management expenses in non-trading loan relationships from the perspective of the company incurring the financing expense. The paragraph applies only to an amount which is a finance expense of a company meeting Condition A in paragraph 54. In such cases sub-paragraph (2) provides for an election for the amount not to be included as a finance expense if the following conditions, set by sub-paragraphs (4)-(8) are met;

- the other party to the finance arrangement ('company B') is in the same worldwide group as company A;
- company B must have an investment business and be either resident in the UK or trading in the UK through a branch;
- company B is allowed a deduction for management expenses under section 1219 CTA in an accounting period which overlaps with the worldwide group's period of account;
- the amount of the deduction is equal to or greater than the relevant amount, and;
- company B would make a loss for corporation tax purposes in that accounting period if the credit corresponding to company A's debit within paragraph 54 is not included in that computation.

150. Sub-paragraph (9) provides that the election must be made jointly by companies A and B within 36 months of the end of the accounting period to which the relevant amount relates.

151. Paragraph 66 is a reciprocal provision to paragraph 65 and deals with stranded management expenses in non-trading loan relationships from the perspective of the company receiving the financing income. It ensures that relevant financing income of company B which meets condition A in paragraph 55 is not treated as an amount of finance income where company A elects to exclude the expense.

152. Paragraphs 67 and 68 exclude relevant amounts paid to charities, designated educational establishments, health service bodies and local authorities from being taken into account in computing any disallowance under the Schedule. This prevents a disallowance being made where a corresponding disregard of amounts receivable is not available because of the tax status of the receiving body.

153. The definition of 'charity' is given as any body of persons or trust established for charitable purposes only. The meanings of 'designated educational establishment' and 'health service body' are given by section 105 of CTA and section 519A of ICTA respectively.

154. The provisions include a regulation-making power to allow the Commissioners to add other public bodies to the list of entities to which payments will be disregarded.

155. Paragraph 69 provides certain defined terms for the purposes of Part 7.

Part 8 – The 'tested expense amount' and 'tested income amount'

156. Part 8 sets out how two key amounts, the 'tested expense amount' and the 'tested income amount are to be calculated.

157. The 'tested expense amount' must be calculated so that, by comparison with the 'available amount' dealt with in Part 8, it may be determined whether the adjustments provided for by Parts 3 and 4 are necessary. The 'tested income amount' is required in calculating the amount of financing income to be exempted from corporation tax by Part 4.

158. Paragraph 70 (1) provides that the 'tested expense amount' for a worldwide group is built up from the sum of each relevant group company's 'net financing deduction'.

159. Sub-paragraphs (2) and (3) explain that the 'net financing deduction' of a company for a period of account is the excess of the company's 'financing expense amounts' over its 'financing income amounts'. Any amounts arising to a company as a result of a transaction which took place when it was not a relevant group company are ignored for this purpose. A transaction in this context means an amount of financing expense or income that is payable or receivable.

160. Sub-paragraph (4) specifies that if the computation of the 'net financing deduction' produces a negative figure, the amount is treated as nil.

161. Sub-paragraph (5) provides that if the 'net financing deduction' is small, as defined by the de minimis limit set by paragraph 72, then the amount is treated as nil.

162. Paragraph 71 contains provision about the tested income amount. Sub-paragraph (1) provides that the 'tested income amount' for a worldwide group is built up from the sum of each UK group company's 'net financing incomes'.

163. Sub-paragraphs (2) and (3) provide that the 'net financing income' of a company for a period of account is the excess of the company's 'financing income amounts' over its 'financing expense amounts'. Any amounts arising to a company as a result of a transaction which took place when it was not a UK group company are ignored for this purpose. A transaction in this context means an amount of financing expense or income that is payable or receivable.

164. Sub-paragraphs (4) and (5) provide for the 'net financing income' to be treated as nil if the computation produces a negative figure or an amount which is small as defined in Paragraph 72.

165. Paragraph 72 provides that the figure used to determine whether a relevant group company's net financing deduction is small, or whether a UK group company's net financing income is small, is £500,000.

166. Sub-paragraphs (2)-(4) provide for this amount to be increased or decreased by Treasury order, subject to affirmative resolution, with prospective effect.

Part 9 –Calculation of the available amount

167. Part 9 deals with the computation of the 'available amount', which in broad terms is the external gross finance expense of the worldwide group of companies. This Part sets out the basic rules for computing the 'available amount', and provides for the external financing expense arising from certain activities to be disregarded in calculating the available amount.

168. Paragraph 73 provides that the 'available amount' for a period of account of the worldwide group is derived from amounts disclosed in the group's financial statements for that period.

169. Sub-paragraph (1) provides a list of the amounts to be included.

170. Sub paragraphs (1)(a) – (1)(d) cover interest and amortised discounts and premiums, together with the ancillary costs of borrowing. Subparagraph (1)(e) refers to financing costs implicit in payments under finance leases. This is intended to cover the interest or finance element of finance lease payments. . Sub-paragraph (1)(f) covers the financing costs relating to debt factoring. Sub-paragraph (1)(g) enables further types of financing costs to be designated as falling within the 'available amount' by regulation.

171. Sub-paragraph (2) excludes from the available amount dividends arising from preference shares (whether those shares are redeemable or non-redeemable) to the extent that those shares are recognised as a liability of the group.

172. Paragraph 74 excludes from the available amount financing costs arising from oil extraction activities if a member of the group is treated as carrying out a separate trade of oil extraction activities, as defined by section 502 of ICTA and the financing costs under consideration are taken into account when calculating the profits of that oil extraction trade for corporation tax purposes.

173. Paragraph 75 excludes from the available amount financing costs relating to profits which are dealt with under the tonnage tax regime provided two conditions are met.

174. Sub-paragraph (2) provides that the group company must be a tonnage tax company for the purposes of the UK tonnage tax regime.

175. Sub-paragraph (3) provides that the external finance amount has been taken into account in calculating the relevant shipping profits of the tonnage tax company or is treated as a non-trading loan relationship credit of the company or companies outside the ring fence under paragraphs 61 or 62 of Schedule 22 to FA 2000.

176. Paragraph 76 excludes from the available amount financing costs relating to profits exempted from corporation tax by virtue of the special rules applying to Real Estate Investment Trusts. The conditions for exclusion are that a group company is treated as carrying out a separate business under section 113 of FA 2006 and that the

external finance amount is brought into account in calculating the profits of that separate tax exempt business.

177. Paragraph 77 confirms that in the absence of any contrary provision, expressions used in Part 9 have the meaning given by IAS.

Part 10 – Other Interpretative provisions

178. Part 10 contains the rules that define which companies make up a group for the purpose of this Schedule and which companies are treated as 'relevant group companies' and 'UK group companies'. This part also explains which accounting standards used to prepare the group consolidated financial statements are acceptable for this Schedule and provides for cases where no such financial statements are prepared.

179. Paragraph 78 defines 'the worldwide group' as any group of entities that is large (see Paragraph 85) and contains at least one company that is tax resident in the UK.

180. Paragraph 79 provides that the term 'group' takes it meaning from IAS. This establishes that the 'worldwide group' defined in paragraph 78 will in the majority of cases be the group of companies whose results are included in the consolidated accounts of the group headed by the ultimate parent.

181. Paragraph 79(3) excludes an entity that is a parent of the ultimate parent of a group from being a member of that group. This means that, unless otherwise provided, the worldwide group whose finance expenses will be compared with the finance expenses of UK members of the group will be limited to the ultimate parent and its subsidiaries.

182. Paragraph 80 defines the 'ultimate parent'. The ultimate parent is a member of a group that is either an entity treated as a 'corporate entity' or a 'relevant non-corporate entity' for the purposes of the Schedule and which is not itself a subsidiary of a corporate entity or a relevant non-corporate entity or a collective investment scheme. A group may contain a number of intermediate parent companies and this rule is intended to identify the top parent company in the group.

183. Paragraph 81 provides that for the purposes of the Schedule a 'corporate entity' is either a body corporate under the law of the UK or any other territory, or any another entity that meets two conditions. The two conditions in sub-paragraphs (2) and (3) are formulated by reference to essential characteristics of a body corporate.

184. Sub-paragraph (4) excludes the UK and foreign governments from the definition of 'corporate entity'.

185. Paragraph 82 defines 'relevant non-corporate entity'. Some publicly listed entities that are not corporate entities can be the ultimate parent of a worldwide group. A "relevant non-corporate entity" must have shares or other interests that are listed on a recognised stock exchange and sufficiently widely held.

186. Paragraph 83 provides that where interests in a corporate or relevant non-corporate entity are stapled to another entity they will be treated as a single corporate or non-corporate entity for the purposes of the Schedule. This provides that the stapled entities and their respective subsidiaries will together be treated as one worldwide group. Subparagraph (3) defines 'stapled' by reference to the nature of the rights attaching to the shares or other interests which one entity has in another.

187. Paragraph 84 treats entities as one corporate entity for the purposes of the Schedule where international accounting standards treat them as a single economic entity by reason of being a business combination achieved by contract. This covers dual headed groups which are not accounted for as an acquisition.

188. Paragraph 85 defines large groups by excluding micro, small and medium enterprises as defined in the Annex to European Commission Recommendation 2003/361/EC of 6 May 2003.

189. Sub-paragraphs (1) and (2) incorporate the Annex for the purposes of deciding whether a business is micro, small or medium sized at any time, with certain qualifications. The effect of paragraph 85(1) is that provided at least one member of the worldwide group is a large company by reference to the definition in the Annex, then the worldwide group is large and the Schedule applies to all the UK members of that group that satisfy the definition of relevant group company.

190. Sub-paragraph (3) provides that the rights and powers of liquidators and administrators will not by themselves result in the loss of an exemption for small and medium sized enterprises under their charge. The Annex provides qualifying ceilings for staff and financial limits. In order to see if a business meets these ceilings, its own data must be aggregated with the data for associated businesses. This paragraph ensures that aggregation is not required by virtue solely of the appointment of a liquidator or administrator.

191. Sub-paragraph (4) removes the option to make a declaration of status when a business cannot ascertain the extent of control over its associated businesses when aggregating data.

192. Sub-paragraphs (5) and (6) simplify the application of the recommendation when deciding whether a business will qualify as small or medium. Qualification will depend on a business's data for each chargeable period without reference to past history. This simplification also means that it is not necessary to provide additional start-up rules for new businesses.

193. Paragraph 86 defines 'UK group company' and 'relevant group company'.

194. Sub-paragraph (2) provides that a UK group company is one which is

- a UK resident company or a company carrying on a trade in the UK through a branch (see sub-paragraph (4)), and
- a member of the worldwide group. It is a member of the worldwide group if it a subsidiary of the ultimate parent.

195. Sub-paragraph (3) provides that a relevant group company is a UK group company which is:

- a UK resident company or a company carrying on a trade in the UK through a branch (see sub-paragraph (4)), and is either
- the ultimate parent of the group, or a relevant subsidiary of the ultimate parent (see sub-paragraph (5)).

196. Sub-paragraph (6) provides that the relevant subsidiary condition is based on the 75% subsidiary test used for group relief. It is supplemented by rules that ensure that a company is also treated as a relevant subsidiary of an ultimate parent where that entity is beneficially entitled to at least 75% of the profits which are available for distribution to equity holders, or 75% of the assets which are available for distribution to equity holders in the course of a winding up.

197. Paragraph 87 provides for which consolidated financial statements of the worldwide group are used in applying the Schedule and provides that the period of account of the worldwide group is the period for which those accounts are drawn up. Amounts disclosed in the financial statements of the worldwide group for a period form the basis of the amount against which the Schedule compares the net finance deductions of UK members of the group to calculate the amount of any disallowance.

198. Paragraph 88 applies where the consolidated financial statements of the worldwide group for a period are not 'acceptable' and the amounts disclosed in those financial statements are materially different from those that would have been disclosed under IAS. Where the paragraph applies, the Schedule will apply as if the group had prepared consolidated financial statements under IAS for the period.

199. Sub-paragraph (3) provides that financial statements are 'acceptable' if:

- they are drawn up in accordance with international accounting standards;
- they meet conditions relating to accounting standards, principles or practice that the Commissioners may specify in regulations; or
- they meet the conditions set out in sub-paragraphs (4) to (6)

200. Sub-paragraphs (4) to (6) set out conditions A to C that financial statements must meet in order to be acceptable. They are that:

- (Condition A) the companies whose results are included in the financial statements must be the same as those that would have been included in financial statements drawn up under IAS; and

- (Condition B) the transactions whose results are relevant to the computation of the available amount under Part 9 included in the financial statements must be the same as those that would have been included in financial statements drawn up under IAS; and

- (Condition C) the amounts which are relevant to the computation of the available amount under Part 9 which are taken from those financial statements are calculated using the effective interest method.

201. Paragraph 89 provides how the Schedule will apply where consolidated financial statements of an ultimate parent and its subsidiaries are not prepared. The paragraph provides that the Schedule will apply as if financial statements had been drawn up under IAS. That is, the Schedule will apply on the basis that particular amounts taken into consideration in Part 9 (calculation of the available amount) will be those that would have been disclosed had the group drawn up consolidated financial statements in accordance with IAS.

202. Sub-paragraphs (2) – (4) provide rules that establish the period of account for the worldwide group where no consolidated financial statements are prepared.

203. Paragraph 90 sets out what is meant by 'amounts disclosed in group's financial statements'. Such amounts may include amounts comprised in a larger disclosed amount, and include an amount disclosed in a joint venture that is a member of the group, however presented. Sub-paragraph (2) excludes capitalised amounts that are disclosed in the financial statements of the group for a period where they have already been included in the balance sheet of the group for an earlier period. Sub-paragraph (3) excludes amounts in respect of group pension schemes or any entity that is not a member of the group.

204. Paragraph 91 deals with the currency denomination: all non-sterling denominated amounts are to be converted into sterling at the average rate of exchange for that accounting period.

205. Paragraph 92 provides for specified terms within the Schedule to take their meaning for the purposes of the Schedule from the definition given to them, for the time being, by IAS.

206. Sub-paragraph (2) provides that the paragraph may be amended by regulation.

207. Paragraph 93 defines a 'relevant accounting period' of a company as any accounting period that fall wholly or partly within the period of account of the worldwide group.

208. Paragraph 94 defines 'the Commissioners', 'the FSA Handbook' and 'HMRC' for the purposes of the Schedule.

Part 11 – Consequential Amendments and Commencement

209. Paragraph 95 adds regulations made under paragraphs 24 to 26, 36 and 38 of this Schedule, which deal with the allocation of disallowed amounts and exempt amounts, to the list of specified provisions given in section 98 of the Taxes Management Act 1970. Failure to comply with a notice given under a provision specified in section 98 may result in a penalty as set out in that section.

210. Paragraph 96 makes the amendment necessary to ensure that the transfer pricing rules at Sch 28AA ICTA take priority over the Schedule. This ensures that adjustments to financing income made under the Schedule will not be reinstated by transfer pricing rules. It also ensures that financing expenses disallowed under the Schedule cannot also be disallowed by the transfer pricing rules.

211. Paragraph 97 gives the commencement rule for the Schedule, which, subject to paragraph 98, takes effect for periods of account of the worldwide group that begin on or after 1 January 2010. The periods of account of the worldwide group are defined in paragraph 87(3) by reference to the consolidated financial statements of the ultimate parent of the group.

212. Paragraph 98 provides an anti-avoidance rule to prevent the ultimate parent of a worldwide group manipulating its accounting date to take advantage of the commencement provisions at paragraph 97. By moving its accounting date from 31 December 2009 to 30 December 2009, a group would ensure that the Schedule did not apply to it for a further 12 months. Paragraph 98 applies where the main purpose, or one of the main purposes, of a group changing its accounting date is to achieve such a result. Its effect is to apply the provisions of Schedule 15 to the accounting period beginning immediately after the changed accounting date.

213. Paragraph 99 explains how the Schedule will deal with amounts that accrue in the financial statements of a company for a period, but are not brought into account for corporation tax purposes until a later period. If those amounts would have been brought into account for the purposes of corporation tax in a period beginning before 1 January 2010 but for one of the statutory provisions listed in sub-paragraph (2), they cannot be treated as either financing expense amounts or financing income amounts of the company. This ensures that the provisions of the Schedule can only apply to amounts that accrued in periods in respect of which the Schedule has effect.

BACKGROUND NOTE

214. In the 2008 Pre-Budget Report, the Government announced a package of reforms to the taxation of companies on their foreign profits, to be introduced in Finance Bill 2009. The package includes the introduction of a measure to restrict the interest and other finance expense that can be deducted in computing the corporation tax payable by the UK members of a worldwide group of companies. In broad terms, the measure limits the UK tax deduction for intra-group finance expense to the external gross finance expense of the worldwide group of companies.

215. Draft legislation covering the interest restriction and other elements of the foreign profits package was published for consultation on 9 December 2008. The consultation period ran until 3 March 2009. Updated draft legislation with additional guidance notes to deal with particular exclusions from the worldwide debt cap measure was published on 26 January 2009. The legislation included in the Finance Act has been amended reflecting comments on the draft released for consultation.

SECTION 36: SCHEDULE 16: CONTROLLED FOREIGN COMPANIES

SUMMARY

1. Section 36 provides for the amendment of the Controlled Foreign Company (CFC) rules in Chapter 4 of Part 17 of the Income and Corporation Taxes Act 1988 (ICTA). The detailed amendments are in Schedule 16.

2. Part 1 of the Schedule repeals the exemption from the CFC rules for overseas companies which pay most of their profits back to shareholders in the United Kingdom. Part 2 of the Schedule provides for the amendment of the special rules for holding companies in the exempt activities exemption. It removes the rules providing exemption for 'superior holding companies' and 'non-local holding companies'. The exemption will in future only relate to the third category, local holding companies.

3. Parts 1 and 2 have effect in relation to a CFC's accounting periods beginning on or after 1 July 2009. Provision is made to split accounting periods which straddle this date.

4. Part 3 of the Schedule contains an amendment consequential to the legislation in Schedule 15, Finance Act 2009. It provides for the chargeable profits of a CFC to be reduced in certain circumstances to avoid double taxation.

5. The changes introduced by this Section are part of the package of measures being introduced as a result of the Government's review of the taxation of foreign profits.

DETAILS OF THE SECTION

6. The Section provides that Schedule 16 has effect to amend the CFC rules.

DETAILS OF THE SCHEDULE

Part 1 – Abolition of Acceptable Distribution Policy Exemption

7. Paragraph 1 removes the reference to the acceptable distribution policy (ADP) exemption in section 748 of ICTA which lists the circumstances in which the CFC charging provision in section 747 of ICTA will be disapplied and repeals the ADP rules in Part 1 of Schedule 25 of ICTA.

8. Paragraph 2 makes consequential changes to ICTA.

9. Paragraphs 3 and 4 amend the rules in Schedule 29 to the Finance Act 2002 concerning the calculation of gains and losses arising to a CFC from intangible assets and carry the effect through to the legislation in Corporation Tax Act 2009.

10. Paragraph 5 makes consequential changes to the relevant Finance Acts.

11. Paragraph 6 states that Part 1 of the Schedule has effect in relation to a CFC's accounting periods beginning on or after 1 July 2009.

12. Paragraph 7 sets out that where a CFC has an accounting period which straddles 1 July 2009 it is to be treated as split into two separate accounting periods in order to facilitate the repeal of the ADP exemption.

13. The first of these periods will begin on the first day of the straddling period and end on 30 June 2009; the second will begin on 1 July 2009 and end on the last day of the straddling period. The CFC's chargeable profits and creditable tax should be apportioned between the two periods on a just and reasonable basis.

14. Paragraph 8(1) makes it clear that the amendments do not affect the application of either:

- the rules in sections 801, 801C and 803A of ICTA concerning the treatment of dividends paid in pursuit of an ADP; or
- the ADP exemption in Part 1 of Schedule 25 to ICTA

in relation to dividends paid on or after 1 July 2009 for periods ending before that date in pursuit of an ADP.

15. Sub-paragraphs (2) and (3) set out a transitional provision which applies where the CFC paid a dividend in the second of the two deemed accounting periods created by paragraph 7. It ensures that the current rules governing how dividends are attributed to accounting periods continue to work appropriately. It does this by saying that the relevant provisions of section 799 of ICTA will have effect as if the reference in it to the last period for which accounts of the CFC were made up were a reference to the first of the two deemed accounting periods provided for by paragraph 7.

16. The purpose of paragraphs 7 and 8 is to ensure that the ADP exemption remains available to profits accruing prior to 1 July 2009. A CFC which pays a dividend on or after 1 July 2009 for an accounting period ending before that date may still qualify for the ADP exemption for that period if the conditions currently in Part 1 of Schedule 25 are fulfilled.

17. Paragraph 9 states that 'accounting period', 'chargeable profits', 'controlled foreign company' and 'creditable tax' take the meaning given to them for the purposes of the CFC rules.

Part 2 – Amendment of Exempt Activities Exemption

18. Part 2 of the Schedule provides for the amendment of the special rules for holding companies in the exempt activities exemption. They remove the rules providing exemption for 'superior holding companies' and 'non-local holding companies'. The exemption will thereafter only relate to the third category, local holding companies.

19. Paragraph 10 amends Part 2 of Schedule 25 to ICTA containing the exempt activities exemption and repeals those elements of it relating to holding companies other than local holding companies. It also removes references to 'superior holding companies' from the legislation and repeals the related definition at paragraph 12A.

20. Paragraph 11 makes consequential changes to the relevant Finance Acts.

21. Paragraph 12 states that the changes in Part 2 have effect for the accounting period of a CFC beginning on or after the commencement date. For 'qualifying holding companies' the commencement date is 1 July 2011; for all other companies the commencement date is 1 July 2009.

22. Paragraph 13 defines a 'qualifying holding company' as a CFC that was an 'exempt holding company' for the duration of the last accounting period to end before 1 July 2009 but specifically excluding an accounting period created by Part 2 of this Schedule.

23. An 'exempt holding company' is a company which throughout a particular accounting period was engaged in exempt activities under the special rules applying to non-local and superior holding companies.

24. The distinction between qualifying and non-qualifying holding companies is fundamental to the operation of the Schedule. It underlies the mechanism by which transitional relief is provided elsewhere in the Schedule.

25. Paragraph 14 contains rules that apply where a CFC has an accounting period that straddles 1 July 2009. In such circumstances the straddling period shall be treated as split into two deemed accounting periods to facilitate the repeal of the superior and non-local holding company rules.

26. The first deemed period will begin on the first day of the straddling period and end on 30 June 2009; the second will begin on 1 July 2009 and end on the last day of the straddling period. The CFC's gross income, chargeable profits and creditable tax should be apportioned between the two periods on a time basis according to their respective lengths.

27. Paragraph 15 contains similar rules which apply to a qualifying holding company which has an accounting period which straddles 1 July 2011.

28. The straddling accounting period is again to be treated as split into two deemed accounting periods. The first will begin on the first day of the straddling period and end on 30 June 2011; the second will begin on 1 July 2011 and end on the last day of the straddling period. The CFC's gross income, chargeable profits and creditable tax should be apportioned between the two periods on a time basis according to their respective length.

29. The rules in paragraphs 14 and 15 are required to ensure that profits accruing in periods straddling 1 July 2009 and 1 July 2011 are treated appropriately. For CFCs which are not qualifying holding companies 1 July 2009 marks the point from which only the local holding company exemption will be available.

30. For a qualifying holding company 1 July 2009 marks the beginning of a two year transitional period in which the superior and non-local holding company rules will continue to be available subject to the provisions of paragraph 17. The transitional period defers the commencement date for qualifying holding companies until 1 July 2011 after which only the local holding company exemption will be available.

31. Paragraph 16 contains the definition of 'relevant accounting period', a term employed in paragraph 17. A relevant accounting period is one that falls within the two year transitional period established for qualifying holding companies by the deferred commencement date.

32. Paragraph 17 contains the special rules that apply to a qualifying holding company in the transitional period. They set out that in relation to a relevant accounting period of a qualifying holding company, paragraphs 6(4) and (4A) of Schedule 25 have effect subject to certain specified conditions. These mean that transitional relief is not automatically available to qualifying holding companies where levels of non-qualifying gross income exceed historic flows.

33. Sub-paragraph (2) sets out these criteria. They say that the non-local and superior holding company rules in paragraphs 6(4) or (4A) of Schedule 25 will only apply if the conditions set out in those paragraphs are satisfied, and additional criteria, referred to as conditions A and B, are also met.

34. Sub-paragraph (3) sets out condition A which is that at all 'material times' the group of companies of which the CFC was a member must have had the same ultimate parent.

35. Sub-paragraph (4) defines 'material times' as at the beginning of 9 December 2008 and all times during the accounting period in question.

36. Sub-paragraph (5) defines Condition B, which is satisfied where the amount X does not exceed amount Y.

37. Sub-paragraph (6) identifies amount X as the amount of the CFC's gross income in the accounting period that is 'non-qualifying gross income', defined in Sub-paragraph (9) as gross income which does not help a CFC satisfy the existing non-local and superior holding company rules.

38. This definition builds on the existing statutory term 'gross income', used in Schedule 25, which broadly speaking refers to the full amount of any income to which a CFC is entitled during an accounting period before any expenses are deducted.

39. Exemption is available under the existing holding company rules where at least 90 per cent of a holding company's gross income during the accounting period comes from companies that it controls and which, if not themselves holding companies, are engaged in exempt activities. There are detailed rules setting out what income can qualify as part of the 90 per cent for each of the different types of holding company.

40. Sub-paragraph (7) establishes that amount Y is the highest amount of non-qualifying gross income arising in an earlier reference period or periods. Sub-paragraph (9) specifies that a reference period is an accounting period of the CFC that is any one of its last three accounting periods ending before 9 December 2008, and an accounting period in relation to which the CFC was an exempt holding company. However where there is no reference period the Schedule specifies a default reference period of 12 months ending on 9 December 2008.

41. Sub-paragraph 8 provides for a time apportionment where amounts X and Y arise in periods of differing length to ensure that the comparison between the two amounts is consistent.

42. The effect of paragraph 17 is to limit the amount of non-qualifying gross income in the transitional periods to the highest amount arising in any of up to three earlier reference periods. As is made clear in paragraph 17(2)(a) the existing gross income test must be satisfied so at least 90 per cent of the CFC's gross income must be qualifying income. However, notwithstanding this, if the amount of non-qualifying gross income in the relevant period exceeds the level set by amount Y then the CFC will fail to qualify for exemption.

43. Paragraph 18 defines 'ultimate corporate parent' and 'group' for the purposes of paragraph 17(3).

44. Paragraph 19 contains an anti-avoidance rule. It applies where a company alters its accounting date so that a particular period that otherwise would have fallen into an accounting period ending on or after 9 December 2008 instead falls into an accounting period ending before that date.

45. Paragraph 20 states that 'accounting period', 'chargeable profits', 'control', 'controlled foreign company', 'creditable tax' and 'gross income' take the meaning given to them for the purposes of the CFC rules.

Part 3 – Reduction in Chargeable Profits for Certain Financing Income

46. Paragraphs 21 and 22 amend ICTA to take account of the introduction of section 751AA.

47. Paragraph 23 inserts the new section into the CFC rules in ICTA. It applies where an apportionment is to be made under section 747(3) and;

a. the chargeable profits of the CFC contain an amount of income in respect of payment made by another company, and;

b. the amount brought into account for corporation tax purposes by the payer is reduced by the rules in Part 3 of Schedule 15.

48. It allows the UK company to which the profits are to be apportioned to apply to the Commissioners for a reduction in the chargeable profits of the CFC. If the Commissioners grant the application those profits are treated as reduced by the specified amount and the CFC's creditable tax are accordingly reduced on a just and reasonable basis.

49. The purpose of the new provision is to ensure that a restriction of an interest deduction under Schedule 15, Finance Act 2009 cannot interact with the CFC rules so as to cause the affected group to suffer double taxation.

50. Paragraph 24 amends the supplementary provision in section 751B, ICTA to take account of section 751AA.

51. Paragraph 25 specifies that the amendments made in Part 3 have effect in relation to accounting periods of CFCs ending on or after 1 January 2010.

BACKGROUND NOTE

52. The CFC legislation is at sections 747 to 756 of and Schedules 24 to 26 to ICTA. It is designed to counter the artificial diversion of profits from the UK by UK resident companies to companies which they control and which are located in low tax territories. It does this, broadly, by apportioning the diverted profits to, and taxing them on, those UK residents with a relevant interest in the non-resident company.

53. The effect of the CFC legislation is limited by a series of exemptions. There are five such exemptions which were designed to exclude from the scope of the rules those CFCs that can be reasonably assumed not to exist so as to artificially divert profits from the UK.

54. The Schedule repeals the ADP exemption and amends the exempt activities exemption to remove the special rules applying to holding companies apart from those applicable to local holding companies.

SECTION 37 SCHEDULE 17: INTERNATIONAL MOVEMENT OF CAPITAL

SUMMARY

1. Section 37 provides for the repeal of the Treasury Consents legislation in sections 765 to 767 of the Income and Corporation Taxes Act 1988 (ICTA) and its replacement with a requirement to report the details of certain transactions whose value exceeds £100 million to HM Revenue and Customs (HMRC). The detailed provisions are in Schedule 17.

2. These changes are being introduced as a result of the Government's review of the taxation of foreign profits and have effect for events or transactions taking place on or after 1 July 2009.

DETAILS OF THE SECTION

3. Section 37 introduces Schedule 17 which provides for the repeal of the Treasury Consents legislation and the introduction of a new reporting requirement in respect of certain international movements of capital.

DETAILS OF THE SCHEDULE

Part 1 – Abolition of the Existing Regime

4. Paragraph 1 repeals the Treasury Consent legislation at section 765 of ICTA the reporting requirement at section 765A together with the offence of failure to comply with section 765 and interpretative provisions at sections 766 and 767.

5. Paragraph 2 contains consequential amendments removing section 765A from the scope of the penalty provisions relating to special returns in section 98 of the Taxes Management Act 1970 (TMA).

6. Paragraph 3 carries the effect of the repeals in paragraph 1 and 2 into the Finance Acts which have previously amended sections 765 to 767.

Part 2 – Reporting Requirement

7. Paragraph 4 describes the reporting requirement. It applies to any UK corporate parent which is a 'reporting body' at the time that a reportable event or transaction occurs. Such reportable events or transactions must be reported to an officer of HMRC within six months.

8. The report must include such information relating to the event or transactions as is specified in regulations made by the Commissioners for Her Majesty's Revenue and Customs (the Commissioners). The purpose of the report is to enable the Commissioners to consider whether or not the event or transaction gives rise to an advantage in relation to UK taxation.

9. Paragraphs 5 and 6 define the situations in which a body corporate will be a 'reporting body'. A group of companies will generally only have one reporting body, which will be the top UK resident holding company, although not necessarily the group's ultimate parent company. However some groups may have more than one reporting body. In such cases the Schedule provides a mechanism whereby the reporting bodies may collectively nominate one of their number to be responsible for all aspects of the reporting requirement.

10. Paragraph 5 sets out a general condition that a body corporate, referred to as 'Body A', can only be a reporting body when it is a 'UK corporate parent' which is defined in paragraph 7 as the top UK resident holding company of a group which is not itself controlled by a UK resident body corporate.

11. However sub-paragraphs (2) to (5) then set out four additional conditions, any one of which must also be met before Body A can be considered to be a reporting body.

12. These rules establish a reporting body to be the parent company of a UK owned group or a UK resident company which heads part of a foreign owned group. If a group is structured as, for example, two or more parallel sub-groups controlled by a foreign parent then the UK resident parents of each sub-group will be reporting bodies in respect of their subsidiaries unless between them they nominate a single reporting body.

13. Paragraph 6 contains the rules governing the nominating process. A nomination can only be made where two or more UK corporate parents are controlled by the same foreign parent, although the arrangement does not have to cover all such corporate parents. Under the arrangement the nominated reporting body will be responsible for all the requirements of the Schedule on behalf of the other parties.

14. Sub-paragraph (3) empowers a party to a nominating arrangement to withdraw from it unilaterally.

15. Sub-paragraphs (4) and (5) enable the Commissioners to make regulations governing the nominating arrangements and specify that such regulations may include provision regarding entry and withdrawal from an arrangement and the related information that must be supplied to HMRC. They may also specify the circumstances in which a body corporate is treated as withdrawing from an arrangement.

16. Paragraph 7 defines 'UK corporate parent' as a UK resident body corporate which controls one or more bodies corporate that are not resident in the UK and is not itself controlled by a UK body corporate.

17. Paragraph 8 sets out what is meant by reportable transactions or events. The basic test is that their value must exceed £100 million. No report is required below that limit.

18. The paragraph goes on to specify that only certain categories of events and transactions are reportable. These categories are:

- an issue of shares or debentures by a foreign subsidiary;
- a transfer by the reporting body, or a transfer caused or permitted by the reporting body, of shares or debentures of a foreign subsidiary in which the reporting body has an interest; or
- any situation which results in a foreign subsidiary becoming, or ceasing to be, a controlling partner in a partnership.

19. Additional categories may be specified in regulations made by the Commissioners.

20. Sub-paragraph (3) sets out that for the purposes of the Schedule a foreign subsidiary is a controlling partner in a partnership if, whether alone or taken together with one or more other partners that are also subsidiaries, it controls the partnership.

21. Sub-paragraphs (4) to (6) empower the Commissioners to make regulations about how the value of an event or transaction is to be determined for the purposes of the reporting requirement.

22. Sub-paragraph (7) specifies that the Commissioners may increase the £100 million limit specified in the Schedule.

23. Paragraph 9 sets out the circumstances in which otherwise reportable transactions are excluded from the reporting requirement. Broadly these cover transactions carried out in the ordinary course of a trade, between residents in the same territory or the giving of any security by a foreign subsidiary to a financial institution. The Commissioners are also empowered to add to these exclusions in regulations.

24. Paragraph 10 establishes that failure to comply with the reporting requirement will result in a penalty being chargeable under section 98 of TMA. Such penalty will not exceed £300 for the initial failure with a further additional penalty not exceeding £60 for each day on which the failure continues after the initial penalty was imposed.

25. Paragraph 11 states that regulations and orders made under Part 2 of the Schedule are to be made by statutory instrument, subject to negative resolution.

26. Paragraph 12 contains interpretative provisions. In particular it sets out that for the purposes of the Schedule 'control' in relation to a body corporate means the power of a person to secure that the affairs of the body corporate are conducted in accordance with that person's wishes, whether this is achieved by:

- the holding of shares or the possession of voting power in or in relation to that or any other body corporate; or
- any powers conferred by the articles of association or other document regulating that or any other body corporate.

27. Where two or more persons taken together have this power then they shall be taken to control the body corporate.

28. 'Control' in relation to a partnership control means the right to a share of more than 50 per cent of the assets, or of more than 50 per cent of the income, of the partnership.

29. Definitions are also included for 'foreign', 'partnership', 'subsidiary', 'transaction' and 'series of transactions'.

Part 3 – Commencement etc.

30. Paragraph 13 specifies that the schedule has effect in relation to events taking place and transactions carried out on or after 1 July 2009.

31. Paragraph 14 contains two transitional provisions. The first provides that any reports in respect of events or transactions occurring before 1 October 2009 should be reported by 1 April 2010. This is intended to allow companies a period of time in which to establish internal procedures to monitor reportable transactions and events.

32. The second specifies that regulations made under the Schedule may come in to force on or after 1 July 2009 so long as they are made within one year of the Finance Act being passed.

BACKGROUND NOTE

33. The situations to which section 765 has been applied over the decades have changed in reaction to significant developments in UK tax law such as the introduction of capital gains tax and the controlled foreign company rules as well as to commercial developments.

34. To ease administration section 765 and its predecessors have provided that the Treasury may issue 'general consents'. If a transaction is within a general consent the company does not have to make a special application or post-transaction notification, it may go ahead and do what it proposes.

35. Section 765A removes from section 765 all movements of capital to which the European Community Directive on Capital Movements applies. But although companies no longer need Treasury consent they are required to report to HMRC any transaction they have carried out to which, but for section 765A, they would have needed special consent.

36. The requirement to apply for consent is regarded by business as an administratively burdensome obstacle to entering into commercial transactions. This legislation therefore removes the consent requirement and modernises the rules, replacing them with a post-transaction reporting requirement targeted at transactions where there is a high risk of potential avoidance activity.

SECTION 38 SCHEDULE 18: CORPORATION TAX: FOREIGN CURRENCY ACCOUNTING

SUMMARY

1. Section 38 and Schedule 18 ensure that where a company computes its profits or losses for corporation tax purposes in a currency other than sterling any losses carried forward to future accounting periods or back to a previous accounting period will be translated into sterling at the same exchange rate as the profits they are offsetting. There are special rules to deal with the situation where the losses in one period are computed for corporation tax purposes in one currency but are being offset against profits for an earlier or later period computed in a different currency.

DETAILS OF THE SCHEDULE

2. Paragraph 2 amends section 92(2) of the Finance Act (FA) 1993 to reflect amendments to section 92D of FA 1993 and the insertion of sections 92DA, 92DB, 92DC and 92DD of FA 1993.

3. Paragraph 3 inserts new subsection (4) to section 92B of FA 1993 and paragraph 4 inserts new subsection (5) to section 92C of FA 1993. These subsections ensure that where any amounts are required to be translated into another currency they are translated at the "appropriate exchange rate". The "appropriate exchange rate" is defined at new section 92E(4) of FA 1993 (see paragraph 45).

4. Paragraph 5 substitutes, in place of the existing section 92D of FA 1993, a new section 92D of FA 1993 and also introduces new sections 92DA, 92DB, 92DC, 92DD and 92DE to FA 1993 that deal with the translation of "carried back amounts" and "carried forward amounts".

5. New section 92D provides the "basic rule" for translating amounts into sterling – the section will apply, subject to the special rules at sections 92DA and 92DB of FA 1993, where any profit or loss is required by section 92B or 92C of FA 1993 to be translated into its sterling equivalent and any such translations should be made by reference to the "appropriate exchange rate".

6. New section 92DA sets out the rules to determine the sterling equivalent of "carried back amounts". Such amounts are defined in new section 92DE(1) of FA 1993.

7. New subsection (1) sets out when section 92DA applies. This is where a company carries back any amount and with regard to that amount the loss is required to be translated into sterling by section 92B or 92C of FA 1993.

8. New subsection (2) sets out that a translation required by this section must be made in accordance with one of three rules, whichever is applicable, set out in the following subsections.

9. New subsection (3) sets out when Rule 1 is applicable and will be the most common situation. This is where the operating currency of the company in the accounting period in which the carried back loss originated and the operating currency of the company in the earlier accounting period in which that loss is utilised are the same.

10. New subsection (4) states that Rule 1 is that the exchange rate for translating any carried back amounts utilised in an earlier accounting period must be the same as the exchange rate used in computing the profits of that earlier accounting period.

11. New subsection (5) sets out when Rule 2 is applicable. This deals with changes in operating currency and applies where losses originating in an accounting period when sterling is not the operating currency are carried back into a period when sterling is the operating currency.

12. New subsection (6) states that Rule 2 is that the rate of exchange for translating the carried back loss must be the spot rate on the last day of the relevant accounting period. The "relevant accounting period" is defined in subsection (9) (see paragraph 15). This will convert non-sterling losses carried back into sterling at the end of the last accounting period where sterling was the operating currency even though the loss may not, necessarily, be utilised in that period. Consequently, the value of those losses, in sterling, will remain the same throughout all periods where sterling is the operating currency.

13. New subsection (7) sets out when Rule 3 is applicable. This deals with changes in operating currency and applies where losses originate in an accounting period in one currency and are carried back into an accounting period where profits and losses are computed in a different non-sterling operating currency.

14. New subsection (8) states that Rule 3 requires two stages. Firstly, any loss carried back into an earlier accounting period is translated into the operating currency of the earlier accounting period at the spot rate on the last day of the "relevant accounting period". The "relevant accounting period" is defined at subsection (9) (see paragraph 15). This will convert the carried back losses into the previous operating currency at the end of the last accounting period where there was a different operating currency even though the loss may not necessarily be utilised in that period. Consequently, the value of those losses, in the previous operating currency, will remain the same throughout all periods where that previous operating currency is the operating currency. Secondly, the carried back amount that has been translated into the operating currency of the earlier accounting period is then translated into sterling at the same rate of exchange as the profits of the earlier accounting period in which the loss is utilised.

15. New subsection (9) defines the "relevant accounting period" for the purposes of subsections (6) and (8). This ensures that the value of losses, in the previous operating currency, will remain the same throughout all periods where that previous operating currency is the operating currency.

16. New section 92DB deals with the situation where amounts calculated in a non-sterling currency are carried forward and utilised against profits in a later accounting period.

17. New subsection (1) sets out when section 92DB applies. This is where a company carries forward any amount and with regard to that amount a loss is required to be translated into sterling by section 92B or 92C of FA 1993.

18. New subsection (2) sets out that a translation required by this section must be made in accordance with one of three rules set out in the following subsections, depending on whichever is applicable.

19. New subsection (3) sets out when Rule 1 is applicable and will be the most common situation. This is where the operating currency of the company in the accounting period in which the carried forward loss originated and the operating currency of the company in the later accounting period in which that loss is utilised are the same.

20. New subsection (4) states that Rule 1 is that the exchange rate for translating any carried forward amounts utilised in a later accounting period must be the same as the exchange rate used in computing the profits and losses of that later accounting period.

21. New subsection (5) sets out when Rule 2 is applicable. This deals with changes in operating currency and applies where losses originating in an accounting period when sterling is not the operating currency are carried forward into a period when sterling is the operating currency.

22. New subsection (6) states that Rule 2 is that the rate of exchange for translating the carried forward loss must be the spot rate on the first day of the "relevant accounting period". The "relevant accounting period is defined at subsection (9) (see paragraph 25).This will convert non-sterling losses carried forward into sterling at the beginning of the first accounting period where sterling is the operating currency even though the loss may not necessarily be utilised in that period. Consequently, the value of those losses, in sterling, will remain the same throughout all periods where sterling is the operating currency.

23. New subsection (7) sets out when Rule 3 is applicable. This deals with changes in operating currency and applies where losses originate in an accounting period in one currency and are carried forward into an accounting period where profits and losses are computed in a different non-sterling operating currency.

24. New subsection (8) states that Rule 3 requires two stages. Firstly, any loss carried forward into a later accounting period is translated into the operating currency of the later accounting period at the spot rate on the first day of the "relevant accounting period." This will convert the carried forward losses into the future operating currency at the start of the first accounting period where there is a different operating currency even though the loss may not necessarily be utilised in that period. Consequently, the value of those losses, in the future operating currency, will remain the same throughout all periods where that future operating currency is the operating currency. Secondly, the carried forward amount that has been translated into the operating currency of the later accounting period is then translated into sterling at the same rate of exchange as the profits of the later accounting period in which the loss is utilised.

25. New subsection (9) defines the "relevant accounting period" for the purposes of subsections (6) and (8). This ensures that the value of losses, in the future operating currency, will remain the same throughout all periods where that future operating currency is the operating currency.

26. New section 92DC of FA 1993 deals with the situation where losses calculated in sterling are carried back and utilised against profits in an earlier accounting period when sterling is not the operating currency.

27. New subsection (1) sets out that section 92DC of FA 1993 applies where three Conditions (A to C) are met.

28. New subsection (2) is Condition A. This is that a company's accounts have either been prepared in sterling or identify sterling as the functional currency.

29. New subsection (3) is Condition B. This is that there is a loss that is to be carried back for offset against profits in a previous accounting period.

30. New subsection (4) is Condition C. This is that the operating currency in the period in which the loss is being offset is not sterling.

31. New subsection (5) sets out the consequences of meeting the three Conditions for section 92DC of FA 1993. Firstly, any loss carried back into an earlier accounting period is translated into the operating currency of the earlier accounting period at the spot rate on the last day of the "relevant accounting period". The "relevant accounting period" is defined at subsection (6) (see paragraph 32). This will convert the carried back losses into the previous operating currency at the end of the last accounting period where there was a different operating currency even though the loss may not necessarily be utilised in that period. Consequently, the value of those losses will remain the same throughout all periods where that previous operating currency is the operating currency. Secondly, the carried back amount is retranslated back into sterling at the same rate of exchange as the profits of the earlier accounting period in which the loss is utilised.

32. New subsection (6) defines the "relevant accounting period" for the purposes of subsection (5)(a). This ensures that the value of losses, in the previous operating currency, will remain the same throughout all periods where the previous operating currency is the operating currency.

33. New section 92DD deals with the situation where losses calculated in sterling are carried forward and utilised against profits in a later accounting period when sterling is not the operating currency.

34. New subsection (1) sets out that section 92DD of FA 1993 applies where three Conditions (A to C) are met.

35. New subsection (2) is Condition A. This is that a company's accounts have either been prepared in sterling or identify sterling as the functional currency.

36. New subsection (3) is Condition B. This is that there is a loss that is to be carried forward for offset against profits in a future accounting period.

37. New subsection (4) is Condition C. This is that the operating currency in the period in which the loss is being offset is not sterling.

38. New subsection (5) sets out the consequences of meeting the three Conditions for section 92DC of FA 1993. Firstly, any loss carried forward into a later accounting period is translated into the operating currency of the later accounting period at the spot rate on the first day of the "relevant accounting period". The "relevant accounting period" is defined at subsection (6) (see paragraph 39). This will convert the carried forward losses into the later operating currency at the start of the first accounting period where there is a different operating currency even though the loss may not necessarily be utilised in that period. Consequently, the value of those losses will remain the same throughout all periods where that later operating currency is the operating currency. Secondly, the carried forward amount is retranslated back into sterling at the same rate of exchange as the profits of the later accounting period in which the loss is utilised.

39. New subsection (6) defines the "relevant accounting period" for the purposes of subsection (5)(a). This ensures that the value of losses, in the later operating currency, will remain the same throughout all periods where the later operating currency is the operating currency.

40. Sections 92DE (1) and (2) of FA 1993 set out the meaning of "carried-back amount" and "carried-forward amount."

41. New subsection (3) clarifies that the references in sections 92DB and 92DD of FA 1993 to the profit against which carried-forward losses are to be offset would be the amount of profit ignoring the deduction of carried forward losses against that profit.

42. New subsection (4) clarifies that subsection (3) applies equally to amounts that are offset as though they are a loss of the later period. This would apply to, for example, expenses of management carried forward and offset in a later period as though they are a loss in the period in which they are utilised under section 1223 of the Corporation Tax Act 2009.

43. Paragraphs 6(1)-(6) make consequential amendments to section 92E of FA 1993.

44. Paragraph 6(7) inserts new subsections (4) and (5) into section 92E.

45. New subsection (4) contains a new definition of "the appropriate exchange rate" for the purposes of section 92B to 92D of FA 1993. This replaces the definition previously at section 92D(2) of FA 1993 and like the previous definition allows for either the average for the accounting period or the spot rate on the day of the transaction(s). The new definition removes any uncertainty that spot rates may be used, on a just and reasonable basis, where there is more than one transaction in the accounting period. It also states that where there is only one transaction, an appropriate spot rate must be used and so in that circumstance there is no choice between using an average rate or a spot rate.

46. New subsection (5) inserts a definition of "operating currency" for the purposes of section 92DA and 92DB of FA 1993.

47. Paragraph 7 provides for the commencement date for the amendments made by this Schedule. The changes apply to accounting periods beginning on or after the commencement (as defined in paragraph 12(3)).

48. Paragraph 8 provides transitional rules where non-sterling losses are carried back and utilised in accounting periods prior to the commencement of this Schedule.

49. Paragraph 8(1) sets out that paragraph 8 applies where there are non-sterling losses arising in an accounting period to which this Schedule applies that are utilised in an accounting period prior to the commencement of this Schedule.

50. Paragraph 8(2) states where the condition in paragraph 8(2) is met then the normal rules relating to non-sterling losses that are carried back and utilised in earlier accounting periods at section 92DA of FA 1993 will not operate.

51. Paragraph 8(3) sets out, where the condition in paragraph 8(2) is met, carried-back losses originating in non-sterling currencies must be translated into sterling at the "appropriate exchange rate" for the accounting period in which the loss arises. The "appropriate exchange rate" is defined at section 92E(4) of FA 1993 (see paragraph 45).

52. Paragraph 9 provides transitional rules where non-sterling losses originate in an accounting period prior to the commencement of this Schedule but are utilised in an accounting period to which this Schedule applies.

53. Paragraph 9(1) sets out when paragraph 9 applies. This being that there are non-sterling losses arising in an accounting period prior to the commencement of this Schedule that are utilised in an accounting period to which this Schedule applies.

54. Paragraph 9(2) sets out, where the condition in Paragraph 9(2) is met, the three steps that must be followed in order to translate carried-forward losses originating in non-sterling currencies into sterling. Step 1 is to translate the loss into sterling at the "appropriate exchange rate" for the accounting period in which the loss arises. Step 2 is to translate the loss from Step 1 (now in sterling) into the original currency at the spot rate of exchange on the first day of the first accounting period to which this Schedule applies. Step 3 is to translate the loss resulting from Step 2 into sterling as per Rules 1, 2 or 3 set out in paragraph 9(4).

55. Paragraph 9(3) sets out when Rule 1 is applicable. This is where the operating currency of the company in the accounting period in which the carried forward loss originated and the operating currency of the company in the later accounting period in which that loss is utilised are the same.

56. Rule 1 in Paragraph 9(4) is that the exchange rate used in translating any carried forward amounts utilised in a later accounting period must be the same as the exchange rate used in computing the profits of that later accounting period.

57. Paragraph 9(5) sets out when Rule 2 is applicable. This deals with changes in operating currency and applies where losses originating in an accounting period when sterling is not the operating currency are carried forward into a period when sterling is the operating currency.

58. Rule 2 in Paragraph 9(6) is that the rate of exchange for translating the carried forward loss must be the spot rate on the first day of the "relevant accounting period". The "relevant accounting period is defined at subsection (9) (see paragraph 61). This will convert non-sterling losses carried forward into sterling at the beginning of the first accounting period where sterling is the operating currency even though the loss may not necessarily be utilised in that period. Consequently, the value of those losses, in sterling, will remain the same throughout all periods where sterling is the operating currency.

59. Paragraph 9(7) sets out when Rule 3 is applicable. This deals with changes in operating currency and applies where losses originate in an accounting period in one currency and are carried forward into an accounting period where profits and losses are computed in a different non-sterling operating currency.

60. Rule 3 in Paragraph 9(8) requires two stages. Firstly, any loss carried forward into a later accounting period is translated into the operating currency of the later accounting period at the spot rate on the first day of the "relevant accounting period." The "relevant accounting period" is defined at subsection (9) (see paragraph 61). This will convert the carried forward losses into the future operating currency at the start of the first accounting period where there is a different operating currency even though the loss may not necessarily be utilised in that period. Consequently, the value of those losses, in the future operating currency, will remain the same throughout all periods where that future operating currency is the operating currency. Secondly, the carried forward amount that has been translated into the operating currency of the later accounting period is then translated into sterling at the same rate of exchange as the profits of the later accounting period in which the loss is utilised.

61. Paragraph 9(9) defines the "relevant accounting period" for the purposes of subsections (6) and (8). This ensures that the value of losses, in the future operating currency, will remain the same throughout all periods where that future operating currency is the operating currency.

62. Paragraph 10 provides transitional rules where sterling losses are carried back into a period prior to the commencement of this Schedule.

63. Paragraph 10(1) sets out the specific conditions for paragraph 10 to apply. These are where sterling losses are carried back and utilised against profits in an accounting period prior to the commencement of this Schedule where sterling is not the operating currency.

64. Paragraph 10(2) sets out that where the conditions in paragraph 10(1) are met then the rules relating to the translation of carried back losses at section 92DC will not apply. The sterling losses carried back will be offset against the profits of the company in the earlier accounting period translated into sterling.

65. Paragraph 11 provides transitional rules where sterling losses are carried forward from an accounting period prior to the commencement of this Schedule into an accounting period after the commencement of this Schedule.

66. Paragraph 11(1) sets out the specific conditions for paragraph 11 to apply. These are where sterling losses originating in an accounting period prior to the commencement of this Schedule are carried forward and utilised against profits in an accounting period after the commencement of this Schedule where sterling is not the operating currency.

67. Paragraph 11(2) sets out that, with one modification (see paragraph 68), the normal rules relating to the translation of losses originating in sterling that are offset against profits computed in a non-sterling currency in a later accounting period will apply (section 92DD of FA 1993).

68. Paragraph 11(3) alters the meaning of "relevant accounting period" in subsection (6) of section 92DD of FA 1993 when that section is applied to losses that meet the conditions at paragraph 11(1). Where this is the case, "relevant accounting period" will mean the first accounting period beginning on or after the commencement of this schedule in which the operating currency is not sterling. This would mean that translation would take place on the first day of that "relevant accounting period".

69. Paragraph 12(2) makes clear that the provisions in subsections (3) and (4) of section 92DE of FA 1993 (that deal with references to the profit against which a carried-forward amount is to be set off) apply in relation to this whole Schedule in the same manner as they apply in relation to sections 92DB and 92DD of FA 1993.

70. Paragraph 12(3) states that "the commencement date" for the purposes of this Schedule means 29 December 2007.

71. Paragraph 13(1) provides that a company can elect to ensure that paragraphs 9 and 11 (the transitional rules that relate to amounts carried forward from earlier periods) does not apply and defers "the commencement date" from 29 December 2007 to the day on which this Act is passed. The election will therefore enable a company to ensure that all brought forward losses at the beginning of the first accounting period beginning on or after Royal Assent are not translated from sterling back into the currency in which the loss originated. This will prevent any companies from being disadvantaged by this Schedule.

72. Paragraph 13(2) sets out the time limit within which any election under Paragraph 10 should be made and ensures that any such election is irrevocable. The normal rules relating to elections at Schedule 1A to the Taxes Management Act 1970 (TMA) will apply.

BACKGROUND NOTE

73. Where a company computes its profits or losses for corporation tax purposes in a currency other than sterling current tax rules require that company to carry forward or back any unused losses in sterling. This rule leads to exchange exposure for both companies and the Exchequer. This exposure has become a significant issue recently for a number of companies whose profits are computed for tax purposes in a currency other than sterling due to exchange rate volatility. This means that the measure of losses translated into sterling when incurred will offset a different measure of profits translated into sterling arising in a previous or subsequent accounting period.

74. In response to this, a written statement presented to Parliament by the Financial Secretary to the Treasury dated 18 December 2008 announced the Government's intention to allow companies to carry forward and back unused losses in the currency in which they were computed.

75. The purpose of this Schedule is therefore to ensure that losses computed in a currency other than sterling offset the same measure of profits computed in that currency for the earlier or later period.

76. There are also rules that seek to remove the impact of currency fluctuations on the value of losses where a company has losses that have been computed in sterling in one accounting period that are then offset in an earlier or later accounting period when the profits of the company are computed in a non-sterling currency.

77. In order to bridge the change in treatment of foreign denominated losses, transitional rules will apply where a company has unused losses brought forward at the start of the first accounting period after the commencement of this section and those losses were computed in a currency other than sterling. In these cases the brought forward losses will be converted back into the currency in which they originated, although an election is available to allow companies to only apply the changes outlined above to losses incurred in accounting periods beginning on or after the date of Royal Assent.

SECTION 39: CERTAIN DISTRIBUTIONS OF OFFSHORE FUNDS TAXED AS INTEREST

SUMMARY

1. Certain distributions from offshore funds are economically similar to payments of yearly interest. Section 39, from 22 April 2009, charges distributions of this type to tax as if they were yearly interest.

DETAILS OF THE SECTION

2. The section inserts a new section 378A into Chapter 2 of Part 4 of the Income Tax (Trading and Other Income) Act 2005.

3. Subsections (1) and (3) of section 378A determine when the section will apply.

4. The test in subsection (3) is similar to that which applies to corporate investors for the purposes of the loan relationships legislation. (See sections 490 and 493 CTA 2009). A distribution is treated as interest if the offshore fund, at any time during the 'relevant period', holds more than 60 per cent of its assets in the form of qualifying investments. The definition of a qualifying investment is set out in section 494 of the Corporation Tax Act (CTA) 2009 and, in summary, refers to interest bearing and economically similar investments.

5. Subsection (2) is the operative part of the new section. It determines the tax treatment of distributions from offshore funds to which the section applies.

6. Subsections (4) and (5) define the 'relevant period', to which the 'qualifying investments test' applies (subsection (3)). The period is normally the last period of account of the fund ending before the date the dividend is paid but there is an exception where that period is less than 12 months. In this case the period to be considered is the 12 month period ending with the last day of that period of account. This is subject to subsection (5)(b) which caters for interim distributions. When the distribution cannot be fully funded from profits available in previous periods then the 'relevant period' is the current period. Subsections (4) and (5) therefore apply, to the extent possible, the qualifying investments tests to the period of account in which profits to be distributed were earned.

7. Subsection (6) of section 378A extends the application of the section to include the case of a manufactured overseas dividend which represents a distribution to which the section would apply.

BACKGROUND NOTE

8. The purpose of the section is to prevent a tax advantage being gained by holding interest bearing assets within an offshore fund structure.

9. Distributions made as dividends from offshore funds and received by individual shareholders were taxed at rates of 10 per cent for basic rate and 32.5 per cent for higher rate taxpayers.

10. From 22 April 2009, where a distribution from an offshore fund takes the form of a dividend the rate will be the dividend tax rate after taking into account the dividend tax credit. However, where the offshore fund is substantially invested in interest bearing, or economically similar, assets as described in paragraph 4 above then any distribution will be treated as interest for income tax purposes.

SECTION 40 AND SCHEDULE 19: INCOME TAX CREDITS FOR FOREIGN DISTRIBUTIONS

SUMMARY

1. Section 40 and Schedule 19 provide for changes to the system of taxation for individuals who own foreign shares. Individuals in receipt of dividends from UK-resident companies or who have small shareholdings (less than 10 per cent) in non-UK resident companies are entitled under current law to a non-payable dividend tax credit.

2. The section and Schedule provide that individuals with shareholdings of 10 per cent or greater in non-UK resident companies will also be entitled to a non-payable tax credit, subject to certain conditions.

DETAILS OF THE SCHEDULE

3. Paragraph 2(2) substitutes new subsection 397A(1) for the current subsections 397A(1) and (2) of the Income Tax (Trading and Other Income) Act 2005 (ITTOIA). This has the effect of removing the bar on tax credits applying to distributions from offshore funds.

4. Paragraphs 2(3) and (4) make consequential amendments to subsections 397A (3) and (7).

5. Paragraph 3 inserts new section 397AA (tax credit under section 397A: conditions).

6. New section 397AA(1) provides that section 397A(1) applies only if one of Conditions A, B or C is met.

7. New section 397AA(2) makes provision for Condition A. Condition A is that the company making the relevant distribution has issued share capital and at the time of receipt the person receiving it is a "minority shareholder" as defined in section 397C of ITTOIA.

8. New section 397AA(3) makes provision for Condition B. Condition B is that the company making the relevant distribution is an offshore fund subject to section 378A of ITTOIA which makes provision for offshore funds which are substantially invested in interest-bearing assets. Individuals receiving distributions from such funds will be treated as having received interest.

9. New section 397AA(4) makes provision for Condition C. Condition C is that the company making the relevant distribution is solely a resident of a "qualifying territory" at the time of receipt. If the relevant distribution is one of a series of distributions made as part of a scheme, Condition C is met if each company in the chain of transactions is resident in a "qualifying territory" at the time of receipt, or the scheme is not a tax advantage scheme. A "tax advantage scheme" is a scheme whose only purpose (or purposes) is to obtain the dividend tax credit and/or some other tax relief on a distribution.

10. Paragraphs 4(2) and (3) make a consequential and a drafting amendment to subsection 397B(2) and (3). "The original dividend" is the real dividend of which the manufactured dividend is representative.

11. Paragraph 4(4) inserts new subsection 397B(3A) which provides that where a person receives a manufactured overseas dividend which is representative of an overseas dividend, the references in new section 397AA to "relevant distribution" and "the company that makes the relevant distribution" are to the original dividend, and the company making it, respectively.

12. Paragraph 4(5) makes a drafting amendment to section 397B(4).

13. Paragraph 5 inserts new section 397BA (meaning of "qualifying territory").

14. New sections 397BA(1) and (2) define a "qualifying territory" as the United Kingdom and any territory which has a Double Taxation Agreement with the UK that contains a "non-discrimination provision".

15. New section 397BA(3) gives HM Treasury the power to make regulations varying the list of qualifying territories.

16. New section 397BA(4) defines "resident" for the purposes of new section 397 AA. A company is a "resident" of a territory if, under its laws, it is liable to tax there by virtue of domicile, residence or management but not only in respect of its income from sources in that territory or capital located there.

17. New section 397BA(5) defines "non-discrimination provision". A "non-discrimination provision" is a provision whereby nationals of a contracting state are not subject to taxation, or any requirement connected with it, that is more burdensome than the nationals of the other contracting state in the same circumstances are subject to.

18. New section 397BA(6) defines "national" in the context of a non-discrimination provision. "National" includes an individual with nationality or citizenship, or a legal person, partnership or association under the laws of the contracting state.

19. New section 397BA(8) provides that regulations under this section shall be subject to the affirmative resolution procedure.

20. Paragraph 6(3) inserts new section 397C(1A) which provides that where a company has more than one class of share, the reference to issued share capital in the definition of "minority shareholder" is to issued share capital of the same class as the share in respect of which the distribution is made. Paragraph 6(4) inserts new subsection (8), which provides that shares are treated as being of a different class if the amounts paid up on them are different (other than by way of share premium).

21. Paragraph 7 makes a consequential amendment to section 398(1) (increase in amount or value of dividends where tax credit available).

22. Paragraph 8 inserts new section 873(4) which disapplies section 873(2) of ITTOIA (orders and regulations made under that Act subject to the negative procedure), in cases where any other Parliamentary procedure is expressly provided for.

23. Paragraph 9 makes provision for consequential amendments to the Taxes Management Act 1970.

24. Paragraph 10 makes provision for consequential amendments to the Income and Corporation Taxes Act 1988.

25. Paragraph 11 makes provision for a consequential amendment to section 171 (2B) of the Finance Act 1993 (Lloyd's underwriters etc: taxation of profits and allowance of losses).

26. Paragraph 12 makes provision for a consequential amendment to the definition of "tax credit" in Schedule 1 to the Income Tax (Earnings and Pensions) Act 2003.

27. Paragraph 13 makes provision for consequential amendments to the Income Tax Act 2007.

BACKGROUND NOTE

28. Dividends received by individual shareholders are taxed at rates of 10 per cent and 32.5 per cent for basic rate and higher rate taxpayers respectively in 2009-10.

29. When dividends from UK resident companies are charged to tax, shareholders are entitled to a non-payable tax credit of one ninth of the distribution under the provisions of section 397(1) of ITTOIA. Because tax is charged on the gross dividend received, including the tax credit, this lowers the effective rate of tax on these dividends at the personal level to 0 per cent for basic rate taxpayers and 25 per cent for higher rate taxpayers. By contrast, until recently, there has been no tax credit available to shareholders in non-UK resident companies.

30. Finance Act 2008 introduced the first stage in a two-part reform of the system of taxing foreign personal dividends. The non-payable tax credit was extended to individuals in receipt of dividends from non-UK resident companies, subject to conditions. From 6 April 2008, a person qualified for the tax credit if they own less than a 10 per cent shareholding in the distributing non-UK resident company and the company was not an offshore fund.

31. Budget 2008 announced legislation in the Finance Bill to deal with the situation of individuals who own 10 per cent or more of the shares in a non-UK resident company. This legislation delivers that announcement.

SECTION 41 SCHEDULE 20: LOAN RELATIONSHIPS INVOLVING CONNECTED PARTIES

SUMMARY

1. Section 41 and Schedule 20 amend the corporation tax rules on loan relationships that apply to connected parties. In certain circumstances, these rules restrict the tax deduction for interest or discount payable on a loan or security, until the interest is paid or the security is redeemed. Under the amended rules, where the connected party to which the interest or discount is payable is a company, such a restriction will be made only where the company is located in a "non-qualifying territory". The change applies for accounting periods beginning on or after 1 April 2009.

DETAILS OF THE SCHEDULE

2. Paragraph 2 amends section 374 of the Corporation Tax Act 2009 (CTA). This section applies where interest payable between companies that are "connected" (as defined in the loan relationships rules) is paid more than 12 months after the end of the accounting period in which it accrues, and the creditor company is not taxable under the loan relationships rules. In such cases, the interest is allowable for tax purposes only when it is paid. Paragraph 2 amends this rule by inserting new subsection (1A) and new subsection (3) in section 374.

3. New subsection (1A) sets out a new condition for section 374 of CTA to apply. This condition is that the creditor company must be resident for tax purposes in a "non-qualifying territory" or effectively managed in a "non-taxing non-qualifying territory" when the interest accrues.

4. New subsection (3) defines terms used in new subsection (1A). "Resident" for these purposes means liable to tax in a territory by reason of domicile, residence or place of management. "Non-qualifying territory" means a territory with which the UK does not have a double taxation agreement, or where there is such an agreement, it does not contain a non-discrimination provision. A "non-taxing non-qualifying territory" means one that does not impose tax by reason of domicile, residence or place of management. The territories to which these definitions apply are, broadly, tax havens.

5. Paragraph 3 amends section 375 of CTA. These sections apply where interest payable on loans made to close companies by participators in those companies is paid more than 12 months after the end of the accounting period in which it accrues, and the creditor is a company that is not taxable under the loan relationships rules. In such cases, the interest is allowable for tax purposes only when it is paid. Paragraph 3 amends this rule by inserting new subsection (4A) in section 375. The amendment does not affect the tax treatment of interest paid to a participator who is not a company, for example an individual shareholder.

6. New subsection (4A) sets out a new condition, the "non-qualifying territory condition" (similar to that in new subsection (1A) in section 374 of CTA) for section 375 to apply.

7. Paragraph 4 amends section 376 of CTA which provides interpretation of section 375 of CTA. It inserts definitions of "resident" and "non-taxing non-qualifying territory" for the purposes of section 375 of CTA which correspond to the definitions that apply for the purposes of new subsection (1A) in section 374 of CTA. Because these definitions apply to the whole of section 375 of CTA, the new definition of "resident" will also apply to subsections (3) and (4) of section 375 of CTA. These subsections deal with exemptions from the section 375 rule where the debt is owed to certain close companies or limited partnerships.

8. Paragraph 5 amends section 377 of CTA. This section applies where interest payable on loans made between companies having a "major interest" (as defined in the loan relationships rules) in each other is paid more than 12 months after the end of the accounting period in which it accrues, and the creditor company is not taxable under the loan relationships rules. In such cases, the interest is allowable for tax purposes only when it is paid. Paragraph 5 amends this rule by inserting new subsection (2) in section 377, which sets out a new condition (similar to that in new subsection 1A in section 374 of CTA) for section 377 of CTA to apply. The definitions of the terms used in this condition similarly correspond to those in new subsection (3) in section 374 of CTA.

9. Paragraph 6 amends section 407 of CTA. This section applies where a discount accrues on deeply discounted securities issued between companies that are "connected" (as defined in the loan relationships rules) and the creditor company is not taxable within the loan relationships rules. In such cases, the discount is allowable for tax purposes only when the security is redeemed. Paragraph 6 amends this rule by inserting new subsection (1A) in section 407 of CTA, which sets out a new condition (similar to that in new subsection 1A in section 374 of CTA) for section 407 of CTA to apply. The definitions of the terms used in this condition similarly correspond to those in new subsection (3) in section 374 of CTA.

10. Paragraph 7 amends sections 409 of CTA. This section applies where a discount accrues on deeply discounted securities issued by a company to a close company participator, and the creditor is a company that is not taxable within the loan relationships rules. In such cases, the discount is allowable for tax purposes only when the security is redeemed. Paragraph 7 provides that this rule applies only where the "non-qualifying territory condition" is met.

11. Paragraph 8 amends section 410 of CTA by inserting new subsection (4A) which sets out the "non-qualifying territory condition". This condition, and its associated definitions, mirror those in new subsections (1A) and (3) in section 374 of CTA.

12. Paragraph 9 sets out the commencement and transitional provisions for the amendments made by the Schedule. The changes have effect for accounting periods beginning on or after 1 April 2009. However, a company may elect, in its corporation tax return for the first accounting period beginning on or after that date, for the amendments not to have effect for that period. Where it does so, the current rules will apply instead. No election may be made for an accounting period ending after 31 March 2011.

BACKGROUND NOTE

13. Under the corporation tax rules on "loan relationships", interest, discount and other profits, gains, losses and expenses arising on loans and similar financial instruments are normally taxed and relieved in accordance with amounts recognised in accounts drawn up under generally accepted accounting practice (an "accruals basis"). However, this principle is modified in a number of circumstances where there are transactions between connected parties. These circumstances include cases involving late payments of interest and discounts, in order to prevent manipulation which might result in a deduction for such interest or discount by a debtor company, where no corresponding amounts are taxed as a receipt of the creditor company.

14. The current rules operate by allowing a tax deduction for late interest and discounts in certain cases where the parties are connected and the creditor is taxable outside the loan relationships rules, only when the interest is paid or when the deeply discounted security is redeemed (a "paid basis").

15. Recent decisions of the European Court of Justice have raised the question of whether the legislation as it currently stands is compatible with European law. HMRC issued a consultation document in July 2008 in which options for changes to the rules were presented. The changes set out in the Schedule are based on responses to the consultation. The effect of the changes is that where the connected creditor is a company, the "paid basis" will apply only if that company is resident or effectively managed in a "non-qualifying territory", which broadly means a tax haven. In all other cases where the connected creditor is a company, the normal loan relationships "accruals basis" will apply.

SECTION 42: RELEASE OF TRADE ETC DEBTS

SUMMARY

1. Section 42 amends the legislation in Corporation Tax Act 2009 (CTA) on the loan relationships of companies. It ensures that where a company is released from a debt that it has incurred in the course of a trade or property business, the debt release is taxed under the rules for loan relationships rather than those for trading or property income. This means that if the debtor company is connected with the creditor (for example, if they are two companies in the same group), no tax charge arises on the debtor and there is no tax relief for the creditor. The change applies to debt releases occurring on or after 22 April 2009.

DETAILS OF THE SECTION

2. Subsections (2) and (3) move the definition of a "release debit" from Chapter 6 of Part 5 of CTA (which deals with releases of debts between connected companies) to section 476 of CTA, which contains definitions that apply for the purposes of the loan relationships rules generally. This is necessary because the term is being applied more widely – it now also applies to debts that are taxed in the same way as loans.

3. Where a creditor company agrees to release a debtor from its liability to repay a loan or debt, the accounts of the creditor company will show a loss (if the company has not already written off the debt as bad). This loss is referred to as a "release debit".

4. Subsection (4) introduces the main elements of the section. The new provision amends the rules on "relevant non-lending relationships" in Chapter 2 of Part 6 of CTA. A "relevant non-lending relationship" is a money debt that does not arise from the lending of money – trade debts are the most common example. Chapter 2 of Part 6 provides for the loan relationships rules (found in Part 5 of CTA) to apply to such debts in defined circumstances and to a defined extent: section 479 of CTA sets out the circumstances, and section 481 the extent.

5. Subsections (5) and (6) do two things. First, subsection (5) amends section 479(2)(c), which deals with the position of the **creditor** company. Section 479(2)(c) applies the loan relationships rules to an "impairment loss" on a money debt – where the creditor writes down a bad or doubtful debt. This means that the creditor does not get tax relief if it is connected with the debtor company. (Two companies are connected if one controls the other, or they are under common control.) The amendment puts it beyond doubt that section 479(2)(c) applies where a debt is released, as well as to an impairment loss.

6. Subsection (5) then adds a new circumstance in which the loan relationships rules will be applied to money debts. This is where a company is released from a debt in respect of which a "relevant deduction" has been allowed for tax purposes – in other words, it covers the position of the **debtor** company.

7. Subsections (8) to (11) amend section 481 of CTA, which sets out how the loan relationships rules apply to "relevant non-lending relationships". In general, all the computational rules (including those relevant to connected companies) will apply, but only in relation to matters specified in section 481(3).

8. Subsection (9) therefore makes amendments to section 481(3) corresponding to those already made to section 479. It makes it clear that, for the creditor, the loan relationships rules apply to a "release debit" as well as to an impairment loss; and it adds a new paragraph which applies those rules to the company that has been released from the debt, provided it has previously had a "relevant deduction".

9. Subsection (11) applies the definition of "relevant deduction" to section 481.

10. Subsection (12) is the commencement provision: the amendments will apply to all debt releases that take place on or after 22 April 2009.

BACKGROUND NOTE

11. The purpose of this section is to correct an anomaly that resulted when impairment losses on trade (or property business) debts were brought within the loan relationships rules by Finance Act 2005. If a trade debt is released by a creditor that is connected with the debtor company, the creditor is denied tax relief under the loan relationships rules. The debtor, however, is still charged to tax under section 94 of CTA – part of the rules on taxation of trade and property income – unless the release is part of a statutory insolvency arrangement.

12. Representations made to the Government indicated that this mismatch was inhibiting group reorganisations being carried out, for example, as part of a merger or acquisition. Groups commonly plan to avoid the tax charge, but at the expense of increased administrative burden and costs.

13. The amendment works by applying the loan relationships rules to the debtor as well as to the creditor. In almost every case this has no effect where the two companies are not connected – in particular, the loan relationships rules continue to give relief to the debtor where the release is part of a statutory insolvency arrangement. But, where the parties are connected, the debtor's "profit" is not taxed, making the transaction neutral in tax terms.

14. The one change affecting debt releases between **unconnected** companies is that, where the debtor is carrying on a UK property business, the profit will now be brought into account as a non-trading loan relationships credit, rather than as property income. This would affect the company's ability to set off surplus property expenses, so that in a very small number of cases the company may be disadvantaged.

SECTION 43 SCHEDULE 21: FOREIGN EXCHANGE: ANTI-AVOIDANCE

SUMMARY

1. Section 43 and Schedule 21 counter avoidance schemes which exploit provisions allowing foreign exchange gains or losses to be disregarded for corporation tax purposes where they arise on loans or currency derivatives that hedge foreign currency risk from a company's investment in foreign business operations. They revoke earlier anti-avoidance provisions in secondary legislation. The changes have effect from 22 April 2009.

DETAILS OF THE SCHEDULE

2. Paragraph 2 contains the main operative provision for loan relationships. Section 328(3) and (4) of CTA 2009 provide that foreign exchange gains or losses arising on a company's loan relationships are left out of account in certain circumstances. In particular, this caters for net investment hedging by a company – where a company, which is exposed to currency risk because it has invested in a foreign operation, such as an overseas subsidiary, borrows in the same currency to hedge that risk. Exchange gains or losses on the borrowing offset the exchange losses or gains arising on the investment.

3. For tax purposes, however, a mismatch occurs because exchange differences on the borrowing are taxable, but those arising on a shareholding are not. Section 328(3) allows exchange gains and losses on a loan relationship, to the extent that the loan is "matched" with shares, to be disregarded for tax purposes where under the accounting policies adopted by the company such exchange differences are taken to reserves. Section 328(4) provides a regulation-making power: this has been used to make similar provision for cases where borrowing is intended as a hedge of currency risk arising from investment in a foreign operation, but where a different accounting treatment is employed.

4. Since exchange rate movements are unpredictable, these "forex matching" provisions are normally just as likely to result in a loss being excluded from tax as a gain. But some avoidance arrangements do away with this unpredictability and use forex matching to procure that exchange gains within a group of companies are sheltered from tax, whereas losses are not. Paragraph 2 inserts a new subsection (4A) into section 328, to provide that that the disregard of exchange gains or losses under section 328(3) or (4) does not apply where the loan relationship on which they arise is part of arrangements that have such a "one-way exchange effect". It follows that if a company is party to arrangements that do not involve any disregard of exchange gains or losses under section 328(3) or (4), it will not have to consider the application of the one-way exchange effect provisions.

5. New subsection (4A)(c) further restricts the operation of the rule by requiring that the arrangements must result in a non-negligible tax advantage for either the taxpayer company or some other company. This guards against the possibility of companies that are not engaged in avoidance being caught by the legislation because, for whatever reason, their hedging arrangements produce a very small "one-way exchange effect". It would also exclude any company whose foreign exchange arrangements operate in an asymmetric manner, but which pays more tax as a result. "Tax advantage" is defined for the purposes of the loan relationships legislation at section 476(1) of CTA 2009. It has a wide meaning that takes in both a decrease in taxable receipts or an increase in allowable deductions.

6. Paragraph 3 inserts new sections 328A to 328H. These set out what is meant by a "one-way exchange effect".

7. New section 328A contains the test for determining whether arrangements have a one-way exchange effect. "Arrangements" are given a wide definition in new section 328H(3).

8. New section 328A(1) provides for there to be a one-way exchange effect if two conditions are fulfilled. The first, in new section 328A(2), excludes arrangements from consideration if they do not include an option or a relevant contingent contract (both of these terms are explained later in the legislation). This means that most commercial hedges of investment in a foreign operation, involving only "plain vanilla" loans, cross-currency swaps or forward currency contracts, will not need to be tested for a "one-way exchange effect".

9. The second condition, in new section 328A(3), provides for a test to be carried out on each of a number of defined "test days" in an accounting period of a company. If the condition is satisfied on any one of those test days, there is a one-way exchange effect. In broad terms the test consists of a comparison between the net allowable exchange losses arising on arrangement instruments ("amount A"), and the taxable gains that would have arisen had the foreign currency involved moved the other way ("amount B"). For the condition to be satisfied, amounts A and B must be unequal.

10. New section 328A(3)(b), however, further requires that the same inequality would not be produced if the rules for forex matching did not exist. (New section 328A(7) explains what is meant by "the matching rules"). This excludes from the anti-avoidance provision those cases where forex matching is not integral to the production of a one-way exchange effect. For example, a group finance company may borrow from a bank, and on-lend the funds to a "water's edge" company that holds shares in an overseas subsidiary. The holding company will not be taxed on exchange differences arising on the internal loan, because it is "matched" to the shares. The finance company might, however, enter into option arrangements designed to limit its losses if the currency of the bank loan appreciates substantially. The option arrangements may produce asymmetry between exchange gains and losses, but this is unrelated to the "forex matching" by the holding company. These arrangements would not be caught by the legislation.

11. New section 328A(4) defines "amount A". It is the sum of "relevant" exchange losses that arise to company A, and companies connected with company A, in accounting periods of the company ending on the test day, less the sum of "relevant" exchange gains arising to those companies in the same accounting periods. Amount A may be negative if the company has more exchange gains than losses.

12. New section 328A(5) contains the definition of "amount B". This introduces the idea of the "counterfactual currency movement assumption". The company must look at what exchange gains and losses would have arisen had the exchange rate in question moved by the same amount in the other direction. Amount B is the sum of "relevant" exchange gains of company A and of companies connected with it, arising – on the basis of this hypothesis - in accounting periods ending on the test day, less the sum of exchange losses computed on the same basis. As with amount A, it may be positive or negative. Amounts A and B will be equal if, for example, they are either both +100 or both -100.

13. New section 328A(6) deals with the case where the "test day" is a day other than the last day of a company's accounting period. For the purposes of arriving at the exchange gains or losses involved in computing amounts A and B, the period is treated as ending on that day. For example, suppose that a company has an accounting period 1 January 2010 to 31 December 2010, but in respect of particular arrangements, 1 September 2010 is a test day. If the company is party to a loan relationship (which is part of the arrangements) both before and after 1 September, it must look at the exchange gain or loss arising on the loan relationship in the period 1 January to 1 September, as if it had drawn up a balance sheet on 1 September.

14. New section 328B sets out when an exchange gain or loss is "relevant" and hence must be included in the computation of amounts A and B. Three conditions must be satisfied. First, it must arise on a loan relationship or a relevant contract (see paragraph 17 below). Second, that loan relationship or relevant contract must be part of the arrangements. Finally, a debit or credit has to be brought into account for CT purposes in respect of the exchange gain or loss – so, in particular, where exchange differences are disregarded because of the "forex matching" rules, they will not enter into the computation. But, in ascertaining whether a debit or credit would be brought into account, the "one-way exchange effect" provisions themselves are ignored (to avoid circularity), as is the effect of the "unallowable purpose" anti-avoidance rules (since these may of themselves create asymmetries).

15. New section 328H(11) applies certain terms from the derivative contracts rules (Part 7 CTA 2009). Thus "relevant contract" in section 328B means an option, a future or a swap. It also includes derivatives that are embedded in other financial instruments or non-financial contracts.

16. New section 328C defines "test day". The avoidance arrangements targeted by these provisions must involve either options, or arrangements having the effect of options (referred to as "relevant contingent contracts"). Such instruments allow one thing to happen in the case of a certain contingency – commonly, the contingency that sterling strengthens (or weakens) against a particular foreign currency – but something else to happen if it does not.

17. Subsection (2) deals with the case where the arrangements involve one or more options. If an option is actually exercised, the day on which the option is exercised is a test day; and the same applies where the company sells or novates the option, or its terms are changed. If it is not exercised in the accounting period, each day on which it might have been exercised is a test day. Finally – to cover cases where a one-way exchange might be produced through changes in fair value, even if it cannot be exercised in the period – the last day of the accounting period is a test day. In practice, it will usually only be necessary to consider one of the possible test days.

18. Subsection (3) of new section 328C makes similar provision where the arrangements include one or more relevant contingent contracts.

19. New section 328D sets out the assumptions that need to be made when applying the counterfactual currency movement hypothesis. It operates with respect to the "relevant foreign currency", which is defined in subsection (6) as the currency in which the loan relationships or derivative contracts, on which the exchange gains or losses arise, are denominated. Arrangements may involve more than one foreign currency. For example, an arrangement may include one loan in US dollars and another loan in euros; or the companies involved in an arrangement may have different functional currencies, so that sterling (for example) may be a "foreign currency" for one company but not another. In such cases, each currency involved that gives rise to exchange differences is a "relevant foreign currency".

20. If the relevant foreign currency appreciates over the accounting period (or deemed accounting period up to the test day) against the operating currency of the company, it must be assumed that the currency had instead depreciated by the same percentage – subsection (2). Similarly, if the currency depreciated by a particular percentage against the operating currency, it must be assumed that it had instead appreciated by the same amount – subsection (3). The same applies if the currency appreciates or depreciates over any part of the period. Suppose, for example, the test is being applied over a period 1 January to 30 June, but the company repaid a foreign currency loan on 31 March. The foreign currency appreciated by 10% in the period 1 January to 31 March, and an exchange loss on repayment of the loan. In applying the counterfactual hypothesis, the company must compute what exchange gain would have arisen on repayment of the loan had the currency depreciated by 10% over the same period.

21. Subsections (4) and (5) provide that except in relation to the treatment of options to which section 328E applies, the counterfactual computation must be made on the basis of what the company has actually done. Thus in the example above, the counterfactual calculation must assume the same loan repayment on 31 March – the company does not need to consider whether, had the exchange rate moved in the opposite direction, it would have done something different.

22. Subsection (7) defines the "operating currency". This is tied to provisions in the 1993 Finance Act for foreign currency accounting – it is the currency in which the company prepares its tax computations. Where, under the tax provisions for loan relationships and derivatives held by a partnership, a company is deemed to be party to a loan relationship or a relevant contract, the "operating currency" in relation to such loans or relevant contracts is the partnership's "operating currency".

23. New section 328E deals with the application of the counterfactual hypothesis where an option is part of the arrangements. Two cases are covered: where the option was exercised on the test day, and where it was not (but was, in fact, exercisable on that day). Where the options was exercised, subsection (4) provides that the calculation should be made in on the basis that it was not exercised if, in all the circumstances, it is more likely than not that the company would have refrained from exercising it under the "counterfactual currency movement assumption". Subsection (5) similarly covers the case where the option was not exercised. If it is more likely than not that the company would have exercised the option had the exchange rate moved the other way, the computation is made on the basis that the option was exercised.

24. New section 328F extends the meaning of "option" for the purposes of applying section 328E and other parts of the one-way exchange effect provisions. For the purposes of the derivative contracts provisions, an option that can only be cash settled is not an "option" (it is a contract for differences). Subsection (1) disapplies this rule. Subsection 2 extends the scope of the provisions that treat derivatives embedded in loan relationships, "hybrid derivatives" or other contracts as separate relevant contracts. These rules only apply where, under Generally Accepted Accounting Practice (GAAP), the embedded derivative is not closely related to the host contract and is accounted for separately. For the purposes of the one-way exchange effect provisions, a financial instrument or other contract contains an option if it contains provisions which could, if they stood alone, be regarded as an option. It does not matter whether the company does, or could, account separately for the option element.

25. New section 328G deals with contracts whose effects are contingent on currency movements, but which are not options (because the holder has no choice over whether a particular provision is triggered). These are referred to as "relevant contingent contracts". In order to be a relevant contingent contract, a contract must contain an "operative condition". This is a condition which alters any right or liability under the contract, contingent on the exchange rate between the relevant foreign currency and the operating currency of the company – subsection (3). The "trigger" may relate directly to an exchange rate, or indirectly – for example, it may relate to an asset whose value is closely tied to an exchange rate.

26. New section 328H contains interpretative provisions. In particular:

27. Subsection (4) provides that, when deciding whether a loan relationship or relevant contract is part of any arrangements, regard must be had in particular to the circumstances in which the company became party to it, its currency, and its likely effect.

28. Subsection (5) defines the currency in which a relevant contract is denominated as the currency of its underlying subject matter.

29. Subsections (6) and (7) make clear what is meant by one currency ("currency A") appreciating or depreciating relative to another currency ("currency B"). Thus suppose currency A is US dollars and currency B is sterling, and $1 is worth £0.60 at the beginning of a period and £0.65 at the end, the US dollar will have appreciated against sterling (0.65 – 0.60)/0.60 x 100% = 8.33%.

30. Subsections (9) and (10) apply the loan relationships definition of "connection" to these provisions. Two companies are connected for an accounting period if, at any time in the period, one company controls the other or they are under common control. Exclusions that apply for loan relationships purposes – for example, two companies that are both under the control of a Government department or Minister of the Crown are not connected – apply here as well.

31. Paragraphs 4 to 6 amend the derivative contracts rules in Part 7 of CTA 2009. For the most part, these changes are analogous to these made for loan relationships. There are, however, some differences.

32. Paragraph 6 amends section 606 CTA 2009, which deals with exchange gains and losses on derivative contracts. The existing section 606(3) disregards exchange gains or losses, which are taken to reserves in the company's accounts, in two circumstances. The first is where the derivative is a currency derivative. This covers the case where a currency swap or forward contract is used to hedge currency risk arising from the company's investment in a foreign operation. The second is where the exchange difference arises from retranslation of the profits of part of a company's business.

33. Subparagraph (4) of paragraph 6 rewrites these cases as two separate conditions. The second case is reproduced in a new section 606(4B). The first case – the "forex matching" case – is in new subsection (4A). But new subsections (4C) and (4D) apply a restriction where the exchange gain or loss is **not** calculated by reference to spot rates of exchange. In such a case, the overall exchange difference is to be treated for the purposes of the derivative contracts computational rules as if it consisted of two elements – an exchange gain or loss calculated by reference to spot rates, and a residual amount. The first element can be matched, the second cannot.

34. This means that where the profit or loss computed on a forward currency contract includes "forward points" – a profit or loss dependent only on interest rates for the currencies concerned, and independent of movements in foreign exchange rates – it is only the "forex" element of the profit or loss and not the forward points that is eligible for matching. This change counters avoidance schemes involving a predictable profit from "forward points" on a currency contract that is eliminated through forex matching, while the corresponding loss arising to the counterparty is utilised for tax. .

35. The residual amount is described by the legislation as an "exchange gain or loss", even though it would not be regarded as such in accountancy terms. This is so that other references in the derivative contracts provisions to exchange gains and losses continue to apply to both elements of the overall amount.

36. A new subsection (4E) makes provision corresponding to that for loan relationships. Exchange gains cannot be matched, either under section 606(3) or through regulations made under section 606(4) where the exchange gain or loss arises from a one-way exchange effect, and they bestow a non-negligible tax advantage.

37. Paragraph 7 inserts new sections 606A to 606H. These function in almost exactly the same way as the corresponding loan relationships provisions. The main difference is in the interpretative provisions, since many of the expressions used (such as "relevant contract") are already defined for the purposes of Part 7.

38. Paragraphs 8 and 9 insert references to the Part 5 and Part 7 one-way exchange effect provisions into the index of defined expressions in CTA 2009.

39. Paragraph 10 revokes SI 2006/843 – The Loan Relationships and Derivative Contracts (Disregard and Bringing into Account of Profits and Losses) Regulations – in its entirety. This statutory instrument disallows losses in certain arrangements that have a "one-way exchange effect", but is rendered otiose by the new primary legislation. It ceases to operate on 22 April 2009, when the primary legislation comes into effect, thus removing any possibility of double taxation.

40. Paragraph 11 is the commencement provision. The new rules apply to accounting periods beginning on or after 22 April 2009. Where a company's accounting period straddles 22 April 2009, exchange gains or losses are to be computed as though there were two separate accounting periods, one ending immediately before 22 April and the next one beginning on that date. The amendments will apply to the second of those notional accounting periods, but not the first.

BACKGROUND NOTE

41. Hedging the exchange risk that arises from investment in "foreign operations", such as overseas subsidiaries, is an important commercial activity for many large groups of companies. The UK first introduced tax rules dealing with net investment hedging in 1993, and subsequently the Government has worked with industry and the professions to remove tax obstacles that might otherwise limit the effectiveness of such hedging. In particular, secondary legislation was introduced in 2004, and has subsequently been developed, to cater for the introduction of International Financial Reporting Standards (IFRS), and new UK accounting standards aligned with IFRS.

42. The "forex matching" rules operate by disregarding exchange gains or losses that arise on financial instruments used to hedge shareholdings in overseas subsidiaries. The disregarded amounts may be brought back into account, as a capital gain or loss, on disposal of the shares, but only where the disposal does not qualify for Substantial Shareholdings Exemption.

43. These rules are intended to operate even-handedly, in other words it is equally probable that a gain or a loss may be left out of account. In a minority of case, however, the rules have been abused. Typically, these avoidance arrangements have no effect on the foreign exchange differences reported in the consolidated accounts of a group. However, the effect on the UK taxable profits is that, where a currency moves in one direction, an exchange loss is brought into account, whereas if the currency moves the other way, there is no corresponding gain brought in for tax. Schemes generally rely on sheltering an exchange gain through matching, while an exchange loss appears in another group company and is claimed for tax.

44. Regulations introduced in 2006 targeted two particular schemes. Subsequently, however, other schemes have been developed that circumvent this legislation. This measure therefore revokes the 2006 Regulations and instead introduces an anti-avoidance rule designed to counteract "one-way exchange effect schemes" more generally, while having minimal impact on the majority of groups that do not use such schemes.

SECTION 44 SCHEDULE 22: TAX TREATMENT OF PARTICIPANTS IN OFFSHORE FUNDS

SUMMARY

1. Section 44 and Schedule 22 provide for a new definition of an "offshore fund" to be used in tax legislation and, in particular, in regulations to be made under section 41 of the Finance Act (FA) 2008. The Schedule also provides for interests in certain "offshore funds" within the new definition to be treated as assets of the investors for the purposes of tax on capital gains (with the consequence that the underlying assets will no longer be treated as assets of the investors).

DETAILS OF THE SCHEDULE

2. Part 1 of the new Schedule provides a new definition of an "offshore fund" and amends the powers set out in FA 2008 to provide in regulations for the tax treatment of participants in offshore funds. In the new Schedule, paragraph 2 inserts sections 40A to 40G into FA 2008.

3. Section 40A of FA 2008 establishes the meaning of "offshore fund". Subsection (1) provides that sections 40A to 40G apply for "this group of sections", that is sections 40A to 42A of FA 2008. Subsection (2) sets out the main definition of the expression "offshore fund"; but it should be noted that this definition is in turn dependent on a definition of the term "mutual fund" – to be found in section 40B. Section 40A(2) limits the meaning of offshore fund to those mutual funds which take one of three forms and which are resident in, or based in, a territory outside the United Kingdom.

4. Paragraph (a) of subsection (2) does not include a limited liability partnership – see subsection (6).

5. Paragraph (b) of subsection (2) includes all mutual funds that are unit trust schemes.

6. Paragraph (c) of subsection (2) does not include a partnership (subsection (3)).

7. "***Co-ownership***" is explained in subsection (6) and is stated not to be restricted to the meaning of that term in the law of any part of the United Kingdom. It takes its meaning from the law of the territory in which the arrangements take effect.

8. Subsection (5) defines what is meant by ***participants*** in arrangements or a fund. This makes clear that it does not matter whether or not the participant has an interest amounting to ownership in the property that is the subject of the arrangements.

9. Section 40B defines the expression "mutual fund" using three conditions, all of which must be met.

10. Condition A in section 40B (subsection (2)) is self-explanatory.

11. Condition B in section 40B (subsection (3)) is that the participants do not have day-to-day control of the property; and subsection (4) explains that having a right to be consulted or to give directions does not itself constitute day-to-day control.

12. Condition C in section 40B (subsection (5)) requires that an investor in the arrangements, as participant, would expect to be able to realise the investment on a basis calculated entirely, or almost entirely, by reference to net asset value ("NAV") or by reference to an index of any description.

13. Condition C must be read in conjunction with section 40E(1), which restricts the ambit of section 40B. An investor in a company would normally only reasonably expect to be able to realise NAV on the liquidation of the company. So section 40E(1)(a) excludes from section 40B any case where a reasonable investor would only be able to realise the investment in the arrangements in the event of a winding-up, dissolution or termination of the arrangements, except in the case where section 40E(1)(b) applies – see paragraphs 16 to 24 below.

14. Section 40C defines "umbrella arrangements" and how they are to be treated for the purpose of the offshore funds definition. Subsection (1) provides that where there are such arrangements, each separate part (usually known as a 'sub-fund') is to be treated as a separate arrangement and the overall arrangements are disregarded. In such a case the overall arrangements do not themselves constitute a mutual fund or an offshore fund.

15. Section 40D deals with a case where there is more than one class of interest in any arrangements. It has the effect that each class of interest is looked at separately for the purpose of determining whether the arrangements constitute a mutual fund, and the main arrangements are disregarded.

16. Section 40E contains the exceptions to the definition of a mutual fund. The effect of subsection (1) is that arrangements are not a mutual fund if the only occasion on which a reasonable investor would expect to be able to realise NAV is winding-up, dissolution or termination of the arrangements, but this is subject to condition X or condition Y being met.

17. Subsection (2) contains Condition X which requires that the arrangements are not such that they are designed to terminate at a fixed date. Subsection (8) provides that a future requirement, such as a vote, which may possibly lead to winding up will not, of itself, mean that the arrangements are designed to terminate on a fixed date.

18. Subsection (3) sets out that if Condition X is not met and the arrangements are designed to terminate at a fixed date, then the arrangements will still not be a mutual fund if Condition Y is met. Condition Y will be met if one or more of three sub-conditions is met.

19. Condition Y1 is that the arrangements do not relate to any "relevant income producing assets". This term is explained in Section 40F.

20. Condition Y2 is that the participants in the arrangements have no entitlement to benefit from the income arising on the assets that are the subject of the arrangements.

21. Condition Y3 is that all of the income arising is required to be paid or credited to participants in such a manner that a UK resident individual would be charged to income tax on the amounts paid or credited.

22. Subsection (7) prevents Condition Y from applying in circumstances where the arrangements are designed to produce a return that is, in substance, equivalent to interest – with the consequence that such an arrangement will be a mutual fund and hence an offshore fund.

23. Section 40F(1) explains the meaning of relevant income producing assets. Subsection (2) ensures that assets are outside the meaning where there is no income after taking account of hedging arrangements. Subsection (3) ensures that interest on cash temporarily held whilst awaiting investment will not, of itself, mean that the cash is regarded as a relevant income producing asset provided that the cash and the interest arising is invested in non- income producing assets as soon as reasonably practicable.

24. Section 40G gives HM Treasury powers to vary the exceptions to the offshore funds definition by regulations.

25. Paragraphs 3, 4 and 5 of the Schedule amend the regulatory powers in sections 41 and 42 of FA 2008 and insert a new section 42A of FA 2008 so that the regulations can be made with reference to the definition of an offshore fund provided in this Schedule. Certain of the regulations are subject to the affirmative procedure (those under 40B(6), 40G(1) and the first regulations under section 41(1)). Regulations made under all other sections are subject to the negative procedure.

26. Paragraph 6 of the Schedule limits the regulatory powers provided by section 41 FA 2008 to ensure that where there are investments made before 1 December 2009, not previously within the definition of a 'material interest in an offshore fund' (see section 759 of the Income and Corporation Taxes Act 1988), these investments will not be subject to the new tax regime to be provided in regulations. A similar protection will apply if investments are made after 1 December 2009, where the investor was obliged to make that investment under a contract entered into before 30 April 2009.

27. Part 2 of the new Schedule inserts a new section 103A into the Taxation of Chargeable Gains Act 1992 (TCGA). The purpose of the new section, introduced by paragraph 8 of the Schedule, is to treat investors' rights in offshore funds as assets for the purposes of tax on capital gains where this is not already the case. The new section 103A of TCGA is similar to section 99 of that Act which applies to unit trusts.

28. Paragraph 11 makes consequential amendments to the taxes acts to introduce references to the new section 103A of TCGA.

29. Paragraph 12, with paragraphs 13 and 14, provides that section 103A will apply to all holdings of persons subject to capital gains tax in offshore funds from 1 December 2009 and that it will apply to holdings by persons within the charge to corporation tax from a date to be appointed by Treasury order.

30. Paragraphs 15, 16 and 17 provide for investors in affected funds to have the option of making an election to backdate the effect of the new section. An election can be made for tax years 2003-04 onwards (and for corporation tax for accounting periods starting on or after 1 April 2003). An election is irrevocable and will therefore apply in all subsequent tax years or accounting periods.

31. Paragraph 18 provides a transitional rule to calculate the acquisition cost for TCGA purposes of interests held at 1 December 2009 (or, for corporate investors, the appointed date) or the date from which it is elected to apply the new section 103A of TCGA if that is earlier. The rule means that existing acquisition costs relating to the assets held will be carried forward to count as the acquisition cost of units or rights in the fund.

BACKGROUND

Part 1 of Schedule

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

33. The new definition of an "offshore fund" uses a characteristics based approach which has been the subject of extensive consultation.

Part 2 of the Schedule

34. 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 of those funds.

35. If such a fund comes within the revised definition of an "offshore fund", a new section of TCGA 1992 will apply similar treatment to rights in such funds subject to transitional rules set out in the details above.

36. Partnerships will not be affected as they will be specifically excluded from the definition of offshore funds.

New tax regime to be in regulations

37. In addition to the new definition of "offshore fund", the Government has announced that a new tax regime to be set out in regulations will start from 1 December 2009. Regulations will be made under powers in FA 2008 (as amended by this Schedule) which will apply to offshore funds as defined by this Schedule. Draft regulations have been published and have been the subject of consultation and will be further updated to reflect the new definition. The first set of the regulations will be subject to the affirmative procedure. The affirmative procedure is used for substantial and important portions of delegated legislation on which a high degree of scrutiny is sought.

38. The draft regulations will be updated to provide specific exceptions to ensure that there will be no double taxation where investors' interests in offshore funds are subject to tax as income under other tax provisions.

SECTION 45: POWER TO ENABLE DIVIDENDS OF INVESTMENT TRUSTS TO BE TAXED AS INTEREST

SUMMARY

1. Section 45 provides a power to make regulations that will allow investment trust companies (ITCs) to have the option to treat dividends as distributions of interest, and to provide that such distributions will be treated as interest payments to their shareholders. This will enable investment trust companies to invest in interest bearing assets tax efficiently.

DETAILS OF THE SECTION

2. Subsection (1) permits regulations to be made allowing companies approved as investment trusts under section 842 of the Income and Corporation Taxes Act 1988 (ICTA) or companies having a reasonable belief that they will be approved as investment trusts under that section, to designate a dividend (or part of a dividend) as an interest distribution. Regulations can also be made so that in the hands of the shareholder, the interest distribution is treated as a payment of yearly interest for an individual or as a loan relationship credit for a company.

3. Subsection (2) provides that the regulation making power includes power to make regulations about:

- when a dividend may or may not be treated as an interest distribution;
- the maximum amount of a dividend that may be designated as an interest distribution;
- when income tax is deducted from the interest distributions;
- accounts and record-keeping; and
- information that an investment trust or prospective investment trust will be required to provide to its shareholders or other persons such as HM Revenue & Customs (HMRC). It allows for a penalty to be levied by HMRC up to a maximum amount of £3,000 for the failure to provide information.

4. Subsection (3) further expands the power in subsection (1). In particular, it allows for other enactments to be applied (with or without modifications). It also permits provisions to be made with respect to different types of ITCs or shareholder or sets of circumstances.

5. Subsection (5) provides that any regulations are made by the House of Commons and are subject to the negative resolution procedure.

BACKGROUND NOTE

6. Investment trust companies (ITCs) are pooled, risk-spreading investment vehicles constituted as limited liability companies. They are publicly listed and invest in a diversified portfolio of shares and other securities with the aim of providing a return to their shareholders.

7. There are special rules that define an ITC as an investment trust for tax purposes under section 842 of ICTA, which if met, allow the company to receive an exemption from corporation tax on their chargeable gains.

8. The current tax treatment for investment trusts that invest in interest bearing assets is that such income is chargeable to corporation tax. The section provides for regulations to be introduced that will allow investment trusts or prospective investment trusts to receive a tax deduction for the interest distribution that they make to their shareholders. This will then enable them to invest in interest producing assets tax efficiently.

9. The new tax treatment for investment trusts or prospective investment trusts moves the point of taxation for income received from interest bearing assets from the investment trust to the shareholder, with the result that shareholders face broadly the same tax treatment as they would have faced had they owned the interest bearing asset directly.

SECTION 46 SCHEDULE 23: INSURANCE COMPANIES

SUMMARY

1. Section 46 and Schedule 23 replace existing guidance on the tax treatment of additions made by a life insurance company to its long term insurance fund (LTIF) with a clear statutory framework. Whilst ensuring that additions brought into account in the company's regulatory return are not taxable receipts it also counteracts the tax benefit which can arise when an addition to the LTIF enables a company to realise a Case I loss that does not reflect an economic loss incurred in the company's life assurance business.

2. The section and Schedule also clarify the transitional rules governing relief for repayments of contingent loans taxed under section 83ZA of the Finance Act (FA) 1989, amend the rules governing the calculation of the 'floor' for gross roll up business investment return, to ensure consistent treatment of foreign business assets and amend section 32 of the Taxation of Chargeable Gains Act 1992 (TCGA).

DETAILS OF THE SCHEDULE

Transfers from non technical account not to be receipts

3. Paragraph 1(1) amends section 83 of FA 1989 so that additions of assets by a life insurance company to its LTIF on or after 22 April 2009 which are brought into account in the company's regulatory return are not taxable receipts.

No deduction for capital allocations to with-profits policy holders

4. Paragraph 2(1) amends section 82 of FA 1989 so that amounts allocated to with-profits policyholders which are capital and not funded out of income brought into account in the regulatory return are not allowable deductions in computing Case I profits. It makes it clear that where amounts are allocated to policy holders in respect of amounts payable in connection with the reattribution of inherited estate those amounts are to be treated as being capital.

Limits on loss relief for addition to non-profits funds

5. Paragraph 3(1) inserts into the Income and Corporation Taxes Act 1988 (ICTA) new sections 434AZA, 434AZB and 434AZC.

6. New section 434AZA restricts the Case I loss of the company's life assurance business available to set off against the company's other income of the accounting period or to surrender as group relief when:

- there has been an addition to a non profit fund of the company; and, in that period of account or a subsequent period of account,
- the company has made a book value election in respect of a non-profit fund or funds; and/or

- arrangements have been entered into the purpose or main purpose of which is to reduce the admissible value of the assets of a non-profit fund or funds.

7. New section 434AZB determines the extent to which the Case I loss is to be restricted. The restriction in respect of a period of account is the least of:

   a. the addition or additions to the company's non-profit fund or funds made in that period of account and/or, to the extent that it is attributable to additions made in earlier periods of account, the unappropriated surplus of a non-profit fund or funds carried forward to that period of account;

   b. any amount(s) shown in Line 51 of Form(s) 14 for the company's non-profit fund or funds and/or any reduction in admissible value of assets, other than structural assets attributable to the arrangements; or,

   c. the amount of the loss arising on the company's life assurance business.

8. When a loss arising in a period of account has been restricted there will be a corresponding reduction in the amounts available to restrict losses in subsequent periods of account.

9. New section 434AZC contains supplementary provisions. Subsection (2) applies section 434AZA and 434AZB to a non-profit part of a with-profit fund. The non-profit part of a with-profit fund is that part of the with-profit fund which belongs to the company and in whose profits the with-profits policyholders are not entitled to participate. The subsection ensures that for this purpose it is treated in the same way as a non-profit fund.

Financing-Arrangement-Funded Transfers to Shareholders ("FAFTS") and Contingent Loans

10. Paragraph 4(1) amends Paragraph 4(5) of Schedule 17 to FA 2008 to make it clear that, for the purposes of calculating any relief on a subsequent repayment of an existing loan, transfers to shareholders which take place on or after 1 January 2008 do not need to be taken into account in computing the relief due. This ensures that the tax treatment on repayment of such a loan is effectively the same as it would have been had section 83ZA of FA 1989 continued in force.

Apportionment: Foreign Business Asset

11. Paragraph 5 provides for the references to foreign business assets (which effectively exclude them from the calculations) in subsections 432E(3)(a), (4) and (4A) to be omitted. When the concept of "foreign business assets" was introduced by Paragraph 10 of Schedule 17 to FA 2008 the intention was to allow the apportionment rules in section 432E(3), commonly known as the "floor", to operate without seeking to distinguish the income from foreign business assets, because it would be impracticable to do so. For the purpose of the apportionment it is necessary for the foreign business assets to be removed from both the numerator and denominator of the apportionment fraction. Paragraph 5 does that by removing all remaining references to "foreign business assets" in the relevant subsections.

12. Paragraph 6 makes consequential amendments to Paragraph 19(4) and (6) of Schedule 7 to FA 2007, again omitting references to foreign business assets.

Value Shifting attributable to transfer of business

13. Paragraph 8(1) amends section 32(1) of TCGA to insert a reference to section 211 of TCGA. As a result, a disposal within section 211, the transfer of an insurance business, will be protected from the application of the anti-avoidance rules in section 30, providing the requirements of section 32(2) are met. The amendment is therefore wholly relieving.

14. Subsection 8(2) provides that the amendment in sub-paragraph (1) shall apply to disposals on or after 22 April 2009.

BACKGROUND NOTE

15. Currently the tax treatment of additions made by a company to its long term insurance fund (LTIF) is governed by a combination of case law and an unpublished concession in guidance. A company may add capital to its LTIF for regulatory or commercial reasons but in certain circumstances amounts are added with the intention of obtaining a tax advantage.

16. The impact of the existing case law and concession is uncertain for both HMRC and the industry. The legislation attempts to remove that uncertainty by providing that the default position for such capital additions is that they are not taxable. It then identifies a number of sets of circumstances where such an addition has been made where reliefs shall be restricted. At the same time the opportunity has been taken to apply consistent treatment to the allowance of "capital" bonuses paid to policyholders – whether those bonuses are funded from a non-taxable capital addition or some other untaxed source.

17. The income and gains of a company's life insurance business are taxed as they are brought into account in the company's regulatory return to the Financial Services Authority (FSA). In general terms the measure seeks to restrict relief when tax-deductible expenditure is incurred but this is not matched by the bringing into account of a corresponding amount of taxable income. Circumstances in which this may occur, are set out in the following three examples, which correspond to the restrictions to relief found in new section 434AZA and the new subsection (2A) of section 82 of FA 1989.

Example 1: Book value election

18. FSA rules permit an insurance company to recognise the total value of its LTIF assets at an amount less than their admissible value. The use of a value less than admissible value is known as 'making a book value election'. Recognising assets at less than admissible value defers the bringing of income and gains into account for both tax and regulatory purposes. When a non-taxable addition to the fund is available to frank tax-deductible expenditure and the company chooses to defer the recognition of taxable income and gains by way of a book value election there will be a tax loss which does not reflect a commercial loss of the life insurance business.

Example 2: Manipulation of admissible value

19. FSA rules prescribe that, in certain circumstances, generally to reflect concentration and counterparty risk, the admissible value of a company's assets must be less than market value. The admissible value of the fund's assets can be manipulated by acquiring or creating assets which have little or no admissible value. The fair value of the assets of the fund is unchanged. A non taxable addition to the fund may allow a company to create a tax effective reduction in admissible value whilst maintaining the value of the fund for regulatory purposes. Effectively this creates a tax loss where there is no commercial loss.

Example 3: Capital allocations to with-profits policy holders

20. The ability of a company to defer recognition of income and gains allows it to smooth the profits allocated by way of bonuses to with-profits policy holders. Currently all amounts allocated to with-profits policy holders are allowable deductions in computing the profits of a company's life assurance business whether or not that allocation is made out of recognised income and gains.

21. In certain circumstances payments may be made which do not represent an allocation of profits to policyholders but are instead of a capital nature, e.g. a payment for giving up rights under the policy. Such capital payments will represent an acceleration of the allocation of the profits of the fund to policyholders and providing this is matched by an acceleration in the recognition of profits this is unobjectionable. In some circumstances allocations of a capital nature will not be funded from recognised income and gains but will instead be funded by an addition to the fund.

Financing-Arrangement-Funded Transfers to Shareholders ("FAFTS") and Contingent Loans

22. Paragraph 4 provides clarification of the rules governing FAFTS. FA 2008 introduced new rules to deal with FAFTS relating to non-profit funds. FAFTs are a type of financing arrangement whereby a loan made to, or financial reinsurance arrangement made by, an insurance company can have the effect of accelerating taxable surplus. For contingent loans these rules replaced the provisions of section 83ZA of FA 1989. Paragraph 4 of Schedule 17 provided transitional rules where a contingent loan was in place when the new rules came into effect (that is in relation to accounting periods beginning on or after 1 January 2008).

Apportionment: Foreign Business Asset

23. Paragraphs 5 to 7 provide clarification of the apportionment rules for with-profit funds set out in section 432E of ICTA. This section provides for an apportionment of life insurance company profits. The changes ensure that, where the company has foreign business, adjustments made for "foreign business assets" are made consistently.

Value Shifting attributable to transfer of business

24. The value shifting provisions at sections 29 to 34 of TCGA are anti-avoidance measures applicable to companies generally. Section 32 is concerned with transfers within groups at artificial values. Where such a transaction gives rise to a capital loss the anti avoidance provisions may apply to restrict or eliminate the loss. For companies generally the value shifting rules do not apply if the disposal of the underlying asset is effected within the group for bona fide commercial reasons and does not form part of a scheme or arrangements of which the main purpose, or one of the main purposes, is avoidance of liability to corporation tax

25. This exemption is not currently available to life insurance companies when they transfer business within their group. They can therefore be exposed to the effect of the anti avoidance provision, even if the transaction is commercial and has no tax avoidance motive. Paragraph 8 extends the protection currently given to other companies to Life companies involved in a commercial transfer of business, providing the relevant conditions are met.

SECTION 47: EQUALISATION RESERVES FOR LLOYD'S CORPORATE AND PARTNERSHIP MEMBERS

SUMMARY

1. Section 47 provides a Treasury power to make regulations which will have the effect of allowing corporate and partnership members of the Lloyd's insurance market to claim tax relief on establishing reserves equivalent to those made by general insurance companies under the equalisation reserves rules made by the Financial Services Authority (FSA). These rules recognise the volatility of certain classes of general insurance business and the possibility of large, but intermittent, losses.

DETAILS OF THE SECTION

2. Subsection (1) contains the power to make regulations applying the provisions of section 444BA of the Income and Corporation Taxes Act 1988, subject to modifications, in relation to "equivalent Lloyd's reserves". Section 444BA is the principal provision governing the relief given to general insurance companies on account of the equalisation reserves they are required to maintain by the FSA.

3. Subsection (2) explains the meaning of "equivalent Lloyd's reserve".

4. Subsection (3) defines the scope of the regulation making power.

5. Subsection (4) contains definitions.

BACKGROUND NOTE

6. Equalisation reserves are created by general insurers to cover claims they may be called upon to pay that arise from classes of business, for example property damage, that can give rise to intermittent but sometimes very large payments.

7. General insurance companies are required by the FSA to make these reserves under legislative rules designed to protect their capital base. When these rules were introduced, the equivalent rules governing the Lloyd's insurance market were very different, and even now the unique structure of the Lloyd's insurance market results in capital maintenance rules significantly different from those of general insurance companies.

8. However, over the years there has been convergence, and the availability of relief to general insurance companies but not to corporate and partnership members of Lloyd's has increasingly been seen as anomalous and a disadvantage to the Lloyd's market.

9. The section provides for a relief to corporate and partnership members of Lloyd's broadly similar to that available to general insurance companies for amounts reflected in equalisation reserves.

SECTION 48 SCHEDULE 24: DISGUISED INTEREST

SUMMARY

1. Section 48 and Schedule 24 make provision for returns from certain arrangements that produce returns that are economically equivalent to interest to be charged to corporation tax in the same way as profits from a loan relationship.

DETAILS OF THE SCHEDULE

Disguised Interest

2. Paragraph 1 amends Part 6 of the Corporation Tax Act 2009 (CTA), which deals with certain matters that are treated as loan relationships, although they are not actually loan relationships. All references below are to the CTA unless otherwise indicated.

3. Paragraph 2 inserts into CTA a reference to the new Chapter 2A which contains the legislation on disguised interest.

4. Paragraph 3 inserts the new Chapter 2A into CTA. References to Chapter 2A below are to the new Chapter 2A.

5. Section 486A is introductory. It provides for Part 5 of CTA (loan relationships) to apply in relation to returns which are economically equivalent to interest. It also refers to exceptions in section 486C to 486E (see notes on the exceptions below).

6. Section 486B(1) contains the legislative principle. Where a company is party to an arrangement that produces for it a return on an amount which is "economically equivalent to interest" then the return is to be taxed as if it were a profit from a loan relationship.

7. Section 486B(2) defines what is meant by a return on an amount that is "economically equivalent to interest".

8. Section 486B(2)(a) reproduces a number of indicia commonly cited in cases on the meaning of interest:

9. The return must be calculated by reference to an amount. In *Euro Hotel (Belgravia) Ltd* 51TC293 Megarry J said:

- "there must be a sum of money by reference to which the payment which is said to be interest is to be ascertained". Thus, the return has to arise from some form of investment or entitlement; and

- it must be reasonable to assume that it is a return by reference to the time value of that amount. In *Bennett v. Ogston* 15 TC 374 Rowlatt J described interest as 'payment by time for the use of money'.

10. Section 486B(2)(b) provides that the rate of return must be reasonably comparable to a commercial rate of interest.

11. Section 486B(2)(c) ensures that, viewed at the "relevant time", there must be no "practical likelihood" that the arrangement will cease to produce the return (unless the person by whom it falls to be produced is prevented from producing it). "Practical likelihood" is the term used by Lord Oliver in *Craven v White 62 TC 1* commenting on Lord Brightman's speech in *Furniss v Dawson* 55 TC 324 describing the cases when the *Ramsay* principle, as understood at the time, would apply. It has now to be understood in the light of the judgment of the House of Lords in *Scottish Provident Institution 76 TC 538* as precluding attempts to manufacture a "falsifying" arrangement.

12. Section 486B(3) defines the relevant time as the later of the time when the company becomes party to the arrangements or the time when the return begins to be produced.

13. It must therefore be clear at the outset that the return will be produced. Thus, although there is no express requirement for the arrangement to be "designed" to produce the return, the return must be initially predictable.

14. Subsections (4) and (5) ensure that the credits and debits in respect of the loan relationship are taxed on an amortised cost basis; this being regardless of whether they are recognised in the accounts of the company that obtains the return. Thus, if the return is capitalised by being included in the value of an asset on the balance sheet, or is not recognised, in the accounts at all, the return must still be recognised using an amortised cost basis so that the whole of the return is recognised on an accruals basis.

15. Section 486B(6) deals with cases where two or more persons are party to an arrangement which in aggregate produces a return to which the legislation would apply if it were produced for just one of them. The taxable return is apportioned between them on a just and reasonable basis.

16. This rule is intended to prevent companies side-stepping the new rule by fragmenting the return so that each return looked at separately does not constitute an interest-like return, but when the return is looked at as a whole it does.

17. Section 486B(7) provides that the only amounts brought into account for corporation tax purposes in relation to a return are those that are brought into account under section 486B. This for instance ensures that any return that is so brought into account is excluded from corporation tax on chargeable gains. See also the comments on section 486C below, which indicate how this provision interacts with that section.

18. Section 486B(8) ensures that the credits and debits to be brought into account include exchange gains and losses that arise as a result of translating the accounts carrying value of the return and the principal amount by reference to which the return falls to be produced.

19. Section 486B(9) defines arrangement as including any agreement, understanding, scheme, transaction or series of transactions (whether or not legally enforceable). It does now however include any arrangement that constitutes a finance lease within the meaning of section 219 of the Capital Allowance Act 2001 (CAA). This ensures that all such arrangements continue to be taxed according to current rules (and in particular that leases that are not long funding leases within the meaning of section 70G of CAA are not brought within the scope of the legislation). Operating leases by contrast are not within the scope of the legislation at all.

20. Section 486C is a scope or boundary rule: it provides that any part of the return that is charged to corporation tax as income of the company or brought into account as income of the company for corporation tax purposes is not charged under the Chapter. The exclusion does not apply where the return would fall to be taxed as income or brought into account as income at any time that is later than the time when it would be taxed under section 486B, meaning that (if the section applies at all) it is not disapplied in relation to income that would be taxed at a time later than under section 486B. But if in consequence Chapter 2A has the effect that some of the income is taxed before it otherwise would be, section 486B(7) then ensures that that income is not taxed again.

21. Section 486C also provides that any exclusion in relation to debits or credits arising from items within the loan relationship, derivative contracts or intangible fixed asset rules is not overridden by anything in Chapter 2A. However, this does not apply in relation to any return that would be taxed as a chargeable gain by virtue of section 641 (which treats profits on certain types of derivative contracts as capital ones).

22. Section 486D(1) provides an important exclusion for any case where it is not the main purpose or one of the main purposes (if there is more than one) of the company being party to the arrangement to obtain a "relevant tax advantage". "Relevant tax advantage" is defined in section 486D(4).

23. Section 486D(2) provides that a company may elect that the Chapter is to apply in relation to a particular arrangement as if section 486D(1) were omitted. Such an election might be advantageous to the "lender" under an arrangement such as a structured finance arrangement who, at least in theory, may otherwise be taxed on a greater amount than under the disguised interest rules.

24. Section 486D(3) provides that an election may not be made by a company in a case where the Chapter applies by virtue of section 486B(6). It also provides that the election must be made no later than the time when the arrangement begins to produce a return for the company, and is irrevocable. This is subject to paragraph 15 of the Schedule, which in all cases allows an election to be made before 1 August 2009, having effect in relation to returns produced on or after the time the election is made.

25. Section 486D(4) provides that "to obtain a relevant tax advantage" means to secure that the return is produced in a way that means that it would be taxed more favourably than it would be if it were charged to tax as income or brought into account as income at the time that the return would be recognised under section 486B.

26. This main purpose test requires consideration of two questions. The first question is whether, as a matter of fact, the return produced by the arrangements for the company is produced in form (such as a capital gain or dividend) that would be taxed more favourably than it would be if that return were taxed in the same way as interest. This is a purely objective matter. The second question is whether it is reasonable to assume that it was a main purpose of the company being party to the arrangements to secure that the return was produced for it so as to give that rise to that advantage.

27. Section 486D(5) provides that the tax avoidance exclusion does not apply where the return is produced for a company that is a controlled foreign company (CFC). This is because it is unclear whether a company that is not within the charge to corporation tax can have a main purpose of avoiding it.

28. For this purpose, a CFC means a company whose profits are apportioned or would be apportioned but for one of the exemptions in section 748(1) of the Income and Corporation Taxes Act 1988 (ICTA).

29. Section 486E introduces the other main exclusion from Chapter 2A and the notion of "excluded shares".

30. Section 486E(1) states that the Chapter will not apply for an accounting period (the "relevant accounting period") for which an arrangement produces a return if the arrangement involves only "relevant shares" held by the company ("holding company") for which the return is produced throughout the "relevant period".

31. Section 486E(2) to (11) contain definitions relevant for construing section 486E(1).

32. Section 486E(2) explains what is meant by "relevant period". It is the period starting with the date on which the company becomes party to the arrangement (or if later when the return begins to be produced) and ending with the end of the accounting period for which it is necessary to ascertain whether the share is a relevant share (or if earlier when company ceases to be party to the arrangement or when the arrangement ceases to produce a return).

33. Section 486E(3) explains what is meant by "involves only" a share. An arrangement involves only a share if (and only if) the return that is produced for the company consists purely of an increase in the fair value of the share. This thus excludes from Chapter 2A all straightforward share investments in "relevant shares" where the only economic exposure that the holding company has to the shares that it holds is to the value of the shares. The legislation also clarifies that where part of a fair value increase is paid as a dividend then that is not to affect the question of whether a return reflects only such an increase.

34. It follows that the legislation is not prevented from applying where the return is derived from a combination of holding the share and some other arrangement such as a forward sale or other derivative. It also follows that it would not be prevented from applying if the arrangement involves some other transaction such as a repo (and see in this connection section 486E(11)). But in any such case it would still be necessary for a tax avoidance purpose (within section 486D) to be present before the legislation could apply.

35. Section 486E(4) defines "fair value" in the same way that it is now defined for loan relationship purposes (see section 313(6) of CTA). It also clarifies that payment of a dividend does not affect the fair value return arising from a share.

36. Section 486E(5) defines "relevant shares" as meaning shares which throughout the "relevant period" are either i) "fully paid up shares" of a "relevant company" or ii) other shares which would be accounted for by the issuer as a financial liability and which produce for the holding company a return economically equivalent to interest for the purposes of Chapter 6A (shares as liabilities). It is not necessary for there to be any charge under Chapter 6A in relation to such a share in order for this exclusion to apply. Section 930I (corporation tax treatment of company distributions) also ensures that such shares do not generally give rise to taxable distributions (subject to section 930M).

37. Section 486E(6) defines "fully paid-up share" for the purposes of subsection (1), in terms similar to section 524(4) of CTA. This requirement is meant to ensure that arrangements such as those within section 524 of CTA will continue to be caught.

38. Section 486E(7) defines "relevant company". A relevant company is a company connected with the holding company, a relevant joint venture company, or a relevant CFC.

39. Section 486E(8) defines "connected" for the purposes of subsection (7) as having its section 466 of CTA meaning. This is equivalent to old section 87 of the Finance Act (FA) 1996.

40. Section 486E(9) defines "relevant joint venture company" as a company in relation to which the holding company has at least a 40 per cent interest provided that one other person also has such an interest.

41. Section 486E(10) provides that section 755D of ICTA is to have effect for the purposes of determining "control" in subsection (9).

42. Section 486E(11) defines a relevant CFC as one whose profits are apportioned to the holding company or are not so apportioned because of an exemption.

43. These exclusions are intended to put beyond doubt that straightforward share investments in relevant companies cannot give rise to a charge at any tier. This is because the only return that arises at each tier is an increase in the value of the relevant shareholding in a group company. So if company A holds all shares in company B which holds all shares in company C, then company B's holding is excluded if the return company B obtains is an increase in value of the company C shares and company A's holding is excluded if its return is an increase in value of the company B shares.

44. Section 486E(12) provides that section 550(3) shall not have effect for the purpose of determining whether shares are held by a company for the purposes of this section (excluded shares). Section 550(3) deems a company to hold shares when as a matter of fact it does not, so this provision ensures that the section 486E exclusions, which depend upon a company holding a share, cannot be engaged by this deeming. On the other hand there is nothing to prevent section 545(2), which deems a company that holds shares under a creditor repo not to hold them, from applying. This means that the exclusions in section 486E do not apply to either the original owner or temporary owner under a repo.

Shares accounted for as liabilities

45. Paragraph 4 inserts a new Chapter 6A into the CTA (Shares accounted for as liabilities). It provides a limited replacement for what were sections 91B to 91E of FA 1996 (now Chapter 7 of Part 6 of CTA - shares with guaranteed returns), particularly for that part dealing with "preference share lending" (mostly old section 91D) as, for the reasons given in the consultation document on principles-based drafting issued in November 2008, it is considered better to deal separately with disguised interest in what are clearly not loans in substance or form on the one hand, and what are simply loans dressed up as investment in preference shares on the other.

46. The Chapter as a whole is headed "Shares accounted for as liabilities". This will cover many shares which are redeemable in accordance with their terms.

47. Section 521A introduces the Chapter and provides for it to treat certain shares held by one company in another company as if they were rights under a creditor loan relationship.

48. Subsection (1) (taken with subsection (3)) provides for the main loan relationships rules in Part 5 (previously Chapter 2 of Part 4 of FA 1996) to apply to the holder of certain shares.

49. Subsections (2) and (6) signpost later sections of CTA and also section 116B of the Taxation of Chargeable Gains Act 1992 (TCGA) dealing with the TCGA implications of changes in the status of certain shares.

50. Subsection (3) states that references in the Chapter to the "investing company" and "issuing company" are respectively to A and B.

51. Subsection (4) ensures that shares already treated as loan relationships - those in a building society - are not included in the meaning of shares. This replicates section 522(6).

52. Subsection (5) prevents a company from being treated as holding shares that are subject to a repo transaction. This is to prevent the investing company from being able to benefit from any exclusion in section 521C (for instance, the connected party exclusion) that depends on the company holding the share. In any such case Chapter 2A may then apply in relation to the share (since the return does not derive wholly from share ownership).

53. Subsection (6) highlights that section 116B of TCGA (previously section 91G(2) of FA 1996) applies to determine the effect for the purposes of corporation tax on chargeable gains when a share begins or ceases to be one to which section 521C applies. See also the note on paragraph 5 of the draft Schedule below.

54. Section 521B(1) is the operative rule.

55. Subsection (2) applies Part 5 (loan relationships) to the holder of the share in relation to the times in that company's accounting period when it holds a share in another company and section 521C applies to the share. The fact that the share is treated as a loan relationship (so that it no longer pays distributions) does not however prevent a dividend paid in respect of that share from being taken into account when considering whether the company (if a controlled foreign company) has satisfied an acceptable distribution policy.

56. Subsection (3) ensures that where relevant to the treatment of the holder, the issuing company is treated as a debtor under the loan relationship deemed by subsection (2). Identification of the debtor may be needed in some cases so that other tax rules, such as transfer pricing, can operate correctly. But as noted below the legislation cannot apply where the share issuer and holder are connected, which means that section 349 (connected companies required to use amortised cost accounting) will not be in point in relation to this provision. On the other hand, subsection (4) prevents debits being claimed in respect of such shares.

57. Subsection (4) provides that no debits may be brought into account by the investing company in relation to any share to which Chapter 6A applies. This replicates the exclusion for such debits currently within section 523(3). Unlike that provision, this does not apply in relation to exchange debits. This provision is necessary to prevent attempts to create artificial tax debits.

58. Subsection (5) ensures that any reference to the share in the Chapter is to the share mentioned in subsection (1).

59. Section 521C contains the conditions a share must meet to be a "share" to which section 521B(2) applies. By virtue of subsection (1) a share is to be treated as a creditor relationship of the investing company if:

- the share would be accounted for as a liability by the issuing company in accordance with generally accepted accounting practice - subsection (1)(a). This means generally accepted accounting practice as defined by section 50 of FA 2004, which for this purpose means either International Accounting Standard (IAS) 32 or the UK equivalent Financial Reporting Standard (FRS) 25. This accounting rule replaces the "redeemability" condition in section 529;

- the share produces for the investing company a return which is economically equivalent to interest (whether through dividends, redemption amount or a combination) – subsection (1)(b). This is different from the wording in section 529, but relies instead on the definitions in Chapter 2A;

- the issuing company and the investing company are not connected companies - subsection (1)(c). This does not replicate any provision in section 529, and provides certainty that a share cannot be treated as a creditor relationship where the issuer and holder are connected companies. Distributions on such shares may however be taxable in accordance with section 930M (schemes in the nature of loan relationships);

- The share is within subsection (3) - subsection (1)(d);

- The share is not an excepted share within section 521D; and

- The investing company holds the share for an unallowable purpose as defined by section 521E. The definition of "unallowable purpose" is based on that in Chapter 2A. See the notes on section 521E below.

60. Subsection (2) defines "economically equivalent to interest" for the purposes of subsection (1) in terms identical to section 486B(2).

61. Subsection (3) defines the "relevant time" for the purposes of section subsection (2). It means the later of the time when the share is first held and the return first begins to be produced.

62. Subsection (4) provides that a share meets the condition in section 486(1)(d) (requirement for condition in subsection (3) to be met) if the share is not already treated as a creditor relationship because of section 490 (unit trusts and offshore funds treated as creditor relationships). This replicates what is currently in section 529 (see section 526(1)(b).

63. Subsection (5) gives "connected" the same meaning as in section 466.

64. Section 521D(1) provides that a share is excepted for the purposes of section 521C(1)(e) (and so excluded from application of the legislation) if:

- it is a qualifying publicly issued share; or
- it is a share that mirrors a public issue (as to which see subsection (3) and (4)).

65. Section 521D(2) provides that a share is a qualifying publicly issued share where it was issued by a company as part of an issue to independent persons (defined as a person not connected with the company) and the investing company and persons connected with it hold less than 10 per cent of that issue.

66. Sections 521D(3) and (4) define the two cases where a share mirrors a public issue.

67. Case 1 is where a company (A) issues shares to independent persons (the public issue) and within 24 hours of that issue, other group companies issue shares (the mirroring shares) to company A on the same or substantially the same terms as the public issue and the total nominal value of the mirroring shares does not exceed the nominal value of the public issue – section 521D(3).

68. Case 2 expands the range of mirroring shares to allow for chains of shares to be issued within a group –section 521D(4).

69. Section 521E(1) provides that a share is acquired by the investing company for an unallowable purpose for the purposes of section 521(1)(f) if the main purpose (or one of the main purposes) for which the company holds the share is to secure a "relevant tax advantage".

70. Section 521E(2) provides that the investing company may elect that Chapter 6A is to apply in relation to shares that produce a return as if section 521(1)(f) were omitted.

71. Section 521E(3) provides that the election must be made no later than the time when the share begins to produced for the company, and is irrevocable. This is subject to paragraph 16 which in all cases allows an election to be made at any time before 1 August 2009, but only in relation to returns arising on or after that date.

72. Section 521E(4) provides that "secure a relevant tax advantage" means secure that the return is taxed more favourably than it would be if it were wholly charged to tax as income or brought into account as income at the time when it would be taxed if the share were a loan relationship.

73. Section 521E(5) provides that the tax avoidance exclusion does not apply where the return is produced for a company that is a CFC. This is because it is unclear whether a company that is not within the charge to corporation tax can have a main purpose of avoiding it.

74. For this purpose, a CFC means a company whose profits are apportioned or would be apportioned but for one of the exemptions in section 748(1) of ICTA.

75. Section 521F deals with the consequences for loan relationships and corporation tax on chargeable gains purposes when a share begins or ceases to meet the conditions in section 521B. This may be because the share begins or ceases to be accounted for as a liability, begins or ceases to be held for an unallowable purpose or the parties become or cease to be connected or for some other reason.

76. Under subsection (2) the investing company is treated for the purposes of the loan relationship rules in Part 5 of CTA as having acquired and disposed of the share immediately before that time for an amount equal to its "notional carrying value".

77. Subsection (3) defines "notional carrying value" as meaning the amount which would have been the carrying value of the share in the investing company's accounts if a period of account had ended immediately before section 521B began or ceased to apply

78. Section 521F(4) defines "carrying value" by reference to section 316 of CTA (previously paragraph 19A(4) of Schedule 9 to FA 1996).

79. The overall effect of section 521F is that the acquisition value for the deemed loan relationship should generally be the accounts carrying value of the shares and the deemed disposal should generally be for an amount equal to the accounts carrying value. It will be rare for the accounts carrying value to differ from the tax carrying value because of the exclusion for connected party shares.

80. Paragraph 5 amends section 116B of TCGA. Section 116B is the rewritten version of section 91G(2) of FA 1996 inserted into TCGA by CTA (so far as it applies for the purposes of corporation tax on chargeable gains) and is reproduced below as it will appear following the amendments:

Shares beginning or ceasing to be shares to which section 521B of CTA 2009 applies

(1) If at any time section 521B of CTA 2009 begins or ceases to apply in the case of a share held by the investing company it is treated for the purposes of this Act [chargeable gains] —

(a) as having disposed of the share immediately before that time for consideration of an amount equal to the notional carrying value of the share at that time, and

(b) as having immediately reacquired it for consideration of the same amount.

(2) In this section—

"notional carrying value" has the same meaning as in section 521E(2) of CTA 2009 (see subsection (3) of that section),

and

"investing company" has the same meaning as it has for the purposes of Chapter 6A of Part 6 of that Act (shares accounted for as liabilities) (see section 521A(3) of that Act)."

81. The effect of this is that (on a share ceasing to meet the conditions in section 521C) the acquisition value for the shares for the purposes of corporation tax on chargeable gains should generally be the accounts carrying value of the shares and (on a share beginning to meet those conditions) the deemed disposal value should generally be the accounts carrying value. As with paragraph 367 of Schedule 1 to CTA, there is no provision for any hold over of gain or loss.

82. Paragraph 6 makes a consequential amendment to the rules on arbitrage in section 26 of F(No.2)A 2005 so that references in subsection (10) to section 91A and 91B of FA 1996 are replaced by equivalent references to Chapter 2A or 6A of Part 6 of CTA.

83. Paragraph 7 makes a number of amendments to Schedule 4 to CTA to reflect new Chapters 2A and 6A.

84. Paragraph 8 signposts the repeals. The most important repeals here are those of sections 91A to 91G of FA 1996 - the rules that treat shares as loan relationships in certain circumstances. It also repeals sections 91H and 91I of FA 1996 and sections 131 to 133 of FA 2004, which cover partnerships. This points up that the rules here go wider than dealing with shares and deal with any arrangements including partnerships and contributions to partnerships as well as shares. The rules on quasi-stocklending at sections 736C and 736D of ICTA, and quasi-interest arising from repos in section 547, are also repealed.

85. Paragraph 9 contains consequential repeals.

86. Paragraph 10 gives the main commencement rule. The disguised interest rules in Chapter 2A have effect in relation to any arrangement to which the company became party on or after 22 April 2009. This is subject to paragraph 12 in relation to certain existing "caught" arrangements.

87. Paragraph 11 states that the amendments and repeals made by paragraphs 2(3), 4 (shares accounted for as liabilities), 5 (amendments and repeals relating to section 116B of TCGA), 6 (arbitrage), 7 (index of expressions), 8 (repeals) and 9 (consequential repeals) come into force on or after 22 April 2009.

88. Paragraph 12(1) gives the transitional rule in respect of existing arrangements in force as at 22 April and provides that the paragraph applies where Chapter 7 of Part 6 (shares with guaranteed returns), or any of the other provisions being repealed applies in relation to anything done by a company before 22 April 2009 which amounts to an arrangement within the meaning of section 486B(7) to which Chapter 2A might apply if a company became party to the arrangement on or after 22 April.

89. Sub-paragraph (2) then provides that the company is to be treated for the purposes of Chapter 2A as having become party to an arrangement on 22 April. This will not automatically trigger the application of Chapter 2A, but merely make it capable of applying if all the other conditions are met in relation to that arrangement.

90. Sub-paragraph (3) provides that paragraph 12 does not apply if paragraph 13 (former section 91A to 91E shares) applies instead.

91. Paragraph 13(1) gives the rule for determining the treatment for the purposes of corporation tax on chargeable gains in a case where Chapter 7 of Part 6 (shares with guaranteed returns) applies in relation to a share held by a company on 21 April 2009.

92. Sub-paragraph (2) provides that section 116B of TCGA is to be treated as applying as if, on 21 April 2009, the share ceased to be one to which section 91A or 91B applied.

93. This deemed disposal (triggered by the version of section 116B of TCGA in force at 21 April 2009) has the effect that any gain or loss originally deferred under section 91G of FA 1996 when the shares as debt rules began to apply (only applicable if they began to apply on 16 March 2005) is crystallised. Thereafter, any return can be brought into account only under Chapter 2A. It also gives rise to a deemed disposal of the (deemed) creditor loan relationship at fair value and a deemed acquisition cost for the purpose of corporation tax on chargeable gains at that value.

94. Sub-paragraph (3) provides that paragraph 13 does not apply if paragraph 14 (section 91D shares which become Chapter 6A shares) applies instead.

95. Paragraph 14 sets out a separate rule for the cases within paragraph 13(3) to which Chapter 6A applies on 22 April 2009.

96. Sub-paragraph (2) provides in this case that Part 5 of CTA applies as if the company has acquired the share on 22 April 2009 for its notional carrying value on that date. There might be a difference between this amount and the closing value of the creditor relationship as at 21 April 2009. This is a tax nothing.

97. Sub-paragraph (3) defines notional carrying value as having its section 521E(2) meaning.

98. Sub-paragraph (4) ensures that section 521E does not come into force by virtue of the coming into force of section 521B.

BACKGROUND NOTE

99. Current tax law contains a number of targeted anti-avoidance rules to ensure that amounts that are economically equivalent to interest are charged to corporation tax in the same way as interest.

100. The section and Schedule replace these piecemeal responses with a rule that sets this principle out comprehensively. It is the result of consultation on the use of "principles-based drafting" to tackle avoidance involving disguised interest. The effect of the legislation is that (subject to the excluded share rule and arrangements not involving tax avoidance) a return equivalent to interest is charged to corporation tax in all circumstances where it would not currently be taxed as income.

101. The new legislation follows two consultation exercises on the use of principles-based drafting to counter avoidance in the areas of financial products. The consultation documents can be accessed at the following references:

a. http://www.hm-treasury.gov.uk/d/pbr08_financialproducts_802.pdf

b. http://www.hm-treasury.gov.uk/d/consult_financialproductsavoidance061207.pdf

SECTION 49 AND SCHEDULE 25: TRANSFER OF INCOME STREAMS

SUMMARY

1. Section 49 and Schedule 25 treat sales and other disposals of rights to receive future income streams as giving rise to income for corporation tax and income tax purposes, unless already provided by tax law. This treatment is subject to a number of express exceptions.

2. The purpose of the section and Schedule is to secure that (unless taxable as income) receipts derived from a right to receive income (and which are an economic substitute for income) are treated as income for the purposes of corporation tax and income tax.

DETAILS OF THE SCHEDULE

3. Part 1 contains rules for taxation of transfers of income streams made by corporate transferors.

4. Paragraph 1(1) sets out that the Part applies where a company makes a transfer to a person of a right to relevant receipts and the transfer of the right is not the consequences of the transfer to that person of the asset from which the receipts arise.

5. The transfer must be the consequence of the transfer of a right, and not simply an application of the transferor's income. Thus, the legislation cannot apply for instance where the trustees of a trust distribute trust income or apply trust income for the benefit of a beneficiary.

6. The requirement that the transfer is not the consequence of the transfer of the underlying asset is intended to make clear that the legislation will not apply in any case where there is an outright sale of the income-producing asset. In other words the legislation deals with the sale of income streams where the seller retains the underlying asset from which the income arises or where the seller transfers the stripped asset to another person, or where there is no underlying asset.

7. Sub-paragraph (1)(b) highlights the exception to the rule that the underlying asset must be transferred in sub-paragraph (3) for transfers of rights to annual payments.

8. Paragraph 1(2) defines relevant receipts as any income which but for the transfer would be charged to corporation tax as income of the transferor or brought into account in calculating profits of the transferor for the purposes of corporation tax. The reason for referring to income that is brought into account in calculating profits is to ensure that the sale of a right to income which would be a component in the calculation of profits from a trade or other business is included as well as sale of pure income. The words "but for the transfer" indicate that the legislation cannot apply where the transferor remains taxable on the income.

9. The requirement that relevant receipts are those which would be receipts of the transferor but for the transfer is included to emphasise that the legislation is not concerned with the *creation* of income receipts for example by the entering into of the contract giving rise to the receipts. A useful distinction has been drawn by, in particular, courts in the United States of America, between a "right to earn income" and a "right to earned income". See in this regard the discussion in *Lattera & Lattera v Commissioner* [437 F.3d 399 - 3rd Circuit Court of Appeals 2006 http://www.ca3.uscourts.gov/opinarch/044721p.pdf]. This legislation, like many of the provisions it replaces such as section 730 of the Income and Corporation Taxes Act 1988 (ICTA), deals with transferable income which the payer would have paid regardless of the transfer with the transfer simply meaning that it is now received by another person.

10. Paragraph 1(3) contains the exception to the requirement that the underlying asset is not transferred and applies where that asset is all rights under an agreement for annual payments. This exception reflects the fact that such an agreement is indistinguishable from a right to relevant receipts so that it is appropriate to treat the outright transfer of the agreement in the same way as a transfer of the right to relevant receipts. The transfer of all rights under an agreement for annual payments is currently taxed as income under section 775A of ICTA. This rule applies only where what the income that is transferred what constitute annual payments in the hands of the transferor. Where the transferor carries on a trade such that the income stream would not have been pure income profit in its hands, then paragraph 1(3) can have no application.

11. Paragraph 1(3) also ensures that where a transfer of an asset is made under an agreement that provides for its repurchase then for the purposes of paragraph 1(1) the asset is to be treated as not having been transferred.

12. Paragraph 1(4) explains that paragraph 2 sets out what happens where this Part applies.

13. Paragraph 1(5) signposts the exclusions from the charge under the legislation set out in paragraphs 3 and 4.

14. Paragraph 1(6) signposts that paragraph 5 makes specific provision for transfers of partnership shares.

15. Paragraph 1(7) indicates that paragraph 6 contains supplementary provision

16. Paragraph 2(1) provides that the "relevant amount" is to be treated as income of the transferor chargeable to corporation tax in the same way and to the same extent as the relevant receipts would have been. By use of the words "to the same extent", the legislation limits the charge to corporation tax on the transfer of relevant receipts in a case where the receipts (although wholly of an income nature) would have not have been wholly taxed as income.

17. For instance, lease rentals payable to a company under a long funding lease within the meaning of Chapter 6A of Part 2 of the Capital Allowances Act 2001 (CAA), although income, are not wholly taxed as income but are taken into account as elements in determining the taxable finance return. The reference to "the same extent" in paragraph 2(1) ensures that if the right to such a rental payment were sold only the part of the consideration that represents the amount that would have been taxed as income is to be charged. So a sale of the right to the finance margin would be taxable, but a sale of the "principal" would not be. Similarly, if the relevant receipts arise from anything which would produce credits or debits in relation to the company under Part 5 (loan relationships), Part 7 (derivative contracts) or Part 8 (intangible fixed assets) but those debits or credits would have been disregarded under those Parts then a transfer of the right to those amounts will be disregarded to the same extent that the receipts themselves would have been.

18. This sub-paragraph, which is the operative provision for the Schedule, brings the relevant amount into account in the same way as that in which the income or other receipts would have been chargeable had there been no transfer of the rights to them.

19. Paragraph 2(2) defines "the relevant amount". Normally it is the amount of the consideration for the transfer of the right to the relevant receipts. But where the amount of the consideration is substantially less than the market value of the right to the relevant receipts (or where there is no consideration) then the excess is additionally to be treated as income of the transferor. The market value rule is intended to apply only exceptionally where it is clear that the transaction is either not at arm's length or where the transaction has been structured to make it appear that there is less "consideration" than the value actually given for the right to relevant receipts. This reflects the concerns that led to the amendment to section 785A of ICTA made by paragraph 1 of Schedule 22 to the Finance Act (FA) 2008, which was designed to block schemes purporting to side-step section 785A by transferring rights to lease rentals in exchange for value which, it was argued, was not "consideration" under English law.

20. Paragraph 2(3) contains the timing rule for the purposes of the charge to tax in relation to the taxable sum identified under paragraph 2(1). In cases where consideration is the measure of the income, it is to be treated as arising when it is, in accordance with generally accepted accounting practice (GAAP), recognised in the transferor's profit and loss account or income statement. Where market value is used, then the excess over the consideration is to be treated as arising at the same time that it would have been recognised if consideration equal to full market value had been received.

21. Paragraph 2(4) gives the timing rule where the rule in sub-paragraph (3) would not involve full recognition of the income. In such a case, the amount that would not be recognised is to be treated as arising at the time that it becomes reasonable to assume that not all the income would, by virtue of sub-paragraph (3), be recognised in an accounting period of the company. Thus the taxable amount identified under paragraph 2(1) (which may be less than the relevant amount) will always be taxed in full, with the timing governed either by sub-paragraph (3) or (4).

22. Paragraph 3 sets out an exception. Paragraph 3 replaces clause 1(6) in the consultation document published containing a draft of this Schedule. The exception applies where and to the extent that the income under paragraph 1(1) is:

- already charged to tax as income;
- brought into account in calculating any income; or
- brought into account for the purposes of CAA.

23. Paragraph 4 recognises that some transfers of the right to relevant receipts are in substance a transfer by way of security only. So the section does not apply if the transferor transfers the rights to the income streams as part of a structured finance arrangement and the consideration is an "advance" to the transferor or a partnership of which the transferor is a member for the purposes of the legislation in sections 774A to 774G of ICTA. This deals with comments made on the consultation document on this point.

24. Paragraph 5 prevents the Part from applying to virtually all transfers of the right to relevant receipts that result from a reduction in a company's share in profits of a partnership of which it is a member. Specifically, it treats the transfer of such a right as the consequence of the transfer of the asset from which those receipts arise if either Condition A or B is met (such that paragraph 1(1)(b) does not then apply, so the Part cannot apply).

25. Condition A is contained in paragraph 5(2) and is that there is a reduction in the transferor's share in the overall partnership property and the reduction in the transferor's entitlement to relevant receipts is in the same proportion. This means that a simple reduction in a partner's interest in a partnership cannot trigger the application of the legislation.

26. Condition B is contained in paragraph 5(3) and is that it is not the main purpose or one of the main purposes of the transfer to secure that the relevant receipts are not charged to corporation tax or income tax on any partner. Thus the legislation can apply only where the main or one of the main purposes is to secure that no partner is charged to such tax on the relevant receipts (and only then if Condition A is not met). It follows that this rule cannot apply so long as the relevant receipts do not cease to be within the charge to tax (and even if they do cease to be within the charge it was a main purpose to secure that result).

27. Paragraph 6(1) provides that certain transactions that may transfer income but arguably do not involve a transfer of the asset from which the income arises are to be treated as transfers of assets. This ensures that the Part will not apply to such income transfers. The transactions in question are the grant or surrender of a lease in land, the disposal of an interest in an oil licence, and the grant or disposal of any interest in intellectual property which constitutes a pre-2002 asset within the meaning of section 881 of the Corporation Tax Act 2009 (CTA).

28. Paragraph 6(2) allows HM Treasury a power by way of order to secure that other transactions shall be treated as the transfer of assets.

29. Paragraph 6(3) further explains the use of the word "transfer" as per paragraphs 1 to 4. It follows the original Clause 1(8) in respect of which the December 2007 consultation document said "Transfer is defined very widely in subsection (8) to include specific realisation events such as sale, exchange, gift or assignment and also any arrangements that equate in substance to a transfer. This might include transactions involving options, total return swaps, etc. It would not, however, cover transactions which amount, in form to a transfer, but, in substance to, say, the giving of security such as in a repo." The paragraph also further explains the use of the phrase "a transfer taking place" in the case of wider non-sale etc arrangements so that it also includes the making of that arrangement.

30. Paragraph 6(4) makes clear that a transfer by a partnership of which a company is a member is to be treated as a transfer to which the Part applies. Similarly a transfer by a company to a partnership of which the company is a member or to the trustees of any trust of which the transferor is a beneficiary counts as a transfer.

31. This ensures that where a partnership enters into a transaction to which the Part applies, each the member of the partnership is charged as if it had disposed of its share of relevant receipts for its share of the consideration received by the partnership. Similarly, if a partner transfers relevant receipts to a partnership then it may be charged but only in relation to those relevant receipts on which it is no longer taxable as part of its share of profits.

32. Paragraph 7 makes similar provision to paragraphs 1 to 6 for income tax. It does so by inserting a new Chapter 5A into Part 13 of the Income Tax Act 2007 (ITA) consisting of new sections 809AZA to 809AZF.

33. These provisions match those in paragraphs 1 to 6 and differ only to the extent necessary to cater for the different structure of income tax. The notes below refer only to the differences.

34. New section 809AZB(3) sets out the default timing rule, which is that the income to be treated as arising in the chargeable period of the transferor in which the transfer takes place. This differs from the corporation tax provision where the default rule is that the income is to be allocated in accordance with GAAP.

35. New section 809AZB(4) and (5) contain a different rule for cases where the relevant receipts would have been taxed as trading income or income from a property business. In cases where consideration is the measure of the income, it is to be treated as arising when it is, in accordance with GAAP, recognised in the transferor's profit and loss account or income statement. Where market value is used, then the excess over the consideration is to be treated as arising at the same time that it would have been recognised if consideration equal to full market value had been received.

36. New section 809AZB(6) gives the timing rule where the transferor is a company within the charge to income tax and the rule above would not involve full recognition of the income. In such a case, the amount that would not be recognised is to be treated as arising at the time that it becomes apparent that not all the income would be recognised in an accounting period of the company.

37. The differences here reflect the fact that whereas a company will always produce accounts, a person within the charge to income tax is likely to do so only in relation to taxation of profits from a trade or property business.

38. Paragraph 8 amends CTA by inserting a new Chapter 2B.

39. Paragraph 8(2) adds a reference to new Chapter 2B in the overview part of Part 6.

40. Sub-paragraph (3) inserts new Chapter 2B consisting of new sections 486F and 486G. (Sections 486A to 486E are part of the "disguised interest" legislation.) The two new sections are intended to ensure that the corporate purchaser of the relevant receipts is treated as party to a loan relationship with the result that the company obtains relief, on an accounts basis, for the cost of acquiring the income stream against any receipts arising from the income stream or from a subsequent sale of the income stream.

41. Section 486F gives the case: where there is an income stream transfer to a company under Part 1 or under the income tax equivalent set out in Chapter 5A of Part 15 of ITA (inserted by paragraph 7 of the Schedule). In such a case section 486G of CTA provides that the consideration for the transfer of the right to relevant receipts is to be treated as a money debt which is owed to the transferee by the person who falls to pay the relevant receipts and that the transfer is to be treated as a transaction for the lending of money.

42. This will have the effect that Part 5 of CTA will apply to the consideration and subsequent receipts so that the transferee will be charged to corporation tax only on the profit recognised in its profit and loss account in respect of the relevant receipts.

43. There is no income tax equivalent of paragraph 7 (treatment of transferee). If a transferee liable to income tax acquired an income stream to which either Chapter 5A of Part 13 of ITA or paragraph 1 of the CTA Schedule applies, it will either be a financial trader or will treat the transaction as a discounting transaction within section 381 of the Income Tax (Trading and Other Income) Act 2005 (ITTOIA).

44. Paragraph 9 sets out the repeals made as a consequence of the legislation. The list is the same as the list in the December 2007 consultation document, with the following exceptions:

- the repeals in sections 34 and 99 of ICTA are omitted (and not replaced by a reference to any section in Part 4 CTA 2009);
- the repeal of sections 279 to 281 of ITTOIA is omitted;
- repeals consequential on those repeals are omitted;
- a repeal of a reference to section 730 of ICTA in section 98 of the Taxes Management Act 1970 (TMA) is added;
- a consequential repeal in section 774E of ICTA is added; and

- an amendment is made to section 785ZB of ICTA (inserted into that Act by FA 2008) as a consequence of the repeal of section 785A.

45. Paragraph 10 sets out the commencement rule. The Schedule has effect in relation to transfers on or after 22 April 2009.

BACKGROUND NOTE

46. In many cases where a person sells or otherwise disposes of a right to receive income (whether one amount or many) without selling the underlying asset from which the income derives, tax law provides that the sum obtained by the seller is taxed as income rather than as a chargeable gain.

47. This may be the result of case law or of specific statutory provisions, the most important of which are sections 730 (dividends), 775A (annual payments) and 785A (chattel lease rentals) of the Income and Corporation Taxes Act 1988 (ICTA).

48. These statutory rules are not comprehensive. There are also differences and inconsistencies in the way the various provisions work, and disclosures made under Part 7 of the Finance Act 2004 and other information shows that they have been the subject of attempts to avoid their operation.

49. The new legislation sets out a general principle that a lump sum received for the sale or transfer of income stream is subject to tax in the transferor's hands in the same way that the income itself would have been (so there is no possibility of converting income into capital). The rule is subject to a number of exceptions.

50. The new legislation follows two consultation exercises on the use of principles-based drafting to counter avoidance in the areas of financial products. The consultation documents can be accessed at the following references:

- http://www.hm-treasury.gov.uk/d/pbr08_financialproducts_802.pdf
- http://www.hm-treasury.gov.uk/d/consult_financialproductsavoidance061207.pdf

SECTION 50 SCHEDULE 26: SAYE SCHEMES

SUMMARY

1. Section 50 and Schedule 26 make amendments to the rules relating to Save As You Earn (SAYE) share option schemes. They simplify certain administrative aspects, and make it possible for HM Revenue & Customs (HMRC) to ease practical difficulties that can arise for companies sending invitations to employees shortly before a change in the certification and bonus rates applying to SAYE contracts.

2. These changes to the current provisions on certified SAYE savings arrangements will:

   - provide for the transfer of certain administrative functions under the legislation from HM Treasury to HMRC;
   - remove the requirement for HMRC to send some documents by post;
   - allow HMRC to specify in the notices of withdrawal and variation of certified savings arrangements that certain savings contracts using the previous specifications entered into after the date of withdrawal or variation will be valid; and
   - reduce from 28 to 15 days the minimum period between the date when a notice with revised SAYE requirements is issued, and the date when the new requirements (including changes to interest rates) come into force.

DETAILS OF THE SECTION

3. Subsection (2) provides for the Schedule to come into force the day after the Budget resolutions are passed.

DETAILS OF THE SCHEDULE

Transfer of certain functions from HM Treasury to HMRC

4. Paragraph 2 amends section 705 of the Income Tax (Trading and Other Income) Act 2005 (ITTOIA), to transfer from HM Treasury to the Commissioners for HMRC responsibility for certifying "linked savings contracts" - contracts used in approved SAYE schemes.

5. Sub-paragraph (2) of paragraph 2 substitutes "Commissioners" for "Treasury" in subsections (1) and (2) of section 705, and sub-paragraph 3 inserts a new subsection (5) explaining the term "Commissioners".

6. Paragraph 3 amends section 706 of ITTOIA, to transfer from HM Treasury to the Commissioners for HMRC powers to withdraw and vary certifications and connected requirements in relation to SAYE savings arrangements.

7. Paragraph 4 amends section 707 of ITTOIA, to transfer from HM Treasury to the Commissioners for HMRC powers to authorise providers of certified savings arrangements.

8. Paragraph 5 makes amendments to section 708 of ITTOIA, to transfer from HM Treasury to the Commissioners for HMRC powers to withdraw and vary the authorisation of providers.

Removal of requirement that certain notices be sent by post

9. Paragraph 6 removes the requirement for certain communications relating to certified savings arrangements and providers to be made by post. It will be possible for these communications to be made electronically in future.

Reduction of notice period for withdrawals and variations

10. Paragraph 7 amends section 706(2)(b) to reduce from 28 to 15 days the minimum period from notification by HMRC and coming into effect of withdrawal or variation of requirements relating to certified savings arrangements.

Power to provide for withdrawals and variations not to affect certain contracts

11. Paragraph 8 amends the provisions of section 706(3) concerning the withdrawal or variation of requirements relating to certified savings arrangements. It will allow HMRC to assist companies that have offered SAYE contracts to their employees shortly before HMRC gives notice of withdrawal or variation of certified SAYE savings arrangements.

12. New subsections (a) and (b) inserted in section 706(3) restate existing rules about the withdrawal and variation of requirements. New subsection (c) has the effect that HMRC may specify that certain SAYE contracts made after a withdrawal and variation will not be affected by the change. This means, for example, that certain savings contract may continue to reflect bonus rates in force before the change. The contracts to which this will apply are to be specified in the notice from the Commissioners for HMRC to savings providers announcing the change.

BACKGROUND NOTE

SAYE schemes

13. SAYE share option schemes approved by HMRC allow employees to save under Save As You Earn contracts and to use the savings should they wish to exercise an option to buy shares in their company. They are all-employee schemes, designed to encourage employees to save, and to acquire a stake in the company they work for.

14. Under SAYE schemes a company offers its employees the option to buy, at a future date, shares in the company at a price set at the outset. Employees can choose to save in a 3 or 5 year savings contract. When the contract reaches maturity, a bonus is added, and the employee can use the proceeds to exercise the option and acquire shares, or alternatively may take the savings with the bonus, in either case free of income tax and National Insurance contributions.

15. The bonus rates to be used in SAYE contracts are set by the Government - at present, by HM Treasury and in future by HMRC, in accordance with a formula agreed with savings providers.

Administrative changes

16. The switch of certain administrative responsibilities from HM Treasury to HMRC and removing the need for communications to be made by post will streamline the process, ending duplication of work and enhancing communication with savings providers.

17. Currently, HM Treasury sets out specifications that linked savings arrangements must meet to be certified. There is a minimum period of 28 days between giving notice of withdrawals or variations (which can include interest rate changes) and the revisions coming into force. Under these changes, HMRC will take over administrative responsibility for the specifications, and the notice period will be reduced to 15 days. This ensures savings providers are notified of changes in certifications much earlier than is the case now.

Invitations issued shortly before a change in requirements for certified savings arrangements

18. The new provisions that HMRC may apply when an invitation to enter into an SAYE contract is issued just before a change in the requirements for certified SAYE savings arrangements reflect concern expressed by companies and administrators about the effect of the current rules.

19. At present if employees wish to enter into the savings contract but their application is accepted on or after the date of the change in the certification requirements, for example as to bonus rates, it is likely (depending on the facts of the case) that the application may be invalid, because the invitation reflects the old SAYE bonus rates which have been withdrawn.

20. The new provisions will have the effect that employers may be allowed to accept applications based on the old arrangements provided they are received within 30 days of the date of withdrawal or variation. For example, if the variation is a change in bonus rates, the previous bonus rate would apply for applications made on the basis of that rate.

21. Requirements for certified SAYE savings arrangements are reflected in a standard specification document, reissued with amendments to savings providers when changes in certified SAYE savings arrangements take place.

SECTION 51 SCHEDULE 27: REMITTANCE BASIS

SUMMARY

1. Section 51 and Schedule 27 make a number of minor amendments to provisions relating to the remittance basis of taxation.

DETAILS OF THE SECTION

2. Section 51 introduces Schedule 27.

DETAILS OF THE SCHEDULE

3. Paragraph 1 introduces Part 1 of the Schedule which amends Chapter A1 of Part 14 of the Income Tax Act 2007 (ITA).

4. Paragraph 2 inserts new subsection 5A in section 809C of ITA. This provides that any income tax charged to an individual under section 424 of ITA is to be excluded when nominating foreign income and gains in situations where that individual has claimed Gift Aid tax relief and has chosen to use the remittance basis.

5. Paragraph 3 amends section 809D(1) of ITA which provides that an individual with unremitted foreign income and gains of less than £2,000 in a tax year does not need to file a self-assessment tax return under the Taxes Management Act 1970 (TMA) in order to use the remittance basis.

6. Paragraph 4 amends section 809E of ITA by inserting a new sub-paragraph (c) and a new subsection (2A).

7. New paragraph (c) provides that individuals with no UK income and gains other than taxed investment income of less than £100 in a tax year can choose to access the remittance basis of taxation for a tax year without making a claim.

8. Paragraph 4(3) amends section 809E(1) of ITA so that it mirrors the amendment made to section 809D of ITA. It provides that relevant individuals are not required to file a self-assessment tax return under TMA in order to use the remittance basis.

9. New subsection 2A defines ‘taxed investment income’ for the purposes of new subsection 1(c) as income or gains within section 946 ITA which have been taxed at source.

10. Paragraph 5 amends section 809H ITA and excludes any income tax charged to an individual under section 424 of ITA when nominating income and gains in situations where that individual has claimed Gift Aid tax relief and has chosen to use the remittance basis.

11. Paragraph 6 amends section 809L of ITA and clarifies that 'remitted to the United Kingdom' for the purposes of Chapter A1 includes situations where property is used to pay interest on a relevant debt.

12. Paragraph 7 amends the definition of a relevant person in section 809M of ITA..

13. Section 809M(2)(e) is amended to provide that references to a close company include subsidiaries of such companies.

14. The new paragraph (ca) of section 809M(3) introduces a definition of a participator in relation to a close company for the purposes of defining a relevant person.

15. Paragraph 8 amends section 809P of ITA to provide a statutory rule for determining the value of a remittance where property forming part of a larger set is remitted to the UK.

16. Paragraph 9 corrects a grammatical error in section 809T of ITA.

17. Paragraph 10 amends section 809X of ITA by making amendments to subsections (4) and (5) to omit the references to relevant foreign income. The effect of the amendments is to extend the current exemption which applies to property purchased out of relevant foreign income to cover property purchased from other sources of foreign income overseas and chargeable gains.

18. Paragraph 11 makes consequential amendments to section 809Z5 of ITA required by the changes made elsewhere in this Schedule.

19. Part 2 of the Schedule amends the Taxation of Chargeable Gains Act 1992 (TGCA), the Income Tax (Trading and Other Income) Act 2005 (ITTOIA) and the Finance Act 2008.

20. Paragraph 12 amends section 14A(3)(b) of TGCA 1992 to clarify its meaning and mirrors the amendment to section 809T of ITA introduced by Paragraph 9 of this Schedule.

21. Paragraph 13 amends section 648 of ITTOIA 2005 by substituting new subsections (2) to (5) to clarify the interaction between the remittance basis and the settlements legislation.

22. Paragraph 14 amends paragraph 86 of Schedule 7 to Finance Act 2008 by inserting a new paragraph (4A) to ensure that the transitional provisions which prevent certain income which arises before 6 April 2008 from being taxed as a remittance if it is brought to the UK on or after that date operate as intended.

BACKGROUND NOTE

23. Individuals who are resident but not ordinarily resident or not domiciled in the UK can choose to use the remittance basis of taxation whereby they are required to pay UK tax on their offshore income and gains only to the extent which they are brought - or remitted - into the UK.

24. Section 25 and Schedule 7 of FA 2008 introduced significant changes to the remittance basis which came into effect from the start of the 2008-2009 tax year.

25. During the passage of Finance Bill 2008 the Government gave an undertaking that HM Treasury and HM Revenue & Customs officials would consult with external stakeholders following Royal Assent to review the legislation to ensure it operated as intended and to identify areas where it could be clarified or improved. The majority of the changes introduced in Finance Act 2009 arise from this consultation.

26. The Act also clarifies the definition of a relevant person and provides a statutory rule for determining the value of a remittance where property forming part of a larger set is remitted to the UK. Both changes are intended to prevent potential abuse of the remittance basis rules.

SECTION 52: EXEMPTION FOR CERTAIN NON-DOMICILED PERSONS

SUMMARY

1. Section 52 provides for an exemption from liability to income tax for certain individuals.

DETAILS OF THE SECTION

2. Paragraph (1) inserts a new Chapter 1A of Part 14 into the Income Tax Act 2007 (ITA).

3. New section 828A of ITA defines the individuals to whom the tax exemption applies as those who are resident but not domiciled in the UK in a tax year, who do not choose to use the remittance basis and who meet conditions A to F in new section 828B.

4. Section 828B sets out conditions which individuals must meet in order to qualify for the tax exemption.

5. New section 828C provides the mechanism for providing the income tax exemption.

6. New section 828D defines various terms for the purpose of for new Chapter 1A.

BACKGROUND NOTE

7. Individuals who are resident but not ordinarily resident or not domiciled in the UK can use the remittance basis of taxation whereby they are required to pay UK tax on their offshore income and gains only to the extent to which they are brought - or remitted - into the UK.

8. Section 25 of and Schedule 7 to the Finance Act 2008 introduced significant changes to the remittance basis, which came into effect from the start of the 2008-2009 tax year for that tax year and all subsequent tax years.

9. During the passage of Finance Bill 2008 the Government gave an undertaking that HM Treasury and HM Revenue and Customs officials would consult with external stakeholders following Royal Assent to review the legislation to ensure it operated as intended and to identify areas where it could be clarified or improved. The majority of the amendments introduced in Finance Act 2009 arise from this consultation.

10. The Act also clarifies the definition of a relevant person and provides a statutory rule for determining the value of a remittance where property forming part of a larger set is remitted to the UK. Both changes are intended to prevent potential abuse of the remittance basis rules.

11. This Section introduces a new income tax exemption for low-income employees working in the UK who meet certain conditions. Such individuals will typically be migrant workers employed in seasonal work in the agricultural or service sectors in UK and in other countries in the same tax year and whose overseas income is subject to tax where it is earned. Previously they were required to file a Self Assessment tax return, even in situations where there was no, or very little, tax to pay. This exemption removes that requirement in most cases.

SECTION 53 AND SCHEDULE 28: TAXABLE BENEFITS: CARS

SUMMARY

1. Section 53 and Schedule 28 provide for the following changes to car benefit from 2011-12:

   - the abolition of the price cap of £80,000 used in the calculation of the cash equivalent of the benefit of a car;
   - the lower threshold to be reduced by 5g/km from 130g/km to 125g/km of CO_2 emissions; and
   - a change to the appropriate percentage for electrically propelled cars from 15 per cent to 9 per cent.

DETAILS OF THE SCHEDULE

2. Paragraph 1 provides for amendments to Chapter 6 of Part 3 of the Income Tax (Earnings and Pensions) Act 2003 (ITEPA) which deals with the taxable car benefit.

Abolition of "price cap"

3. Paragraph 2 has the effect that the interim sum will no longer be capped at £80,000.

4. Paragraphs 3 to 5 make consequential amendments.

Reduction of lower threshold

5. Paragraph 6 substitutes a new table for the existing table in section 139(4) of ITEPA and sets the lower threshold at 125g/km for 2011-12 and subsequent tax years.

Electrically powered cars

6. Paragraph 7 is a simplification measure. It reduces the appropriate percentage in one step instead of two for electrically propelled cars first registered in or after 1998. The percentage set out in section 140(3) of ITEPA is amended from 15 per cent to 9 per cent. The appropriate percentage for these cars is currently 15 per cent but this is subject to a reduction of 6 per cent by regulation 4 of the Income Tax (Car Benefits) (Reduction of Value of Appropriate Percentage) Regulations 2001 (SI 2001/1123). The combination gives a net appropriate percentage of 9 per cent (15 per cent - 6 per cent). Regulation 4 will be revoked by secondary legislation before April 2011 to leave the net appropriate percentage for electric cars at its current value of 9 per cent.

7. Paragraph 8 makes a consequential amendment to section 142 of ITEPA, which covers cars registered before 1998. Sub-paragraph 8(a) removes the appropriate percentage for electrically propelled cars and substitutes a figure of 32 per cent for all other cars that are not within section 142(2) of ITEPA. The removal of the appropriate percentage for electrically propelled cars registered before 1998 reflects the fact that no such vehicles exist. Sub-paragraph 8(b) omits subsection 4 of section 142 of ITEPA, which defines electrically propelled cars, because this subsection is no longer required.

BACKGROUND NOTE

8. Where a company car is available for private use, a tax charge arises on the benefit in kind of the provision of the car. The employer calculates the benefit by reference to the list price and the CO_2 emissions of the car. The level of CO_2 emissions identifies the appropriate percentage, which starts at 15 per cent. This increases by 1 per cent for every increase in 5g/km of CO_2 emissions above the lower threshold up to a maximum of 35 per cent, subject to reductions given by regulations made by HM Treasury. The lower threshold is set in the legislation for the relevant tax year. In broad terms, the list price is then multiplied by the appropriate percentage to find the cash equivalent of the benefit.

9. To promote environmentally friendly driving, FA 2006 introduced a special lower appropriate percentage of 10 per cent for qualifying low emission cars effective from April 2008. These are cars that emit 120g or less of CO_2 per km driven.

10. A 3 per cent supplement is added to the appropriate percentage for diesel cars, though this is disregarded for cars approved to Euro IV emissions standards and registered before that standard became mandatory on 1 January 2006.

11. Reductions to the appropriate percentage apply for alternatively fuelled vehicles such as hybrids, bi-fuel and electric cars.

12. Currently, when calculating the cash value of the car benefit, the list price is capped at £80,000.

13. This section and Schedule make three main changes. Firstly, they abolish the price cap of £80,000 so that drivers of expensive company cars pay a fair amount of tax.

14. Secondly, they reduce the lower threshold from 130g/km to 125g/km of CO_2. This reduction means that the 15 per cent appropriate percentage will now apply to all company cars with CO_2 emissions between 121g and 129g/km. The reduction will come into force from 6 April 2011. Since the reforms to company car tax took effect in April 2002, the lower threshold has been set two years in advance. This is to provide certainty to employers and company car drivers when making decisions on new cars and to encourage car users to drive more environmentally friendly vehicles.

15. Thirdly, they simplify the way drivers of electrically propelled cars arrive at the appropriate percentage. Currently the percentage applicable to electrically propelled cars is 9 per cent, but this is achieved through a mix of primary and secondary legislation. Drivers of such cars will continue to pay tax on 9 per cent of the list price of the car, but this rate will in future be set out only in primary legislation.

SECTION 54: TAXABLE BENEFIT OF CARS: PRICE OF AUTOMATIC CAR FOR DISABLED EMPLOYEE

SUMMARY

1. Section 54 provides that disabled drivers of automatic cars who hold a disabled person's badge (blue badge) are entitled to use the list or notional price of an equivalent manual car instead of the list or notional price of the automatic car they actually drive, when computing the car benefit charge.

DETAILS OF THE SECTION

2. Subsection (2) provides for a consequential amendment of section 116(3) of the Income Tax (Earnings and Pensions) Act 2003 (ITEPA).

3. Subsection (3) provides for a consequential amendment of section 121(1) of ITEPA.

4. Subsection (5) inserts a new section 124A after section 124. The new provision concerns the computation of the benefit charge based on an equivalent manual car where an automatic car is provided for a disabled employee. In particular, section 124A(3) sets out how the equivalent manual car is to be identified, and section 124A(4) defines an automatic car.

5. New section 124A(5) clarifies when, for the purposes of this section, a car is available to an employee. It confirms that the car needs to be made available to the employee by reason of the employee's employment but without the car being transferred to the employee.

BACKGROUND NOTE

6. Currently where a company car is made available to an employee for private use, a tax charge arises on the benefit in kind of the availability of the car. In almost every case, the employer calculates the benefit by reference to the list price and the CO_2 emissions of the car. The same method is used for all drivers, regardless of any disability the driver might have.

7. However, for disabled drivers there are currently a number of targeted measures within company car tax in recognition of the fact that, because of their disability, they might need to drive a car with a higher benefit charge than would otherwise be the case. For example:

- subject to certain conditions, the cost of accessories provided for disabled drivers is excluded from the calculation of the company car benefit (section 125(2)(c) of ITEPA); and

- drivers who hold a disabled person's badge and who have to use automatic company cars are able to use the CO_2 figure for the equivalent manual car in the calculation of the benefit where this is lower than that of the automatic car they actually drive (section 138 of ITEPA).

8. This new measure extends the existing legislation in section 122 on "the price of the car" to allow disabled drivers holding a disabled person's badge (blue badge) to use the list or notional price of an equivalent manual car to work out the benefit charge instead of the list or notional price of the automatic car they actually drive, where this is to their advantage.

9. The objective of this measure is to remove a tax disadvantage that certain disabled company car drivers suffer because they need to drive automatic cars on account of their disability.

10. This change brings the method used to determine the price of the car into line with the method used to determine the CO_2 emissions. From 2009-10, where the disabled driver has to drive an automatic because of their disability, the CO_2 emissions figure and list or notional price of an equivalent manual car can be used to calculate the car benefit. This is consistent with the Government's wider objectives of supporting the disabled.

SECTION 55: EXEMPTION OF BENEFIT CONSISTING OF HEALTH-SCREENING AND MEDICAL CHECK-UP

SUMMARY

1. Section 55 amends sections 266(3) and 267(2) of the Income Tax (Earnings and Pensions) Act 2003 (ITEPA) and inserts a new section 320B into the Act. The effect of these changes is to exempt from tax the provision to employees of one health-screening and one medical check-up each year. They also exempt from tax the provision of a non-cash voucher or credit-token used to facilitate the provision of such health-screening assessment or a medical check-up.

DETAILS OF THE SECTION

2. Subsection (2) amends section 266(3) of ITEPA which sets out a list of tax exempt benefits in respect of which the provision of a non-cash voucher does not give rise to tax liability under Chapter 4 of Part 3 of ITEPA. Subsection (2) amends this provision by adding a new sub-paragraph (g) covering health-screening assessments and medical check-ups that meet the conditions laid down in the new section 320B. The effect of this is to remove the tax charge that would otherwise arise where the employer arranges for the provision of these medicals by means of non-cash vouchers.

3. Subsection (3) amends section 267(2) of ITEPA. Section 267(2) sets out a list of tax exempt benefits in respect of which the provision of credit tokens does not give rise to tax liability. Subsection (3) amends this provision by adding a new sub-paragraph (i) covering health-screening assessments and medical check-ups that meet the conditions laid down in the new section 320B. The effect of this is to remove the tax charge that would otherwise arise where the employer arranges for the provision of these medicals by means of credit tokens.

4. Subsection (4) inserts new section 320B into ITEPA. New section 320(B)(1) exempts from tax the provision to an employee of one health-screening assessment and one medical check-up. New section 320B(2) restricts the exemption to one health-screening assessment and one medical check-up provided by an employer in a tax year. Where the employee has more than one employer at the same time, the tax exemption will only apply to one health-screening assessment and one medical check-up provided by any of them.

BACKGROUND NOTE

5. It had long been the stated practice of HM Revenue & Customs (HMRC) that where an employer provides their employees with a periodic health-screening or a medical check- up it should not be considered a taxable benefit.

6. HMRC introduced the Income Tax (Exemption of Minor Benefits) (Amendment) Regulations 2007 (SI 2007/2090) to formally exempt from tax the provision of health-screening and medical check-ups that are made available by employers to all their employees. However, the power that was exercised to introduce these regulations contained a restriction that meant that for the exemption to apply the medical had to be generally available to all employees on similar terms.

7. HMRC accepts that SI 2007/2090 could adversely affect the tax-free status of check-ups provided by some employers to less than the full workforce (for example only to staff in a particular age group) for good medical or business reasons. This section meets this difficulty by exempting from tax the provision of one health-screening assessment and one medical check-up in any tax year but without the condition requiring these medicals to be offered to all employees. This means that where an employer restricts qualifying health assessment screenings or medical check-ups to part of the workforce they will be exempt from tax. The section also exempts from tax non-cash vouchers and credit tokens provided for qualifying health-screenings and medical check-ups. By virtue of the Income Tax (Exemption of Minor Benefits) (Revocation) Regulations 2009 (SI 2009/695), SI 2007/2090 will cease to have effect once this Section is enacted (with or without modifications).

SECTION 56: MEPS' PAY, ALLOWANCES AND PENSIONS UNDER EUROPEAN PARLIAMENT STATUTE

SUMMARY

1. Section 56 extends the application of "double taxation relief" under the Income and Corporation Taxes Act 1988 (ICTA) to European Community tax deducted from the pay, transitional allowances and pensions of members of the European Parliament (MEPs) under the new Statute for Members of the European Parliament (2005/684/EC, Euratom). The section also amends the Income Tax (Earnings and Pensions) Act 2003 (ITEPA) to provide that payment of transitional allowances to MEPs under the Statute will be treated as termination payments in line with the current treatment of other, similar payments.

DETAILS OF THE SECTION

2. Subsection (1) provides that Part 18 of ICTA (double taxation relief) will apply to tax paid for the benefit of the European Communities on certain types of income under the Statute as if it were payable under the law of a territory outside the UK.

3. Subsection (2) provides for the amendment of section 291 of ITEPA (termination payments to MPs and others ceasing to hold office) by treating payments of transitional allowances under the Statute in the same way as termination payments to MEPs under the similar, existing scheme under the European Parliament (Pay and Pensions) Act 1979.

BACKGROUND NOTE

4. By decision of the European Parliament, the Statute for members of the European Parliament (2005/684/EC, Euratom) has been adopted. It sets out common pay and conditions for MEPs effective from the first European Parliament following elections in 2009. Newly-elected MEPs will be subject to the pay and conditions defined in the Statute although those re-elected may choose to retain their existing remuneration package.

5. The consequence of the new salary payment regime is that Members of the European Parliament will be paid by the European Community, which will be subject to tax by the Community ("tax for the benefit of the communities"). Those members who are UK resident for tax purposes will also be liable for UK tax on their earnings.

6. The normal method for relieving this kind of double tax is to give credit for the tax suffered in the overseas jurisdiction by way of a "double tax treaty". However, because the UK does not have a double tax treaty with the European Community, the double tax cannot be relieved in this way.

7. However, the UK can give credit for double taxation suffered unilaterally where a treaty is not in existence or the treaty does not help with the specific income in point.

8. The issue and therefore the need for this section is that section 790(4) of ICTA refers to "credit for tax paid under the law of the **territory** outside of the United Kingdom". As the European Community is not a "territory", legislation is needed to extend this provision to the European Community.

9. Therefore when an MEP's salary is taxed by the European Community and (to the extent the MEP is UK resident) the UK, this section will extend Part 18 of ICTA and allow the MEP to claim credit relief (against the MEP's UK tax liability) for the tax paid in the European Community.

10. The section also provides that payments of transitional allowance under the Statute will be treated as termination payments from 6 April 2009, thereby bringing their tax treatment into line with that of the similar resettlement grants payable under the existing arrangements for MEPs as well as payments to Westminster MPs and members of the devolved assemblies and the greater London Assembly under similar, existing schemes.

SECTION 57: TAX UNDERLYING DIVIDENDS

SUMMARY

1. Section 57 amends the definition of the rate that applies to the "mixer cap" in section 799(1)(b) and (1A) of the Income and Corporation Taxes Act 1988 (ICTA), so that it reflects the rate of tax applicable to a foreign dividend. This change will ensure that the "mixer cap" will work in the same way as it always has, and that its application will not be affected by the recent change in the corporation tax (CT) rate.

DETAILS OF THE SECTION

2. Subsection (2) amends the definition of the mixer cap rate at section 799(1A) so that the mixer cap rate matches the actual or, as the case may be, average corporation tax rate applicable to the profits of the company receiving the dividend for the period of receipt.

3. Subsection (4) amends section 801(2) so that the mixer cap rate applied at each lower tier of a dividend chain is applied according to the CT rate applicable to the profits of the company for the period in which the dividend referred to in Section 801(1) is received.

4. Subsection (5) amends the version of section 799(1A) set out in subsection 801(2B) in the same way as subsection (2) of this section.

BACKGROUND NOTE

5. In general, UK companies are taxed on all of their income or chargeable gains no matter where they arise, but where the income has a foreign source Part 18 of ICTA provides relief for double taxation that may arise as a result of tax due in both jurisdictions.

6. Where a dividend is received from a foreign company, relief is available for foreign taxes paid directly on that dividend and, in certain circumstances, for tax paid on the profits out of which the dividend is paid. The latter is referred to as "underlying tax". Apart from dividends from St Kitts and Burma, the latter relief is available only to companies and the amount is subject to a limit imposed by the "mixer cap".

7. The purpose of the mixer cap is to limit the relief for underlying tax suffered by reference to the amount of CT due on the foreign dividend. The mixer cap has always worked in this way, but the lowering of the CT rate for the financial year 2008 created an anomaly. It became clear that the mixer cap could operate in such a way as to limit double taxation relief beyond the amounts intended by the original mixer cap legislation.

8. The proposed changes apply only to companies and ensure that the mixer cap will continue to apply as intended, and as it would have done had the CT rate not been changed. The amount of relief available to companies will not now be limited by the unintended consequences of the interaction between the operation of the mixer cap and the change in the rate of CT.

9. To ensure that the mixer cap never applies at a rate lower than the effective rate applying to a dividend, the changes generally have retrospective effect from 1 April 2008. To limit potential disadvantages, the change made by subsection (4) has effect from 22 April 2009.

SECTION 58 SCHEDULE 29: MANUFACTURED OVERSEAS DIVIDENDS

SUMMARY

1. Section 58 and Schedule 29 contain provision to counter avoidance of corporation tax involving manufactured overseas dividends (MODs).

DETAILS OF THE SCHEDULE

2. Paragraph 1 amends Schedule 23A of the Income and Corporation Taxes Act 1988 (ICTA), which contains provision for the corporation tax treatment of manufactured payments. The amendments ensure that the borrower under a debtor repo (sale and repurchase agreement) is not able to claim relief for overseas tax in excess of the amount of tax actually borne.

3. Paragraph 1(2) amends paragraph 4(4) of Schedule 23A, which treats a company that receives a MOD as receiving it after deduction of overseas tax.

4. Sub-paragraph (3) inserts new sub-paragraph 4A after paragraph 4 of Schedule 23A.

5. New paragraph 4A(1) introduces a new rule for determining the amount of overseas tax treated as suffered where a MOD is treated as paid under paragraph 13(1) of Schedule 13 to Finance Act (FA) 2007 (requirement to deduct tax from manufactured payments). Paragraph 13(1) of Schedule 13 applies where an overseas dividend is paid during the period of a creditor repo and requires the "lender" under that repo to account for income tax under section 922(2) of the Income Tax Act 2007 (ITA) as if it had paid a MOD to the original holder of the securities at the time the dividend is payable. The new rule provides that the recipient shall be treated as if the MOD were received after deduction of tax of amount A.

6. New paragraph 4A (2) provides that amount A may be one of three amounts:

- where sub-paragraph (3) applies it is the amount of tax deducted under section 922(2) of the ITA. This is the same as the current rule in paragraph 4(4) of Schedule 23A;

- where sub-paragraph (4) applies it is the amount deducted under section 922(2) less the excess of the actual amount of MOD payment over the amount deducted under section 922(2) of ITA; and

- in any other case it is nil.

7. New paragraph 4A(3) applies where a MOD is actually paid to the recipient and it equals the relevant net amount. The relevant net amount is the gross amount of the real overseas dividend less any tax which must be deducted under section 922(2) of ITA. So if the gross amount of the dividend were 100 and the amount of tax deducted under section 922(2) were 15 then the relevant net amount would be 85.

8. But new paragraph 4A(3) does not apply where it is reasonable to assume that, in deciding the repurchase price of the securities, account was taken of the amount of the MOD actually paid. Thus, it will not apply if the repurchase price is lower than it would be if the price reflected only the finance return implicit in the repo so that in substance a MOD greater than the relevant net amount is paid by the dividend manufacturer.

9. The language used here is similar to that formerly used in section 737A(2)(d) of ICTA 1988 (deemed manufactured payments under certain repo arrangements) before its repeal for corporation tax purposes in 2007.

10. New paragraph 4A(4) applies where a MOD is actually paid to the recipient and it exceeds the relevant net amount. In such a case the overseas tax is reduced by the excess. The effect is that if the gross amount of the dividend were 100, the amount deducted under section 922(2) of ITA were 15, but the actual MOD paid was 90 then the overseas tax would be treated as 10. This reflects the fact that in substance only 10 of overseas tax is economically borne by the recipient.

11. But new paragraph 4A(3) does not apply where it is reasonable to assume that, in deciding the repurchase price of the securities, account was taken of the amount of the MOD actually paid.

12. New paragraphs 4A(5) and (6) provide that the "repurchase price of the securities" means the price at which the payer of the MOD is entitled or obliged to sell the securities back to the recipient of the MOD, and that securities for this purpose means the securities in respect of which the MOD is paid.

13. New paragraph 4A(7) defines "relevant net amount" as the excess of the gross amount of the overseas dividend (as determined under paragraph 4(5) of Schedule 23A) less the amount of tax required to be deducted under section 922(2) of ITA.

14. Paragraph 2 provides that where a person receives a MOD by virtue of 736B of ICTA (deemed MODs in the case of certain stocklending arrangements) then the recipient is not treated as suffering overseas tax. This change to the rules for stocklending simply aligns those rules with the new position for repos.

15. Paragraph 3 gives the commencement rule. The legislation applies in relation to overseas dividends paid on or after 22 April 2009.

BACKGROUND NOTE

16. The current manufactured overseas dividend (MOD) rules and regulations aim to give the recipient of a MOD (or any payment deemed to be a MOD) the same relief for foreign tax as the recipient of the real dividend. The amendment ensures that no relief is given by way of a credit or deduction where the recipient of a MOD has not borne the economic cost of the foreign tax.

17. The measure will counter a complex tax-driven scheme which involves the sale and repurchase (repo) of a foreign shareholding between two group companies. Part of the repo agreement involves what is in substance the obligation to pay an amount that represents an overseas dividend. The MOD rules apply to this deemed payment and although the recipient receives an amount representing the full amount of the overseas dividend without any deduction of foreign tax, it nonetheless claims an entitlement to a deduction for the foreign tax.

SECTION 59: DOUBLE TAXATION: PAYMENTS MADE BY REFERENCE TO FOREIGN TAX

SUMMARY

1. Section 59 deals with situations where double taxation relief is claimed for foreign tax but, by reference to that tax, a payment is made by a tax authority to either the claimant or a connected person. The section limits the relief to the amount of the foreign tax paid minus the payment made to the claimant or connected person.

DETAILS OF THE SECTION

2. Subsection (2) introduces a new section 804G into the Income and Corporation Taxes Act 1988 (ICTA). The new section provides for the credit for foreign tax to be reduced by the amount of any payment made by a tax authority to the claimant or a person connected with the claimant by reference to the foreign tax.

3. New section 804G(1) will apply if credit falls to be allowed for foreign tax to any person and a payment is made by a tax authority to that person, or to any connected person, by reference to the foreign tax. In such cases, the amount of the credit is to be reduced by an amount equal to that payment.

4. Subsections (3) to (7) make consequential changes to section 806 of ICTA, which gives the time limits for claims for credit in respect of foreign tax. Section 806(2) allows a claim to be made or amended at any time if the amount of foreign tax is varied and requires taxpayers who have made a claim for credit to advise HMRC if the amount of foreign tax is subsequently reduced. The amendments ensure that section 806 applies to a payment as described in section 804G(1) as it does to a repayment of foreign tax.

5. Subsection (9) introduces new subsections (3A) and (3B) into section 811 of ICTA. Section 811 allows deductions from taxable profit to be made for foreign tax.

6. New subsection (3A) will apply if income of a person has been reduced under section 811(1) by any sum and a payment is made by a tax authority to that person, or to any connected person, by reference to the foreign tax. In such cases, the amount of that person's income is to be increased by an amount equivalent to that payment.

7. Subsections (10) to (12) make consequential amendments to subsections (4) to (8) of section 811. Subsections (4) to (8) provide that if the foreign tax is reduced a corresponding adjustment to the amount of income may be made at any time. A taxpayer who deducts foreign tax from income must advise HMRC by notice if the amount of tax is subsequently reduced. The effect of the amendments is that section 811(4) to (8) also apply where a payment as described in new subsection (3A) is made.

8. The term "connected person" throughout the section is defined by reference to section 839 ICTA.

9. Subsection (13) provides that the provisions in the section will have effect in relation to payments that are made on or after 22 April 2009.

BACKGROUND NOTE

10. The UK believes it is important for business operating internationally that relief for double taxation should be available. But where credit is claimed for foreign tax and a payment is made by a tax authority either to that person or to a connected person by reference to that tax then relief should be restricted to the net amount.

11. This section will therefore limit the relief given to the amount of the foreign tax paid minus the payment made by a tax authority.

SECTION 60: DOUBLE TAXATION RELIEF ANTI-FRAGMENTATION

SUMMARY

1. Section 60 amends two of the rules contained in legislation introduced in Finance Act 2005 to limit the credit for foreign tax paid on trade receipts of a bank or a company associated with a bank to no more than the corporation tax arising on the relevant part of the trade profits. The clause ensures that, in calculating the amount of double taxation relief (DTR) available, a) a reasonable proportion of a bank's notional funding costs over all its transactions must be deducted, and that this cannot be avoided by the bank allocating a specific source of funds to specific transactions and b) clarifies the existing legislation that prevents banks avoiding the intention of the DTR legislation by artificially arranging for income to be received by a non-banking company in the bank's group.

DETAILS OF THE SECTION

2. Subsections (1) and (2) amend section 798A of the Income and Corporation Taxes Act 1988 (ICTA) by introducing after section 798(3) new subsections (3A), (3B) and (3C) to limit the amount of the DTR for foreign tax paid on trade receipts.

3. The new subsection (3A) applies new subsection (3B) to banks and companies connected with banks which have not taken into account a reasonable apportionment of their funding costs in calculating their allowable double taxation relief.

4. Subsection (3B) requires that the allowable deductions and expenses, a reasonable apportionment of which is required to be deducted under section 798A(3) (a), (b) and (c), include a bank's notional funding costs.

5. Subsection (3) defines the expressions used in subsections (3A) and (3B).

6. Subsections (3) and (4) amend section 798B of ICTA by inserting after section 798B(4) new subsections (4A), (4B) and (4C). These subsections will ensure that where there is an avoidance scheme which arranges for an item of income to be received by an investment company for the purpose of avoiding the effect of section 798A, then provided it is reasonable to suppose that the receipt would have been a trade receipt if it had been received by a connected company, it will be treated as trading income for the purposes of calculating DTR.

7. The amendments will have effect in relation to credits for foreign tax which relate to payments of foreign tax or income received in respect of which foreign tax has been deducted on or after 22nd April 2009.

BACKGROUND NOTE

8. Section 798A of ICTA alters the way that section 797(1) limits the allowance of credit for foreign tax against corporation tax in respect of trade income. It limits the amount of the credit for foreign tax paid on trade receipts to no more than the corporation tax arising on the relevant part of the trade profits.

9. It does this by requiring companies to deduct direct expenses and a reasonable proportion of their allowable deductions and expenses which include overheads when calculating the amount of profit attributable to the foreign tax and hence the amount available to credit against their corporation tax.

10. Where the taxpayer is not a bank or a company connected with a bank, there is no change to the existing legislation but the new legislation puts it beyond doubt that banks and companies connected with banks will be required to include their funding costs within these deductions and expenses.

11. The existing section 798B(4) counters the use of avoidance schemes by banks which attempt to avoid the requirement to deduct overheads and expenses by artificially diverting trading income into investment subsidiaries which are not subject to the same requirement. The new clause clarifies the existing rule and puts it beyond doubt that from 22 April 2009, where there is an avoidance scheme or arrangement, any item of income which it is reasonable to assume would be trade income if received by a bank will be treated as trade income of the investment subsidiary.

SECTION 61 AND SCHEDULE 30: FINANCIAL ARRANGEMENTS AVOIDANCE

SUMMARY

1. Section 61 and Schedule 30 contain provision to counter avoidance involving certain financial arrangements.

DETAILS OF THE SCHEDULE

Paragraph 1: Interest payments: arrangements appearing very likely to produce post-tax advantage

2. Paragraph 1 of the Schedule inserts new section 384A into the Income Tax Act 2007 (ITA). This is headed "Restriction on relief where arrangements minimise risk to borrower"

3. New subsection (1) of section 384A provides that relief will not be available for interest paid by a person on a loan if the loan is made as part of arrangements which appear very likely to produce a "post tax advantage" and the arrangements seem to have been designed to reduce any income tax or capital gains tax to which the borrower (or someone like the borrower) would be liable apart from the arrangements.

4. Subsection (2) provides that arrangements appear very likely to produce a post-tax advantage if one might reasonably assume there is no more than an insignificant risk of a 'post-tax advantage' not being produced.

5. This is a two-part test. It is firstly necessary to ascertain whether, within the meaning of the legislation, it is very likely that the incomings from the arrangements will exceed the outgoings on an after-tax basis. If that is the case then it is also necessary to ascertain whether the arrangements seem to have been designed to reduce income tax or capital gains tax liability that would have arisen independently of the arrangements. Subsection (10) explains in what circumstances arrangements are to be treated as designed to do this.

6. Subsection (3) defines what is meant by 'produce a post-tax advantage'. It means that the arrangements will produce an amount payable to the borrower or a connected person (or to someone else for the benefit of the borrower or person connected with the borrower) of an amount (or aggregate amount) that after making the appropriate tax adjustments is at least equal to the aggregate of the amount needed to meet the borrower's obligations (in respect of interest and principal) under the loan and any capital that the borrower has invested from his own resources. Where the loan is a limited recourse one the obligations may vary according to the results of the business in which it is invested.

7. "Appropriate tax adjustment" is defined in subsections (8) and (9). The adjustment ensures that the value of the tax relief for the interest (due apart from the new rule) is taken into account in determining the amount payable to the person (and that additional tax payable by the person as a result of the arrangements is also taken into account).

8. This is intended to ensure that relief for interest is not available in any case where there is no more than an insignificant risk that the payments to which the wider scheme arrangements give rise will not produce a profit. The new measure will thus deny relief for interest if the loan is made as part of arrangements that are certain (ignoring insignificant risk) to produce a post-tax surplus for the investor by virtue of the interest being eligible for relief, provided that the arrangement seems designed to reduce tax to which the borrower would been liable apart from the arrangements. The legislation will not catch genuine commercial investments in business where there is significant uncertainty as to whether the level of return will secure a post-tax surplus for the investor.

9. Subsections (5) and (6) are anti-falsifying provisions. They ensure that the legislation will still apply if the arrangements include provision to secure that in the event of a post-tax advantage not being produced an amount not significantly less will still arise. Thus, the legislation would still apply if the arrangements gave rise to a say 30 per cent (more than insignificant) chance of a post tax advantage not being produced if in that event the investor is still certain to receive an amount not significantly less. This reflects the fact that an avoider may be willing to live with significant risk of a trivial loss if the alternative outcome is a significant post-tax profit.

10. Subsection (7) ensures that a sum is treated as payable to a person if that person directly or indirectly receives the benefit of any asset. In any such case, the sum treated as payable to the person is equal to the value of the asset.

11. Subsection (8) explains how to make the "appropriate tax adjustments" for the purpose of subsection (3) or (6). If "A" exceeds "B" the excess is to be deducted from the amount produced. If B exceeds A the excess is to be added to the amount produced.

12. Subsection (9) defines "A" and "B". "A" is the amount of any income tax, capital gains tax or tax under the law of a territory outside the UK to which the borrower becomes liable as a result of the arrangements. "B" is the aggregate amount by which the borrower's liability to income tax and capital gains tax would be reduced in consequence of the arrangements. This includes but is not limited to reduction in tax resulting from a claim under the interest relief provisions. For this purpose A and B are each to be computed independently of the other and it is to be assumed that relief for the interest is not blocked by subsection (1).

13. Subsection (10) explains that arrangements seem very likely to have been designed to reduce any tax liability that would arisen independently of the arrangements if and only if it would be reasonable to assume from all or any relevant circumstances that the arrangements or any part of then were so designed. This would, for instance, apply if the scheme is a marketed one and the marketing literature indicates that the arrangements are intended to reduce tax liability that would arise independently of the scheme.

14. Subsection (12) defines "related transaction" as a transaction that it would be reasonable to assume would not have been entered into or effected independently of the arrangements. Thus, a hedging agreement would be a related transaction in

relation to a borrowing or investment if it would be reasonable to assume that the hedge would not have been taken out apart from the loan or investment. Similarly, anything that produces sums payable to or for the benefit of the borrower will be taken into account in determining whether a "post-tax advantage" arises provided that this is linked to the arrangements.

15. Much of the wording in the new section is taken from the "guaranteed return provisions" in sections 559 to 566 of the Income Tax (Trading and Other Income) Act 2005 (previously Schedule 5AA to the Income and Corporation Taxes Act 1988 (ICTA)).

16. Paragraph 1(2) provides that the amendment has effect in relation to interest paid on or after 19 March 2009.

Paragraphs 2 and 3: amounts not fully recognised for accounting purposes

17. Paragraph 2(1) amends section 311 of the Corporation Tax Act 2009 (CTA) (loan relationships: amounts not fully recognised for accounting purposes). Section 311 deals with cases where a company is, or is treated as being party to a creditor loan relationship as respects which the company does not fully recognise all amounts in its accounts. Where the section applies the company is required to recognise for tax purposes the full amount of the credits and debits on the loan relationship.

18. Sub-paragraph (2)(a) inserts a new Condition C into section 311 so that it now applies where Condition A, B or C (not just A or B) is met.

19. Sub-paragraph (2)(b) amends section 311(2) so that it applies where an amount is not fully recognised as a result of the application of generally accepted accounting practice (GAAP) to the creditor relationship and either the relevant debtor relationship (Condition A), relevant capital contribution (Condition B) or relevant securities (new Condition C).

20. Sub-paragraph (3) amends section 311(3)(b) (Condition A) so that it refers to "the creditor relationship and debtor relationship". This is to put it beyond doubt that non-recognition of amounts in respect of the creditor relationship must be the consequence of the non-recognition of amounts in respect of the linked debtor relationship. Thus, the fact that in accordance with GAAP an amount is not recognised in respect of an unrelated debtor relationship – for instance, one used in a hedging arrangement – would not result in amounts in respect of that unrelated relationship having to be fully recognised. This reflects existing practice.

21. Sub-paragraph (4) amends section 311(4)(b) so that a similar linkage is required in respect of Condition B (capital contribution) cases.

22. Sub-paragraph (5) inserts new Condition C. This is that the company has issued securities that form part of its capital (whether or not the issuer has received cash for their issue) and an amount is not fully recognised in respect of the application of GAAP to the securities and the creditor relationship. Condition C responds to new avoidance disclosures that seek to work around section 311.

23. Sub-paragraph (6) makes a consequential amendment to section 311(6) so that in determining whether an amount is fully recognised for the purposes of section 311 regard can now be had to any securities issued by the company within sub-paragraph (5).

24. Sub-paragraph (7) provides that section 311 and 312 (amounts not fully recognised for accounting purposes) are added to the list of tax provisions that must be taken into account in calculating the carrying value of a loan relationship for the purposes of section 317(5).

25. Sub-paragraph (8) contains the commencement rule: except where sub-paragraph (9) applies the amendments have effect in relation to periods of account beginning on or after 22 April 2009.

26. Sub-paragraph (9) provides that where a period of account begins before but ends on or after 22 April the amendment operates as if one period of account ended just before that date and the other commenced on that date. This means the amendments made by paragraph 2 apply immediately in relation to the new deemed period of account (so that an immediate credit may crystallise).

27. Paragraph 3 inserts new sections 599A and 599B into Part 7 of CTA (derivative contracts). These largely reproduce for derivative contract purposes the loan relationship rules in section 311 and 312 of CTA. They thus require full tax recognition of profits and losses in respect of a company's derivative contracts.

28. New section 599A is modelled on section 311. Section 599A(1) states that section 599B will apply for determining the debits and credits to be brought into account by a company in respect of its derivative contracts where the circumstances are as set out in section 599A(2).

29. New section 599A(2) sets out the case. A company is or is treated as party to a derivative contract and an amount is not fully recognised in respect of the derivative contract as a result of the application of GAAP to the contract and either a relevant capital contribution (Condition A) or securities issued by the company (Condition B).

30. New section 599A(3) specifies that Condition A is that an amount has been contributed to the company that forms part of its capital and an amount is not fully recognised in respect of the contribution as a result of the application of GAAP to the contribution and the contract in question.

31. New section 599A(4) is similar to section 311(5) and provides it is not necessary for an amount to form part of a company's share capital for it to be treated as a contribution to the capital of the company.

32. New section 599A(5) specifies that Condition B is that the company has issued securities that form part of its capital and an amount is not fully recognised in respect of the securities as a result of the application of GAAP to the securities and contract.

33. Section 599A(6) states that an amount is not fully recognised in respect of a contract, contribution or securities if no amount is recognised in respect of it or if amounts in respect of it are only partially recognised.

34. New section 599B(1) provides that where section 599A applies, the debits and credits to be brought into account must be determined in accordance with subsection (2).

35. Subsection (2) says that an amount in respect of the whole of the contract must be brought into account.

36. Subsection (3) provides that the debits and credits brought into account by virtue of section 599B must be determined on a fair value basis of accounting.

37. Subparagraph (2) provides that sections 599A and 599B (amounts not fully recognised for accounting purposes) are added to the list of tax provisions that must be taken into account in calculating the carrying value of a derivative contract for the purposes of section 702(3).

38. Sub-paragraph (3) contains the commencement rule: except where sub-paragraph (4) applies the amendments have effect in relation to periods of account beginning or after 22 April 2009.

39. Sub-paragraph (4) provides that where a period of account begins before but ends on or after 22 April the amendment operates as if one period of account ended just before that date and the other commenced on that date. This means the amendments made by paragraph 3 apply immediately in relation to the new deemed period of account (so that an immediate credit may crystallise).

Paragraph 4: Loan relationships involving connected debtor and creditor where debits exceed credits

40. Paragraph 4(1) amends section 418 of CTA (loan relationships treated differently by debtor and creditor). Section 418 was introduced in 2008 to block schemes that involved the provision of intra-group finance through the use of convertible securities. In these schemes the debtor company sought to bring into account larger debits than the creditor's credits as a result of the adopting of differing accounting methods in relation to the securities.

41. Sub-paragraph (2) substitutes a new section 418(1)(b). This replaces the existing Conditions A to C in section 418 with two new conditions A and B. Both conditions must be met (as well as the requirement in section 418(1) that debtor and creditor are connected) in order for the legislation to apply.

42. New subsection (2) specifies that Condition A. is that the rights under the loan relationship specified in section 418(1) include provision by virtue of which the creditor company is or may become entitled or be required to acquire (whether by conversion or otherwise) any shares in any company. This is similar to the language used in section 92 of the Finance Act (FA) 1996 before its repeal in 2005.

43. New subsection (3) specifies that Condition B is that the debits brought into account by the debtor under Part 5 of CTA in respect of the debtor relationship exceed the credits brought into account by the creditor as respects the creditor relationship when looked at for the corresponding accounting period. This test is carried out without reference to any credits the creditor may be required to bring into account under section 418.

44. The effect of new Conditions A and B is that section 418 now applies to all forms of intra-group convertible debt, not just those where the debtor divides the loan between debt and a derivative financial instrument/equity.

45. Paragraph 4 (4) inserts new subsections (6A) to (6C) into section 418.

46. New subsection (6A) provides that for the purposes of section 418 the creditor company is to be treated as party to a loan relationship notwithstanding that it has transferred those rights under a repo or stock loan (or where the transfer is by way of security under a mortgage within section 26 of the Taxation of Chargeable Gains Act 1992). This responds to avoidance disclosures that seek to disapply the legislation by means of such transactions.

47. New subsection (6B) provides that the creditor company is to be treated as remaining party to the relationship in any case not within subsection (6A) where the company disposes of the relationship with the "relevant avoidance intention".

48. New subsection (6C) defines the relevant avoidance intention as the intention of eliminating or reducing the credits to be brought into account for the purposes of Part 7.

49. Paragraph 4(5) amends subsection (7) of section 418 so that section 418A (as well as section 418) supplements section 419.

50. Paragraph 4(7) introduces new section 418A into CTA. This section ensures that the amendments made to section 418 do not prevent that section applying clearly in cases where convertible debt is in accordance with GAAP treated as divided between a host contract and a derivative financial instrument or equity instrument.

51. New section 418A(1) provides that the section applies where the debtor or the creditor company in accordance with GAAP treats the rights and liabilities under the loan as divided between rights and liabilities under a loan relation (" host contract") and a derivative financial instrument or equity instrument.

52. New section 418A(2) provides that where the debtor treats the rights and liabilities under the loan relationship in accordance with subsection (1), section 418 shall apply as if the references in section 418(3)(a) to the loan relationship were to the host contract (that is, the part of the actual loan relationship that is treated by the debtor as a loan for accounting purposes).

53. New section 418A(3) provides that where the creditor treats the rights and liabilities under the loan relationship in accordance with subsection (1), section 418 shall apply as if the references in section 418(3)(b) to the loan relationship were to the host contract (that is, the part of the actual loan relationship that is treated by the creditor as a loan for accounting purposes).

54. Paragraph 4(8) provides that the amendments have effect for debits and credits arising on or after 22 April 2009.

Paragraph 5: Credits and debits for manufactured interest

55. Paragraph 5 inserts additional wording into the rules dealing with manufactured interest payments made by companies to clarify that the payer or recipient of such amounts is generally to be taxed on them only to the extent that they are recognised in accordance with GAAP.

56. Sub-paragraph (1) inserts at the end of section 540(3) of CTA (manufactured interest treated as interest under a loan relationship for accounting periods ending on or after 1 April 2009) wording that ensures that the credits and debits to be brought into account by a payer or recipient of manufactured interest are those that are recognised under GAAP. This is subject to any other provision in the rules in Part 5 (loan relationships) or the manufactured payment unallowable purpose rule in paragraph 7A of Schedule 23A to ICTA overriding GAAP.

57. Sub-paragraph (2) inserts equivalent wording into section 97(2) of FA 1996, which is the pre-CTA version of section 540(3) of CTA for periods ending before 1 April 2009.

58. Sub-paragraph (3) contains the commencement rule, which is that it is generally to apply in relation to manufactured interest whenever paid. However, the inserted wording will not apply to manufactured interest which is treated by section 737A(5) of ICTA as paid before 27 January 2009.

BACKGROUND NOTE

Paragraph 1:

59. The interest relief rules encourage investment in certain small businesses carried on commercially and with a view to profit. The return on a normal investment in such a business would not be a guaranteed one such that after deducting obligations under the loan from sums to which the investment gives rise the investor was certain to be able to exit with a profit. But in schemes notified to HM Revenue & Customs (HMRC), arrangements are in place that mean that after the availability of the interest relief for the interest is taken into account the investor cannot fail to make a profit.

60. The new measure will deny relief for interest if the loan is paid as part of an arrangement that is certain (ignoring insignificant risk) to allow the investor to exit the arrangement with more money than was originally invested. It will not affect genuine commercial investments in business where there is uncertainty as to the return that will be produced from the arrangements.

Paragraphs 2 and 3:

61. Section 595 of CTA provides that the amounts to be brought into account for the purposes of derivative contracts rules in Part 7 of CTA are those that, in accordance with GAAP, are recognised in determining a company's profit or loss for the period.

62. In certain circumstances, where a derivative contract of a company is matched with shares or similar securities issued by it then it may be permissible under GAAP for the contract or amounts arising in respect of the contract not to be recognised in determining the company's accounting profits or losses for the period.

63. It is HMRC's view that such non-recognition or de-recognition is not observed for tax purposes where the accounting treatment does not fairly represent the profits. But sections 599A and 599B codify the treatment, and prevent companies arguing that where a receipt under a derivative contract is matched with the payment of a dividend on "liabilities", there is no net liability to tax, even though no deduction is due for the dividend under the Corporation Tax Acts.

Paragraph 4:

64. In FA 2008, the Government acted to block a scheme that involved the raising of intra-group finance through the issue of convertible securities (a loan that may be converted into shares of the issuing company). The debtor company claimed for tax purposes larger debits than the credits on which the creditor company was chargeable. The legislative response was to require the creditor company to bring in additional credits equal to this excess.

65. This rule has generally been effective in countering the notified schemes but recently new schemes have been notified to HMRC that although again relying on intra-group convertibles to produce an accounting/tax mismatch, are claimed not to be countered by the 2008 fix.

66. The amendments ensure that the creditor company is required to bring into account additional credits in all cases where an intra-group loan involving convertible debt would allow the debtor company to claim debits in excess of the amounts that the creditor would otherwise have to bring into account.

Paragraph 5:

67. Paragraph 5 deals with manufactured interest payments made by companies.

68. Manufactured interest arises where under an arrangement for the transfer of debt securities (Government or corporate debt instruments) one party is required to pay to the other an amount that is representative of interest on those securities.

69. The amendments made by paragraph 5 are a response to the recent High Court case of DCC Holdings (UK) Ltd v HMRC [2008] EWHC 2429. It has been suggested that the analysis that in DCC led to the Judge allowing a deduction for a deemed section 737A of ICTA manufactured payment might lead to claims by companies for deductions for real payments of manufactured interest in excess of the amounts appearing in accounts prepared in accordance with GAAP.

70. This view appears to be based on comments in the case concerning the nature of the deemed loan relationship under which the manufactured interest is treated as payable. Some of the comments suggest the possibility that the Judge might have reached the same conclusion as to the deductibility of the manufactured interest even if a real payment had been made.

71. HMRC does not accept that this is the case, and other comments indicate that the Judge was concerned only with deemed payments, but the measure puts beyond doubt that the taxable amounts in respect of payments of manufactured interest are (subject to any express rule to the contrary) those that are recognised in accordance with GAAP. This ensures that all parties to transactions that involve the payment or receipt of manufactured interest are taxed in a fair and sensible way.

SECTION 62: TRANSFERS OF TRADE TO OBTAIN TERMINAL LOSS RELIEF

SUMMARY

1. Section 62 addresses scenarios where trade cessation artificially occurs as a result of it being transferred to a person or persons outside the scope of Corporation Tax and it can be established that this is part of a scheme or arrangement, the main purpose or one of the main purpose of which is to access 'terminal loss relief'.

2. In such circumstances 'terminal loss relief' will not be available to the transferring entity and neither will carried forward losses relating to the trade be transferred to the receiving entity for set off against future profits.

DETAILS OF THE SECTION

3. Paragraph 1 introduces subsection 2E into section 393A ICTA 1988 and provides that subsection 2A of section 393A ICTA 1988 does not apply where two criteria are satisfied. Those criteria being:

   a. a trade ceases by virtue of its transfer to a person or persons outside the scope of Corporation tax; and

   b. the transfer is part of a scheme or arrangement the main purpose or one of the main purpose of which is to gain access to 'terminal loss relief'.

4. Paragraph 2 provides that the amendment made by paragraph 1 has effect in relation to cessations of trade on or after 21 May 2009.

BACKGROUND NOTE

5. Section 62 acts to counter a specific avoidance scheme (and variants of it) disclosed to HMRC that exploits Corporation Tax rules providing that losses arising in a trade in the 12 months prior to its cessation, may be carried back for set off against profits made in the previous 3 years ('Terminal Loss Relief').

SECTION 63 SCHEDULE 31: SALE OF LESSOR COMPANIES ETC: ANTI-AVOIDANCE

SUMMARY

1. Section 63 and Schedule 31 make changes to Schedule 10 to the Finance Act (FA) 2006 to ensure that it applies appropriately to the sale of an intermediate lessor company.

DETAILS OF THE SECTION

2. Paragraph 2 makes changes to paragraph 6(3) of Schedule 10 to FA 2006 to remove the reference to plant or machinery that the company "owns" and substitute "relevant plant or machinery".

3. Paragraph 3 makes changes to paragraph 7 of the Schedule.

4. Sub-paragraph (2) substitutes new sub-paragraphs (2) and (3).

5. New sub-paragraph (2) introduces new sub-paragraph (3) which defines the relevant plant or machinery value and makes new sub-paragraph (3) subject to new paragraph 7A.

6. New sub-paragraph (3) defines the balance sheet amounts in respect of plant or machinery to be taken into consideration for the purposes of condition A. Firstly, in new sub-paragraph (3)(a), it ensures that the amount includes amounts shown in the company's balance sheet in respect of plant or machinery at the start of the day, and secondly, in new sub-paragraph (3)(b), it ensures that the amount includes amounts shown in the company's balance sheet at the end of the day in respect of relevant transferred plant or machinery.

7. New sub-paragraph (3A) defines "relevant transferred plant or machinery" as plant or machinery that appeared in the balance sheet of an associated company at the start of the day. The combined effect of new sub-paragraph (3)(b) and new sub-paragraph (3A) is to capture assets transferred to the lessor company in the course of the relevant day from associated companies.

8. Sub-paragraph (3) makes clear that these amounts are for the purposes of this paragraph only by substituting "the purposes of this paragraph" for "this purpose".

9. Sub-paragraph (5) introduces new sub-paragraph (10). The new sub-paragraph provides a signpost to paragraph 9 of the Schedule which defines an associated company.

10. Paragraph 4 insert new paragraph 7A into Schedule 10. New paragraph 7A makes adjustments to the aggregate if certain conditions are met. When the conditions are met any amount included in the aggregate in respect of the plant or machinery is deducted and the market value of the plant or machinery is added to the aggregate. If the aggregate is nil the market value will constitute the relevant plant or machinery value.

11. New sub-paragraph (2) introduces these conditions, conditions A and B.

12. New sub-paragraph (3) makes general provisions for condition A. The condition will be satisfied if the plant or machinery falls into the terms of the condition at the start of the relevant day or at the end of the relevant day having been acquired from an associated company on that day.

13. New sub-paragraph (4) sets out the terms of condition A. Condition A is satisfied if the company is the lessee of the plant or machinery under a long funding finance lease or treated as the owner under a hire purchase or similar contract under section 67 of the Capital Allowances Act 2001 (CAA).

14. New sub-paragraph (5) sets out condition B. Condition B is satisfied if the company is the lessee of the plant or machinery under a long funding operating lease at the start of the relevant day, or is the lessee of the plant or machinery under a long funding operating lease at the end of the relevant day and it was acquired from an associated company on that day.

15. Paragraph 5 makes changes to paragraph 17 of the Schedule.

16. Sub-paragraph (2) introduces a reference to new paragraph 17A in sub-paragraph (1) and substitutes new sub-paragraphs (1)(a) and (aa) for sub-paragraph (1)(a).

17. New sub-paragraph (1)(a) excludes plant or machinery where the company has not incurred qualifying expenditure for the purposes of part two of CAA. New sub-paragraph (1)(aa) excludes plant or machinery where the company is the lessor under a long funding lease.

18. Sub-paragraph (3) substitutes new sub-paragraph (2). The new sub-paragraph signposts new sub-paragraph (2A) and the effect of new paragraph 17A.

19. New sub-paragraph (2A) defines the amounts to be included in the aggregate for the purposes of "PM" in paragraph 16. Firstly, in (2A)(a), it ensures that the amount includes amounts shown in the company's balance sheet in respect of plant or machinery at the start of the day, and secondly, in (2A)(b), it ensures that the amount includes amounts shown in the company's balance sheet at the end of the day in respect of relevant transferred plant or machinery.

20. New sub-paragraph (2B) defines "relevant transferred plant or machinery" as plant or machinery that appeared in the balance sheet of an associated company at the start of the day. The combined effect of new sub-paragraph (2)(b) and new sub-paragraph (2B) is to capture assets transferred to the lessor company in the course of the relevant day from associated companies.

21. Sub-paragraph (4) makes clear that these amounts are for the purposes of this paragraph only by substituting "the purposes of this paragraph" for "this purpose" in sub-paragraph (3).

22. Paragraph (6) inserts new paragraph 17A. New paragraph 17A makes adjustments to the aggregate if certain conditions are met. When the conditions are met any amount included in the aggregate in respect of the plant or machinery is deducted and the market value of the plant or machinery is added to the aggregate. If the aggregate is nil the market value will constitute the relevant plant or machinery value.

23. New sub-paragraph (2) introduces these conditions, conditions A and B.

24. New sub-paragraph (3) makes general provisions for condition A so that it is clear that the condition will be satisfied if the plant or machinery satisfies the conditions at the start of the day or if it satisfies the conditions at the end of the day having been acquired from an associated company on that day.

25. New sub-paragraph (4) sets out condition A. Condition A is satisfied if the company is the lessee of the plant or machinery under a long funding finance lease or treated as the owner under a hire purchase or similar contract under section 67 of CAA.

26. New sub-paragraph (5) sets out condition B. Condition B is satisfied if the company is the lessee of the plant or machinery under a long funding operating lease at the start of the relevant day, or is the lessee of the plant or machinery under a long funding operating lease at the end of the relevant day and it was acquired from an associated company on that day.

27. Paragraph 7 makes changes to paragraph 22(2) (migration) by substituting “in respect of which an amount would be shown in a balance sheet of the company drawn up immediately before the relevant day” for assets "owned by the company".

28. Paragraph 9 adds new sub-paragraph (5A) in paragraph 41 (definitions). It ensures that "long funding finance lease", "long funding lease" and "long funding operating lease" have the same meaning as in Part 2 of CAA (Leasing Reform).

29. Paragraph 10 makes consequential changes to paragraph 42 (index) to accommodate the new definitions.

30. Paragraph 11 repeals paragraph 2(3) of Schedule 6 to FA 2007.

31. Paragraph 12 brings the schedule into effect where the relevant day is on or after 13 November 2008.

BACKGROUND NOTE

32. The Schedule will make changes to Schedule 10 to FA 2006, to ensure that lessors of plant or machinery, whether acting as head lessor or intermediate lessor have parity of treatment for the purposes of the operation of Schedule 10.

33. Schedule 10 to FA 2006 calculates an amount of income by reference to the difference between the balance sheet value of assets owned by the lessor company and their tax written down value. The charge recovers the tax timing advantage derived from a claim to capital allowances.

34. Disclosures revealed that lessor companies had sought to avoid the consequences of Schedule 10 by entering into sale and finance leaseback arrangements so that the lessor company no longer owned the asset subject to a lease but continued to benefit from the availability of capital allowances. Schedule 10 does not take into consideration assets where the lessor does not own the asset so that the sale of the intermediate lessor company would escape the effect of Schedule 10 even though it had continued to benefit from the capital allowances.

35. The Schedule will remove the requirement for the lessor company to own an asset subject to a lease and make provisions for ascertaining a value in respect of an asset whether or not that asset is reflected on the balance sheet of the lessor company. As a result the sale of an intermediate lessor company will attract an appropriate charge.

36. Where the sale and finance leaseback takes place on the same day as the sale of the company there is still a possibility that no charge under Schedule 10 would arise as a consequence of paragraph 40 of Schedule 10. Paragraph 40 removes assets from the calculation of the Schedule 10 charge where the sale of the asset on the relevant day comes within section 228K of CAA. While section 228K applies in principle to a sale and finance leaseback transaction it may in practice give rise to no charge and as a result the sale of the lessor company could still be achieved without tax effect. This opportunity will be blocked by the repeal of paragraph 40.

SECTION 64 SCHEDULE 32: LEASES OF PLANT OR MACHINERY

SUMMARY

1. Section 64 and Schedule 32 introduce legislation to counter avoidance involving the leasing of plant or machinery.

DETAILS OF THE SCHEDULE

Disposal values: commencement of long funding finance leases

2. Paragraph 1 amends the disposal value to be brought into account on granting a long funding lease.

3. Sub-paragraph (2) replaces item 5A in the Table at section 61(2) of the Capital Allowances Act 2001 (CAA) with revised text. The description of the disposal event is unchanged but the disposal value is now found by taking the greater of the market value of the plant or machinery and the qualifying lease payments.

4. Sub-paragraph (3) inserts a new subsection (5A) into section 61 of CAA; this defines the "qualifying lease payments" for the purposes of item 5A. These are the minimum payments under the lease excluding the gross return on investment, i.e. the 'interest' element in the lease rental payments, and so much of any payment included in the lease rental in respect of charges for services or payments to cover qualifying tax to be paid by the lessor. Any initial payment made by the lessee is included in the calculation of the qualifying lease payments and thus will not be taxed on the lessor under section 785B of the Income and Corporation Taxes Act 1988 (ICTA) or section 809ZB of the Income Taxes Act 2007 (ITA).

5. Sub-paragraph (4) repeals subsections (6) to (9) of section 61 of CAA. These subsections relate to the meaning of the expression "net investment in the lease" and are no longer relevant as the revised disposal value does not use this concept.

6. Paragraph 2 repeals paragraph 4 of Schedule 20 to Finance Act (FA) 2008 which introduced subsections (6) to (9) of section 61 of CAA.

7. Paragraph 3 amends section 25A of the Taxation of Chargeable Gains Act 1992 (TCGA) so that it is consistent with the changes made to section 61 of CAA by paragraph 1.

8. Sub-paragraph (3) substitutes for subsections (4) to (4D) a definition of "relevant disposal value". For long funding finance leases this is the value at item 5A of the Table in section 61(2) of CAA and for long funding operating leases it is the value at item 5B of that Table.

9. Paragraph 5 contains commencement provisions.

Disposal values: termination etc of long funding leases

10. Paragraph 6 amends section 66 of CAA by inserting a reference to section 70E of CAA. This puts beyond doubt that the definition of disposal receipt at section 60 of CAA includes a disposal under section 70E.

11. Paragraph 7 amends the definition at section 70E of CAA of the disposal value when a long funding lease comes to an end. It also provides that a disposal value is brought into account when the leased asset ceases to be used wholly for a qualifying activity.

12. Sub-paragraph (2) replaces the phrase "the lease terminates" at section 70E(1)(c) with the phrase "a relevant event occurs".

13. Sub-paragraph (3) inserts new subsection (1A) into section 70E of CAA which defines a relevant event. A relevant event occurs where the lease terminates *or* the plant or machinery begins to be used wholly or partly for purposes other than that of the qualifying activity *or* the lessee's qualifying activity permanently ceases.

14. Sub-paragraph (4) substitutes the phrase "relevant event" for the phrase "termination of the lease" at section 70E(2)(a). This means that a relevant event is a disposal event, with the effect that the disposal value to be brought in by a lessee under a long funding lease is given by section 70E rather than by the general rules at section 61 of CAA.

15. Sub-paragraph (5) replaces subsections (3) to (8) of section 70E of CAA with new subsections (2A) to (2H).

    c. New subsection (2A) provides a formula for calculating the disposal value to be brought into the capital allowances computations of a lessee when the lessee's deemed ownership of the leased asset ends, either because the lease terminates or because the plant or machinery ceases to be used wholly for the purpose of a qualifying activity. The formula deducts from the lessee's qualifying expenditure on the plant or machinery at the commencement of the lease an amount referred to as "the qualifying amount" and adds any relevant rebate received.

    d. New subsection (2B) provides the definition of "the qualifying amount" for the lessee under a long funding operating lease. "The qualifying amount" is the aggregate amount of the reductions made under section 502K of ICTA or section 148I of the Income Tax (Trading and Other Income) Act 2005 (ITTOIA).

    e. New subsection (2C) provides the definition of "the qualifying amount" for the lessee under a long funding finance lease. "The qualifying amount" is the aggregate of the amounts paid to the lessor by the lessee. This amount includes any initial payment and also includes any payment made under a guarantee. It excludes the amounts mentioned in new subsection (2D).

f. New subsection (2D) provides that the amounts to be excluded from the "qualifying amount" in subsection (2C) are so much of any payments under the leases as represent finance charges, any service charges and qualifying UK or foreign tax to be paid by the lessor. The meaning of "qualifying UK or foreign tax" is given in section 70YE of CAA.

g. New subsection (2E) provides for an adjustment to the qualifying amount where the lease rentals exceed an arm's length amount. This will ensure that the disposal value brought in results in the lessee obtaining capital allowances for the arm's length cost of the asset.

h. New subsection (2F) provides the definition of the relevant rebate.

Paragraph (a) defines relevant rebate as any amount that is calculated by reference to the termination value of the plant or machinery and which is payable either directly or indirectly for the benefit of the lessee or to any person connected to the lessee. It is the amount generally referred to as a lease rental rebate.

Paragraph (b) defines relevant rebate where the disposal value occurs as a result of a change in the use of the plant or machinery or the cessation of the qualifying activity. In those circumstances it is the amount that would have been payable had the lease terminated at that date and the plant or machinery been sold for its market value.

i. New subsection (2G) makes it clear that relevant rebate, as defined at subsection (2F), is an amount that would reasonably be expected to have been paid if the lease transaction had been between parties acting at arm's length in cases where either a low or no rental rebate is paid because the transaction is not at arm's length.

j. New subsection (2H) provides that the disposal value given by the formula in new subsection (2A) cannot be less than nil.

16. Paragraph 8 provides the commencement rule for relevant events within the meaning of section 70E(1A) of CAA.

Capital receipts treated as income

17. Paragraph 9 makes amendments to section 785C of ICTA which ensure that where an initial payment is brought in as a disposal value it is not also taxed as income under section 785B of ICTA.

18. Sub-paragraph (4) inserts new subsections (9A) and (9B) into section 785C of ICTA. New subsection (9A) says that a capital payment is not relevant to the extent that it is an initial payment under a long funding lease and a disposal receipt under section 61 of CAA falls to be brought into account by the lessor on the granting of the lease.

19. Paragraph 10 makes amendments to section 809ZB of ITA that, for income tax, mirror those made by paragraph 9 for corporation tax.

20. Sub-paragraph (2) provides that in relation to payments made under leases whose inception is before 22 April 2009 and for which a disposal receipt under section 61 of CAA falls to be brought into account no relevant payment arises under section 785C(9A) of ICTA and section 809ZB(9A) of ITA.

Transfer and long funding leaseback: restrictions on lessee's allowances

21. Paragraph 12 amends subsection 51A(10) of CAA by inserting a reference to new section 70DA(2). This makes it clear that no annual investment allowance is available to the lessee under a transfer and long funding leaseback arrangement.

22. Paragraph 13 amends subsection 52(5) of CAA by inserting a reference to new section 70DA. This makes it clear that no first year allowance is available to the lessee under a transfer and long funding leaseback arrangement.

23. Paragraph 14 amends subsection 57(3) of CAA to ensure that a person's available qualifying expenditure does not include an amount excluded by new section 70DA.

24. Paragraph 15 inserts new section 70DA after section 70D of CAA. This section has a similar effect to sections 217 and 218 of CAA which deny first year allowances and limit the qualifying expenditure in an arrangement where an existing business asset is sold and leased back to the same person or someone connected to them. That legislation only applies to a claim by new owners of the plant or machinery who leases it back to the original seller or someone connected to them. Because the lessee under a long funding lease is deemed to own the leased asset it is the lessee in a transfer and long funding leaseback arrangement who has the qualifying expenditure and so is the person to whom new section 70DA applies.

25. Subsection (1) sets out the circumstances where new section 70DA applies. These are where a person (S) transfers (see subsection (7)) plant or machinery to another person (B) and after the transfer the plant or machinery is used by S or a person connected to S (CS) and is available to be so used because it has been leased under a long funding lease.

26. Paragraph 16 inserts new subsection (1C) into section 70H of CAA. This ensures that where the arrangements involve a transfer and long funding leaseback as defined in new section 70DA(1) the lessee is not entitled to treat the lease as a non-long funding lease. This makes it clear, in case of any doubt, that the lessee cannot claim a deduction for the capital element of their lease rental payments.

27. Paragraph 17 provides that the amendments made by paragraphs 12 to 16 apply to leasebacks where the term of the lease commenced on or after 13 November 2008. The definition of commencement is in paragraph 27.

Transfer followed by hire purchase etc: restrictions on hirer's allowances

28. Paragraph 18 amends subsection 51A(10) of CAA by inserting a reference to new section 229A(2). This makes it clear that no annual investment allowance is available to the lessee under a hire purchase etc and long funding leaseback arrangement.

29. Paragraph 19 amends subsection 52(5) of CAA by inserting a reference to new section 229A. This makes it clear that no first year allowance is available to the lessee under a hire purchase etc and long funding leaseback arrangement.

30. Paragraph 20 amends subsection 57(3) of CAA to ensure that a person's available qualifying expenditure does not include an amount excluded by new section 229A.

31. Paragraph 21 inserts new section 229A after section 229. This section has the same effect as sections 217 and 218 of CAA which deny first year allowances and limit the qualifying expenditure in an arrangement where an existing business asset is sold and leased back to the same person or someone connected to them. That legislation only dealt with a claim by new owners of the plant or machinery who leased it back to the original seller or someone connected to them. New section 229A covers cases where capital allowance entitlement arises to a person under a contract that means that they shall or may become the owner of the plant or machinery where this contract follows a transfer by the person of the same plant or machinery.

32. Paragraph 22 provides that the amendments made by paragraphs 18 to 21 apply to leasebacks where the lease commenced on or after 13 November 2008.

Finance leaseback

33. Paragraph 23 amends section 216(1)(b)(i) of CAA. It inserts after "S" the phrase "or by a person (other than B) who is connected with S".

34. Paragraph 24 amends section 221(1)(b)(i) of CAA. It replaces the phrase "qualifying activity carried on by S" with "an activity carried on by S or by a person (other than B) who is connected with S".

35. Paragraph 25 provides that the amendment made by paragraph 23 has effect where the date of the relevant transaction is on or after 22 April 2009. Where section 216(1)(b) of CAA is relevant for the purposes of an election under section 227 of CAA, the amendment made by paragraph 24 applies where the date of the transaction referred to at section 227(1)(a) of CAA is on or after 22 April 2009.

36. Paragraph 26 provides that the amendment made by paragraph 24 has effect where the date of the relevant transaction is on or after 22 April 2009. Where section 221(1)(b) of CAA is relevant for the purposes of section 228A of CAA the amendment made by paragraph 24 applies where the date of the transaction referred to at section 228A(2)(a) of CAA is on or after 22 April 2009.

Interpretation

37. Paragraph 27 says that the words "commencement" and "inception" in this Schedule have the meanings given in section 70YI of CAA and so are in line with the long funding lease rules generally.

BACKGROUND NOTE

38. Schedule 32 counters disclosed avoidance schemes involving the leasing of plant or machinery. HMRC does not accept that these schemes achieve their aim. In addition it amends legislation covering the tax position of a lessee at the end of a long funding lease and makes small changes to the definitions of "sale and leaseback" and "sale and finance leaseback".

The lease and long funding leaseback schemes

39. The lease and leaseback avoidance involves an asset owner who has claimed capital allowances on that asset granting a long funding finance lease of the asset to another person who leases the asset back to them under a long funding operating lease. The intention is that the lessor receives a lump sum that is commercially equivalent to a loan which is neither taxed as income nor brought into their capital allowances computation, leaving the lessor with a continuing entitlement to capital allowances over and above the net cost of the asset to them. The timing of the benefit can be enhanced if the lessee under the leaseback can claim a first year allowance.

40. This measure will ensure that the person granting the long funding lease is taxed on the lump sum received and that on reacquisition there is capital allowance symmetry. It also removes the lessee's entitlement to first year or annual investment allowances.

The sale and long funding leaseback scheme

41. The sale and leaseback avoidance scheme is also based on arrangements that are commercially equivalent to a secured loan. An owner sells plant or machinery used in their business to a finance provider and leases it back when it is worth more than its original cost to the owner. The aim is that the seller will obtain increased capital allowances entitlement where in substance they have received a loan and there has been no change in the use of the asset.

42. This measure provides a rule that limits the qualifying expenditure that can be claimed by the lessee under the long funding leaseback to the amount that has been brought in as disposal proceeds by the seller (or head lessor). Where the seller or head lessor has not claimed capital allowances the qualifying expenditure will be limited to the lower of market value or the cost, to the seller, of the plant or machinery.

Lessees under long funding leases

43. Lessees under a long funding lease are entitled to claim capital allowances and when the lease ends a disposal value must be brought into account. The disposal rules (in section 70E of CAA) do not work as intended and give an unintended tax benefit in certain circumstances.

44. This measure provides a revised formula for calculating the disposal proceeds to be brought into account by the lessee under a long funding finance lease. In addition the disposal rules at section 70E of CAA now ensure that a lessee who emigrates during the period of the long funding lease brings into account an appropriate disposal value.

The "sale and leaseback" and "sale and finance leaseback" definitions

45. The definitions of "sale and leaseback" and "sale and finance leaseback" at sections 216 and 221 of CAA are aimed at avoidance involving connected party leasing arrangements that:

- seek tax relief in excess of the cost to the seller's group, or
- effectively sell capital allowance entitlement to third parties.

The existing definitions do not cover arrangements involving the leaseback to a person connected to the seller who is already leasing the asset and continues to do so.

46. This measure amends the definitions to ensure that they include arrangements involving a leaseback to a continuing user of the asset.

SECTION 65 AND SCHEDULE 33: LONG FUNDING LEASES OF FILMS

SUMMARY

1. Section 65 and Schedule 33 introduce legislation to prevent the avoidance of tax involving long funding leases of films.

DETAILS OF THE SCHEDULE

2. Paragraph 1 introduces new section 502GD into the Income and Corporation Taxes Act 1988 (ICTA).

3. New section 502GD provides that where a company is (or has been) the lessor of a film, the taxation of its rental income from those leases is not affected by the rules that apply to long funding leases.

4. Paragraph 2 introduces new section 148FD into the Income Tax (Trading and Other Income) Act 2005 (ITTOIA). It is the income tax equivalent of section 502GD of ICTA.

5. New section 148FD provides that where a person is (or has been) the lessor of a film the taxation of its rental income from those leases is not affected by the rules that apply to long funding leases.

6. Paragraph 3 gives the commencement rules for paragraphs 1 and 2. These paragraphs only apply where the inception of the long funding lease is on or after 13 November 2008. The meaning of 'inception' is given by section 70YI(1) of the Capital Allowances Act 2001 (applied by paragraph 9 of this Schedule).

7. Paragraph 4 introduces paragraphs 5 to 8 of the Schedule. These paragraphs provide transitional rules that apply to long funding finance leases of films, the inception of which was before 13 November 2008 and which have not ended by that date.

8. Paragraph 5 applies to certain chargeable periods and disapplies the rules that restrict the amount of a lessor's income that may be taxed under a long funding finance lease.

9. Paragraph 5(1) disapplies the rules in section 502B of ICTA (in the case of corporation tax) or section 148A of ITTOIA (in the case of income tax). This transitional rule applies to periods of account that meet the conditions in paragraph 5(2).

10. Paragraph 5(2) provides that this paragraph only applies to periods of account that begin on or after 13 November 2008 and to which no part of any rental due to be paid before that date refers.

11. Paragraph 6 provides further transitional rules that apply to lessors where paragraph 5 does not apply to the chargeable period.

12. Paragraph 6(1) provides that the paragraph applies to chargeable periods that end on or after 13 November 2008 and to which paragraph 5(2) does not apply. Where this sub-paragraph applies the lessor is treated as receiving an amount of income in addition to that which is brought into account as representing the finance charge element of the lease rentals. This amount is known as the relevant amount.

13. Paragraph 6(2) defines the "relevant amount" as the proportion of the 'capital' element of the rentals (referred to here as that part of the rentals as would not reasonably be regarded as reflected in the rental earning for that period of account) which are payable on or after 13 November 2008 and which relate to the period of account.

14. Sub-paragraph (3) applies for the purpose of sub-paragraph (2) where a rental is paid for a period of time that begins before 13 November 2008 and does not fall wholly within the period of account. Where this sub-paragraph applies the rental is apportioned to the period of account on a time basis.

15. Paragraph 7 provides that (where the conditions in paragraph 4 are met) section 502C of ICTA or section 148B of ITTOIA do not apply. These sections apply for corporation tax and income tax respectively and make provision for the taxation of exceptional items arising in connection with the lease.

16. Paragraph 8 applies where the conditions in paragraph 4 are met and ensures that a lessor is entitled to an appropriate deduction if it makes a refund of rentals at the end of the lease term.

17. Paragraph 8(1) provides that if a deduction in respect of a refund of rentals (described as a sum calculated by reference to the termination value) is otherwise prohibited by section 502D of ICTA or section 148C of ITTOIA then a deduction in respect of that refund is allowed.

18. Paragraph 8(2) provides that the amount of the deduction is limited to the amount brought into account in computing income under paragraph 5 or 6 of this Schedule.

BACKGROUND NOTE

19. This section and Schedule counter avoidance involving the leasing of films under long funding leases of plant or machinery.

20. Partnerships typically acquired or produced films and leased them to other companies to be exploited over a period of up to 15 years (referred to here as "sale and leaseback arrangements"). The partnerships were able to claim relief for the cost of those films under section 42 of the Finance (No.2) Act 1992, section 48 of the Finance (No.2) Act 1997 or sections 138 to 140 of ITTOIA.

21. The rents under the lease are taxable and, in effect, these sale and leaseback arrangements allow the partners to defer their tax liability for up to 15 years.

22. The avoidance involves the partnerships ending the existing leases and replacing them with new leases that are intended to qualify as long funding finance leases of plant or machinery.

23. If these new leases are long funding finance leases the majority of the rents receivable will not be taxed as section 148A of ITTOIA (for income tax) or section 502B of ICTA (for corporation tax) will apply. In effect, the partnerships will have replaced a taxable income stream with one that is largely untaxed.

24. Although the known avoidance involves partnerships, it is possible that others could seek to avoid tax using the same methods. Therefore the new rules are not limited to partnerships.

SECTION 66 AND SCHEDULE 34: REAL ESTATE INVESTMENT TRUSTS

SUMMARY

1. Section 66 and Schedule 34 amend provisions in Part 4 of the Finance Act (FA) 2006 relating to Real Estate Investment Trusts. The following areas are covered in the Schedule:

   - a new measure to stop exploitation of the Real Estate Investment Trust (REIT) regime where businesses restructure to gain the benefits of the regime;
   - the Schedule removes an unintended barrier to joining the regime;
   - the Schedule allows that a charge to tax incurred by a REIT for breaching the profit finance cost ratio may be waived in particular circumstances; and
   - the remainder of the Schedule clarifies and makes more consistent the existing legislation.

DETAILS OF THE SCHEDULE

2. Paragraph 2(1) amends section 104 of FA 2006 by introducing a new subsection (3). Subsection (3) allows a business with 'tied premises' to treat the rental income from those premises as part of the property rental business of a REIT. ('Tied premises' are where a company supplies goods to a third party for sale on premises which the company rents to the third party. For example pubs may be tied premises.) Before the amendment such income would have been trading income and not eligible to be in the REIT regime.

3. Paragraph 3 amends two subsections of section 106 of FA 2006 (Conditions for Company).

4. Paragraph 3(2) allows that two of the conditions of section 106 do not have to be met on the first day the REIT joins the regime.

5. Paragraph 3 (3) and (4) allow REITs to issue convertible preference shares where previously they could not. The amendments also make consequential amendments concerning the definition of these shares arising from changes to Income and Corporation Taxes Act 1988.

6. Paragraph 4 amends section 108 of FA 2006 (Conditions for balance of business) to align the conditions for the balance of business asset test for a single company REIT with those for a group REIT.

7. Paragraph 4(1) amends the condition for single companies by removing the condition that the asset has to be property involved in the relevant property rental business and inserting the condition that the asset has to be one that would be in the accounts of the tax exempt property rental business.

8. Paragraph 5 amends section 109 of FA 2006 (Notice), which is about the conditions in section 106 that are to be met on joining the REIT regime. Section 109 allows that

Condition 3 of section 106 (the company being listed on a recognised stock exchange) and Condition 4 (that the company is not a 'close' company) do not have to be met on joining the regime provided that:

- Condition 3 is met on the first day the REIT is in the regime; and
- Condition 4 is met after the first day in the regime.

Previously section 109 tied these two conditions together. The amendment breaks this link.

9. Paragraph 5(2) inserts into section 109 subsections (2A)-(2C) to allow that Condition 3 of section 106 (the REIT not being listed on a recognised stock exchange) can be relaxed if the REIT provides assertions that this condition will be met apart from on the first day and the other conditions of section 106 will be met throughout the accounting period.

10. Paragraph 5(3) amends section 109 by removing the subsection that resulted in the two conditions being tied together.

11. Paragraph 5(4) amends section 109(5) to change the assertions to be provided by the REIT in the circumstance when Condition 4 of Section 106 (the company not being a close company) is not met on joining the REIT regime.

12. Paragraph 5(5) allows, having separated the two conditions, the possibility that both conditions are not met on the first day and details the assertions to be provided in this circumstance.

13. Paragraph 5A (1) amends section 115 by introducing new sub sections 3A and 3B.

14. Section 3A allows HMRC Commissioners to waive the charge incurred by a REIT for breaching the profit: financing- cost ratio in particular circumstances. The charge arises if the financing costs of the property rental business exceed 80% of the profits from that business. The charge, which is to Corporation Tax, is on the amount by which the limit is exceeded.

15. The Commissioners may only waive the charge if they think that the REIT is in severe financial difficulties at a time in the accounting period for which the charge arises; the REIT breached the profit: financing-cost ratio because of circumstances which arose unexpectedly; and the REIT could not reasonably have taken action to avoid the breach.

16. Section 3B allows regulations to be made to specify the criteria to be applied in determining whether to waive the charge.

17. Paragraph 5A (2) allows the amendments to apply with retrospective effect.

18. Paragraph 6 makes a change to section 118 of FA 2006 (Funds awaiting re-investment). Section 118 allows that where a REIT disposes of a property used in its tax exempt property rental business, then the funds from the disposal are regarded as

an asset involved in the property rental business for two years for the purpose of the balance of business asset test of section 108.

19. Paragraph 6(1) clarifies how such funds can be apportioned where there has been some tax exempt use and some non exempt use. The result is that such periods totalling in aggregate at least a year will be recognised for the apportionment.

20. Paragraph 7 inserts a new section 136A into FA 2006. This section deals with restructuring by companies with the aim of meeting REIT conditions and tests.

21. New section 136A(1) grants HM Treasury a power to make regulations about the application of the REIT regime where there is a connection between a REIT company and another person.

22. New section 136A(2) explains what is meant by a REIT company for the purpose of section 136A.

23. New section 136A(3) gives examples of what may be included in the regulations.

BACKGROUND NOTE

24. Real Estate Investment Trusts were introduced with effect from 1 January 2007. The rules for the regime are contained in part 4 of the Finance Act 2006 and in regulations.

25. Companies and groups of companies whose main business is the rental of property can elect to become Real Estate Investment Trusts (REITs), subject to meeting certain conditions relating to the REIT itself, the properties being rented and the business of the REIT.

26. A REIT has to distribute 90 per cent of the profits from its property rental business as distributions to shareholders. There is also a charge on entering the REIT regime.

27. A REIT is exempt from UK tax on income and gains of its property rental business but pays tax on the profits and gains from other activities.

28. The changes announced in the section and Schedule will:

- prevent (in certain circumstances specified by regulations) companies from restructuring with the aim of meeting the REIT requirements and conditions. The amendment will not apply to restructuring where control of non qualifying activities is severed to result in the property rental business qualifying as a REIT;
- remove a barrier to entry for businesses with ‘tied premises’;
- allow the charge incurred for breaching the limit of the profit finance cost ratio to be waived in certain circumstances; and
- clarify and make consistent parts of the existing legislation.

SECTION 67: DEDUCTIONS FOR EMPLOYEE LIABILITIES

SUMMARY

1. Section 67 will ensure that employee liabilities will only be relieved where they are not derived from arrangements the main purpose, or one of the main purposes, of which is the avoidance of tax. It will apply to individuals who seek to use sections 346 and 555 of the Income Tax (Earnings and Pensions) Act 2003 (ITEPA) to obtain tax relief using tax avoidance arrangements. It will have no impact on those using the relief who are not attempting to avoid tax. It will have effect from 12 January 2009.

DETAILS OF THE SECTION

2. Subsection (2) inserts a new subsection (2A) into section 346 of ITEPA.

3. New subsection (2A) prevents any deduction under section 346 of ITEPA where a payment is made as part of arrangements for which tax avoidance is either the main purpose or one of the main purposes.

4. New section 556A prevents any deduction under section 555 where a payment is made as part of arrangements for which tax avoidance is either the main purpose or one of the main purposes.

5. Subsection (4) provides that the new rules in section 346(2A) and section 556A have effect for payments made on or after 12 January 2009.

BACKGROUND NOTE

6. Section 346 of ITEPA enables employees to claim deductions from earnings for payments of employment-related liabilities and of insurance premiums to indemnify against such liabilities. Any deduction due is given against earnings from the employment for the year in which the payment is made. Section 555 of ITEPA makes like provision in respect of former employees but also provides for the deduction to be set against the former employee's general income arising in the tax year in which the payment is made.

7. This section counters avoidance involving the abusive use of deductions for employment-related liabilities and is introduced in response to arrangements that involve the creation of a contrived liability through deliberate default.

8. The changes introduced by this measure were announced on 13 January 2009 by a Written Ministerial Statement tabled by the Financial Secretary to the Treasury. A Technical Note explaining who would be affected and how was published on the HM Revenue & Customs website on 12 January 2009.

SECTION 68: EMPLOYMENT LOSS RELIEF

SUMMARY

1. Section 68 will ensure that employment losses will only be relieved where they are not derived from arrangements the main purpose, or one of the main purposes, of which is the avoidance of tax. It will apply to individuals who seek to use section 128 of the Income Tax Act 2007 (ITA) to obtain tax relief using tax avoidance arrangements. It will have no impact on those using the relief who are not attempting to avoid tax. It will have effect from 12 January 2009.

DETAILS OF THE SECTION

2. New subsection (5A) provides that no claim is allowed under section 128 of ITA for losses derived from arrangements the main purpose, or one of the main purposes, of which is the avoidance of tax.

3. Subsection (2) provides that the new subsection (5A) has effect from 2009-10 onwards, and also in relation to 2008-09 claims made under section 128 only where a loss is occasioned by an act or omission occurring on or after 12 January 2009.

4. Subsection (3) ensures that where a person has made a claim for relief during the period 12 January 2009 to 1 April 2009 no penalty is payable on the ground that any return, statement or declaration made in connection with the claim contained an inaccuracy if it would not have done so but for the new subsection (5A).

5. Subsection (4) modifies the reference to due date in section 59C of the Taxes Management Act 1970 so that in relation to tax which would not be payable but for the new subsection (5A) the reference in section 59C to the due date becomes the later of 1 April 2009 and the due date. The effect of this is that a person who has made a claim for relief that is precluded by the new subsection (5A) and would otherwise be liable to surcharges under section 59C will not be liable to such surcharges provided they re-order their affairs and pay any additional tax due in accordance with the proposed changes within 28 days starting on the 1 April 2009.

BACKGROUND NOTE

6. Section 128 of ITA enables employees to claim relief in respect of a loss made in an employment. Allowable losses may be offset against general income arising in the loss making year, the previous year or both. These provisions counter avoidance involving the abusive use of reliefs available for losses associated with employment. They are introduced in response to arrangements that involve the creation of a loss through deliberate default and are a variant of tax avoidance arrangements using relief for employment-related liabilities, for which counter-measures were announced on 13 January 2009 and publicised on the HM Revenue & Customs website on 12 January 2009.

7. The changes introduced by this measure were announced on 1 April 2009 by a Written Ministerial Statement tabled by the Financial Secretary to the Treasury. A Technical Note explaining who would be affected and how was published on the HM Revenue & Customs website on 1 April 2009. This Note also included further detail about the provisions relating to penalties and surcharges for people who have made a claim between 12 January 2009 and 1 April 2009.

SECTION 69: NO LOSS RELIEF FOR LOSSES FROM CONTRACTS FOR LIFE INSURANCE ETC

SUMMARY

1. Section 69 affects the taxation of certain life insurance policies, life annuity contracts and capital redemption policies. It addresses income tax avoidance by putting beyond any doubt that income tax loss relief does not arise from offshore life insurance policies. The measure has effect for 2009-10. Transitional provisions may also apply to 2008-09 for certain transactions taking place on or after 1 April 2009.

DETAILS OF THE SECTION

2. Subsection (1) amends section 152(8) of the Income Tax Act 2007 (ITA). This ensures that gains from policies and contracts falling within section 531(3) of the Income Tax (Trading and Other Income) Act 2005 (certain life insurance policies, offshore capital redemption policies and contracts for life annuities) will not be eligible income for the purposes of claiming income tax loss relief under section 152(1) of ITA.

3. Subsection (2) provides that subsection (1) will apply to losses relating to the years 2009-10 onwards. This means that there is no scope to claim income tax loss relief for any losses relating to 2009-10 and subsequent years.

4. Subsection (3) provides that in certain circumstances, subsection (1) will also apply for 2008-09 so there is no scope to claim income tax loss relief:

- in relation to new policies or contracts made on or after 1 April 2009;
- for policies or contracts varied on or after 1 April 2009 so as to increase the benefits secured. For this purpose, the exercise of an option in the policy or contract, on or after 1 April 2009, is treated as a variation;
- where all or part of the rights are assigned on or after 1 April 2009 to the person claiming a deduction; or
- where all or part of the rights conferred by the policy or contract become held, on or after 1 April 2009, as security for a debt.

5. Subsection (4) provides that where claims for income tax loss relief relating to 2008-09 or an earlier tax year have been made and part of those losses remain unused in 2009-10 or subsequent years, there will be no deduction available under section 153 of ITA for the unused losses in 2009-10 and subsequent years.

BACKGROUND NOTE

6. The Government's intention to legislate was announced in a written ministerial statement by the Financial Secretary to the Treasury on 1 April 2009 and details of the measure were given in a News Release, draft legislation and explanatory note published by HM Revenue & Customs (HMRC) on the same day.

7. Gains from offshore life insurance policies are taxed as income under special rules which may give rise to a tax charge when chargeable events, such as the surrender, assignment or maturity of a policy, take place. These rules apply income tax to gains when they arise but do not provide income tax loss relief should the calculation from a chargeable event give a negative result.

8. Sections 152 and 153 of ITA apply to certain sources of miscellaneous income, including gains from offshore life insurance policies. Although some of these sources can give rise to allowable income tax losses as well as profits, the chargeable event regime governing life insurance policies simply ensures that any taxable gains over the life of the policies are restricted to economic gains. It does not provide for income tax loss relief.

9. Avoidance schemes identified by HMRC purport to create loss relief from offshore life insurance policies which can be set off against offshore income gains. This section will remove the scope for income tax loss relief to be created from offshore policies and will put beyond any doubt the Government's long standing view that income tax loss relief is not available.

SECTION 70: INTANGIBLE FIXED ASSETS AND GOODWILL

SUMMARY

1. Section 70 introduces legislation to confirm the tax treatment of goodwill provided for by the corporate intangible fixed assets regime ('the regime') at Part 8 of the Corporation Tax Act 2009 (formerly Schedule 29 to the Finance Act 2002)

2. Section 70 confirms that for the purposes of the regime, goodwill includes 'internally-generated goodwill', and that all goodwill is created in the course of the carrying on of a business and is subject to rules determining whether goodwill is treated as being created before or after 1 April 2002.

3. Corresponding amendments are made to the rules governing whether assets representing non-qualifying expenditure are treated as being created before or on or after 1 April 2002.

DETAILS OF THE SECTION

4. Subsection (2) provides for an amendment to section 712(2) of the Corporation Tax Act 2009 (CTA) to confirm that the meaning of an 'intangible asset' also includes an internally-generated asset.

5. Subsection (3) provides for a new subsection to be inserted in section 715 of CTA. New section 715(4) confirms that for the purposes of the regime all goodwill is created in the course of carrying on a business. This confirms, for example, that no goodwill is created by the acquisition of a business or by the accounting recognition/capitalisation of goodwill.

6. Subsection (4) provides for consequential amendments to section 883 of CTA so that the interface with and references to other sections being amended operate correctly.

7. Subsection (5) provides for amendments to section 884 of CTA to confirm that goodwill is treated as created before 1 April 2002 if the business was carried on at any time before that date by the company or a related party, and otherwise is treated as created on or after 1 April 2002.

8. Subsection (6) provides for amendments to section 885 of CTA to confirm that an asset is treated as created before 1 April 2002 if the asset was held at any time before that date by the company or a related party and it represents expenditure that under the law as it stood before 1 April 2002 is not qualifying expenditure for the purposes of any allowance under the Capital Allowances Act 2001. In all other cases, the asset is treated as created on or after 1 April 2002.

9. Subsection (7) provides for the amendments made by the section to have effect in relation to accounting periods beginning on or after 22 April 2009, and that in relation to those accounting periods the amendments are treated as always having had effect. The amendments apply for the purposes of calculating the future tax consequences of past transactions.

10. Subsection (8) provides that where an accounting period starts before 22 April 2009 and ends on or after that date, then for the purpose of applying the amendments, the period from 22 April 2009 to the end of the current accounting period will be treated as a separate notional accounting period.

BACKGROUND NOTE

11. The corporate intangible fixed assets regime was originally introduced as Schedule 29 to the Finance Act 2002, following consultation, and is now contained in Part 8 of the Corporation Tax Act 2009. It deals with the corporation tax treatment of intangible fixed assets such as patents, trademarks and design rights as well as the tax treatment of goodwill.

12. Currently, some companies are taking a contrary interpretation to HM Revenue & Customs (HMRC) of certain rules governing the treatment of goodwill. The purpose of this section is to confirm that the rules governing the treatment of goodwill operate as intended, and in the way HMRC considers that they do already.

13. The section confirms that for the purposes of the corporate intangible asset regime goodwill includes 'internally-generated' goodwill, and that all goodwill is created in the course of the carrying on of a business and is subject to rules determining whether goodwill is treated as being created before or on or after 1 April 2002.

14. The legislation applies for the purposes of accounting periods beginning on or after 22 April 2009, and the part of any accounting period straddling this date which falls on or after 22 April. This includes for the purposes of calculating the future tax consequences of past transactions.

SECTION 71: TAXABLE BENEFIT OF LIVING ACCOMMODATION: LEASE PREMIUMS

SUMMARY

1. Section 71 changes the rules for taxing the benefit in kind charge where employees are provided with living accommodation by reason of their employment. This is to stop attempts to avoid tax through the payment of a lease premium rather than a full market rent for the use of the accommodation. The section introduces a rule that means the value of the lease premium will be taken into account when working out the benefit in kind charge.

DETAILS OF THE SECTION

2. Subsection (1) indicates that Chapter 5 of Part 3 of the Income Tax Earnings and Pensions Act 2003 (ITEPA) is amended by the section. The Chapter sets out the rules under which living accommodation provided to an employee, or a member of the employee's family or household, by reason of the employee's employment is a taxable benefit in kind.

3. Subsection (2)(a) amends section 105(3) of ITEPA, which defines the "rental value of the accommodation", so that it is qualified by new subsections (4) and (4A).

4. Subsection (2)(b) substitutes a new section 105(4) of ITEPA and inserts new subsections (4A) and (4B).

5. New section 105(4) sets out two criteria that have to be satisfied before new section 105(4A) applies. It also defines the term "the relevant period" for the purposes of the amendments introduced by the section.

6. Paragraph (a) of new section 105(4A) provides that subsection 105(3) of ITEPA does not apply to the relevant period and paragraph (b) applies instead. Paragraph (b) provides that the rental value of the accommodation is the rental amount payable in respect of the lease for the period by the person at whose cost the accommodation is provided.

7. New section 105(4B) defines the reference in new sections 105(4) and (4A) of ITEPA to 'a rental amount payable by P in respect of the relevant period' as being the sum of the rent for the period payable by that person and any amount attributed to the period in respect of a lease premium in accordance with new sections 105A and 105B of ITEPA.

8. Subsection (3) of the section inserts a new section 105A and 105B into ITEPA.

9. New section 105A(1) provides for amounts in respect of a lease premium, payable in relation to a lease with a term of 10 years or less, to be attributed to the taxable period if the net amount of the lease premium is greater than zero. It provides that this attribution does not apply if the living accommodation is part of premises used mainly for a purpose other than the provision of living accommodation.

10. New section 105A(2) sets out the formula for working out the amount of any lease premium to be attributed to a taxable period. This is dependent on the term of the lease, the number of days in the relevant period and the net amount of the lease premium payable in relation to the lease.

11. New section 105A(3) refers to new section 105B for provision about the application of new section 105A to certain leases with break clauses.

12. New section 105A(4) defines the "net amount payable in relation to lease by way of a lease premium" for the purposes of new section 105A.

13. New section 105A(5) defines the term "lease premium" for the purposes of new section 105A and new section 105B.

14. New section 105A(6) further defines "premium" as including a grassum in relation to the application of the section to leases in Scotland.

15. New section 105B(1) provides that the section applies to a lease which contains one or more relevant break clauses. The subsection also introduces the term "original lease" in respect of such leases.

16. New section 105B(2) defines "break clause" and "relevant break clause" for the purposes of the section.

17. New section 105B(3) provides that the term of the lease and the net amount payable by way of a lease premium for the purposes of new section 105A are to be determined on the assumption that any relevant break clause is exercised in such a way that the term of the lease is as short as possible.

18. New section 105B(4) deems, for the purposes of new section 105A the parties to a lease to be parties to a further lease if a relevant break clause is not exercised in such a way that the term of the original lease is as short as possible and introduces the term "notional lease" in respect of such leases. Paragraphs (a) and (b) of the subsection set out how the term of a notional lease is to be determined.

19. New section 105B(5) sets out how the end of the term of a notional lease is to be determined.

20. New section 105B(6) sets out how the net amount payable for the purposes of new section 105A in relation to a notional lease by way of a lease premium is to be determined where the term of the notional lease ends in accordance with paragraph (a) of subsection (5) of new section 105B.

21. New section 105B(7) set out how the net amount payable for the purposes of new section 105A in relation to a notional lease by way of a lease premium is to be determined where the term of the notional lease ends in accordance with paragraph (b) of subsection (5) of new section 105B.

22. New section 105B(8) defines the meaning of "relevant proportion" for the purposes of subsection (7) of new section 105B.

23. Subsection (4) of the clause provides that it will only have effect for leases entered into on or after 22 April 2009. The clause will not apply to leases entered into before that date, except where the lease has been extended after that date.

24. Subsection (5) deals with lease extensions to which the new rules apply by virtue of subsection (4). It provides that the additional term of the lease created by the extension is treated as the whole of the term of the lease for the purposes of the new rules, and that those rules only apply to a lease premium paid in respect of the additional term of the lease starting on or after that date.

25. Subsection (6) defines "lease premium" for the purposes of the clause as having the same meaning as in new sections 105A and 105B.

BACKGROUND NOTE

26. Where an employee (or a member of their family or household) is provided with accommodation by reason of the employee's employment there is a tax charge on the benefit to the employee of that accommodation. Where rent is paid by the person at whose cost the accommodation is provided the charge is based on the actual rent paid (less any amount made good by the employee), where that is more than the annual value of the accommodation. However, some arrangements are being entered into that involve upfront payments, which are described as a lease premium, and payment of a very small rent in order to try to avoid paying tax.

27. The section ensures that where a lease premium is paid for a lease of 10 years or less, the same tax treatment will follow as if the lease premium were actual rent paid. The taxable amount in any tax year will be treated as the amount of the lease premium spread over the duration of the lease plus the amount of any rent paid by the person at whose cost the accommodation is provided less any amount made good by the employee. The new rules will not apply where the lease is in respect of living accommodation which forms part of premises which is used by the person at whose cost the accommodation is provided, mainly for a purpose which is not the provision of living accommodation.

SECTION 72 AND SCHEDULE 35: SPECIAL ANNUAL ALLOWANCE CHARGE

SUMMARY

1. Section 72 and schedule 35 introduces an income tax charge at 20 per cent for certain individuals on certain pension contributions and benefits accrued. This special annual allowance charge is on pension contributions and benefits accrued in excess of a special annual allowance of £20,000 for individuals whose relevant income is £150,000 or more. This may be increased up to £30,000 for those with a pattern of non-regular pension savings. The special annual allowance charge will not apply in respect of an individual's normal pattern of regular pension contributions or the normal way in which their pension benefits accrued before 22 April 2009. The schedule also enables high-income individuals to ask their schemes to refund pension contributions that they have paid in the 2009-2010 tax year, which may otherwise create a liability to the special annual allowance charge. The repayments are subject to a 40 per cent income tax charge on the scheme, recovering the individual's tax relief.

DETAILS OF THE SCHEDULE

2. Paragraph 1 introduces schedule 35 and provides for a new charge to income tax for certain members of pension schemes. This income tax charge is to be called the special annual allowance charge.

3. Paragraph 1(1) provides that the charge to income tax applies only to high-income individuals and sets out that the charge arises where the total adjusted pension input amount (as defined in paragraphs 3-16) exceeds the special annual allowance.

4. Paragraph 1(2) defines "high-income individual" by reference to the individual's "relevant income". The method for calculating an individual's relevant income is set out in paragraph 2.

5. Paragraph 1(3) provides that there are further definitions essential to the calculation of an individual's liability to the special annual allowance charge in paragraphs 3 to 16 of the Schedule.

6. Paragraph 1(4) sets the amount of the special annual allowance. This is subject to the provisions of paragraph 17.

7. Paragraph 1(5) provides for the amount of the special annual allowance specified in sub-paragraph (4) to be reduced by the amount of any protected pension input amounts and by certain pre-22 April 2009 pension input amounts attributable to contributions under money purchase arrangement that are not cash balance arrangements. Protected pension input amounts are defined in paragraphs 7 to 14 of the Schedule. Pre-22 April 2009 pension input amounts are defined in paragraph 16 of the Schedule.

8. Paragraphs 1(6) and 1(7) provide that the high-income individual is liable to pay the special annual allowance charge including when the individual is not resident, not ordinarily resident and not domiciled.

9. Paragraphs 1(8) and 1(11) set the rate of the special annual allowance charge and provide that the amount subject to the charge is not to be treated as income for any other tax purpose.

10. Paragraph 1(9) provides that the amount subject to the special annual allowance charge is reduced by any amount that is also subject to the annual allowance charge for the same tax year. The annual allowance charge arises under section 227 of the Finance Act (FA) 2004. It applies in respect of members of registered pension schemes when the pension input amounts in respect of the member for a tax year are higher than the annual allowance for that tax year. Income tax is charged on the excess at 40 per cent under section 227. The annual allowance is £245,000 in the 2009-2010 tax year and £255,000 in the 2010-2011 tax year. The definition of pension input amounts is set out in sections 229 to 237 of FA 2004.

11. Paragraph 1(10) provides that the special annual allowance charge is part of the individual's income tax liability for the tax year.

12. Paragraph 2 provides how to calculate "relevant income" for the purposes of determining whether an individual member of a registered pension scheme is a high-income individual and so potentially liable to pay the special annual allowance charge under paragraph 1.

13. Paragraph 2(1) and 2(4) provide how to calculate an individual's relevant income for the tax year. The amount of relevant income is:

- the total income of the individual for the tax year (Step 1);
- plus any pension contributions paid by the individual in respect of which there was a deduction in determining total income (Step 2);
- less any income tax deductions and reliefs other than for pension contributions that are deductible at Step 2 of the calculation of income tax liability in section 23 of the Income tax Act 2007 (Step 3);
- less the total pension contributions for which relief is due in the tax year up to a maximum of £20,000 (Step 4 and sub-paragraph (4) of Paragraph 2);
- plus taxable employment income that the individual has agreed to give up under a post-22 April 2009 salary sacrifice scheme (Step 5);
- less relief for charitable donations (step 6).

14. Paragraph 2(2) provides that an individual whose relevant income in the tax year is less than £150,000 is nonetheless a high-income individual for the purposes of the special annual allowance charge in that tax year if the individual's relevant income in either of the two preceding tax years was £150,000 or more.

15. Paragraph 2(3) provides that an individual shall be treated as subject to the special annual allowance charge if they have entered into a scheme one the main purposes of which is to reduce their relevant income to below £150,000 in order to prevent them from being subject to the special annual allowance charge.

16. Paragraphs 2(5) and 2(6) define when a post-22 April salary sacrifice scheme exists.

17. Paragraphs 3 to 16 provide how to calculate the "total adjusted pension input amount". In accordance with sub-paragraph (1) of paragraph 1 of this Schedule, the special annual allowance charge arises when the total adjusted pension input amount for an individual is higher than the special annual allowance as calculated for that individual.

18. Paragraph 3(1) introduces the provisions about how the total adjusted pension input amount is calculated.

19. Paragraph 3(2) provides that the total adjusted pension input amount is determined by first calculating what the total pension input amount would be if the provisions of sections 229 to 237 of FA 2004 were modified in accordance with paragraphs 4 and 5 of Schedule 35, unless paragraph 6 applies. Under the existing provisions of Part 4 of FA 2004, an individual is liable to the annual allowance charge for a tax year if the total adjusted pension input amount calculated in accordance with section 229 to section 237 of FA 2004 for the pension input period ending in the tax year exceeds the annual allowance for that tax year.

20. Paragraph 3(3) provides that the amount so calculated under sub-paragraph (2) is then reduced by any protected pension input amounts and relevant refunded amounts and, in the 2009-2010 tax year only, by pre-22 April 2009 pension input amounts. These amounts are determined in accordance with the later paragraphs of this Schedule.

21. Paragraph 4(1) modifies section 229(3) of FA 2004 for the purposes of the special annual allowance charge. Section 229(3) of FA 2004 prevents any pension input amounts from arising in relation to an arrangement in the tax year, in which an individual either dies or becomes entitled to all the benefits under that arrangement, when determining whether an individual is liable to the annual allowance charge under section 227 of FA 2004. Sub-paragraph (1) modifies the provisions by prescribing two conditions, one of which must be satisfied in order for section 229(3) to be taken into account when calculating the total adjusted pension input amount and so the amounts in respect of which the special annual allowance charge arises.

22. Paragraph 4(2) provides the first condition, Condition A, applying to defined benefits arrangements. If this condition applies, no amounts in respect of the arrangement will form part of the total adjusted pension input amount which is used to calculate the individual's liability to the special annual allowance charge.

23. Paragraph 4(3) provides the second condition, Condition B, applying to arrangements under occupational pension schemes, public service pension schemes and group personal pension schemes. If this condition applies, no amounts in respect of the arrangement will form part of the total adjusted pension input amount which is used to calculate the individual's liability to the special annual allowance charge.

24. Paragraph 5 provides that the total adjusted pension input amount is calculated by reference to the pension input amounts relating to tax years rather than by reference to the amounts relating to pension input periods ending in the tax year.

25. Paragraph 6(1) provides that paragraph 6 applies when there is an avoidance scheme whose purpose is to avoid either the lifetime allowance charge, the annual allowance charge or the special annual allowance charge by reducing the pension input amount calculated in accordance with sections 229 to 237 of FA 2004 as modified by paragraphs 4 and 5 of this Schedule.

26. Paragraph 6(2) provides that when paragraph 6 applies the amount calculated in accordance with paragraph 6(3) is substituted in the calculation of the total adjusted pension input amount for the individual if it gives a higher amount than would otherwise be calculated under paragraph 3(2).

27. Paragraphs 6(3) and 6(4) provide the method of calculation that may be applicable for the purposes of sub-paragraph (2) of paragraph 3 when there is an avoidance scheme to which paragraph 6 applies. The method of calculation is to deduct the arm's length assignment value of the entitlements of the individual under the arrangements at the beginning of the tax year from the assignment value of those entitlements at the end of the tax year in order to measure the increase in value. This calculation is made on the assumption that the rights under the scheme can be assigned and are valued without taking into account any power to reduce those entitlements.

28. Paragraph 6(5) provides for when an arrangement ceases to exist during the tax year.

29. Paragraph 6(6) provides that when carrying out the calculation according to sub-paragraphs (3) and (4), the closing value of the individual's rights is adjusted in accordance with section 236 of FA 2004 but irrespective of the type of arrangement under a pension scheme. In connection with the annual allowance charge, section 236 of FA 2004 applies only to defined benefit arrangements. It provides for a number of adjustments to the closing value of a defined benefit arrangement when calculating the total pension input amounts in respect of that arrangement in order to determine whether and how much of an annual allowance charge arises under section 227 of FA 2004.

30. Paragraph 7 introduces paragraphs 8 to 14 of the schedule, which defines "protected pension input amounts". A protected pension input amount is deducted both in determining the total adjusted pension input amount (paragraph 3) and in determining the amount of the special annual allowance (sub-paragraph (5) of paragraph 1).

31. Paragraph 8(1) provides when paragraph 8 applies in relation to a defined benefits arrangement under an occupational pension scheme or a public service pension scheme that existed on 21 April 2009.

32. Paragraph 8(2) provides that the pension input amount calculated in accordance with sections 229 to 237 of FA 2004, as modified by paragraphs 4 and 5 of this Schedule, (or the amount substituted for that by paragraph 6 when there is an avoidance scheme) is a protected pension input amount to the extent it is attributable to added year contributions.

33. Paragraph 8(3) defines "relevant added year contributions".

34. Paragraphs 8(4) and 8(5) provide that the pension input amount calculated in accordance with sections 229 to 237 of FA 2004, as modified by paragraphs 4 and 5 of this Schedule, (or the amount substituted for that by paragraph 6 when there is an avoidance scheme) is a protected pension input amount if there is no material change to the scheme rules on or after that date to the way in which the individual's benefits are calculated under the arrangement. But if there is such a material change the amount so calculated is prevented from being a protected pension input amount only to the extent attributable to that change.

35. Paragraph 8(6) provides that sub-paragraph (5) will not reduce the protected pension input amount provided the material change to the way in which the benefits are calculated affects at least 50 active members of the scheme. The definition of "active member" is in section 151 of FA 2004.

36. Paragraph 8(7) defines "the relevant end date" for the purposes of sub-paragraph (3) and (4) of paragraph 8.

37. Paragraph 9(1) provides when paragraph 9 applies in relation to a cash balance arrangement under an occupational pension scheme or a public service pension scheme that existed on 21 April 2009.

38. Paragraph 9(2) provides that the pension input amount calculated in accordance with sections 229 to 237 of FA 2004 as modified by paragraphs 4 and 5 of this schedule (or the amount substituted for that amount by paragraph 6 when there is an avoidance scheme) is a protected pension input amount to the extent that it is attributable to relevant additional voluntary contributions.

39. Paragraph 9(3) defines "relevant additional voluntary contributions".

40. Paragraphs 9(4) and 9(5) provide that, in addition to an amount that is a protected pension input amount by virtue of sub-paragraph 2, the pension input amount calculated in accordance with sections 229 to 237 of FA 2004 as modified by paragraphs 4 and 5 of this Schedule (or the amount substituted for that amount by paragraph 6 when there is an avoidance scheme) is a protected pension input amount to the extent it is attributable to contributions paid under an arrangement to which paragraph 9 applies in the period beginning with 22 April 2009. This is on condition that there is no material change to the scheme rules determining how the individual's benefits are calculated. But if there is such a material change to the scheme rules the pension input amount that is not a protected pension input amount is only the amount that is attributable to that change.

41. Paragraph 9(6) provides that sub-paragraph (5) will not reduce the protected pension input amount in respect of the individual so long as the material change to the way in which the benefits are calculated affects at least 50 active members of the scheme.

42. Paragraph 9(7) defines "the relevant end date" for the purposes of sub-paragraph (3) and (4) of paragraph 9.

43. Paragraph 10(1) provides when paragraph 10 applies in relation to money purchase arrangements (other than a cash balance arrangements) under an occupational pension scheme, a public service pension scheme or a group personal pension scheme that existed on 21 April 2009.

44. Paragraph 10(2) provides that a pension input amount calculated in accordance with sections 229 to 237 of FA 2004 as modified by paragraphs 4 and 5 of this Schedule (or the amount substituted for that amount by paragraph 6 when there is an avoidance scheme) is a protected pension input amount to the extent it is attributable to relevant additional voluntary contributions under a money purchase arrangement to which paragraph 10 applies.

45. Paragraph 10(3) defines "relevant additional voluntary contributions".

46. Paragraphs 10(4) and 10(5) provide that, in addition to an amount that is a protected pension input amount by virtue of paragraph 10(2), the pension input amount calculated in accordance with sections 229 to 237 of FA 2004 as modified by paragraphs 4 and 5 of this Schedule (or the amount substituted for that amount by paragraph 6 when there is an avoidance scheme) is a protected pension input amount to the extent it is attributable to contributions paid in the period beginning with 22 April 2009, paid at least quarterly, and payable at that rate under an agreement made before 22 April 2009.

47. Paragraph 10(6) defines "the relevant end date" for the purposes of sub-paragraphs (3), (4) and (5) of paragraph 10.

48. Paragraph 11(1) provides when paragraph 11 applies to a money purchase arrangement (other than a cash balance arrangement) that existed on 21 April 2009 and that is neither under an occupational pension scheme nor a public service pension scheme nor forms part of a group personal pension scheme.

49. Paragraph 11(2) provides how to determine the amount of protected pension input amount in respect of a money purchase arrangement to which paragraph 11 applies.

50. Paragraph 11(3) provides that paragraph 11 may apply to an individual who did not become an active member until after 21 April 2009 if an application for the individual to become an active member was received by the scheme administrator before noon on 22 April 2009.

51. Paragraph 11(4) defines "relevant end date" for the purposes of sub-paragraphs (1) and (2) of paragraph 11.

52. Paragraph 12(1) provides when paragraph 12 applies in relation to hybrid arrangements. A hybrid arrangement is an arrangement under a registered pension scheme under which the benefits it provides in respect of the member may ultimately be either defined benefits, cash balance benefits or other money purchase benefits or any two out of these three types of benefits. Hybrid arrangements are defined in subsection (8) of section 152 of FA 2004.

53. Paragraphs 12(2) to 12(5) provide how to determine the amount of the protected pension input amount in respect of a hybrid arrangement by applying to it whichever of the provisions in paragraphs 8 to 11 are appropriate.

54. Paragraph 13(1) provides when paragraph 13 applies in relation to new and reactivated arrangements under an occupational pension scheme, public service pension scheme or group personal pensions scheme.

55. Paragraph 13(2) provides that there can be no protected pension input amounts in respect of a new or reactivated arrangement if:

- either the benefits the employer provides under the arrangement fall outside the normal pattern of benefits that the employer provides to its employees generally; or

- there are not at least 20 other persons who have arrangements under the scheme accruing benefits on the same basis as the individual and who are also employees of the same employer.

56. Paragraph 13(4) provides that in relation to arrangements to which paragraph 13 applies the pension input amount calculated in accordance with sections 229 to 237 of FA 2004 as modified by paragraphs 4 and 5 of this schedule (or the amount substituted for that amount by paragraph 6 when there is an avoidance scheme) is a protected pension input amount except to the extent it is attributable to added years contributions and to additional voluntary contributions.

57. Paragraph 13(6) provides that if the arrangement is under an occupational pension scheme or group personal pension scheme paragraph 13 does not apply unless either the benefits are calculated by reference to the individual's earnings from the employment or the employer pays contributions under the arrangement in respect of the individual.

58. Paragraphs 13(3), (5) and (7) provide definitions.

59. Paragraph 14 provides an anti-avoidance rule in connection with the calculation of protected pension input amounts. It operates when there is a scheme to increase the amount of protected pension input amounts and so reduce the amount in respect of which there is a liability to either the special annual allowance charge, the annual allowance charge or the lifetime allowance charge. When paragraph 14 applies in relation to an individual there will be no protected pension input amount in respect of the individual under the arrangement that the avoidance scheme relates to or under any other arrangement in respect of the individual in the tax year.

60. Paragraph 15(1) provides that the relevant refunded amount is determined by reference to the contributions refund lump sum, which it cannot be more than. The relevant refunded amount is deducted in the calculation of the total adjusted pension input amounts and consequently reduces the amount on which the individual is liable to the special annual allowance charge.

61. Paragraph 15(2) defines a contributions refund lump sum. It can be paid only to a high-income individual, it has to be paid within 12 months after the end of the tax year, it cannot be an authorised lump sum payment under any other provision in Part 4 of FA 2004 and it cannot exceed the adjusted contributions amount for the tax year.

62. Paragraphs 15(3) and 15(4) define the adjusted contributions amount as the amount of relevant relievable pension contributions after deducting any relevant deductions.

63. Paragraph 15(5) provides that contributions under an occupational pension scheme, a public service pension scheme or group personal pension scheme may not be refunded by the scheme unless they are additional voluntary contributions but not relevant additional voluntary contributions.

64. Paragraph 15(6) provides that contributions under a pension scheme that is not an occupational pension scheme, a public service pension scheme or a group personal pension scheme may not be refunded by the scheme unless one of two conditions is met:

- either the contributions do not give rise to protected pension input amounts under paragraph 11(2); or

- they are contributions paid between 6 April 2009 and 21 April 2009 and they are not paid under an agreement for the payment of regular contributions.

65. Paragraph 15(7) defines the "relevant deductions".

66. Paragraph 16(1) introduces paragraph 16 which provides how to determine how much of the pension input amounts for the 2009-2010 tax year are pre-22 April 2009 pension input amounts. Pre-22 April 2009 pension input amounts do not give rise to the special annual allowance charge but they are:

- deducted in the calculation of the adjusted contributions amount for the 2009-2010 tax year; and

- deducted from the individual's special annual allowance for that tax year.

67. Paragraph 16(2) makes provision in respect of pre-22 April 2009 pension input amounts under defined benefit arrangements and cash balance arrangements

68. Paragraph 16(3) makes provision in respect of pre-22 April 2009 pension input amounts under money purchase arrangements that are not cash balance arrangements and provides that paragraph 16 does not apply to contributions paid on a quarterly or more frequent basis.

69. Paragraphs 16(4) and 16(5) make provision in respect of pre-22 April 2009 pension input amounts under hybrid arrangements equivalent to those under defined benefit, cash balance and other money purchase arrangements.

70. Paragraph 17 makes provision for an increased special annual allowance.

71. Paragraph 17(1) provides that paragraph 17 applies where the average of the infrequent money purchase contribution amounts for the years 2006/7, 2007/8 and 2008/9 exceeds £20,000. This average is titled 'the relevant mean'.

72. Paragraph 17(2) provides that where the relevant mean of infrequent money purchase contribution amounts for the years 2006/7, 2007/8 and 2008/9 is greater than £20,000 but less than £30,000 then the special annual allowance set by paragraph 1(4) is that average. This sub-paragraph also amends the references to £20,000 in paragraph 1(5) to that figure in such circumstances.

73. Paragraph 17(3) provides that where the relevant mean is £30,000 or more then the special annual allowance set by paragraph 1(4) is £30,000. This sub-paragraph also amends the references to £20,000 in paragraph 1(5) to that figure in such circumstances.

74. Paragraph 17(4) defines 'infrequent money purchase contributions amount'. These are relevant contributions paid in a tax year to money purchase arrangements (other than cash balance arrangements) of registered pension schemes which are paid less frequently than on a quarterly basis.

75. Paragraph 17(5) provides a limit on the infrequent money purchase contribution amounts for any year. These cannot exceed the annual allowance in place for the tax year. The annual allowance is set by Section 228 Finance Act 2004 and by regulations made under that section.

76. Paragraph 17(6) provides that for the purpose of this paragraph relevant contributions are either relievable pension contributions made by or on behalf of that individual or contributions paid by an employer of that individual in respect of that individual. This definition is used in sub-paragraph 4 to identify contributions.

77. Paragraph 18 provides that the contributions refund lump sum paid by a registered pension scheme is an authorised payment. It is consequently not liable to the unauthorised member payment charge (section 208 of FA 2004) the unauthorised member payment surcharge (section 209 of FA 2004) or the scheme sanction charge (section 240 of FA 2004) but it is liable to tax at the same rate as the top rate applicable to short service refund lump sums.

78. Paragraphs 19(1) to 19(4) provides powers to HM Treasury to amend the earlier paragraphs of the Schedule in secondary legislation.

79. Paragraph 19(5) provides that a statutory instrument to amend the rate of the special annual allowance charge is subject to affirmative resolution procedures in the House of Commons

80. Paragraph 19(6) provides that a statutory instrument to amend paragraphs 2 to 18 of the Schedule is subject to negative resolution procedures.

81. Paragraph 20 provides a power to HM Treasury to make regulations applying the provisions of Schedule 35 to people who have been members of overseas pension schemes that were not currently-relieved non-UK pension schemes and to those who are or have been members of currently-relieved non-UK pension schemes.

82. Paragraph 21 provides for the commencement of Schedule 35 and also provides a power for HM Treasury to make regulations switching off the special annual allowance charge from the beginning of a particular tax year.

83. Paragraph 22 provides that individuals who have elected for enhanced protection are not exempted from the special annual allowance charge.

84. Paragraph 23 provides definitions.

BACKGROUND NOTE

85. In the Budget, the Chancellor announced changes to the tax relief available on pension savings for individuals whose income is £150,000 or higher.

86. The Government intends to restrict the availability of tax relief to basic rate on contributions to registered pension schemes for individuals whose income is £150,000 or higher with effect from 6 April 2011.

87. In anticipation of that new restriction, the Government is introducing new rules to apply from 22 April 2009 to restrict higher rate tax relief on pension contributions for individuals - see Budget Note 47: "Pensions: limiting tax relief for high income individuals (anti-forestalling)" for details.

88. The restrictions will apply to people:

- whose income is £150,000 or higher;
- who change their normal ongoing regular pension savings; and
- whose total pension savings exceed £20,000 (which is increased up to £30,000 for those with a pattern of non regular contributions).

SECTION 73: FINANCIAL ASSISTANCE SCHEME

SUMMARY

1. Section 73 allows HM Treasury to make regulations about how tax provisions will apply in relation to the financial assistance scheme.

DETAILS OF THE SECTION

2. Subsection (1) provides that HM Treasury may make regulations about how the "relevant taxes" will apply in relation to the financial assistance scheme and to any person in connection with the financial assistance scheme.

3. Subsection (3) confirms that such regulations may impose, exempt or relieve from tax.

4. Subsection (4) sets out the types of tax for which the regulations may make provision (the "relevant taxes").

5. Subsection (5) allows the regulations to provide for the taxation of assistance payments made by the financial assistance scheme.

6. Subsection (6) sets out some of the types of tax exemption and relief for which the regulations may in particular provide.

7. Subsection (7) provides that the regulations may have effect from any time before they are made if they do not increase any person's tax liability.

8. Subsection (8) provides that the regulations may provide for individuals, who receive assistance payments made by the financial assistance scheme, to be subject to the same tax treatment as if the payments had been received from a registered pension scheme.

9. Subsection (9) allows the regulations to amend any existing legislation, and to make consequential, supplementary or transitional provisions.

10. Subsection (10) and (11) provide for the regulations to be made by statutory instrument subject to the negative resolution procedure in the House of Commons.

BACKGROUND NOTE

11. The financial assistance scheme was established under section 286 of the Pensions Act 2004. The scheme provides assistance to members of certain defined benefit occupational pension schemes that are no longer able to meet all their pension obligations.

12. The scope of the financial assistance scheme has been expanded both through regulations and the Pensions Acts of 2007 and 2008. In the future the financial assistance scheme will take in the assets of the qualifying pension schemes. The scheme will then make assistance payments to members of those pension schemes in lieu of their retirement benefits.

13. As the financial assistance scheme is not a registered pension scheme, individuals who receive assistance payments from it will not necessarily benefit from the same tax treatment as if the payments were made by such a scheme. Tax charges may apply to some assistance payments received by individuals, such as certain lump sum payments, which would not arise if the payment were made by the original registered pension scheme. Regulations will be made to ensure that individuals who receive assistance payments from the financial assistance scheme will be subject to the same tax treatment as if they had received pension benefits from the pension scheme.

SECTION 74: FSCS INVOLVEMENT IN RELATION TO INSURANCE IN CONNECTION WITH PENSIONS

SUMMARY

1. Section 74 provides a power to make regulations in connection with how taxes apply after an intervention by the Financial Services Compensation Scheme (FSCS) in relation to registered pension schemes. The power will have effect on and after the date of Royal Assent.

DETAILS OF THE SECTION

2. Subsections (1)-(10) provide that HM Treasury may make regulations in relation to how taxes apply when there is an intervention by the FSCS in connection with registered pension schemes.

3. Subsection (6) provides that the regulations can have retrospective effect, but only if they do not increase any person's tax liability.

4. Subsections (7)-(8) provide that the regulations may amend primary and secondary legislation.

BACKGROUND NOTE

5. The Financial Services Compensation Scheme (FSCS) is an independent body established by Part 15 of the Financial Services and Markets Act 2000. It is the UK's statutory fund of last resort for customers of authorised financial services firms, including insurers, banks, building societies and investment firms.

6. The FSCS protect policyholders of insurance companies authorised by the Financial Services Authority that are unable, or likely to be unable, to meet claims made against them.

7. Insurance companies can make pension provision which benefits from tax privileges in return for providing members with an income in retirement. Such pension provision can be registered as a registered pension scheme. They can also provide pensions in the form of annuities and transfer tax-relieved pension savings to other registered pension schemes. In doing so they must abide by the pensions tax rules or there will be tax charges that recoup the tax relief.

8. Individuals who have tax-relieved pension savings with an insurance company that gets into financial difficulties and becomes subject to an intervention by the FSCS may find that unexpected tax consequences arise from that intervention. In particular, tax is chargeable if a pension is reduced; the FSCS rules generally only allow 90 per cent of a pension to be paid by way of compensation.

9. Also, as the FSCS is not a registered pension scheme, it will not benefit from the same tax exemptions available to a registered pension scheme.

10. The section would provide the power to make regulations adapting the tax treatment applicable where the FSCS intervenes.

SECTION 75: POWER TO MAKE RETROSPECTIVE NON-CHARGING PROVISION

SUMMARY

1. Section 75 provides that any order or regulations made under the pensions tax rules in Part 4 of the Finance Act (FA) 2004 may apply retrospectively if they do not increase any person's tax liability. The section amends section 282 of FA 2004. The changes will have effect on and after the date of Royal Assent.

DETAILS OF THE SECTION

2. Subsection (1) inserts new subsections (A1) and (A2) into section 282 of FA 2004 to amend the powers to make an order or regulations under Part 4 of FA 2004.

3. New subsection (A1) provides that any order or regulations made under Part 4 may have retrospective effect if they do not increase any person's tax liability.

4. New subsection (A2) provides that the new general power in subsection (A1) does not limit other existing specific powers in Part 4 that allow an order or regulations to apply retrospectively.

5. Subsections (2)-(3) remove various existing provisions that allow an order or regulations to apply retrospectively if they do not increase any person's tax liability. These are no longer needed if they are replaced by the new general power in subsection (A1).

BACKGROUND NOTE

6. The pensions tax rules are set out in Part 4 of the Finance Act 2004. Further detailed rules are provided in orders and regulations made under powers in Part 4.

7. Many of the order and regulation-making powers in Part 4 already specifically provide that the order or regulations may take effect retrospectively if they do not increase any person's tax liability.

8. The proposed changes extend this so that those orders and regulations on pensions tax issues which currently cannot apply retrospectively, may do so provided they do not increase any person's tax liability.

SECTION 76 SCHEDULE 36: VAT: PLACE OF SUPPLY OF SERVICES ETC

SUMMARY

1. Section 76 and Schedule 36 implement the first phases of changes to the place of supply rules covered by the amendment to Directive 2006/112/EC made by Directive 2008/08/EC by incorporating all place of supply of services rules into a new section 7A of and Schedule 4A to the Value Added Tax Act 1994 (VATA). This legislation will have effect on 1 January 2010 (where not specifically stated), 1 January 2011 and 1 January 2013.

DETAILS OF THE SCHEDULE

2. Paragraph 2 makes a consequential amendment to section 6(14A) of VATA arising from the amendment made to section 7 of VATA by paragraph 2 of Schedule 36.

3. Paragraph 3 amends section 7 of VATA so that the section only applies to the place of supply of goods.

4. Paragraph 4 amends VATA by inserting after section 7 a new section 7A to determine the place of supply of services.

5. New section 7A(1) provides that new section 7A determines the country in which services are supplied for the purpose of VATA.

6. New section 7A(2) determines the place of supply for services.

7. New section 7A(3) determines the place of supply for the right, option or priority with respect to a supply of services.

8. New section 7A(4) defines the term a 'relevant business person' for the purposes of VATA.

9. New section 7A(5) provides that subparagraph 7A(2) has effect subject to Schedule 4A to VATA.

10. New section 7A(6) provides that HM Treasury may by Order amend section 7A(4) of and Schedule 4A to VATA or make provision for exceptions to section 7A(2).

11. New section 7A(7) provides that an order under subsection (6) may include incidental, supplemental, consequential and transitional provisions.

12. Paragraph 5(2) substitutes section 8(1) and (2) of VATA so that where the circumstances in section 8(2) apply, services received by a relevant business person who belongs in the UK from a person who belongs in a country other than the UK are treated as if they were a taxable supply made in the UK by the recipient in the course or furtherance of a business carried on by the recipient.

13. Paragraph 5(3) amends section 8 of VATA by inserting a new subsection (4A) so that section 8(1) does not apply to supplies described in Schedule 9 of VATA.

14. Paragraph 5(4) amends section 8(5) by removing reference to Schedule 5 of the VATA and provides that HM Treasury may, by Order, amend new subsection 4A by altering the descriptions of services within that subsection.

15. Paragraph 5(5) removes section 8(6) of VATA.

16. Paragraph 5(6) amends section 8(7) by removing reference to Schedule 5 of the VATA and provides that HM Treasury may by Order amend new Section 8(4A) by making further provisions to that subsection as they see fit.

17. Paragraph 5(7) amends section 8(8) of VATA by replacing "addition to or variation of that Schedule" with "amendment of subsection (4A) and "the Schedule" with "that subsection".

18. Paragraph 6 substitutes section 9 of VATA which determines, for the purposes of section 7A, Schedule 4A and section 8 of VATA whether a person who receives a supply or makes a supply (including a supply treated as made by virtue of the reverse charge mechanism in section 8) belongs in one country or another.

19. Paragraph 7 makes consequential amendments to section 43 of VATA and replaces references to Schedule 5 with the new section 7A(2)(a).

20. Paragraph 8 amends section 96 of VATA (interpretation) to provide that the term relevant business person has the meaning given by section 7A(4).

21. Paragraph 9 adds orders made under section 7A(6) to the list of Orders requiring Parliamentary approval.

22. Paragraph 10 amends Section 97A to apply to supplies of services which become treated as made in the UK by virtue of any order made under section 7A(6).

23. Paragraph 11 inserts a new Schedule 4A to VATA which deals with special rules in relation to the place of supply of services.

24. Paragraph 1 of Schedule 4A provides that a supply of services made in relation to land is to be treated as made in the country where the land is situated.

25. Paragraph 2 of Schedule 4A provides that a supply of services of passenger transport is to be treated as made in the country and/or countries in which the transportation takes place, in proportion to distance covered.

26. Paragraph 3(1) and (2) of Schedule 4A provides that the place of supply of services consisting of the short-term hire of transport is the country in which the transport is put at the disposal of the person by whom it is hired but this rule is qualified by

    - paragraph 3(3) which provides that where, under the general rule in section 7A, the place of supply of such services would be treated as occurring in the UK, then, to the extent that they are so used and enjoyed, the services will be treated as made in the country in which they are used and enjoyed if that country is not a Member State; and

- paragraph 3(4) which provides that where, under the general rule in section 7A, the place of supply of such services would be treated as occurring in a country that is not a Member State, then, to the extent that they are so used and enjoyed, the services will be treated as made in the UK if they are used and enjoyed in the UK.

27. Paragraph 4 of Schedule 4A provides that the place of supply of cultural, artistic, sporting, scientific, educational and entertainment or similar services is the country where the services are physically carried out.

28. Paragraph 5 of Schedule 4A provides that general restaurant and catering services are to be treated as occurring in the country where they are physically carried out, other than those services that are provided for by paragraph 6 of Schedule 4A.

29. Paragraph 6 of Schedule 4A provides that the place of supply of restaurant and catering services provided on board a ship, aircraft or train in connection with the transportation of passengers within the EC is the country in which the relevant point of departure is located.

30. Paragraph 7 of Schedule 4A provides an exception from the general place of supply rules in section 7A of VATA in relation to supplies comprising the hire of goods (other than a means of transport) so:

- where, under the general rule in section 7A, the place of supply of such hire of goods would be treated as occurring in the United Kingdom, then, to the extent that they are so used and enjoyed, the services will be treated as made in the country in which they are used and enjoyed if that country is not a Member State; and

- where, under the general rule in section 7A, the place of supply of such hires would be treated as occurring in a country that is not a Member State, then, to the extent that they are so used and enjoyed, the services will be treated as made in the UK if they are used and enjoyed in the UK.

31. Paragraph 8 of Schedule 4A provides an exception from the general place of supply rules in section 7A of VATA in relation to the telecommunications services defined in paragraph 8(2) and radio or television broadcasting services so:

- where, under the general rule in section 7A, the place of supply of such services would be treated as occurring in the UK, then, to the extent that they are so used and enjoyed, the services will be treated as made in the country in which they are used and enjoyed if that country is not a Member State; and

- where, under the general rule in section 7A, the place of supply of such services would be treated as occurring in a country that is not a Member State, then, to the extent that they are so used and enjoyed, the services will be treated as made in the UK if they are used and enjoyed in the UK.

32. Paragraph 9 of Schedule 4A provides an exception from the place of supply rules in section 7A(2)(a) of VATA in relation to electronically supplied services to a relevant business person (examples of which are given in paragraph 9(3) provided, as paragraph 9(4) makes clear, they are more than a mere communication between a supplier and customer by electronic mail) so:

- where, under the rule in section 7A(2)(a), the place of supply of such services would be treated as occurring in the UK, then, to the extent that they are so used and enjoyed, the services will be treated as made in the country in which they are used and enjoyed if that country is not a Member State; and

- where, under the general rule in section 7A(2)(a), the place of supply of such services would be treated as occurring in a country that is not a Member State, then, to the extent that they are so used and enjoyed, the services will be treated as made in the UK if they are used and enjoyed in the UK.

33. Paragraph 10 of Schedule 4A provides for an exception from the general rule in section 7A(2)(b) so that supplies made to a person who is not a relevant business person via intermediaries is treated as made in the same country as the related supply.

34. Paragraph 11 of Schedule 4A provides for an exception from the general rule in section 7A(2b) so that supplies comprising the transportation of goods made to a person who is not a relevant business person occur in the country in which the transportation takes place in proportion to the distances covered but this exception does not apply where the transportation begins in one Member State and ends in another.

35. Paragraph 12 of Schedule 4A provides for an exception from the general rule in section 7A(2)(b) so that supplies made to a person who is not a relevant business person that comprise a transportation of goods that begins in one Member State and ends in another are treated as made in the Member State in which the transportation begins.

36. Paragraph 13 of Schedule 4A provides for an exception from the general rule in section 7A(2)(b) so that supplies made to a person who is not a relevant business person that comprise ancillary transport services are treated as made where the services are physically performed.

37. Paragraph 14 of Schedule 4A provides for an exception from the general rule in section 7A(2)(b) so that supplies made to a person who is not a relevant business person that comprise the valuation of, or carrying out of work on, goods are treated as made where the services are physically performed.

38. Paragraph 15 of Schedule 4A provides for an exception from the general rule in section 7A(2)(b) so that a supply comprising electronically supplied services as described in paragraph 9 of Schedule 4A by a person who belongs in a country which is not a Member State (other than the Isle of Man) to a person ("the recipient") who, is not a relevant business person and belongs in a Member State, will be treated as made in the country in which the recipient belongs.

39. Paragraph 16 of Schedule 4A provides for an exception from the general rule in section 7A(2)(b) so that a supply falling within one of the descriptions listed in paragraph 16(2) made to a person ("the recipient")who is not a relevant business person and belongs in a country which is not a Member State (other than the Isle of Man), will be treated as made in the country in which the recipient belongs.

40. Paragraph 12 omits Schedule 5 to VATA (services supplied where received).

41. Paragraph 13 is a consequential amendment to ensure the continuation of the special place of supply rule in Article 5 of the Value Added Tax (Tour Operators) Order 1987 (S.I. 1987/1806) in relation to supplies of services by tour operators.

42. Paragraph 14 provides for the times from which the changes made by the Schedule have effect.

43. Paragraphs 15 and 16 amend Schedule 4A to VATA in relation to supplies made on or after 1 January 2011 by omitting paragraph 4 of Schedule 4A and inserting into that Schedule paragraphs 9A and 14A.

44. Paragraph 9A of Schedule 4A provides an exception from the place of supply rule in section 7A(2)(a) of VATA so that services in respect of admission to cultural, artistic, sporting, scientific educational, entertainment or similar events and ancillary services relating to the admission to such event made to a person who is a relevant business person will be treated as made in the country in which the events actually take place.

45. Paragraph 14A of Schedule 4A provides for an exception from the general rule in section 7A(2)(b) so that a supply comprising cultural, artistic, sporting, scientific, educational, entertainment or similar activities (and ancillary services relating to such activities) which is made to a person who is not a relevant business person is to be treated as made in the country in which the activities take place.

46. Paragraphs 17 and 18 amend Schedule 4A to the VATA in relation to supplies made on or after 1 January 2013 by inserting into that Schedule paragraph 13A.

47. Paragraph 13A of Schedule 4A provides for an exception from the general rule in section 7A(2)(b) so that a supply comprising the "long-term hire" of transport to a person who is not a relevant business person is treated as occurring in the country where the recipient belongs, (but there is an exception from this rule in relation the long-term hire of a pleasure boat).

48. Paragraph 19 introduces a transitional provision to avoid double taxation on services which are subject to the changes covered by this Schedule.

BACKGROUND NOTE

49. This section and Schedule make changes to the rules governing the place of supply for VAT purposes.

50. These changes are required to implement the first phases of changes in the VAT Place of Supply of Services Directive (Directive 2008/08/EC) into UK law. These changes were agreed as part of the VAT Package of legislation adopted in February 2008.

51. From 1 January 2010 the new general rule for the place of supply of services will tax business to business supplies of services at the place where the customer is established and no longer at the place where the supplier is established, as is the case at present.

52. For business to consumer supplies of services, the general rule for the place of supply will continue to be the place where the supplier is established.

53. As now, there are exceptions to the general rule for certain services, with a view to achieving taxation in the place of consumption. In the main these will be implemented on 1 January 2010, with further changes being introduced from 1 January 2011 and 1 January 2013.

54. This legislation includes provisions implementing the following European Community legislation: Directive 2008/08/EC. A Transposition Note setting out how the Government will transpose into UK law the main elements of this Directive is annexed below.

ANNEX A

Transposition Note: Articles 2(1), (6) and (7), 3 and 4 of Directive 2008/08/EC: Amending Chapter 3 of Title V, Section 1 of Chapter 1 of Title XI and Article 196 of Directive 2006/112/ EC as regards the place of supply of services.

A table setting out how the various Articles are transposed into UK law is below.

The proposals for the changes to the place of supply of services for supplies to business customers contained in Directive 2008/8/EC were originally submitted to the EU Scrutiny Committee in January and February 2004 (EM and SEM 5051/04) with a RIA. The proposals were passed by the House of Commons on 16 March 2004 and the House of Lords on 25 May 2004. Subsequent amended proposals were submitted to the Committee on 30 September 2005 (EM 11439/05) in relation to supplies to business and private consumers. These were passed by the House of Commons on 28 February 2006 after a standing committee debate on 16 February 2006 and by the House of Lords on 15 March 2006.

The proposals were adopted by Finance Ministers in the February 2008 ECOFIN

References to Articles in the table below relate to the amended Articles of Directive 2006/112/EC.

Article	**Objective**	**Implementation** (of the VAT Act 1994)
Article 43	Article 43 provides that a taxable person who also carries out activities or transactions that are not taxable supplies of goods or services within Article 2(1) is regarded as a taxable person in relation to all services rendered to him for the purposes of the place of supply rules and further extends the meaning of taxable person in this context to include a non-taxable legal person who is identified for VAT purposes in a Member State.	Section 7A(4)
Article 44	Article 44 provides that the general place of supply rule for services made to business customers is where the customer belongs.	Section 7A(2)(a)
Article 45	Article 45 provides that the general place of supply rule for services made to non-business customers is where the supplier belongs.	Section 7A(2)(b)
Article 46	Article 46 provides that the place of supply of services by intermediaries to non-business customers is where the supply being arranged takes place.	Schedule 4A, paragraph 10
Article 47	Article 47 provides that the place of supply of services connected with land is where the land is situated.	Schedule 4A, paragraph 1

Article 48	Article 48 provides that the place of supply of passenger transport is where the transport takes place, proportionate to the distances covered.	Schedule 4A, paragraph 2
Article 49	Article 49 provides that the place of supply of the transport of goods to non-business customers, other than the intra-Community transport of goods, is where the transport takes place, proportionate to the distances covered.	Schedule 4A, paragraph 11
Article 50	Article 50 provides that the place of supply of intra-EC transport of good to non-business customers is the place of departure.	Schedule 4A, paragraph 12
Article 51	Article 51 defines the meaning of the term "intra-EC transport of goods" and the term "the place of departure".	Schedule 4A, paragraph 12
Article 52	Article 52 provides that Member States need not apply VAT on the element of intra-EC transport of goods to non-business customers that takes place over waters that do not form part of the Community.	Schedule 4A, paragraph 12
Article 53	Article 53 provides that the place of supply of services and ancillary services related to cultural, artistic, sporting, educational, entertainment and similar services as well as organising such activities is where the activities are physically carried out.	Schedule 4A, paragraph 4
Article 54	Article 54 provides that the place of supply of ancillary transport services and valuation and work on goods supplied to non-business customers is where the services are physically carried out.	Schedule 4A, paragraphs 13 and 14
Article 55	Article 55 provides that restaurant and catering services, other than those performed on board ships, aircraft, or trains during a section of transport within the Community, are supplied where physically carried out.	Schedule 4A, paragraph 5
Article 56	Article 56 provides that the short time hire of a means of transport is supplied where the means of transport is actually put at the disposal of the customer.	Schedule 4A, paragraph 3
Article 57	Article 57 provides that the place of supply of restaurant and catering services onboard ships, aircraft or trains during a section of passenger transport within the Community is at the point of departure of the passenger transport.	Schedule 4A, paragraph 6

Article 58	Article 58 provides that the place of supply of electronically supplied services supplied to non-business customers that belong in a Member State by a taxable person that belongs outside of the Member States is the place where the customer belongs.	Schedule 4A, paragraph 15
Article 59	Article 59 provides that the place of supply of certain specified intangible services when supplied to non-business customers that belong outside of the Member States is where the customer belongs.	Schedule 4A, paragraph 16
Article 59a	Article 59a allows Member States discretion, in relation to supplies whose place of supply is governed by Articles 44 (supplies to business customers), 45 (supplies to non-business customers), 56 (short-term transport hires) and 59 (intangible services to non-business customers (but excluding electronically supplied services)) and which, under those rules, would otherwise be treated as occurring in the Member State concerned or outside the Member States, to be treated as occurring where they are used and enjoyed if that use and enjoyment occurs in the Member State concerned or outside the Member States as appropriate.	Schedule 4A, paragraphs 3, 7, 8 and 9
Article 59b	Article 59b requires Member States to treat telecommunications services and radio and television broadcasting services supplied by taxable persons belonging outside the Member States to non-business customers belonging in the Member State concerned as occurring in that Member State to the extent that such services are used and enjoyed there.	Schedule 4A, paragraph 8
Article 192a	Article 192a states that a supplier that has a fixed establishment within the territory of the Member State where tax is due on a supply shall be regarded as not established in that Member State if the fixed establishment does not intervene in that supply.	Section 9
Article 53 (from 1 January 2011)	Article 53 introduced on 1 January 2010 is modified from 1 January 2011 so that it governs only the place of supplies comprising admission to cultural, artistic, sporting, scientific, educational, entertainment or similar events made to business customers and fixes the place of such supplies as the place where such events actually take place.	Schedule 4A, paragraph 9A (from 1 January 2011)

Article 54 (from 1 January 2011)	Article 54 is modified from 1 January 2011 so that, in addition to the services governed by it with effect from 1 January 2010, it will also govern the place of supply of cultural, artistic, sporting, educational, entertainment and similar activities supplied to non-business customers by fixing their place of supply as the place where those activities actually take place.	Schedule 4A, paragraph 14A (from 1 January 2011)
Article 56 (from 1 January 2013)	Article 56 introduced on 1 January 2010 is modified from 1 January 2013 so that the place of supply of the hire (other than a short-term hire) of a means of transport to a non-business customer is where the customer belongs, unless it is a pleasure boat; the place of supply of such pleasure boat hires will be the place where it is actually put at the disposal of the customer if this takes place at the supplier's place of business or fixed establishment.	Schedule 4A, paragraph 13A (from 1 January 2013)
Article 196 (from 1 January 2010)	Article 196 provides that business customers and non-business customers that are identified for VAT purposes must account for VAT chargeable on supplies made to them by suppliers who do not belong in the same Member State as them if the supply is treated as made in the Member State where the customer belongs by virtue of Article 44.	Section 8

SECTION 77: REPAYMENT TO THOSE IN BUSINESS IN OTHER STATES

SUMMARY

1. Section 77 amends the Value Added Tax Act 1994 (VATA) to enable the UK to fulfil its legal obligations under EC law (principally Directive 2008/9/EC) in respect of a revised EU-wide scheme enabling, subject to meeting certain legal requirements, a business established in a Member State to obtain refunds of VAT it incurs in another Member State from the tax authority of that state.

DETAILS OF THE SECTION

2. Subsection (2) amends section 39(3) of VATA by amplifying and extending the current power afforded to the Commissioners for HM Revenue and Customs ('the Commissioners') by section 39(1), to embody in Regulations a scheme for making VAT repayments to non-UK businesses by providing:

   - that repayments should be made only to the extent specified in the regulations;
   - that the power to treat a repayment claim as if it were a VAT return may be in respect of such period as may be prescribed by the regulations;
   - the regulations may require the payment of interest to or by the Commissioners (including in relation to repayment of interest wrongly paid); and
   - the time by which and manner in which claims must be made.

3. Subsection (3) inserts a new section 39A, which provides that the Commissioners must put in place and maintain the necessary arrangements to allow businesses in the UK to submit claims to other Member States.

4. Subsection (4) inserts a new sub-paragraph (ha) into section 83(1), which provides refund claimants with a clear right of appeal against any decision by the Commissioners to refuse payment of a claim.

BACKGROUND NOTE

5. Businesses which are registered for VAT can normally recover VAT they incur on business expenses by claiming it on their VAT return. They cannot, however, recover VAT incurred in other EC Member States (MS) in this way. The Cross Border Refund Scheme enables them to recover this VAT.

6. Under the current scheme, covered by Directive 79/1072/EEC, businesses submit paper claims direct to the MS in which they incurred VAT (the Member State of Refund - MSREF). The system is lengthy and burdensome, and claims are often paid late or not at all.

7. A new EC Refund Directive comes into force on 1 January 2010, which requires MS to set up a new electronic refund system. From that date, businesses will submit claims to other MS electronically in their own MS (the Member State of Establishment - MSEST). They will receive electronic notifications that their claim has been received and forwarded by the MSEST, and received by the MSREF.

8. The current paper-based system for obtaining refunds of VAT will be replaced from 1 January 2010 by a common electronic system covering every Member State. Businesses seeking repayment of VAT from a Member State in which they are not established must submit their claim to that country via the electronic portal of their own country.

9. Where a repayment claim is made via a country's electronic portal, it is required to make the administrative arrangements to ensure that the claim is forwarded to the country from which repayment is requested. Upon receipt of a claim for repayment addressed to it, a Member State must determine whether the claimant is entitled to the repayment within strict time limits (with a requirement to pay interest in cases of late repayment), and afford a right of appeal against a refusal to make repayment.

10. The revised scheme will apply to all repayment claims made on or after 1 January 2010 including claims made in relation to certain VAT incurred before that day. Legislative amendments made by this section enable the Commissioners for HM Revenue & Customs to fulfil their obligations to facilitate UK businesses in obtaining refunds from other Member States and, by means of Regulations, to enable businesses established in other Member States to obtain refunds of VAT incurred in the UK.

11. Businesses will benefit from longer timescales in which to submit their claims compared with the current system, while there will be shorter and more certain timescales in which MSREF must notify their decisions and make payments. Where MSREF fail to meet these deadlines, they must pay interest to the business. Businesses will also have a right of appeal against decisions made by MSREF.

12. MSREF will have powers to impose penalties against businesses who submit fraudulent claims, or claims which are inaccurate due to deliberate or careless conduct by the business.

13. A Transposition Note setting out how the Government will transpose into UK law the main elements of this Directive is below.

Transposition Note: Council Directive 2008/9/EC

Transposition Note setting out how the VAT Act 1994 and other legislation implement the changes to the Cross-Border VAT Refund Scheme.

The Directive

Council Directive 2008/9/EC of 12 February 2008 is concerned with the procedure whereby a business registered for VAT in one Member State can recover VAT incurred, for business purposes, in another Member State. The current paper based system will be replaced by an electronic one. Businesses will have a longer period in which to submit their claims, but there will be shorter and more certain time limits within which Member States will have to pay refunds. Where these are not met, the Member State concerned will have to pay interest to the refund applicant. The Directive takes effect on 1 January 2010.

Introduction

This Directive replaces Council Directive 79/1072/EEC where the Cross Border Refund provisions are currently contained. These are transposed in section 39 of the VAT Act 1994, and Part XX (Regulations 173-184) of the VAT Regulations 1995 (SI 1995/2518). The significant changes to existing provisions are made in Article 7 to provide for electronic submission of claims, Article 15 to allow extended time limits for submission of claims, Articles 19, 21 and 22 to specify more certain time limits for Member States of Refund to notify decisions and make payment, and Articles 26 and 27 to provide for interest to be paid to the applicant where these time limits are not met. The remaining Articles provide the supporting framework for the operation of the new electronic system.

Articles	Objective	Implementation
Article 7	Provides that refund claims shall be submitted via an electronic portal in the Member State of Establishment.	VAT Act 1994, section 39(3); Draft Regulation 11
Article 9	Provides that information on types of expenditure shall be provided using standard codes.	VAT Act 1994, section 39(3); Draft Regulations 15(h) and 17.
Article 10	Sets out the requirement for claims to be accompanied by scanned copy invoices for expenditure exceeding certain limits, if required by the Member State of Refund.	VAT Act 1994, section 39(3); Draft Regulations 11 and 12.
Article 11	Provides that the Member State of Refund may require the applicant to describe his business activity by means of standard codes.	VAT Act 1994, section 39(3); Draft Regulation 14(c).

Articles	Objective	Implementation
Article 12	Provides that the Member State of Refund may specify the language(s) to be used in refund claims and additional information.	VAT Act 1994, section 39(3); Draft Regulation 11(b).
Article 13	Sets out the requirement for partially exempt businesses who use a single pro-rata rate to notify any change in that rate.	VAT Act 1994, section 39(3); Draft Regulation 7(1)(b).
Article 15	Sets the time limit for submission of claims at nine months from the end of the calendar year in which the VAT was incurred.	VAT Act 1994, section 39(3); Draft Regulation 18(1).
Article 17	Sets minimum monetary amounts for which claims may be submitted at EUR 400 where the claim covers less than a calendar year but more than three months, and EUR 50 where the claim covers a calendar year or the remainder thereof (or equivalent in national currency in both cases).	VAT Act 1994, section 39(3); Draft Regulation 10.
Article 18	Requires the Member State of Establishment to put in place the necessary electronic means through which businesses can submit claims which are then directed to the appropriate Member State of Refund.	VAT Act 1994, section 39A.
Article 19(1)	Requires the Member State of Refund to notify the applicant electronically that it has received the claim.	VAT Act 1994, section 39(3). Draft Regulation 18(4).
Article 19(2)	Requires the Member State of Refund to notify the applicant electronically of its decision to approve or refuse the claim, within four months of receipt.	VAT Act 1994, section 39(3). Draft Regulations 19(1) and 22

Articles	Objective	Implementation
Article 21	Sets out further time limits, up to a maximum of eight months, in which the Member State of Refund can request further information and notify the applicant of its decision to approve or refuse the claim.	VAT Act 1994, section 39(3). Draft Regulations 19(1), 20, 21 and 22.
Article 22	Provides that the Member State of Refund must pay any approved amount within ten working days of the time limits set out in Article 19(2) and 21.	VAT Act 1994, section 39(3)(ba); Draft Regulations 26 and 27.
Article 23	Provides that applicants may appeal against any decision according to the procedures applying in the Member State of Refund	VAT Act 1994, section 83(1)(ha).
Article 24	Provides that the Member State of Refund may recover VAT, penalties and interest where refunds have been obtained incorrectly or fraudulently.	VAT Act 1994, sections 39(3)(b)(ii) and 73(2); draft Regulation 9 (assessment of VAT incorrectly or fraudulently claimed). VAT Act 1994, section 72 (criminal penalties). Finance Act 2007, Schedule 24 (civil penalties). VAT Act 1994, section 74 (interest on VAT incorrectly or fraudulently claimed). VAT Act 1994, section 39(3)(ba); draft Regulation 28 (assessment of repayment interest incorrectly paid).
Article 25	Provides that the Member State of Refund may adjust the amount to be repaid in respect of any adjustments made under Article 13.	VAT Act 1994, section 39(3)(c); Draft Regulations 7(2) and 7(3).

Articles	Objective	Implementation
Articles 26/27	Requires that the Member State of Refund must pay interest to the applicant where payment is not made in accordance with the time limit in Article 22.	VAT Act 1994, section 39(3)(ba); Draft Regulation 27.

SECTION 78: INFORMATION RELATING TO CROSS-BORDER SUPPLIES OF SERVICES TO TAXABLE RECIPIENTS

SUMMARY

1. Section 78 enables regulations to be made which will require businesses to submit EC Sales Lists for cross border supplies of services. The current requirement only applies to supplies of goods.

DETAILS OF THE SECTION

2. Subsection (2) amends sub-paragraph 2(3) of Schedule 11 to the VAT Act 1994 (VATA) to introduce a new sub-paragraph describing the transactions that sub-paragraph 2(3) applies to.

3. Subsection (3) inserts new sub-paragraph (3ZA) into paragraph 2 of Schedule 11 to VATA. The new sub-paragraph specifies that EC Sales Lists can be required for both supplies of goods and services between EU Member States.

BACKGROUND NOTE

4. Currently, Council Directive 2006/112/EC ('the Principal VAT Directive') requires a taxpayer who makes cross border supplies of goods to submit a recapitulative statement ('EC Sales List') which provides information about those supplies.

5. The Principal VAT Directive has been amended by Council Directive 2008/8/EC (the amending directive). The amending directive makes changes to the rules governing the place of supply of services. In addition from 1 January 2010 the recipients of the majority of cross border supplies of services between taxable persons will be required to account for VAT on them under the reverse charge mechanism in accordance with Article 196 of the Principal VAT Directive and a taxpayer who supplies such services will be required to submit an EC Sales List in respect of them.

6. The requirement to submit an EC Sales List is implemented in UK legislation by Part IV of the Value Added Tax Regulations 1995. The power to make those regulations is contained in paragraph 2(3) of Schedule 11 to VATA. That power only applies to supplies of goods. This section extends the application of the power to supplies of services and enables the Commissioners for HM Revenue and Customs to implement the amendments to the EC sales list requirements in the Principal VAT Directive by amending the Value Added Tax Regulations.

Annex 1

Transposition Note: Council Directive 2008/8/EC
This Note sets out how section 78 is operative in implementing the amendment to the rules concerning the submission of recapitulative statements (known as EC Sales Lists in the UK).

The Directive

Council Directive 2006/112/EC ('the Principal VAT Directive') imposes a common system of value added tax applicable in all Member States. Council Directive 2008/8/EC ('the amending directive') amends the Principal VAT Directive's rules governing the place of supply of services and also makes other consequential amendments, in particular to the rules governing a taxable person's obligations to make a recapitulative statement about that person's cross-border supplies.

Introduction

Chapter 6 of the Principal VAT Directive (Articles 262 to 271) requires every VAT registered person making intra community taxable supplies of goods to submit a recapitulative statement about those supplies. This requirement is implemented by Part IV of the Value Added Tax Regulations 1995. Paragraph 2(3) of Schedule 11 to VATA provides the vires for those regulations. Sub-paragraphs 9 and 10 of Article 2 of the amending directive amend Articles 262 and 264(1) of the Principal VAT Directive so that, with effect from 1 January 2010, every VAT registered person will also be required to make a recapitulative statement about intra community supplies of services where those services are subject to a reverse charge in accordance with Article 196 of that Directive. In order to implement the amendments to Articles 262 and 264(1) by amendment to the VAT Regulations the vires in paragraph 2(3) of Schedule 11 to the VATA need to be enhanced so that the power to regulate applies not only to the movement of goods between Member States but also to the supply of services to a person in a Member State other than the United Kingdom where that supply is subject to a reverse charge. Section 78 amends paragraph 2 of the VATA to provide the necessary vires.

Articles	Objective	Implementation
Article 2	Requires every taxable person to submit a recapitulative statement (EC Sales List) of that person's taxable cross border supplies of services (which are subject to the reverse charge in accordance with Article 196 of Council Directive 2006/112/EC) ar cross-border supplies of goods.	To be implemented by an amendment to Part IV of the Value Added Tax Regulations 1995 using the regulatory powers provided for in Paragraph 2(3) of Schedule 11 to VATA.
Article 2 (1)	Specifies the information required in the recapitulative statement (EC Sales List) for both taxable cross border supplies of services (which are subject to the reverse charge in accordance with Article 196 of Council Directive 20 /112/EC) in addition to the cross-border supply of goods.	To be implemented by amendment to Part IV of the Value Added Tax Regulations 1995 under the regulatory powers provided for in paragraph 2(3) of Schedule 11 to VATA.

SECTION 79: EFFECT OF VAT CHANGES ON ARBITRATION OF RENT FOR AGRICULTURAL HOLDINGS

SUMMARY

1. Section 79 amends the Agricultural Holdings Act 1986 (AHA) so that the exercise or revocation of the option to tax or a change in the rate of VAT does not qualify as a change of rent for the purposes of AHA.

DETAILS OF THE SECTION

2. Subsection (1) provides for an amendment to paragraph 4 of Schedule 2 to AHA. The exercise or revocation of the option to tax by a landlord or a change in the rate of VAT applicable to the lease will not affect the right of either party to the lease to apply for an arbitration of rent.

3. Subsection (2) provides that the amendment will apply to options, revocations or VAT rate changes that have effect before the date of Royal Assent.

4. Subsection (3) clarifies that the reference to "option to tax" also includes an "election to waive exemption" if made before 1 June 2008. Similarly, any references to the "exercise or revocation" of such an option include the "making or revocation" of such an election.

BACKGROUND NOTE

5. On 18 December 2008, the High Court ruled in the case of Mason v Boscawen that the VAT charged on rent is part of the rent for the purposes of the Agricultural Holdings Act 1986.

6. It was noted that a change in the rate of VAT chargeable is a change of rent which therefore, prevents the parties to a lease from referring the rent to arbitration for a period of three years from the date of the rate change. The exercise or revocation of the option to tax by a landlord also has the same effect.

7. The section causes changes in the VAT chargeable on rents to be disregarded for the purposes of the rent arbitration provisions of the AHA. It is effective for rate changes, options or revocations which occurred before the date of Royal Assent.

SECTION 80: STAMP DUTY LAND TAX: EXERCISE OF COLLECTIVE RIGHTS BY TENANTS OF FLATS

SUMMARY

1. Section 80 provides for the stamp duty land tax relief at section 74 of the Finance Act (FA) 2003 to be amended to remove the references to a statutory right to enfranchise (RTE) company.

DETAILS OF THE SECTION

2. Subsection (2) substitutes a new subsection (1) of section 74 of FA 2003, so that the section applies where a chargeable transaction is entered into by a nominee or appointee of qualifying tenants of flats in exercise of rights under Part 1 Landlord and Tenant Act 1987 or Chapter 1 of Part 1 of the Leasehold Reform, Housing and Urban Development Act 1993.

3. Subsection (3) amends subsection (2) of section 74 of FA 2003, to provide that the rate of tax is determined by dividing the consideration for the transaction by the number of qualifying flats.

4. Subsection (4) substitutes a new subsection (4) into section 74 of FA 2003, to define "flat", "qualifying tenant" and "qualifying flat".

5. Subsection (6) amends a reference to section 74 in section 55 of FA 2003 (which determines the amount of tax chargeable) to reflect the amended heading.

BACKGROUND NOTE

6. Leaseholders in blocks of flats have certain statutory rights to acquire the freehold of the block. These are a right of first refusal if the landlord wishes to sell (under Part 1 of the Landlord and Tenant Act 1987) and a right to require the landlord to sell the freehold if a majority of the leaseholders request it (under Chapter 1 of Part 1 of the Leasehold Reform, Housing and Urban Development Act 1993). These acquisitions are undertaken by nominees or appointees (either an individual or a company) on behalf of the participating leaseholders.

7. Stamp duty land tax (SDLT) is charged at higher rates for higher levels of consideration. This means that individual leaseholders may pay a higher rate of SDLT in respect of their contribution to the purchase than would be the case if they were able to purchase the freehold of their individual flat.

8. SDLT legislation therefore includes a relief which sets the rate of tax charged according to the consideration given for the freehold divided by the number of flats in respect of which the right is being exercised.

9. When SDLT was introduced, legislation was being enacted to provide that the right under the 1993 Act must be exercised by a statutory Right to Enfranchise (RTE) company. The relief therefore refers to purchases by a RTE company. However, the RTE company provisions have never been commenced, so the SDLT relief could not be claimed.

10. This section removes the references to RTE companies and allows the relief to be claimed.

SECTION 81: STAMP DUTY LAND TAX: REGISTERED PROVIDERS OF SOCIAL HOUSING

SUMMARY

1. Section 81 provides for profit-making registered providers of social housing to claim the stamp duty land tax relief for acquisitions by Registered Social Landlords (RSLs). It also provides for lessees of shared ownership leases and beneficiaries of shared ownership trusts provided by registered providers of social housing to benefit from special stamp duty land tax treatment.

DETAILS OF THE SECTION

2. Subsection (3) inserts a new subsection (A1) into section 71 of Part 4 of the Finance Act (FA) 2003, to provide that a land transaction under which the purchaser is a profit-making registered provider of social housing is exempt from charge if the transaction is funded with the assistance of a public subsidy.

3. Subsection (4) amends section 71(4) of Part 4 of FA 2003 to take account of new subsection (A1).

4. Subsection (6) amends paragraph 5 of Schedule 9 to FA 2003 to provide that a registered provider of social housing that is not a housing association is a "qualifying body" in connection with a shared ownership lease if the purchase, construction or adaptation of the premises for use as a dwelling, by that body or a person connected with it, has been funded with the assistance of a grant or other financial assistance under section 19 of the Housing and Regeneration Act 2008.

5. Subsection (7) amends paragraph 7 of Schedule 9 to FA 2003 to provide that a registered provider of social housing that is not a housing association is a "qualifying body" in connection with a shared ownership trust if the purchase, construction or adaptation of the premises for use as a dwelling, by that body or a person connected with it, has been funded with the assistance of a grant or other financial assistance under section 19 of the Housing and Regeneration Act 2008.

6. Subsection (8) provides that the amendments made by the section have effect for transactions where the effective date is on or after the date of Royal Assent.

BACKGROUND NOTE

7. The Housing and Regeneration Act 2008 introduces a new regime of registered providers of social housing, to replace RSLs in England. These can be either non-profit (like RSLs) or profit-making bodies. Consequential provisions in the Housing and Regeneration Act 2008 amend stamp duty land tax legislation in Part 4 of FA 2003, to add references to non-profit registered providers to existing references to RSLs.

8. Profit-making registered providers will be subject to the same regulatory regime, will address the same housing priorities and will be able to apply for public funding on the same basis as non-profit registered providers.

9. This section allows profit-making registered providers to claim the stamp duty land tax relief for acquisitions by RSLs. It also allows clients of these bodies who acquire a shared ownership lease, or participate in a shared ownership trust, to benefit from the favourable stamp duty land tax treatment afforded to these schemes. As these providers may also undertake commercial housing provision, the favourable treatment is only available where the acquisition or, respectively, the shared ownership scheme, is assisted by public subsidy.

SECTION 82: STAMP DUTY LAND TAX: RENT TO SHARED OWNERSHIP

SUMMARY

1. Section 82 provides for a simplification of the stamp duty land tax rules as they apply to "rent to shared ownership" schemes.

DETAILS OF THE SECTION

2. Sub-paragraph (1) inserts new paragraphs 13 and 14 at the end of Schedule 9 to Finance Act (FA) 2003.

3. New paragraph 13(2) defines a "rent to shared ownership lease scheme" as one in which a qualifying body grants an assured shorthold tenancy to a person or persons and subsequently grants a shared ownership lease to one or more of them.

4. New paragraph 13(3) provides that transactions in connection with the scheme are not treated as linked to each other.

5. New paragraph 13(4) provides that the tenant's possession of the dwelling under an assured shorthold tenancy is disregarded in determining the effective date of the grant of the shared ownership lease.

6. New paragraph 14(2) defines a "rent to shared ownership trust scheme" as one in which a social landlord grants an assured shorthold tenancy to a person or persons and one or more of them subsequently becomes a purchaser under a shared ownership trust.

7. New paragraph 14(3) provides that transactions in connection with the scheme are not treated as linked to each other.

8. New paragraph 14(4) provides that the tenant's possession of the dwelling under an assured shorthold tenancy is disregarded in determining the effective date of the declaration of the shared ownership trust.

9. Sub-paragraph (2) provides that the amendment made by the section has effect for cases where the effective date of the grant of the shared ownership lease or the declaration of the shared ownership trust is on or after 22 April 2009.

10. Sub-paragraph (3) provides that possession of the property under the assured shorthold tenancy is disregarded in determining the effective date for this purpose.

BACKGROUND NOTE

11. "Rent to shared ownership" (generally known as "Rent to Homebuy") is a scheme under which the grant of a shared ownership lease (or the declaration of a shared ownership trust) is preceded by the grant of an assured shorthold tenancy at a subsidised rent in order to allow the tenant to occupy the property while saving for a deposit.

12. Depending on the details of the scheme and the amounts of consideration involved, the stamp duty land tax (SDLT) rules may result in unexpected liabilities at a time when the purchaser is least able to bear them.

13. In particular, a charge may arise retrospectively on the assured shorthold tenancy (and any other preceding land transaction) when the shared ownership lease is granted or the shared ownership trust is declared. In some other cases, the shared ownership lease (or shared ownership trust) may become chargeable when the tenant takes up occupation under the assured shorthold tenancy, but before the lease is granted (or the trust is declared).

14. This Section simplifies the SDLT treatment of these schemes so that a charge arises only on the shared ownership lease when it is granted, or on the shared ownership trust when it is declared.

SECTION 83 SCHEDULE 37: STAMP TAXES IN THE EVENT OF INSOLVENCY

SUMMARY

1. Section 83 and Schedule 37 provide relief from stamp duty and stamp duty reserve tax (SDRT) where, under a stock lending or sale and repurchase arrangement, securities are not returned to the originator because of the insolvency, on or after 1 September 2008, of one of the parties.

DETAILS OF THE SECTION

2. Subsection (1) introduces amendments to Part 3 (stamp duty) and Part 4 (stamp duty reserve tax) of the Finance Act (FA) 1986.

3. Subsection (2) provides that the amendments made by the Schedule have effect where one of the parties to a stock lending or repurchase arrangement (repo) becomes insolvent on or after 1 September 2008.

2. Subsection (3) provides that this section and Schedule will cease to have effect if the provisions of sections 107 to 110 of FA 1990 repealing stamp duty and SDRT are brought into effect.

DETAILS OF THE SCHEDULE

PART 1

3. Paragraph 2 inserts a new section 80D into FA 1986.

4. Subsection (1) of new section 80D provides that the section applies where A and B have entered into an arrangement to which section 80C applies, the conditions in subsections (2A) and (3) of that section are fulfilled, stock is transferred to A or his nominee and the conditions in subsection 80D(2) are fulfilled.

5. New section 80D(2) sets out the conditions that must be fulfilled for the section to apply. These are that A and B are not connected persons, have entered into a stock lending arrangement or a repo, and it becomes apparent, after B has transferred the stock to A or his nominee, that the stock will not be returned to B or his nominee, because of the insolvency of A or B, and the solvent party acquires replacement stock within thirty days of the date on which the insolvency occurs.

6. New section 80D(3) provides that, where collateral is provided under the arrangement, stamp duty will not be chargeable on any instrument by means of which replacement stock is transferred to the solvent party or his nominee where the solvent party uses the collateral provided to make the acquisition or, where the amount of collateral is insufficient, the solvent party uses his own funds to make up the balance of the cost of the replacement purchase.

7. New section 80D(6) restricts the application of subsections (3) and (4) to purchases of replacement stock up to the amount of stock that will not be transferred as a result of the insolvency.

8. New section 80D(8) provides that the stamp mentioned in subsection (7) may be a stamp of such kind as the Commissioners for Her Majesty's Revenue and Customs may prescribe.

9. New sections 80D(9) and (10) define what is meant, for the purposes of the section, by a person 'becoming insolvent', 'collateral' and replacement stock'.

10. Paragraph 3 of the Schedule amends section 88 (1C) of FA 1986 so that that section only applies where new section 80D does not.

PART 2

11. Paragraph 5 inserts a new section 89AB into FA 1986.

12. Subsection (1) of new section 89AB provides that the section applies where P and Q have entered into an arrangement to which section 89AA applies, the only reason that the conditions in subsections (2A) and (3) of that section are not fulfilled is because chargeable securities of the same kind and amount as those transferred to P or his nominee are not returned to Q or his nominee, and the conditions in subsection 89AB(2) are fulfilled.

13. The conditions in new section 89AB(2) are that P and Q are not connected persons, that, after Q has transferred securities under the arrangement, either P or Q becomes insolvent, and it becomes apparent that, as a result of the insolvency, the securities will not be returned to Q or his nominee in accordance with the arrangement.

14. New section 89AB(3) provides that SDRT charges under section 87 of FA 1986 will not apply to the transfer of securities to P or his nominee or Q or his nominee under the arrangement.

15. New section 89AB(4) provides that sub-sections (5) and (6) apply where the solvent party to the arrangement acquires replacement securities before the end of the period of 30 days beginning with the date on which the insolvency occurs.

16. New section 89AB(5) provides that, where collateral is provided under the arrangement, SDRT will not be chargeable on any agreement to transfer replacement securities to the solvent party or his nominee where the solvent party uses the collateral provided to make the acquisition, or where the amount of collateral is insufficient, the solvent party uses his own funds to make up the balance of the cost of the replacement securities.

17. New section 89AB(6) provides that, where no collateral is provided, SDRT will not be chargeable on any agreement to transfer replacement stock to the solvent party or his nominee.

18. New section 89AB(7) provides that subsections (5) and (6) apply where the replacement purchase is effected by more than one agreement or by agreements with more than one person..

19. New section 89AB(8) restricts the application of subsections (5) and (6) to purchases of replacement securities up to the amount of securities that will not be transferred as a result of the insolvency.

20. New sections 89AB(9) (10) define what is meant, for the purposes of the section, by a person 'becoming insolvent', 'collateral' and 'replacement securities'.

BACKGROUND NOTE

21. A stock lending arrangement involves the transfer of securities from a lender to a borrower, under an agreement that provides for securities of the same kind and amount to be returned to the lender at a prescribed date. Although described as a "loan", the transactions involve the transfer of full title to the securities.

22. A sale and repurchase arrangement or 'repo' involves the transfer of securities from a seller to a purchaser under an agreement that provides for the purchaser to sell back to the seller at a later date securities of the same kind and amount. Again, the transactions involve the transfer of full title to the securities.

23. Because of the essentially temporary nature of the changes of ownership of the securities, the stamp duty and SDRT legislation includes special rules that ignore the transfer from the lender/seller to the borrower/purchaser and the return of the equivalent securities in the opposite direction.

24. Where securities of the same kind and amount are not, however, returned to the lender/seller for whatever reason, an SDRT charge arises in the hands of the borrower/purchaser on the basis that the original transfer is then regarded as an outright sale.

25. But where the failure to return the securities results from the insolvency of the other party, the imposition of an SDRT charge on the original transfer will reduce funds available to the creditors of the insolvent entity and/or restrict the ability of the solvent entity to restore his original position.

26. This section and Schedule will prevent that charge arising by providing that in this particular circumstance the normal rules will not apply.

27. Where the solvent party to an arrangement does not have stock returned to him, he may wish to replace those stocks by means of a purchase in the market. But where this occurs, a further stamp duty or SDRT charge arises even though he is simply trying to put himself back in the same position as he would have been in had the arrangement not terminated.

28. This section and Schedule prevent that outcome, in cases of insolvency, by removing the SDRT charge from purchases of replacement securities of the same kind and amount as those originally transferred.

29. Where, under a stock lending arrangement, the borrower provides collateral in the form of other chargeable securities and the arrangement terminates owing to insolvency, the lender will be regarded as having purchased the collateral securities for consideration represented by the value of the original securities lent. This will produce another unexpected SDRT charge and this section and Schedule will also remove that charge. The lender will therefore be able to restore his position without the penalty of additional SDRT charges that arise through no fault of his own.

30. Section 32 and Schedule 13 complement this section and Schedule, giving relief from tax on chargeable gains where securities borrowed under a stock loan arrangement are not returned to the lender in broadly similar circumstances.

SECTION 84 AND SCHEDULE 38: CAPITAL ALLOWANCES FOR OIL DECOMMISSIONING EXPENDITURE

SUMMARY

1. Section 84 and Schedule 38 amend the rules providing for tax relief for decommissioning costs to ensure that companies can claim relief for decommissioning costs only for the accounting period in which the work is actually carried out. The Government has become aware of arrangements that have been entered into which seek to establish a claim for tax relief for decommissioning costs several years in advance of any decommissioning work being carried out. These arrangements are an attempt to undermine the integrity of the North Sea ring fence. The change will have effect in relation to decommissioning costs incurred on or after 22 April 2009.

DETAILS OF SCHEDULE

2. Paragraph 2 amends section 163 of the Capital Allowances Act 2001 (CAA) to provide that general decommissioning expenditure must be incurred wholly or substantially to comply with an approved abandonment programme, or conditions associated with the approval of an abandonment programme. Sub-paragraph (3) inserts new subsection (3A) to this effect.

3. Paragraph 3 extends and amends section 164 of CAA to provide that the costs allowable for relief will be those costs of the accounting period that relate to the decommissioning work that is actually carried out in the accounting period.

4. New subsection 164 (1A) provides that Condition A applies in one or more of the situations where R incurs general decommissioning expenditure in the relevant chargeable period in respect of decommissioning:

   (a) carried out in that period;
   (b) carried out in a previous chargeable period; or
   (c) that has not been carried out until the relevant chargeable period.

5. Sub-paragraph (4) inserts new subsections (3)(aa), (ab) and (ac) into section 164 of CAA which provide what an election to have a special allowance must also specify.

6. Sub-paragraph (7) inserts new subsections (5A), (5B), (5C) and (5D) into section 164 of CAA.

7. New subsection (5B) provides that if the general decommissioning expenditure is not proportionate to the decommissioning work carried out in the chargeable period, then only the expenditure that is proportionate will be allowable.

8. New subsection (5D) provides, for subsections (5B) and (5C), definitions of "allowable expenditure", "non-allowable expenditure", "relevant decommissioning", "specified decommissioning period" and "specified expenditure period".

9. Paragraph 4 amends section 165 of CAA to provide for notional accounting periods within the post-cessation period.

10. Sub-paragraph (3) inserts new subsections (1A), (1B) and (1C) into section 165 of CAA.

11. New subsection (1A) provides that the decommissioning provision is met in relation to a notional accounting period if the former trader incurs general decommissioning expenditure in the relevant period in respect of decommissioning carried out in certain periods.

12. New subsection (1B) provides the meaning of "notional accounting period" for periods within the post-cessation period.

13. New subsection (1C) provides the meaning of "termination event" in relation to a notional accounting period.

14. Sub-paragraph (5) substitutes in section 165(4) of CAA a revised definition of "relevant decommissioning cost"

15. Sub-paragraph (6) inserts new subsections (4B), (4C), and (4D) into section 165 of CAA.

16. New subsection (4B) provides that if the general decommissioning expenditure is not proportionate to the decommissioning work carried out in the decommissioning period, then only the expenditure that is proportionate will be allowable.

17. New subsection (4D) provides, for subsections (4B) and (4C), definitions of "allowable expenditure", "decommissioning period", "expenditure period", "non-allowable expenditure" and "relevant decommissioning".

18. Sub-paragraph (7) inserts new subsections (6A) and (6B) into section 165 of CAA.

BACKGROUND NOTE

19. Companies that are party to North Sea licences for the production of oil and gas have a legal obligation to decommission installations and structures within those licensed areas at the end of the field's productive life.

20. Companies have to meet fully the costs of decommissioning but do obtain tax relief for all of those costs, which they can set against their ring fence corporation tax and supplementary charge profits.

21. Relief for decommissioning costs is given through the capital allowances legislation which provides that where a person is carrying on a ring fence trade and incurs general decommissioning expenditure, a special capital allowance is available, equal to the whole amount of decommissioning expenditure that is incurred in the period in question.

22. The Government has become aware of arrangements that have been entered into which seek to establish a claim for tax relief for decommissioning costs several years in advance of any decommissioning work actually being carried out. This undermines a fundamental general principle that relief is given in the accounting period, for costs incurred in respect of the work actually carried out in that accounting period.

23. The proposed change addresses this situation by ensuring that tax relief for decommissioning costs will only be given in respect of those costs that relate to the work actually carried out in the accounting period.

SECTION 85 SCHEDULE 39: BLENDED OIL

SUMMARY

1. Section 85 and Schedule 39 dispenses with the requirement for companies to routinely provide documentation to support the way they allocate oil between two or more oil fields for petroleum revenue tax (PRT) purposes, and simplifies the legislation.

DETAILS OF THE SCHEDULE

2. Paragraph 2 replaces section 63 of Finance Act (FA) 1987 with a new section 63 which removes the information requirement contained in the current section 63(3) and also removes the penalty provisions in current sections 63(3) and (4).

3. New section 63(1) applies the new section where, before its disposal or appropriation, oil is mixed with oil from another field or fields.

4. New section 63(2) provides that the blended oil should be allocated to each of the relevant participators on a just and reasonable basis.

5. New section 63(3) provides that, in making the allocation, the quantity and quality of the oil derived from each of the fields from which the oil has been mixed must be taken into account.

6. New section 63(4) provides that the participators may select a method for allocating the oil.

7. New section 63(5) provides that subsection (4) above is subject to Schedule 12 of FA 1987. Schedule 12 allows HM Revenue & Customs (HMRC) to propose an alternative method of allocation and confers on each participator a right of appeal against HMRC's proposed allocation method.

8. New section 63(7) provides that the normal allocation rules in new section 63(2) apply for chargeable periods where oil is blended for only part of that chargeable period.

9. Paragraph 3(2) provides that paragraphs 1 and 2 of Schedule 12 (together with their headings) are replaced with new paragraphs 1 and 2.

10. New paragraph 1 is concerned with interpretation

11. New paragraph 1(1) defines, for the purposes of Schedule 12, the terms "HMRC" and "method of allocation".

12. New paragraph 1(2) defines a reference to a "suitable method of allocation" as a reference to a method that secures a just and reasonable allocation of blended oil.

13. New paragraph 2 concerns unsuitable methods of allocation.

14. New paragraph 2(1) provides that new paragraph 2 will apply if a method of allocation that either has been used or is proposed to be used appears to HMRC not to be suitable.

15. New paragraph 2(2) allows HMRC to give notice to all of the participators in the fields from which oil has been mixed (that is, all those affected by the allocation) and to propose amendments to the method of allocation.

16. New paragraph 2(3) provides that, if HMRC gives notice then the allocation of the blended oil is to be redetermined, or determined, in accordance with the proposed amendments contained in the notice under sub-paragraph (2).

17. New paragraph 2(4) provides that sub-paragraph (3) is subject to the following provisions of Schedule 12, to any subsequent notices given under paragraph 2, and to any amendment to or replacement of the method of allocation made by the participators in the fields from which the oil has been mixed.

18. Paragraph 3(3) amends paragraph 3(1) of Schedule 12 by substituting "HMRC" for all occurrences of "the Board" and "paragraph 2(2)" for "paragraph 2(a)".

19. Paragraph 3(4) amends paragraph 3(2) of Schedule 12 by substituting "HMRC" for all occurrences of "the Board".

20. Paragraph 3(5) amends paragraph 3 of Schedule 12 by inserting two new sub-paragraphs (3) and (4).

21. New paragraph 3(3) provides that if the method of allocation is amended in accordance with paragraph 3 of Schedule 12 (appeals), the amended method will be used to determine the allocation of blended oil for the purposes of section 63 of FA 1987.

22. New paragraph 3(4) provides that sub-paragraph (3) is subject to any subsequent notice given under paragraph 3 of Schedule 12, and any further amendment to, or replacement of, the method of allocation as made by the participators in the fields from which the oil has been mixed.

23. Paragraph 3(6) omits paragraph 4 of Schedule 12.

24. Paragraph 4 provides that the Schedule has effect in relation to chargeable periods beginning after 30 June 2009.

BACKGROUND NOTE

25. Blended oil is the result of the commingling (or mixing or blending) of oil from two or more oil fields (for the purposes of the Petroleum Revenue Tax (PRT) legislation "oil" can refer to hydrocarbons such as crude oil or gas). For example, the Brent blend is made up of a number of oil fields that are commingled before travelling down the Brent pipeline to shore.

26. In such cases it is important to establish for tax purposes the contribution each of the originating fields makes to the blend once it reaches the shore and is then sold. The commingling rules formalise for tax purposes the commercial arrangements in place for the allocation of oil to the various field owners.

27. The new rules do away with the need for companies routinely to provide details of changes made to an allocation methodology (which happens for example when a new oil field commences production). Instead HMRC will only ask for information where it appears that the allocation method is not made on a just and reasonable basis.

SECTION 86 SCHEDULE 40: OIL: CHARGEABLE GAINS

SUMMARY

1. Section 86 and Schedule 40 amend the chargeable gains legislation as it applies to disposals of licences and assets used within a ring fence trade.

2. Where licences for developed areas in the UK Continental Shelf (UKCS) are swapped between companies, these will be treated as disposals which give rise neither to a gain nor a loss, for chargeable gains purposes, to the extent that the value of one licence swapped is matched by another licence.

3. In addition, where a company disposes of business assets used in connection with a UKCS field, to the extent that the proceeds are reinvested in other UKCS field assets, any gain that arises shall not be a chargeable gain.

DETAILS OF THE SECTION

4. Section 86 introduces Schedule 40 which provides for circumstances where oil licences are swapped and has effect for disposals made on or after 22 April 2009.

5. Schedule 40 also provides for circumstances where the consideration on the disposals of assets is reinvested and has effect in relation to disposals on or after 22 April 2009, whether or not the reinvestment takes place before, on or after that date.

DETAILS OF THE SCHEDULE

6. Paragraph 2 makes consequential amendments to the rebasing rules at section 35(3) of the Taxation of Chargeable Gains Act 1992 (TCGA).

7. Paragraph 3 inserts new subsection (5A) in section 55 of TCGA. Section 55 concerns assets owned on 31st March or acquired on a no gain/no loss disposal.

8. New subsection (5A) provides that a disposal is also a no gain/no loss disposal if the effect of one of new sections 195B, 195C or 195E is that no gain or loss accrues to the person making the disposal. When one of the new sections has that effect, section 55(6)(b) of TCGA which relates to indexation allowance does not apply.

9. Paragraph 4 extends the application of section 175(2C) TCGA to the no gain/no loss provisions in new sections 195B, 195C and 195E. Section 175(2C) disapplies roll-over relief where the no/gain no loss provisions apply to an acquisition of new assets by a member of a group of companies. .

10. Paragraph 5 inserts new sections 195A, 195B, 195C, 195D and 195E.

11. New section 195A applies sections 195B to 195E of TCGA and defines terms used in those sections and section 196 of TCGA.

12. New section 195B applies to a licence-consideration swap. That is where the only consideration given by either party is the disposal of one or more licences.

13. New section 195C applies to a mixed-consideration swap.

14. New section 195D also applies to a mixed-consideration swap.

15. New section 195E applies to the giver of mixed consideration in a mixed consideration swap..

16. Paragraph 6 of the Schedule amends section 196 which is an interpretation provision.

17. Paragraph 7 inserts references to sections 195B, 195C and 195E in paragraph 1(2) of Schedule 3 to TCGA (assets held on 31st March 1982).

18. Paragraph 8 provides that Part 1 of this Schedule applies to disposals made on or after 22 April 2009.

19. Paragraph 10 inserts in section 198 of TCGA a new subsection (3) which provides that where the roll-over relief provisions in sections 152 and 153 TCGA apply to a material disposal and the asset which constitutes the new assets for the purposes of a ring fence trade is a depreciating asset, then section 154(2)(b) (cessation of use of an asset) shall apply as if the reference to a trade was a reference solely to a ring fence trade.

20. Paragraph 11 inserts in section 198 of TCGA a new subsection (2A) which provides that subsection (1) is subject to section 198(3)(a) of TCGA.

21. Paragraph 12 inserts new sections 198A to 198F after section 198 of TCGA.

22. New section 198A provides that if a person makes a claim, roll-over relief does not apply to the consideration for the disposal and any gain arising to the claimant is not a chargeable gain.

23. Subsection (1) applies the section if a person makes a disposal and acquisition which is a "ring fence reinvestment" (the term is defined at new section 198E(2)) and qualifies for roll-over relief.

24. New section 198B provides for a claim to be made in respect of a ring fence reinvestment where only part of the consideration is reinvested.

25. New section 198C provides for the provisional application of sections 198A and 198B.

26. Subsection (1) provides that the section applies where a person carrying on a ring fence trade disposes of old assets or an interest in old assets and makes a declaration in that person's return for the chargeable period in which the disposal takes place. Details of the subject matter of the declaration are at paragraphs (a) to (e).

27. Subsection (3) provides a day when the declaration shall cease to have effect. If the declaration is wholly or partly withdrawn before the relevant day or is wholly or partly superseded before the relevant day by a valid claim under either section 198A or 198B, the declaration will cease to have effect, to the extent it is withdrawn or superseded, on the day on which it is withdrawn or superseded. To the extent that it is not withdrawn or superseded, the declaration will cease to have effect on the relevant day.

28. Subsection (4) provides the machinery for unwinding the effect of the declaration.

29. Subsection (6) defines the "relevant day".

30. New section 198D prevents companies from making double claims and lays down the circumstances in which a claim may be withdrawn and replaced by a new claim.

31. New section 198E defines "ring fence investments" for the purposes of sections 198A to 198G.

32. New section 198F lays down the conditions to be met if a disposal and acquisition are to qualify for roll-over relief.

33. New section 198G lays down the conditions to be met if a disposal and acquisition is to qualify for section 153 relief.

34. Paragraph 13 provides that Part 2 applies in relation to disposals made on or after 22 April 2009 (whether the acquisition in which the consideration is reinvested takes place before, on or after that date).

BACKGROUND NOTE

35. The Government recognises the importance of reducing the distortionary impact of the North Sea fiscal regime on investment decisions and helping facilitate asset trades. Under the existing law, where companies swap pre-development oil licences, these swaps do not give rise to chargeable gains.

36. Under this Schedule, that approach will be extended to all UKCS licence swaps. Where development licence interests are disposed of, to the extent that the consideration for the disposal is another licence, the consideration will be deemed to be the allowable costs plus indexation, giving a no gain/no loss transfer. Where there is a swap and an additional amount is paid over as consideration that amount remains within the chargeable gains regime.

37. In addition, where there is a disposal of assets used in connection with a UKCS field and the proceeds are reinvested in other ring fence assets, either one year before or up to three years after the disposal then, subject to a claim, the gain shall be treated as not being a chargeable gain.

38. The effect of these changes is that a number of transactions will no longer give rise to chargeable gains, making it easier for licence interests and ring fence assets to get into the hands of those most likely to invest in them. But where the assets are sold and the proceeds are not reinvested in the UKCS, then the disposals will be taxed in the normal way.

SECTION 87 SCHEDULE 41: OIL PRODUCTION ASSETS PUT TO CERTAIN OTHER USES

SUMMARY

1. Section 87 and Schedule 41 introduce amendments to existing legislation to facilitate the re-use of existing North Sea infrastructure. There are tax consequences when assets move out of the ring fence corporation tax (RFCT) and petroleum revenue tax (PRT) regimes. These consequences include the impact on tax allowances that have already been given; the treatment of future income and expenditure; and the availability of relief for decommissioning costs.

DETAILS OF SCHEDULE

PART 1: PETROLEUM REVENUE TAX (PRT)

Allowance of decommissioning and restoration expenditure

2. Paragraph 1 amends sections 3(1C) and 3(1D) of the Oil Taxation Act (OTA) 1975. These sections provide that, where a qualifying asset has been used for a purpose other than in connection with the field in which the costs have been allowed, then any decommissioning costs in connection with that asset will be restricted by reference to the use made of the asset. This paragraph lifts this restriction if the non-field use is for a qualifying purpose which includes a use otherwise than in connection with that field, if the use occurs in the UK or UK Continental Shelf (UKCS) and is not used wholly or partly for an oil purpose.

Amounts which are not chargeable tariff receipts

3. Paragraph 2 removes from the charge to PRT any income that arises from any other use of an asset, except use wholly or partly for an oil purpose.

No reduction of allowable expenditure

4. Paragraph 3 applies in respect of deemed disposals. Where a qualifying asset ceases to be used in connection with a taxable field and is used for another purpose, paragraph 8 of Schedule 1 to OTA 1983 deems a disposal giving rise to a disposal receipt. This disposal receipt is based on a time apportioned restriction of the allowable cost of the asset in respect of the use made of the asset. This paragraph prevents such a disposal receipt from arising where the other purpose is a qualifying purpose.

PART 2: CAPITAL ALLOWANCES

General decommissioning expenditure

5. Paragraph 5 provides for an amendment to section 163 of the Capital Allowances Act 2001 (CAA), extending the meaning of "general decommissioning expenditure" to include expenditure incurred in decommissioning assets used in a change of use trade, where those assets had originally been brought into use for the purposes of a ring fence trade.

6. Sub-paragraph (3) amends subsection (4ZA) by replacing paragraphs (a) and (b) with new paragraphs, which determine the amount by which general decommissioning expenditure is to be reduced where the decommissioned plant and machinery was not brought into use wholly for a qualifying purpose or had, at any time since it was brought into use, not been used for qualifying purposes. .

7. Paragraph 6 amends section 165(4A) of CAA 2001 (general decommissioning expenditure after ceasing ring fence trade) by substituting "general decommissioning expenditure" for "abandonment expenditure"

Commencement

8. Paragraph 7 deals with the commencement dates of legislation within this Part.

BACKGROUND NOTE

9. When oil and gas production ceases there are a number of ways in which North Sea oil and gas infrastructure can be re-used or modified to ensure it does not simply have to be decommissioned. Potential change of use projects include gas storage, carbon capture and storage and wind, or other power generation, which bring with them benefits such as improved energy security and low-carbon energy production.

10. However, it is apparent that there are significant tax barriers discouraging the use of assets for activities other than oil and gas production.

11. The issue that arises with a change of use project is that there may be a period prior to decommissioning where the infrastructure is not used for a PRT or ring fence trade purpose.

12. Within the PRT regime there are a number of possible effects. For example:

    a. a PRT exit charge may arise where an asset the cost of which has been allowed for PRT ceases to be used for a PRT purpose and is used for another purpose. Such a charge is calculated on a time basis by reference to the use of the asset and could be considerable;

    b. any income that arises from a change of use activity may well fall within the scope of PRT by being a tariff receipt within Section 6 of OTA 1983; and

    c. section 3(1C) of OTA 1975 restricts the amount of PRT decommissioning costs allowable by reference to the extent to which the asset is used for a change of use purpose.

13. This section and Schedule remove the exit charge, take any change of use income out of the scope to PRT and allow the decommissioning costs in full as long as the change of use is otherwise than in connection with that field and carried out within the UK or UKCS, and is not used wholly or partly for an oil purpose.

14. Within the ring fence corporation tax (RFCT) regime it may be that the ring fence trade is continuing at the same time as the change of use activity, or it could also be the case that the ring fence trade has already ceased. In those circumstances, decommissioning costs will fall outside RFCT, as the assets are being used for the purposes of a non-ring fence activity.

15. Under the current rules a non-ring fence change of use activity will normally deny companies access to previous periods' ring fence profits, against which to offset their decommissioning costs. In those circumstances there is evidence to suggest that companies may be unable to consider change of use projects and thus extend the economic life of their assets and infrastructure, by employing them in some other economically viable activity.

16. Nearly all decommissioning expenditure is capital in nature and is therefore relieved, within the RFCT regime, under the capital allowances legislation.

17. Section 163 of CAA provides 100 per cent first year allowances (FYA) relief for general decommissioning expenditure in respect of all decommissioning expenditure which has been incurred on decommissioning plant or machinery which has been brought into use for the purposes of a ring fence trade. The main conditions are that the:

    - expenditure is on decommissioning plant or machinery; and
    - decommissioning is of plant or machinery which is, or forms part of, an offshore installation or a submarine pipeline, or when last in use for the purposes of a ring fence trade, was, or formed part of, such an installation or pipeline.

18. However, under current rules, the amount of general decommissioning expenditure that can qualify for 100 per cent relief is reduced where the decommissioned plant and machinery was brought into use for the purposes of another trade. The amount of relief is reduced where the decommissioned plant and machinery was brought into use:

- partly for the purposes of the ring fence trade and partly for the purposes of another trade; or
- wholly for the purposes of the ring fence trade, but has, at any time since, not been used wholly for those purposes.

19. The proposed changes within this section and Schedule extend the availability of 100 per cent FYA to all general decommissioning expenditure incurred for the purposes of any ring fence trade of any person, or for any other use within the UK or UKCS.

SECTION 88 SCHEDULE 42: FORMER LICENSES AND FORMER OIL FIELDS

SUMMARY

1. Section 88 and Schedule 42 provide that a company will continue to be a participator for the purposes of the petroleum revenue tax (PRT) legislation until the point when decommissioning has been completed, even though it has ceased to be a licensee (and thus within the scope of PRT) because of an event such as the expiry of a licence.

DETAILS OF THE SCHEDULE

PART 1: PERSONS WHO CEASE TO BE LICENSEES BECAUSE OF CESSATION EVENTS

2. Paragraph 2(2) amends the definition of "participator" in section 12(1) of the Oil Taxation Act (OTA) 1975 to include a person who was previously a licensee but has ceased to be a licensee as a result of a "cessation event". This sub-paragraph also makes minor consequential amendments to subsection (1).

3. Sub-paragraph 2(3) inserts a new subsection (1A) after subsection (1).

4. New subsection (1A) defines the terms "cessation event", "current participator", "former participator" and "default payment".

5. Paragraph 3 amends the definitions of "current participator" and "former participator" in paragraph 2C(2) of Schedule 5 to OTA 1975 to include the new definition of "participator" introduced by paragraph 2(2) of this Schedule).

6. Paragraph 4 provides that Part 1 of this Schedule has effect in relation to persons who cease to be licensees because of cessation events occurring in chargeable periods beginning after 30 June 2009.

PART 2: AREAS TREATED AS CONTINUING TO BE OIL FIELDS

7. Paragraph 6 inserts after the reference to Schedule 1 to OTA 1975 in the entry for "oil field" in section 12(1) of that Act words to the effect that Schedule 1 includes provision about areas that are to be treated as continuing to be oil fields.

8. New paragraph 6 provides that if an area has ceased to be an oil field (or part of one) by virtue of not being part of a licensed area then the said area is to be treated as continuing to be an oil field (or part of one). However this provision will cease if either the area is decommissioned or the area becomes part of a licensed area again.

9. New paragraph 7 provides for determining whether an area treated as being an oil field (or part of one) under paragraph 6 is decommissioned for the purposes of that paragraph. An area is decommissioned for those purposes if either an approved decommissioning programme has been carried out to the satisfaction of the Secretary of State (of the Department of Energy and Climate Change) or, where the area is not subject to a UK offshore decommissioning regime, HM Revenue & Customs (HMRC) are satisfied that decommissioning has been completed. In the latter case the new paragraph provides a right of appeal. Definitions are provided for "qualifying assets", "relevant area" and "UK offshore decommissioning regime".

10. Paragraph 8 provides that Part 2 of this Schedule has effect in relation to areas that cease to be oil fields, or parts of oil fields, in chargeable periods beginning after 30 June 2009.

BACKGROUND NOTE

11. When an oil field comes to the end of its productive life, the companies that are licensed by the Department of Energy and Climate Change (DECC, previously the DTI/BERR) to extract oil from that field are responsible for the costs of decommissioning the field, i.e. removing all the pipelines, platforms etc and returning the sea bed to its natural state.

12. Although the licensee companies have to meet the decommissioning costs in full (there is no Government subsidy), the costs are fully relievable for petroleum revenue tax (PRT) purposes. However this assumes that the company is still a licensee and is thus still within the charge to PRT. Otherwise the decommissioning costs will not be available for relief.

13. However, the oldest licences (1st round) are due to expire in 2010 and if no action is taken, companies will no longer be able to extract oil from fields in that (expired) licence area. What DECC proposes to do is, on expiry of the licence, extend the term of the licence (but only in respect of the producing fields) for each field until such time as the company ceases production of oil from it. When the last such field on a licence ceases production, the licence itself will expire.

14. However, once the licence has expired companies will still be required to decommission the field infrastructure, and if they are no longer licensees then they will not get relief for PRT in respect of their decommissioning costs.

15. This section and Schedule deem a company still to be a licence holder for the purposes of the PRT legislation where is has ceased to be so by virtue of the expiry of a licence and, furthermore, for the relevant field to continue to exist. As a result the company will still be able to claim relief for its decommissioning costs. In addition, any income the company receives following cessation of production (e.g. tariff or disposal receipts) will be subject to PRT.

SECTION 89: SCHEDULE 43: ABOLITION OF PROVISIONAL EXPENDITURE ALLOWANCE:

SUMMARY

1. Section 89 and Schedule 43 provide that the Provisional Expenditure Allowance (PEA) legislation no longer applies.

DETAILS OF THE SCHEDULE

2. Paragraph 2 abolishes PEA by providing that it is not to be calculated in respect of a future chargeable period.

3. Paragraph 3 makes amendments which are consequential upon the abolition of the allowance, but subject to Paragraph 4.

4. Paragraph 3(3) omits subsections (9)(a) (which calculates provisional expenditure allowance) and subsections (10) and (11) (which make certain adjustments to the provisional expenditure allowance calculation).

5. Paragraph 3(4) omits paragraph 11 of Schedule 17 to Finance Act (FA) 1980 which makes certain further adjustments to the provisional expenditure allowance calculation when a participator transfers its interest in an oil field.

6. Paragraph 3(5) provides that paragraph 3 only has effect for future chargeable periods, i.e. those beginning after 30 June 2009.

7. Paragraph 4 contains saving provisions. This paragraph only applies if provisional expenditure allowance has been calculated in respect a chargeable period which occurred before the PEA was abolished.

8. Paragraph 4(2) provides that, for future chargeable periods, the saved provisions (defined in subparagraph (3)) will continue to have effect as if they had not been amended by paragraph 3.

BACKGROUND NOTE

9. Under the PRT rules, oil companies have to submit a formal claim in order to obtain relief for their costs, and that claim is then considered by HM Revenue & Customs (HMRC). Sometimes oil companies would not get immediate relief for these costs. In the early days of oil exploration, when companies incurred substantial start-up costs, this deferral of relief could have a big impact on their cash-flow. PEA was therefore introduced to ensure that companies obtained partial advance relief in respect of these costs.

10. Now that North Sea exploration is long-established, and the large start-up costs have already been incurred, PEA is no longer needed. Furthermore, Government has become aware that the operation of PEA has had unintended and detrimental consequences to a few companies which have suffered a tax charge when their PEA has been clawed back in a later period.

11. Government, with the agreement of industry, has therefore repealed the PEA legislation.

SECTION 90 SCHEDULE 44: SUPPLEMENTARY CHARGE: REDUCTION FOR CERTAIN NEW OIL FIELDS

SUMMARY

1. Section 90 and Schedule 44 introduce a new allowance, a Field Allowance, which can reduce a company's adjusted ring fence profits from oil and gas production in the UK and UK Continental Shelf (UKCS).

2. The allowance is available to certain categories of new oil and gas fields in the UK/UKCS – small fields, ultra heavy oil fields and ultra high pressure/high temperature fields. Allowances from a company's interests in all qualifying fields in an accounting period are then pooled and offset against adjusted ring fence profits. Any unused amounts in the pool are carried forward to the next accounting period.

DETAILS OF THE SECTION

3. Section 90 amends section 501A of the Income and Corporation Taxes Act 1988 (ICTA) (supplementary charge in respect of ring-fence trades) to make it subject to Schedule 44, which provides for the reduction of supplementary charge on companies that are, or have been, licensees in new fields for accounting periods ending on or after 22 April 2009.

DETAILS OF THE SCHEDULE

4. Paragraph 2 provides that a company's pool of field allowances for an accounting period are the amount of the company's pool of field allowances that are carried forward from the previous accounting period plus the aggregate of field allowances activated in the accounting period.

5. Paragraphs 3 and 4 provide the rules for determining the amount of field allowances that are carried forward into a future accounting period.

6. Paragraph 5 provides that from the day a new oil field is licensed, a company that is an initial licensee in that field will hold a field allowance for that field. The amount of field allowance will be determined by the company's equity share in the field.

7. Paragraph 7 applies if a company holds a field allowance. The unactivated amount of that allowance is the difference between:

    a. the amount of field allowance the company has received (including where a company adds to an existing equity share) and
    b. the field allowance already activated and reductions made in the field allowance by virtue of disposals of equity.

8. Paragraph 8 provides that four conditions are to be met in respect of a new oil field for the activation of field allowance where there is no change in equity share during the accounting period.

9. Paragraph 9 provides the rules for determining the amount of field allowance to be activated in an accounting period when all conditions in paragraph 8 are met.

10. Paragraph 10 introduces Part 5 which deals with the situation where a company's equity share in a new oil field changes during the accounting period. The paragraph lists the four conditions which must be met if Part 5 is to apply.

11. Paragraph 11 divides the accounting period into reference periods. This facilitates the application of Part 5 where a company is not a licensee for a whole accounting period or where the equity share changes.

12. Paragraph 12 provides the calculation of field allowance for each reference period.

13. Paragraph 13 introduces Part 6 which concerns the treatment of transfers of field allowance.

14. Paragraph 14 provides the calculation for the remaining field allowance which a company ("the transferor") has, after it has disposed of some of the equity interest in a new oil field. This is the unactivated field allowance immediately prior to the disposal, multiplied by the equity disposed of as a proportion of the equity held post-disposal.

15. Paragraph 15 provides the calculation of field allowance where a company acquires an equity interest in a new oil field. If the transferee already holds a field allowance for the new oil field, the unactivated amount of the field allowance is increased by the amount reduced for the seller in paragraph 14, pro-rated if the acquirer does not acquire all of the equity disposed of by the seller. This calculation also provides the amount of field allowance acquired where the transferee did not hold a field allowance for the new oil field at the time of acquisition.

16. Paragraph 17 also contains powers for the list of field descriptions and allowances to be amended by statutory instrument.

17. Paragraphs 18 to 24 provide details of the total field allowance and the types of new oil field which will qualify for the allowance.

BACKGROUND NOTE

18. The UKCS is facing increasing challenges as an oil and gas producing basin, however there remain significant reserves to be recovered. Having engaged in extensive discussions on the question of fiscal incentives, the Government believes that a correctly targeted and designed incentive could, over the life of the UKCS, lead to an increase in investment and production.

19. This section introduces a 'Field Allowance', which is targeted on those commercially marginal, but economic, fields facing the greatest challenges within the UKCS. Those are smaller oil and gas fields, fields comprised of heavy oil and high pressure/high temperature fields.

20. Each field in these categories which is given development consent by the Department of Energy and Climate Change on or after 22 April 2009 will qualify for the new Field Allowance.

21. An amount of allowance is 'activated' each year based on the amount of income the company has from the qualifying field, up to a preset annual maximum.

22. The allowances are then pooled and offset against a company's profits liable to the Supplementary Charge, i.e. the additional 20 per cent charge that companies with ring fence profits pay, on top of ring fence corporation tax.

23. Companies repeat the process each year until they have used up all their unactivated field allowance. Any unused allowances in the pool are carried forward for offset in future years. When a company disposes of an interest in a field which has unactivated field allowances, those allowances are transferred to the acquirer.

SECTION 91 AND SCHEDULE 45: OIL: MISCELLANEOUS AMENDMENTS

SUMMARY

1. Section 91 and Schedule 45 simplify a number of provisions relating to petroleum revenue tax (PRT) and make amendments to existing definitions.

DETAILS OF THE SCHEDULE

The Oil Taxation Act (OTA) 1975

2. Paragraph 1 removes the provision for allowing a participator to spread "supplemented" expenditure giving relief for up to 20 chargeable periods and the provision for allowing companies to claim certain expenditure incurred before the introduction of PRT.

3. Sub-paragraphs (2) and (3) amend Schedule 3 to OTA 1975 by omitting paragraphs 9 and 10 which allow participators to spread the relief they get for certain costs (supplemented expenditure) over a number of chargeable periods.

4. Sub-paragraph (4) amends Schedule 4 to OTA 1975 by omitting paragraph 3. This provision allowed companies to claim certain expenditure incurred before the introduction of PRT. Since such expenditure is subject to a six year time limit the legislation is no longer required.

OTA 1983

5. Paragraph 2 removes an alternative formula for calculating tariff receipts allowance from OTA 1983.

6. Sub-paragraph (2) omits section 9(3) and paragraph 3 of Schedule 3 to OTA 1983. This applies an alternative formula for calculating tariff receipts allowance for chargeable periods ending on or before 30 June 1987 and is thus no longer required.

7. Sub-paragraph (3) removes the now redundant references to subsection (3) that appear elsewhere in section 9.

8. Sub-paragraph (4) omits sections 13 and 14 of, and Schedule 5 to OTA 1983 (transitional provision for expenditure incurred on or before 31 December 1983) as these rules are no longer applicable.

Finance Act (FA) 1993

9. Paragraph 3 addresses a renumbering issue in FA 1993.

The Income and Corporation Taxes Act 1988 (ICTA)

10. Paragraph 4 amends the ring fence corporation tax (CT) legislation to fully align the definition of a consortium, for the purposes of determining whether or not companies are associated, with the general CT definition.

BACKGROUND NOTE

11. This section and Schedule have repealed the following four items of legislation:

- spreading of supplement (paragraph 9 of Schedule 3 to OTA 1975) allows companies to elect to spread relief for qualifying "supplemented" expenditure for up to 20 chargeable periods. The legislation does not currently appear to serve any useful purpose;

- pre-PRT expenditure (paragraph 3 of Schedule 4 to OTA 1975) applies to certain expenditure incurred prior to 13 November 1974. The normal time limit for claiming expenditure for PRT is six years and in any event HM Revenue & Customs (HMRC) is not aware of any outstanding claims under this legislation;

- Tariff Receipts Allowance – alternative calculation (section 9 of OTA 1983) provides a volume based allowance against tariff receipts similar to that of the Oil Allowance being relieved against sales of oil. Section 9(3) of OTA 1983 provides an alternative calculation for chargeable periods ending on or before 30 June 1987. The legislation is relatively complicated and is no longer applicable; and

- transitional provisions for certain rules within OTA 1983 – section 13 and Schedule 5 to this Act provide transitional rules for periods ending before or straddling 1 July 1982 in respect of the application of these new rules. These transitional rules are no longer applicable.

12. In addition, the section and Schedule make two further changes:

- the first involves renumbering Schedule 20A to FA 1993 (as inserted by Part 1 of Schedule 33 to FA 2008) as Schedule 20B to that act as there already exists a Schedule 20A (Lloyd underwriters), which was inserted by FA 2004; and

13. the second involves an amendment to section 502 of ICTA (interpretation of Chapter 5 of Part 12), in section (3A) to fully align the ring fence corporation tax definition of a consortium, for the purposes of determining whether or not companies are associated, with the general corporation tax definition..

SECTION 92: HMRC CHARTER

SUMMARY

1. Section 92 requires HM Revenue & Customs (HMRC) to prepare and maintain a Charter. The Charter must set out the standards of behaviour and values to which HMRC will aspire in dealing with taxpayers and others.

DETAILS OF THE SECTION

2. Subsection (1) inserts a new section 16A into the Commissioners for Revenue and Customs Act 2005.

3. New section 16A(1) requires the Commissioners for Her Majesty's Revenue and Customs to prepare a Charter.

4. New section 16A(2) specifies that the Charter must include standards of behaviour and values to which HMRC will aspire in its dealings with taxpayers and others.

5. New section 16A(3) specifies that the Commissioners must regularly review the Charter and publish revisions as appropriate.

6. New section 16A(4) requires the Commissioners to report annually on how well HMRC is doing in living up to the standards in the Charter.

7. Subsection (2) requires the Commissioners to introduce the Charter before the end of 2009.

BACKGROUND NOTE

8. HMRC does not presently have a single document that sets out the rights and responsibilities of taxpayers and other persons that HMRC deals with. The possibility of introducing a Charter was proposed in a consultative document issued on 19 June 2008 which suggested that there was no need for a Charter to be supported by legislation. But most respondents argued that a legal foundation would be the best way of ensuring that the Charter would be an effective and enduring document. The Government then announced that a clause giving the Charter explicit legislative backing would be included in the 2009 Finance Bill.

9. HMRC held a second consultation on the content of the Charter. That consultation closed on 12 May 2009. The Charter, revised to take into account responses to this consultation, will be launched in autumn 2009.

SECTION 93 AND SCHEDULE 46: DUTIES OF SENIOR ACCOUNTING OFFICERS OF LARGE COMPANIES

SUMMARY

1. Section 93 and Schedule 46 provide that senior accounting officers of qualifying companies are required to take reasonable steps to ensure that the company establishes and maintains appropriate tax accounting arrangements. Qualifying companies must notify HMRC of the name of the senior accounting officer. The section includes a power to impose penalties on both senior accounting officers and companies who fail to comply with these requirements. The change has effect in relation to financial years beginning on or after the day this Act is passed.

DETAILS OF THE SCHEDULE

2. Paragraph 1 establishes that the senior accounting officer of a qualifying company must take reasonable steps to ensure that the company and any subsidiaries establishes and maintains appropriate tax accounting arrangements. Also that the senior accounting officer takes reasonable steps to monitor those arrangements and identify any respects in which they are not appropriate. This is referred to as the 'main duty'.

3. Paragraph 2 requires the senior accounting officer to certify to HMRC either:

   - that the company any its subsidiaries had appropriate tax accounting arrangements throughout the financial year; or

   - stating whether it did; giving an explanation of the respects in which the arrangements are not appropriate, and stating whether an explanation has been provided to the company auditors.

   The paragraph also prescribes the form this certificate should take and sets a time limit for submission of the certificate: not later than the end of the period for filing the company's accounts for the year concerned, unless, a later date is prescribed by HMRC.

4. Paragraph 3 requires a large company to notify HMRC of the name of anyone who was its senior accounting officer at any time during the year and how and by when this should be done.

5. Paragraph 4 provides for a penalty of £5,000 on the senior accounting officer for a failure to comply with the 'main duty'. This penalty is, however, limited to once per year per company.

6. Paragraph 5 provides for a penalty of £5,000 on the senior accounting officer for a failure to provide the certificates required or for providing a certificate that contains a careless or deliberate inaccuracy. It is also provided that where a certificate is made neither carelessly nor deliberately, it will be treated as such if the senior accounting officer discovers the inaccuracy and does not take reasonable steps to notify HMRC.

7. Paragraph 6 explains how the penalties apply if there were more that one senior accounting officer during the year. Effectively this makes only one person who was senior accounting officer liable to a penalty being the last in post to have failed in relation to the matter being penalised.

8. Paragraph 7 imposes a penalty on the company if it fails to notify HMRC of the name of its senior accounting officer.

9. Paragraph 8 provides for an escape from any of the penalties for failures under this section where there is reasonable excuse for the failure.

10. Paragraph 9 sets out the arrangements and time limits for assessing penalties.

11. Paragraph 10 sets out the arrangements and time limits for appealing against any penalty under this section.

12. Paragraph 11 sets out when penalties must be paid and provides for any penalty under this section to be enforced as if it were income tax charged in an assessment.

13. Paragraph 12 provides for the amount of the penalties under this section to be revalorised in Regulations to take account of changes in the value of money.

14. Paragraph 13 applies certain relevant provisions of the Taxes Management Act 1970 to the provisions of this section.

15. Paragraph 14 sets out what is meant by 'appropriate tax accounting arrangements'. It also lists those taxes and duties to which this Schedule will apply.

16. Paragraph 15 sets out what is meant by a 'qualifying company' and provides for HM Treasury regulations to exclude, but not add to, the types of company to be considered 'qualifying companies' for the purpose of these provisions.

17. Paragraph 16 sets out what is meant by 'senior accounting officer'.

18. Paragraph 17 concerns the arrangements for making regulations under this Schedule.

19. Paragraph 18 provides the meaning of a variety of terms included throughout this Schedule.

BACKGROUND NOTE

20. Large companies make a major contribution to the Exchequer. Inadequate tax accounting arrangements within such companies (or groups) can lead to misreporting of tax liabilities of very large amounts.

21. Currently, there is no legal obligation on any particular director or company officer to ensure that the company has appropriate tax accounting arrangements. This section and Schedule will make the senior accounting officer of a company personally responsible for doing so.

22. Ensuring appropriate tax accounting arrangements are in place is no more than compliant companies will be doing already. The requirement on senior accounting officers to take reasonable steps to ensure appropriate tax accounting should in most instances merely underpin that good practice.

23. Where large companies have not established appropriate tax accounting arrangements to enable accurate tax reporting, tax is at risk. Senior accounting officers of such companies will be required by this section to take appropriate action to remedy that situation.

SECTION 94: PUBLISHING DETAILS OF DELIBERATE TAX DEFAULTERS

SUMMARY

1. Section 94 provides for the Commissioners of HM Revenue and Customs (HMRC) to publish information (including names) of persons who have been penalised for deliberate defaults: inaccuracies, failing to notify, and certain VAT and Excise duty wrongdoings where the tax lost exceeds £25,000. No details will be published if the person has made a full disclosure either unprompted or prompted. Any details must be published within 12 months from the relevant penalties becoming final and may not continue to be published beyond 12 months from when first published.

DETAILS OF THE SECTION

2. Subsection (1) provides that the Commissioners may publish information about any person who has incurred relevant tax penalties where the potential lost revenue, incurred in consequence of an investigation by HMRC, exceeds £25,000.

3. Subsection (2) lists the relevant tax penalties all of which are for deliberate or deliberate and concealed defaults. They are inaccuracy in documents, including inaccuracies attributable to supply of false information or withholding information by a person, failure to notify, unauthorised VAT invoice, putting product to use attracting higher (excise) duty, knowingly supplying such product, and handling goods subject to unpaid excise duty.

4. Subsection (3) gives statutory references for definitions of potential lost revenue for each relevant tax penalty. Broadly, this is the amount of tax unpaid or undeclared as a result of the default to which the penalty percentage is applied.

5. Subsection (4) specifies the information that may be published including the name, address, nature of any business, amount of penalties and potential lost revenue, period covered and such further information as may be required to make clear the person's identity.

6. Subsection (5) provides for the information to be published in any manner considered appropriate. It is envisaged this would be in quarterly lists on the HMRC website.

7. Subsection (6) requires the Commissioners to inform the person they are considering publishing information and to give the person a reasonable opportunity to make representations.

8. Subsection (7) provides that the Commissioners may not publish any information until the relevant tax penalties have become final, which is defined in subsection (12).

9. Subsection (8) provides that if information is to be published it must be within one year of the day the penalties have become final.

10. Subsection (9) provides that the information must not be published, or continue to be published, after one year from the day of first publication.

11. Subsections (10) give exemption from publication for those whose penalties have been reduced for disclosure, whether prompted or unprompted, by the full extent permitted.

12. Subsection (11) explains that a penalty becomes final either when all appeal avenues have expired or been finally determined or when a contract settlement, including relevant penalties, is made.

13. Subsections (12) to (15) provide for Treasury orders to vary the financial limit (by negative resolution) and for an appointed day order to commence the provisions.

BACKGROUND NOTE

14. Publishing details (including names) aims to deter deliberate tax defaulters; reassure those who do pay the right tax; and encourage those who do not, to come forward and bring their tax affairs up to date.

15. The publication scheme is founded on definitions in the penalty regimes enacted in Finance Acts 2007 and 2008, which apply across the taxes and duties HMRC administer. In addition to the specific exemptions from publication for those making disclosure there may be some exceptional circumstances where publication will not be appropriate.

SECTION 95 AND SCHEDULE 47: AMENDMENT OF INFORMATION AND INSPECTION POWERS

SUMMARY

1. Section 95 and Schedule 47 amend Schedule 36 to the Finance Act (FA) 2008 (Schedule 36) which contains HM Revenue & Customs' (HMRC) new information and inspection powers. The section also allows for the repeal, by statutory instrument, of several other information and inspection powers that are no longer required.

DETAILS OF THE SECTION

2. The section introduces Schedule 47 which amends Schedule 36.

3. Subsections (2) to (5) provide a power to make statutory instruments containing provisions or savings in consequence of or in connection with Schedule 36. This will allow the repeal of several information and inspection powers that are no longer required together with related provisions.

DETAILS OF THE SCHEDULE

4. Paragraph 2 inserts new paragraph 3(2A) into Schedule 36 to make clear that applications to the tribunal for approval of taxpayer or third party notices are heard without the taxpayer being present.

5. Paragraph 3(2) inserts new paragraph 5(3A) into Schedule 36 to make clear that applications to the tribunal for approval of notices under paragraph 5 of Schedule 36 are heard without the taxpayer being present.

6. Sub-paragraph (3) amends paragraph 5(4) of Schedule 36. The existing paragraph refers to a notice being given with the approval of the tribunal. Strictly speaking the tribunal approves the application rather than the notice and this change makes this clear.

7. Paragraph 4 inserts new paragraph 6(4) into Schedule 36. This makes it clear that there is no right of appeal under the Tribunals, Courts and Enforcement Act 2007 against a decision of the tribunal to approve the issue of an information notice.

8. Paragraph 5(2) amends the definition of "business assets" in paragraph 10 of Schedule 36 to make it clear that HMRC has no power to inspect documents other than statutory records unless they are trading stock or plant in the business.

9. Sub-paragraph (3) inserts new paragraph 10(4). In general "documents" other than "business documents" are not subject to inspection. But certain documents may be either trading stock or plant in the business, and this new provision makes it clear that such documents may be inspected.

10. Paragraph 6 amends paragraph 11 of Schedule 36 to clarify and extend the scope of documents that can be inspected.

11. Paragraph 7 amends paragraph 12(5) of Schedule 36. The existing paragraph refers to a notice being given with the approval of the tribunal. Strictly speaking the tribunal approves the inspection rather than a notice and this change makes this clear.

12. Paragraph 8(2) inserts new paragraph 13(1A) into Schedule 36. This makes it clear that applications to the tribunal to approve an inspection of a business under Part 2 of Schedule 36 are heard without the taxpayer being present.

13. Paragraph 8(3) inserts new paragraph 13(3) into Schedule 36. This makes it clear that there is no right of appeal under the Tribunals, Courts and Enforcement Act 2007 against a decision of the tribunal to approve an inspection.

14. Paragraph 9(4) makes a consequential amendment to paragraph 21(8) of Schedule 36 and makes it explicit that the checking of payroll giving does not require the opening of a formal enquiry into a tax return.

15. Paragraph 9(5) inserts new paragraph 21(9) into Schedule 36. This makes it clear that the information powers are switched on or off for a particular person who has made a return only in relation to the capacity in which that person has made that return.

16. Paragraph 10(2) clarifies paragraph 35(2) of Schedule 36 and ensures that the references in paragraph 3(5) to "naming the taxpayer" are amended appropriately where a third party notice is given to check the tax position of a parent undertaking and any of its subsidiary undertakings.

17. Sub-paragraph (3) inserts new paragraphs 35(4) and (4A) into Schedule 36. These provisions modify the rules that apply when a third party notice is given to a parent undertaking to check the tax position of more than one subsidiary undertaking. New paragraph 35(4) makes corresponding minor changes to those made to paragraph 35(2) above. New paragraph 35(4A) clarifies and adds to the modifications in existing paragraph 35(4). In particular, the parent undertaking may appeal against such a third party notice on any grounds (except in relation to statutory records), rather than the more restricted appeal rights applying to third party notices generally.

18. Sub-paragraph (4) amends paragraph 35(5) which concerns notices under paragraph 5 to a parent undertaking for checking the tax position of subsidiaries whose identities are not known. This is partly to reflect the changes made above to paragraph 5 of Schedule 36 and also to make it clear that although HMRC is not required to obtain tribunal approval for a notice, it may choose to do so. In addition, the parent undertaking's appeal rights are extended.

19. Paragraph 11(2) inserts new paragraph 37(2) into Schedule 36. This provides that paragraph 21 of Schedule 36 operates as intended in a partnership situation where the partnership tax return or a partnership claim or election has been submitted by any of the partners. In addition what was paragraph 37(2)(b) is no longer necessary in the light of changes made to paragraph 21 of Schedule 36 by paragraph 9 of this Schedule.

20. Sub-paragraph (3) amends paragraph 37(3) so that it applies to all third party notices, including notices issued to one partner for the purpose of checking another partner's tax position. The changes here mirror those made to the procedures for checking group companies by paragraph 10 of this Schedule.

21. Sub-paragraph (4) makes changes to paragraph 37(4) to clarify how that sub-paragraph works and reflect the fact that paragraph 37(3) will now apply more widely by virtue of the change made above.

22. Sub-paragraph (5) inserts new paragraph 37(5) into Schedule 36. This provision modifies the rules that apply when a third party notice is given to a partner to check the tax position of more than one other partner. It clarifies and adds to the modifications in existing paragraph 37(5). In particular, the partner receiving the third party notice may appeal on any grounds (except in relation to statutory records), rather than the more restricted appeal rights applying to third party notices generally.

23. Sub-paragraph (6) amends paragraph 37(6) which concerns notices under paragraph 5 to a partner for checking the tax position of other partners whose identities are not known. This is partly to reflect the changes made to paragraph 5 of Schedule 36 by paragraph 3 of this Schedule and also to make it clear that although HMRC is not required to obtain tribunal approval for a notice, it may choose to do so. In addition, the appeal rights of the partner receiving the notice are extended.

24. Paragraph 12 inserts new paragraphs 37A and 37B into Schedule 36. The existing powers to ask for information in relation to a herd basis election and counteraction provisions are being repealed and Schedule 36 will be used instead. No specific provision is required to achieve this since both concern income tax and corporation tax, to which Schedule 36 already applies.

25. The effect of new paragraph 37A is that the restrictions on giving a taxpayer notice where a tax return had been made (paragraph 21 of Schedule 36) do not apply in relation to a taxpayer notice in relation to a herd basis election. Such a restriction would be inappropriate here since HMRC checks on herd basis elections are conducted outside the normal mechanism of a return and enquiry. Herd basis election rules are in Chapter 8 of Part 2 of the Income Tax (Trading and Other Income) Act 2005 (ITTOIA) and Chapter 8 of Part 3 of the Corporation Tax Act 2009.

26. New paragraph 37B has a similar effect in relation to a taxpayer notice given to a person to whom a counteraction provision may apply. Counteraction provision is defined in new paragraph 37B(3).

27. Paragraph 13(2) provides for some tidying of paragraph 39 of Schedule 36, without any change of meaning.

28. Paragraph 13(3) and Paragraph 14 make consequential amendments to the headings of paragraphs 39 and 40 of Schedule 36 to reflect the introduction of a new penalty under paragraph 15 below.

29. Paragraph 15 inserts new paragraph 40A into Schedule 36 which provides for a penalty to apply where a person carelessly or deliberately provides inaccurate information or produces inaccurate documents in response to an information notice. Such a penalty existed in section 98(2) of the Taxes Management Act 1970 (TMA) for notices under former information provisions but the replacement is being incorporated into Schedule 36.

30. Paragraph 16 makes minor changes to paragraph 41 of Schedule 36 to improve clarity.

31. Paragraph 17 provides for consequential amendments to paragraph 46 of Schedule 36.

32. Sub-paragraph (4) inserts new paragraphs 46(3)-(5) into Schedule 36 which determine the relevant date within 12 months of which a penalty assessment must be made. The existing rules are now applied to standard or daily default penalties only, and to ensure that the time limit works properly in relation to daily default penalties a third "latest date" is added.

33. Paragraphs 18, 19 and 20 provide for consequential amendments to paragraphs 47, 48 and 49 of Schedule 36.

34. Paragraph 21(3) inserts new paragraph 63(3A) into Schedule 36 which amplifies the definition of VAT in paragraph 63(3) of Schedule 36. New sub-paragraph (3A)(a) repeats what was previously in paragraph 63(3) of Schedule 36. New sub-paragraph (3A)(b) represents new material. The effect is that Schedule 36 will apply for the purposes of amounts accounted for under a particular VAT scheme which are not VAT but are treated as if they were.

35. Paragraph 22(2) amends the definition of tax position in connection with claims, elections, applications and notices. The purpose of the amendment is to narrow the scope of tax position so that it relates only to claims, etc, made by taxpayers themselves rather than documents given by a third person in connection with someone else's tax position. This is in line with the original policy intention, but clarifies the law.

36. Paragraph 22(3) inserts new paragraph 64(2A) into Schedule 36. This makes it explicit that a person's tax position includes matters relating to the withholding of income, for example, as part of payroll giving.

BACKGROUND NOTE

37. Schedule 36 to FA 2008 contains a new set of information and inspection powers to replace the separate main powers that existed for checking a person's position for income tax, capital gains tax and corporation tax on the one hand and VAT on the other. Those new powers also apply to PAYE, the construction industry scheme, student loan repayments and national insurance contributions. They came into force on 1 April 2009.

38. This Schedule makes amendments to clarify points that have been raised and ensure that the powers work as intended.

39. It also introduces a penalty into Schedule 36 to apply where any person deliberately or carelessly provides any incorrect documents or information in response to an information notice issued under Part 1 of Schedule 36. Such a penalty existed in section 98(2) of TMA for fraudulently or negligently providing information etc under information powers that have been replaced by Schedule 36.

40. Section 95 also provides a power to make statutory instruments containing provisions or savings in consequence of or in connection with Schedule 36 to FA 2008. This will allow the repeal of a significant number of information and inspection powers that are no longer required together with related provisions. These powers presently apply to particular types of tax check. The aim is that HMRC will use Schedule 36 instead. This represents alignment, helping both taxpayers and HMRC by putting all the powers in one place. The new powers allow HMRC to ask for a wider range of information in some circumstances, but provide more explicit safeguards for the way in which HMRC asks for information.

SECTION 96 AND SCHEDULE 48: EXTENSION OF INFORMATION AND INSPECTION POWERS TO FURTHER TAXES

SUMMARY

1. Section 96 and Schedule 48 amend Schedule 36 to the Finance Act (FA) 2008 (Schedule 36). They extend HM Revenue & Customs' (HMRC) powers to obtain information and inspect businesses to matters concerning insurance premium tax, inheritance tax (IHT), stamp duty land tax (SDLT), stamp duty reserve tax (SDRT), petroleum revenue tax, aggregates levy, climate change levy and landfill tax. The section also provides for the Schedule to come into force on a day appointed by Treasury order, made by statutory instrument.

DETAILS OF THE SECTION

2. Subsection (1) amends paragraph 63(1) of Schedule 36 which specifies the taxes to which Schedule 36 applies. That Schedule makes provision about the powers of HMRC officers to obtain information and inspect businesses in respect of income tax, capital gains tax (CGT), corporation tax (CT) and VAT. The scope of the Schedule will now be widened to include the further taxes listed.

3. Subsections (3) and (4) provide that the amendments made by the section and the Schedule will come into force on a day appointed by the Treasury by an order made by statutory instrument and that different days may be appointed for different purposes.

4. Subsections (5) to (8) provide a power to make statutory instruments containing provisions or savings in consequence of or in connection with Schedule 36 as extended.

DETAILS OF THE SCHEDULE

5. Paragraph 2 makes a consequential amendment to paragraph 5(4)(b) of Schedule 36 to reflect the inclusion of the new taxes into Schedule 36.

6. Paragraph 3 inserts new paragraph 10A into Schedule 36. This provides a power for HMRC to inspect business premises and assets and relevant documents on the premises. It is very closely modelled on the existing paragraph 10 of Schedule 36 but it now applies to an "involved third party" which is a new concept within Schedule 36. It allows HMRC to inspect the premises, assets and documents of certain involved third parties in order to check a person's tax position, but only for a relevant tax. These new terms are defined by new paragraph 61A which is inserted by paragraph 14 below.

7. Paragraph 4 makes consequential amendments to paragraph 12 of Schedule 36.

8. Paragraph 5 inserts new paragraphs 12A and 12B into Schedule 36. New paragraph 12A(1) provides a power for HMRC to enter and inspect any premises for the purpose of valuing the premises with respect to income tax or CT. "Premises" is defined in paragraph 58 of Schedule 36. An example of the use of this power will be when a dwelling is transferred to or made available to an employee in return for services. The power replaces and updates that in section 110 of the Taxes Management Act 1970 (TMA) which will be repealed.

9. New paragraph 12A(2) provides a power for HMRC to enter premises and inspect the premises and any other property on the premises for the purpose of valuing, measuring or determining the character of the premises or property.

10. Under new paragraph 12A(3) the power in new paragraph 12A(2) only applies if the valuation etc is reasonably required to check any person's tax position as regards the specified taxes. This power replaces the powers in section 111 of TMA, section 220 of the Inheritance Tax Act 1984 (for IHT), section 94 of FA 2003 (for SDLT) and Regulation 20 of SI 1986/1711 which applies section 111 of TMA to SDRT.

11. New paragraph 12A(4) allows for other persons to accompany the HMRC officer if necessary (for example an expert external valuer who may value an asset such as a rare painting).

12. New paragraph 12B sets restrictions on carrying out inspections for valuation purposes under new paragraph 12A. The effect is that an inspection can only be carried out if one of two conditions is met. The first is that the relevant person (defined in sub-paragraph (3)) must have agreed the time of the inspection and been given a written notice. The alternative condition is that the inspection has been approved by the tribunal. In that case any relevant person specified by the tribunal must be given at least seven days' notice in writing of the inspection.

13. New paragraph 12B(5) and (6) mirror the rules in paragraph 12 of Schedule 36 about the content of the notice given at the time of inspection. In addition, new paragraph 12B(7) requires that an officer must produce evidence of authority if required to do so.

14. Paragraph 6(2) inserts a cross-reference to paragraph 39 of Schedule 36 (penalties), for clarity.

15. Paragraph 6(3) amends paragraph 13(1A) of Schedule 36 which is inserted by Schedule 47 allows applications to the tribunal for approval of an inspection visit to be without notice to the respondent. This is now made subject to new paragraph 13(2A) inserted by paragraph 6(5).

16. Paragraph 6(5) inserts new paragraphs 13(2A) and (2B) into Schedule 36 which cover the tribunal's approval of inspections for new paragraph 12A (valuation), in the same way that paragraph 13(2) of Schedule 36 covers tribunal approval of inspection under paragraphs 10, 10A and 11 of Schedule 36. It adds conditions at new sub-paragraphs (b), (c) and (d) which only apply to inspections for valuation purposes. These provide for the person whose tax position is being checked and the occupier to be given a reasonable opportunity to make representations to the officer and for the tribunal to be given a summary of the representations made. The provisions relating to the occupier making representations do not apply if the tribunal is satisfied that the occupier cannot be identified.

17. Paragraph 7 amends paragraph 17(b) of Schedule 36 so that the power to record information extends to recording information about property and goods.

18. Paragraph 8(2) amends paragraph 21(7) of Schedule 36. Paragraph 21 of Schedule 36 restricts HMRC's power to ask for information to check an income tax, CGT or CT position for a period for which a tax return has been submitted. This replicates the existing arrangements (the enquiry window). This restriction does not apply for checks in relation to VAT which does not have an equivalent enquiry mechanism.

19. This amendment has the effect that the rules which apply to VAT will now apply more widely, to all the taxes now being brought within the scope of Schedule 36. There is an exception of SDLT (for which, see below), as that tax does have an enquiry window.

20. Paragraph 9 inserts new paragraph 21A into Schedule 36 to incorporate the SDLT enquiry window. This paragraph mirrors the existing paragraph 21 and provides the same restriction on asking for information in respect of SDLT as is provides for income tax, CGT and CT.

21. Paragraph 11 inserts new paragraphs 34A, 34B and 34C into Schedule 36. This introduces the concept of "involved third parties" and contains special provisions for pension schemes.

22. New paragraph 34A is closely modelled on the existing paragraph 34 of Schedule 36 but it now applies to an "involved third party" (defined in new paragraph 61A below). It allows HMRC to give such a person a third party or unknown taxpayer information notice in order to check any other person's tax position, but only for relevant information, relevant documents and for a relevant tax. Involved third parties are all persons who stand in a special position in relation to a taxpayer for a particular tax.

23. Sub-paragraphs (2) to (5) disapply certain provisions of Schedule 36 which relate to third party notices. The effect of this is that involved third parties are treated as if they were first parties (taxpayers) rather than third parties in relation to approval and copying of notices. Similarly, an involved third party may not appeal against a requirement in a notice to provide information or documents which form part of their statutory records. Sub-paragraph (6) cross refers to definitions in new paragraph 61A (see below).

24. New paragraph 34B provides for pension schemes' rules similar to those that will apply to involved third parties. There are additional special rules, taken from the existing information power in section 252 of FA 2004, about to whom copies of notices must be given.

25. New paragraph 34C defines a number of terms used in new paragraph 34B. The regulation envisaged in the definition of "prescribed" will be laid in time to come into force alongside this Schedule.

26. Paragraph 12 amends paragraph 35 of Schedule 36 taking into account other changes made by Schedule 47 to this Act. The amendments reflect the insertion of new paragraph 21A. The special rules that apply to taxpayer notices where a return is held for the relevant period are extended to SDLT as that tax also has an enquiry window.

27. Paragraph 13 inserts a new paragraph 37(2A) into Schedule 36 to reflect the insertion of new paragraph 21A.

28. Paragraph 14 inserts a new paragraph 61A into Schedule 36. This defines certain terms used in the new inspection and information powers which apply to involved third parties. It contains a table which sets out what the terms "involved third parties", "relevant information and relevant documents" and "relevant tax" mean in nine different cases. Involved third parties are persons who have obligations under current legislation to provide information in relation to certain taxes in the same way as the taxpayer and are defined in line with the current legislation.

29. Paragraph 15(1) provides for amendments to paragraph 62 of Schedule 36 which defines "statutory records" for the purpose of the information and inspection powers contained in Schedule 36, and presently reflects the scope of Schedule 36 as originally enacted by referring to records required to be kept under the Taxes Act or VAT legislation.

30. Sub-paragraphs (2) and (3) replace references to VAT legislation by a wider reference to any other tax legislation. This is a consequential amendment to reflect the changes made to the scope of the taxes now to be covered by Schedule 36.

BACKGROUND NOTE

31. Schedule 36 to FA 2008 contains a new set of information and inspection powers which apply in checking any person's tax position in relation to income tax, CT, CGT and VAT. They came into force on 1 April 2009.

32. The main effect of this section and Schedule is to apply Schedule 36 to FA 2008 to many of the other taxes and duties administered by HMRC, from a date to be appointed. Once complete, this will be a major piece of modernised cross-tax legislation.

33. There are some information powers in a range of taxes that are not adequately covered by the existing powers in Schedule 36 to FA 2008. To address this it has been necessary to introduce the concept of an "involved third party". This reflects the approach of existing law to persons who are neither taxpayers (first parties) nor conventional third parties such as banks. These persons are closely involved in a potentially taxable event or transaction and are currently required to provide information about that activity. In relation to these persons some of the normal rules that apply to third party information notices are relaxed and HMRC will be able to inspect the premises of such parties.

34. The amended Schedule 36 to FA 2008 also now contains an entry power for valuation purposes which brings together several existing powers into a single aligned power. The power to enter and inspect premises in Schedule 36 to FA 2008 only applies to business premises, but it is often necessary to value private premises or assets on such premises, e.g. for IHT, the valuation of all types of property is an essential form of check.

35. The valuation power introduced in Schedule 48 contains safeguards which go beyond those in current legislation. In particular, a valuation inspection can only be carried out with either the agreement of the relevant person (usually the occupier) or the tribunal. There is no facility to make an unannounced visit.

SECTION 97 AND SCHEDULE 49: POWERS TO OBTAIN CONTACT DETAILS FOR DEBTORS

SUMMARY

1. Section 97 and Schedule 49 provide that HM Revenue & Customs (HMRC) may issue notices requiring third parties to provide contact details for those in debt to HMRC.

DETAILS OF THE SCHEDULE

2. Paragraph 1 provides that a number of conditions must be satisfied before HMRC can issue a formal notice. The first is that a person owes a sum to HMRC, and HMRC reasonably requires up-to-date contact details to be able to collect the debt. "Contact details" mean an address or other information about how the debtor may be contacted. The debt must arise under or by virtue of an enactment, or under a contract settlement. "Under or by virtue of an enactment" brings in those debts arising from taxes, duties etc imposed by statute. "Contract settlements" are defined in paragraph 8 and are contractual agreements made in connection with a person's liability, usually as the result of an enquiry covering a number of years.

3. Second, an officer of Revenue and Customs must have reasonable grounds to believe that the third party has contact details that differ from the latest held by HMRC.

4. The third condition defines who the third party can be and so prevents HMRC formally requiring information from neighbours or relatives who have no business relationship with the debtor.

5. The fourth condition prevents HMRC formally requiring information from charities that acquire the contact details in the course of providing advice without charge.

6. Paragraph 2 provides that an officer of Revenue and Customs may serve a notice on a third party requiring the production of contact details. The requirement for a written notice does not preclude earlier requests, whether orally or otherwise. The notice must name the debtor, and in practice HMRC would provide sufficient other information to identify the debtor including the latest address it holds.

7. Paragraph 3 provides that where a third party is required to provide contact details, it must be done within the period, at the time, and in the means and format reasonably specified in the notice. The notice does not need to specify means or form but in practice a response may be in writing, by telephone or otherwise. Confirmation that no different address is held from that which HMRC has provided will satisfy the notice.

8. Paragraph 5 provides that a person who fails to comply with a notice is liable to a penalty of £300. The procedures for penalties are the same as those for the information power to check a person's tax position under Schedule 36 to the Finance Act (FA) 2008.

9. Paragraph 6 provides that the Treasury may make regulations to alter the penalty in paragraph 5 where there is a change in the value of money.

BACKGROUND NOTE

10. HMRC makes every effort to ensure that the address information it holds is accurate and up-to-date. It uses a range of techniques to trace tax debtors who go missing, including the extensive use of commercial databases. However, there remain some who cannot be traced and in 2007 the Department wrote off £300 million for this reason.

11. This section and Schedule allow HMRC to require relevant third parties to disclose address and contact details of missing debtors, where those details are reasonably required to collect what is owed. Relevant third parties are those who HMRC has reason to believe have more recent contact details than it holds. They are explicitly restricted to companies, local authorities and local authority associations and those who HMRC reasonably believes to have, or have had, a business relationship with the debtor.

12. This measure was the subject of initial consultation in June 2007 and further consultation in December 2008 (*Payments, Repayments and Debt: the Next Stage*). Draft legislation was published for consultation in January 2009, and a response document together with a final Impact Assessment was published in April 2009.

SECTION 98 AND SCHEDULE 50: RECORD-KEEPING

SUMMARY

1. Section 98 and Schedule 50 amend existing legislation to align the record-keeping rules for environmental taxes (aggregates levy, climate change levy and landfill tax), insurance premium tax (IPT) and stamp duty land tax (SDLT). The section also provides for the Schedule to come into force on a day appointed by Treasury order.

DETAILS OF THE SCHEDULE

2. Paragraph 1(1) introduces the amendments to paragraph 1 of Schedule 7 to the Finance Act 1994 (FA) 1994. This contains the record-keeping rules for IPT.

3. Paragraph 1(2)(a) inserts new paragraphs 1(3)(a) to (c) into Schedule 7 to FA 1994. This makes clear that HM Revenue & Customs (HMRC) may reduce the period for which records must be retained for IPT. Different reduced retention periods may be specified for different cases.

4. Paragraph 1(3) replaces paragraphs 1(4) to (6) of Schedule 7 to FA 1994 with a new sub-paragraph (4). The effect is to replace the existing power for HMRC to approve preservation of information instead of records with a general rule that such preservation is acceptable, subject to any conditions and exceptions set by HMRC in writing.

5. Paragraph 2 repeals a provision which is no longer required.

6. Paragraph 3 introduces the amendments to Part 4 of FA 2003. This contains the record-keeping rules for SDLT.

7. Paragraph 5(3) inserts new paragraph 9(2A) into Schedule 10 to FA 2003, which defines "the relevant day". This is either the sixth anniversary of the effective date of the transaction, or an earlier day specified by HMRC. This allows HMRC to reduce the period for which records must be retained by specifying this in writing. Different reduced retention periods may be specified for different cases.

8. Paragraph 5(4) inserts new paragraphs 9(4)-(6) into Schedule 10 to FA 2003. New paragraph 9(4) introduces a new power for HMRC to specify by regulation the records and supporting documents that must be kept.

9. New paragraph 9(5) contains provision about the scope of regulations under paragraph 9 of Schedule 10 to FA 2003. It allows for the possibility of tertiary legislation to specify records.

10. Paragraph 6 substitutes a new paragraph 10 into Schedule 10 to FA 2003. This restates existing law which allows the preservation of information in any form and there is a new power for HMRC to specify, in writing, conditions and exceptions to this general rule.

11. Paragraph 9(2) substitutes a new paragraph 4(2) into Schedule 11 to FA 2003. This restates the current six year retention period but now allows HMRC to reduce the period for which records must be retained by specifying this in writing. Different reduced retention periods may be specified for different cases.

12. Paragraph 9(4) inserts new paragraphs 4(4)-(6) into Schedule 11 to FA 2003. New sub-paragraph (4) introduces a new power for HMRC to specify by regulation the records and supporting documents that must be kept.

13. New sub-paragraph (5) contains provision about the scope of regulations under paragraph 4 of Schedule 11 to FA 2003. It allows for the possibility of tertiary legislation to specify records.

14. Paragraph 10 substitutes a new paragraph 5 in Schedule 11 to FA 2003. This restates existing law which allows the preservation of information in any form and there is a new power for HMRC to specify conditions and exceptions to this general rule in writing.

15. Paragraph 11 makes a consequential change.

16. Paragraph 13(2) repeals paragraph 3(3) and (4) of Schedule 11A to FA 2003 which contains provisions about evidence of records that are required to be preserved. These are no longer needed.

17. Paragraph 13(3) inserts new sub-paragraphs (4A) to (4C) into paragraph 3 of Schedule 11A to FA 2003.

18. New sub-paragraph (4A) introduces a new power for HMRC to specify by regulation the records and supporting documents that must be kept.

19. New sub-paragraph (4B) contains provision about the scope of regulations under paragraph 3 of Schedule 11A to FA 2003. It allows for the possibility of tertiary legislation to specify records.

20. Paragraph 14 inserts new paragraph 3A into Schedule 11A to FA 2003. This restates existing law which allows the preservation of information in any form and there is a new power for HMRC to specify conditions and exceptions to this general rule in writing.

21. Paragraph 15 introduces the amendments to Schedule 7 to FA 2001. That Schedule includes record-keeping rules for aggregates levy.

22. Paragraph 16(2) replaces paragraphs 2(4) and (5) of Schedule 7 to FA 2003 with new sub-paragraph (4). The effect is to replace the existing power for HMRC to approve preservation of information instead of records with a general rule that such preservation is acceptable, subject to any conditions and exceptions set by HMRC in writing.

23. Paragraph 16(3) makes consequential amendments.

24. Paragraph 17 repeals paragraph 3 of Schedule 7 to FA 2003 which contains provisions about evidence of records that are required to be preserved. This is no longer needed.

25. Paragraph 18 introduces amendments to Schedule 6 to FA 2000. This contains the record-keeping rules for climate change levy.

26. Paragraph 19(2) replaces paragraphs 125(4) and (5) with new sub-paragraph (4). The effect is to replace the existing power for HMRC to approve preservation of information instead of records with a general rule that such preservation is acceptable, subject to any conditions and exceptions set by HMRC in writing.

27. Paragraph 19(3) makes consequential amendments to paragraph 125(9) of Schedule 6.

28. Paragraph 20 omits paragraph 126 of Schedule 6 to FA 2000 which contained provisions about evidence of records that are required to be preserved. This is no longer needed.

29. Paragraph 21 replaces paragraphs 2(4) to (7) of Schedule 5 to FA 1996 with a new sub-paragraph (4). That Schedule includes record-keeping rules for landfill tax. The effect is to replace the existing power for HMRC to approve preservation of information instead of records with a general rule that such preservation is acceptable, subject to any conditions and exceptions set by HMRC in writing. This paragraph also has the effect of omitting existing provisions about admissibility of documents in proceedings which are no longer needed.

BACKGROUND NOTE

30. Schedule 37 to FA 2008 introduced a common format for rules about keeping records for income tax, capital gains tax (CGT), corporation tax (CT) and VAT. It introduced a new flexibility for HMRC to shorten the periods for which records need to be retained for income tax, CGT and CT. It also introduced new regulation-making powers for HMRC in relation to specifying records and formats which can also be exercised by tertiary legislation. Regulations can be made when there is a need for legislative certainty on particular records. Schedule 37 aligned the rules about preserving information instead of records and preserving information in any form and means, providing HMRC with flexibility to adapt to change, particularly with the increasing use of technology for keeping records.

31. The provisions of this Schedule make corresponding changes, from a day to be appointed, to the record-keeping requirements that apply to environmental taxes (aggregates levy, climate change levy and landfill tax), insurance premium tax and stamp duty land tax.

32. The changes in this Schedule also support the new compliance checking powers for these taxes and allow for a cross-tax approach to be taken by HMRC.

SECTION 99 AND SCHEDULE 51: TIME LIMITS FOR ASSESSMENTS, CLAIMS ETC

SUMMARY

1. Section 99 introduces Schedule 51 which contains provisions amending time limits that apply to assessments and claims in respect of insurance premium tax (IPT), inheritance tax (IHT), stamp duty land tax (SDLT), petroleum revenue tax (PRT), aggregates levy, climate change levy and landfill tax . The section also provides for the Schedule to come into force on a day appointed by Treasury order, made by statutory instrument.

DETAILS OF THE SCHEDULE

2. Paragraph 1 provides for Schedule 7 to the Finance Act (FA) 1994 to be amended. The following paragraphs introduce and change time limits that apply to IPT claims and assessments.

3. Paragraph 2 extends the time limit for recovering overpaid IPT at paragraph 8(4) of Schedule 7 to FA 1994 from 3 to 4 years.

4. Paragraph 3 extends the time limit for claiming interest from HM Revenue & Customs (HMRC) at paragraph 22(9) of Schedule 7 to FA 1994 from 3 to 4 years.

5. Paragraph 4(2) changes the normal IPT assessing time limit from 3 to 4 years. It also restructures paragraph 26(1) of Schedule 7 to FA 1994 so that the time limit is geared to "the relevant event", but without any change of effect.

6. Paragraph 4(3) inserts new paragraph 26(1A) into Schedule 7 to FA 1994 which defines "the relevant event". This definition is the same as that previously given at sub-paragraph 26(1) of Schedule 7 to FA 1994.

7. Paragraph 4(4) makes a consequential amendment.

8. Paragraph 4(5) replaces paragraph 4(4) of Schedule 7 to FA 1994 with new paragraphs 4(4) and 4(5). The existing assessing time limit of 20 years in cases of fraud or where a person has failed to register is retained, but the reference to a tax loss due to "fraud" is changed to a tax loss "brought about deliberately". This is in line with changes made in Schedule 24 to FA 2007 (penalties for incorrect returns) and elsewhere. It is also made clear that a loss brought about deliberately includes a loss resulting from a deliberate inaccuracy in a document given to HMRC.

9. Paragraph 5 provides for the Inheritance Tax Act 1984 (IHTA) to be amended. The following paragraphs introduce and change time limits that apply to IHT claims and assessments.

10. Paragraph 6 inserts new section 131(2ZA) into IHTA. It introduces a new time limit of 4 years from the transferor's death for a claim under section 131(2)(b) of IHTA.

11. Paragraphs 7 to 10 introduce a new time limit of 4 years under the relevant sections of IHTA.

12. Paragraph 11(2) amends section 240(2) of IHTA. This reduces the period allowed for HMRC to bring proceedings to recover additional tax under section 240(2) of IHTA (i.e. in a case where an account has been delivered) from 6 to 4 years.

13. Paragraph 11(3) replaces section 240(3) of IHTA with new subsections (3) to (6). New subsection (4) provides that the time limit remains at 6 years where the underpayment has been brought about carelessly. New subsection (5) increases the time limit to 20 years where the loss of tax is brought about deliberately. New subsection (6) provides that the new time limit at new subsection (7) applies in cases where no account has been delivered, and there is no deliberate loss of tax. New subsection (7) provides a 20 year time limit on proceedings to recover additional tax in such cases. New subsection (8) provides that these behaviour descriptions include the behaviour of a settlor in certain cases.

14. Paragraph 12 inserts new section 240A into IHTA.

15. New subsection (1) provides that the new section supplements the new time limits in section 240 of IHTA.

16. New subsection (2) provides that a loss of tax is brought about carelessly by any person if the person fails to take reasonable care to avoid bringing about that loss. This corresponds with the definition of careless at paragraph 3(1)(a) of Schedule 24 to FA 2007.

17. New subsection (3) provides that where information is provided to HMRC by someone who later discovers that the information was inaccurate but does not take reasonable steps to inform HMRC, any loss of tax brought about by this is to be treated as having been brought about carelessly. This corresponds with the definition at paragraph 3(2) of Schedule 24 to FA 2007.

18. New subsection (4) provides that where a loss of tax is brought about by a deliberate inaccuracy in a document, it is to be treated as brought about deliberately. This is to ensure that in cases where a penalty is due for deliberate inaccuracy under paragraph 3 of Schedule 24 to FA 2007, the corresponding increase in time limit also occurs.

19. Paragraph 13 amends section 241(1) of IHTA by reducing the period in which repayment of an excess tax payment may be claimed from 6 to 4 years.

20. Paragraph 14 provides for FA 2003 to be amended. The following paragraphs introduce and change time limits that apply to SDLT claims and assessments.

21. Paragraph 15(2) amends paragraph 25(3) of Schedule 10 to FA 2003 reducing the period in which HMRC may make a determination of SDLT chargeable if no return is delivered from 6 to 4 years.

22. Paragraph 15(3) amends paragraph 27(2)(a) of Schedule 10 to FA 2003 by reducing the period during which a self assessment must be made if it is to replace a determination from 6 to 4 years.

23. Paragraph 15(5) amends paragraph 31(1) of Schedule 10 to FA 2003. This provides that the normal SDLT assessing time limit is reduced from 6 to 4 years.

24. Paragraph 15(6) replaces paragraph 31(2) of Schedule 10 to FA 2003 with new sub-paragraphs (2) and (2A).

25. New sub-paragraph (2) provides that the time limit remains at 6 years where there is a loss of tax brought about carelessly.

26. New sub-paragraph (2A) provides that it is increased to 20 years where the loss of tax is brought about deliberately by the purchaser or a "related person". This increase to 20 years also occurs where the loss of tax is attributable to a person's failure to notify HMRC that they are liable to tax, as required by section 76(1) or paragraph 3(3)(a), 4(3)(a) or 8(3)(a) of Schedule 17A to FA 2003, or where a person has failed to disclose an avoidance scheme as required by sections 309, 310 or 313 of FA 2004.

27. Paragraph 15(7) amends paragraph 31(4)(a) of Schedule 10 to FA 2003. This increases the period during which HMRC may make an assessment on personal representatives from 3 to 4 years.

28. Paragraph 15(8) inserts new paragraph 31(6) into Schedule 10 to FA 2003. It defines a "related person" in relation to a purchaser for the purpose of the new behaviour-related time limits.

29. Paragraph 15(9) inserts new paragraph 31A into Schedule 10 to FA 2003. New sub-paragraph (1) provides that this supplements the time limits in new sub-paragraphs (2) and (2A).

30. New sub-paragraph (2) provides that a loss of tax is brought about carelessly by any person if the person fails to take reasonable care to avoid bringing about that loss. This corresponds with the definition of careless at sub-paragraph 3(1)(a) of Schedule 24 to FA 2007.

31. New sub-paragraph (3) provides that where information is provided to HMRC by someone who later discovers that the information was inaccurate but does not take reasonable steps to inform HMRC, any loss of tax brought about by this is to be treated as having been brought about carelessly. This corresponds with the definition at paragraph 3(2) of Schedule 24 to FA 2007.

32. New sub-paragraph (4) provides that where a loss of tax is brought about by a deliberate inaccuracy in a document, it is to be treated as brought about deliberately. This is to ensure that in cases where a penalty is due for deliberate inaccuracy under paragraph 3 of Schedule 24 to FA 2007, the corresponding increase in time limit also occurs.

33. Paragraph 15(10) amends paragraph 34(2) of Schedule 10 to FA 2003 by reducing the period in which a claim for relief may be made in respect of a mistake in a return from 6 to 4 years.

34. Paragraph 16(2) amends paragraph 8(2) of Schedule 14 to FA 2003. It reduces the period during which HMRC may make a determination of penalties or bring proceedings for penalties from 6 to 4 years from the date the penalty was incurred or, in the case of daily penalties, first incurred. This date is referred to by later paragraphs as "the relevant date", from which certain time limits run.

35. Paragraph 16(3) amends sub-paragraph 8(3) of Schedule 14 to FA 2003. This provides that the 3-year time limit on making a determination of penalties or bringing proceedings is subject to the longer time limits allowed by paragraph 8 of Schedule 14 to FA 2003.

36. Paragraph 16(4) inserts new paragraphs 8(4A) to (4C) into Schedule 14 to FA 2003. The time limit remains at 6 years where the penalty relates to a loss of tax brought about carelessly and is increased to 20 years where it relates to a loss of tax brought about deliberately or where certain obligations have not been met. The extended time limits for assessing penalties mirror those for assessing a loss of tax and the new rules in paragraph 31A of Schedule 10 to FA 2003, described above, also apply.

37. Paragraph 17 provides for the Oil Taxation Act 1975 (OTA 1975) to be amended. The following paragraphs introduce and change time limits that apply to PRT claims and assessments.

38. Paragraph 18(2) corrects the entry in the Table at Schedule 2 to OTA 1975 relating to section 33(1) of the Taxes Management Act 1970 (TMA). This does not change the effect of the provision.

39. Paragraph 18(3) omits the entries in the Table relating to sections 34 and 36 of TMA (assessing time limits) so that those provisions do not apply to PRT. Instead the following paragraphs make similar provision in OTA 1975.

40. Paragraph 19 inserts new paragraph 10(1A) into Schedule 2 to OTA 1975. It provides that the normal PRT assessing time limit is 4 years instead of the current 6 years.

41. Paragraph 20(2) inserts new paragraphs 12(1A) and (1B) into Schedule 2 to OTA 1975.

42. New sub-paragraph (1A) provides a normal 4 year time limit for the making or amending of PRT assessments

43. New sub-paragraph (1B) provides that the time limit does not apply to an amendment made to relieve allowable losses or made in consequence of allowing such relief.

44. Paragraph 20(3) amends paragraph 12(2) of Schedule 2 to OTA 1975. It reduces the normal time limit for making a further assessment from 6 to 4 years.

45. Paragraph 21 amends paragraph 12A(1) of Schedule 2 to OTA 1975. It reduces the period during which HMRC may make an assessment from 5 to 4 years.

46. Paragraph 22 inserts new paragraph 12B into Schedule 2 to OTA 1975. This provides extended assessing time limits in cases where a "relevant situation", defined at new sub-paragraph (3), has been brought about carelessly or deliberately by the participator or a person acting on the participator's behalf.

47. New sub-paragraph (1) provides that where the relevant situation is brought about carelessly, the time limit is 6 years.

48. New sub-paragraph (2) provides that where the relevant situation is brought about deliberately, the time limit is 20 years.

49. New sub-paragraph (3) defines "relevant situation" to be a loss of tax, an underassessment of profit, an overstated loss or a lack of any assessment.

50. New sub-paragraph (4) defines "relevant chargeable period", from the end of which these time limits run. This is usually the chargeable period to which the assessment relates, but if the assessment is under paragraph 12(2) of Schedule 2 to OTA 1975, i.e. an assessment where the deficiency results from an excessive allowable loss accruing in a subsequent period, then it is that subsequent period.

51. New sub-paragraph (5) makes provision for where a participator acts in partnership with others. This provision was previously in the Table at paragraph 1(1) of Schedule 2 to OTA 1975.

52. New sub-paragraph (6) requires HMRC to take into account any relief or allowance the assessed person would have been entitled to in the period covered by the assessment. This mirrors the provision in section 36 of TMA which previously applied to PRT.

53. New sub-paragraph (7) clarifies that this requirement only applies if the person assessed so requires, again mirroring section 36 of TMA.

54. New sub-paragraph (8) applies the definitions of "careless" and "deliberate" at section 118 of TMA, to PRT, aligning these definitions with those for penalties in Schedule 24 to FA 2007.

55. New sub-paragraph (9) clarifies that where a person takes over the position of responsible person for an oilfield and they discover that information provided by their predecessor was inaccurate, then section 118(6)(b) of TMA applies as if the information had been provided by themselves.

56. Paragraph 23(2) amends paragraph 2(1) of Schedule 5 to OTA 1975 by reducing the normal period for making a claim for expenditure from 6 to 4 years.

57. Paragraph 23(3) amends paragraph 2(7)(c) of Schedule 5 to OTA 1975. This means that in cases where HMRC has agreed to a deferral of the responsible person's return and the earlier of the time that the return is delivered or the latest time for the delivery of the return following the agreed deferral is now more than 2 years (previously 4 years) after the end of the claim period, then the time limit for making the claim is extended to 2 years after the earlier of the deferred delivery date and the date of delivery of the return. The effect is to ensure that there is always a minimum of 2 years in which to check a claim.

58. Paragraph 24(2) restructures paragraph 9(1) of Schedule 5 to OTA 1975 so that HMRC may give a notice of variation within a period labelled "the permitted period".

59. Paragraph 24(3) repeals paragraphs 9(1A) to (1C) and 9(2A) of Schedule 5 to OTA 1975. These sub-paragraphs formerly set out the old time limits for a notice of variation.

60. Paragraph 24(4) inserts new paragraphs 9(2B) and (2C) into Schedule 5 to OTA 1975. New sub-paragraph (2B) defines "the permitted period" for a notice of variation to be in the normal case the period of 4 years from the date of the original notice under paragraph 3 of Schedule 5 to OTA 1975.

61. New sub-paragraph (2C) extends this period to 6 years if the inaccuracy is careless and to 20 years if the inaccuracy is deliberate

62. Paragraph 24(6) inserts new paragraphs 9(12) and (13) into Schedule 5 to OTA 1975.New sub-paragraph (12) provides that a loss of tax is brought about carelessly by a responsible person or someone acting on their behalf if the person fails to take reasonable care to avoid bringing about that loss. This corresponds with the definition of careless at sub-paragraph 3(1)(a) of Schedule 24 to FA 2007.

63. New sub-paragraph (13) provides that where information is provided to HMRC by the responsible person for an oil field (or someone who acts on their behalf), and that person later discovers that the information was inaccurate but does not take reasonable steps to inform HMRC, the inaccuracy is to be treated as having been brought about carelessly. This is also the case where the inaccuracy is discovered by someone who becomes the responsible person for the oil field, or who acts on their behalf. This corresponds with the definition at sub-paragraph 3(2) of Schedule 24 to FA 2007.

64. Paragraph 25(2) amends paragraph 1 of Schedule 6 to OTA 1975 by reducing the period for making a claim for expenditure from 6 to 4 years.

65. Paragraph 25(3) makes a consequential amendment to the entry relating to paragraph 9 of Schedule 5 to OTA 1975 in the Table in paragraph 2 of Schedule 6 to OTA 1975. This ensures that where this provision referred to the old time limits in Schedule 5 to OTA 1975, it will now refer to the new time limits there.

66. Paragraph 26 makes a consequential amendment to the entry relating to paragraph 9 of Schedule 5 to OTA 1975 in the Table in paragraph 1(3) of Schedule 7 to OTA 1975. This ensures that where this provision referred to the old time limits in Schedule 5 to OTA 1975, it will now refer to the new time limits there.

67. Paragraph 27 provides for Part 2 of FA 2001 (which includes Schedules 5, 8 and 10 to that Act) to be amended. The following paragraphs change time limits that apply to aggregates levy claims and assessments.

68. Paragraph 28 amends section 32(1) of FA 2001. It extends the period for reclaiming overpaid aggregates levy from 3 to 4 years.

69. Paragraph 29(2) amends paragraph 4(1)(b) of Schedule 5 to FA 2001 by extending the normal assessing time limit from 3 to 4 years.

70. Paragraph 29(3) replaces paragraph 4(3) of Schedule 5 to FA 2001 with new sub-paragraphs (3) and (3A).

71. New sub-paragraph (3) extends the assessing time limit to 20 years where the loss of tax is brought about deliberately or where a person has failed to register. The new term "deliberately" is in line with changes made in Schedule 24 to FA 2007 (penalties for incorrect returns) and elsewhere.

72. New sub-paragraph (3A) clarifies that a loss brought about deliberately includes a loss resulting from a deliberate inaccuracy in a document given to HMRC.

73. Paragraph 29(4) amends paragraph 4(4) of Schedule 5 to FA 2001 by extending the period for making an aggregates levy assessment required by reason of some conduct of a deceased person from 3 to 4 years.

74. Paragraph 30 amends paragraph 2(10) of Schedule 8 to FA 2001 by extending the period for making a claim for interest on a repayment from 3 to 4 years.

75. Paragraph 31(2) amends paragraph 4(1) of Schedule 10 to FA 2001. It extends the normal period in which HMRC may make an aggregates levy penalty assessment from 3 to 4 years.

76. Paragraph 31(3) replaces paragraph 4(2) of Schedule 10 to FA 2001 with new sub-paragraphs (2) and (2A).

77. New sub-paragraph (2) extends the assessing time limit to 20 years where the loss of tax is brought about deliberately or where a person has failed to register. The new term "deliberately" is in line with changes made in Schedule 24 to FA 2007 (penalties for incorrect returns) and elsewhere.

78. New sub-paragraph (2A) clarifies that a loss brought about deliberately includes a loss resulting from a deliberate inaccuracy in a document given to HMRC.

79. Paragraph 31(4) amends paragraph 4(3) of Schedule 10 to FA 2001. It extends the period for making an AGL penalty assessment required by reason of some conduct of a deceased person from 3 to 4 years.

80. Paragraph 32 provides for Schedule 6 of FA 2000 to be amended. The following paragraphs change time limits that apply to climate change levy claims and assessments.

81. Paragraph 33 amends paragraph 64(1) of Schedule 6 to FA 2000. It extends the period for reclaiming overpaid climate change levy from 3 to 4 years.

82. Paragraph 34 amends paragraph 66(10) of Schedule 6 to FA 2000 by extending the period for making a claim for interest on a repayment from 3 to 4 years.

83. Paragraph 35(2) amends paragraph 80(1)(b) of Schedule 6 to FA 2000. It extends the normal assessing time limit from 3 to 4 years.

84. Paragraph 35(3) replaces paragraph 80(3) of Schedule 6 to FA 2000 with new sub-paragraphs (3) and (3A).

85. New sub-paragraph (3) extends the assessing time limit to 20 years where the loss of tax is brought about deliberately or where a person has failed to register. The new term "deliberately" is in line with changes made in Schedule 24 to FA 2007 (penalties for incorrect returns) and elsewhere.

86. New sub-paragraph (3A) clarifies that a loss brought about deliberately includes a loss resulting from a deliberate inaccuracy in a document given to HMRC.

87. Paragraph 35(4) amends paragraph 80(4) of Schedule 6 to FA 2000. It extends the period for making a climate change levy assessment required by reason of some conduct of a deceased person from 3 to 4 years.

88. Paragraph 36(2) amends paragraph 108(1) of Schedule 6 to FA 2000. It extends the normal period in which HMRC may raise a climate change levy penalty assessment from 3 to 4 years.

89. Paragraph 36(3) replaces paragraph 108(2) of Schedule 6 to FA 2000 with new sub-paragraphs (2) and (2A).

90. New sub-paragraph (2) extends the assessing time limit to 20 years where the loss of tax is brought about deliberately or where a person has failed to register. The new term "deliberately" is in line with changes made in Schedule 24 to FA 2007 (penalties for incorrect returns) and elsewhere.

91. New sub-paragraph (2A) clarifies that a loss brought about deliberately includes a loss resulting from a deliberate inaccuracy in a document given to HMRC.

92. Paragraph 36(4) amends paragraph 108(3) of Schedule 6 to FA 2000. It extends the period for making a climate change levy penalty assessment required by reason of some conduct of a deceased person from 3 to 4 years.

93. Paragraph 37 provides for Schedule 5 to FA 1996 to be amended. The following paragraphs change time limits that apply to landfill tax claims and assessments.

94. Paragraph 38 amends paragraph 14(4) of Schedule 5 to FA 1996. It extends the period for reclaiming overpaid landfill tax from 3 to 4 years.

95. Paragraph 39 amends paragraph 29(8) of Schedule 5 to FA 1996. It extends the period for making a claim for interest on a repayment under paragraph 29 of Schedule 5 to FA 1996 from 3 to 4 years.

96. Paragraph 40(2) amends paragraph 33(1) of Schedule 5 to FA 1996 by extending the normal assessing time limit from 3 to 4 years. The time limit applies to both assessments to landfill tax and to associated penalties. Time limits run from the "relevant event", which is defined below.

97. Paragraph 40(3) inserts new paragraph 33(1A) into Schedule 5 to FA 1996. It defines "relevant event" as the end of the accounting period or the date of the event giving rise to a penalty. The use of this term simplifies the drafting without changing meaning.

98. Paragraph 40(5) replaces paragraph 33(4) of Schedule 5 to FA 1996 with new sub-paragraphs (4) and (4A). These provisions apply to both assessments to landfill tax and to associated penalties.

99. New sub-paragraph (4) extends the assessing time limit to 20 years where the loss of tax is brought about deliberately or where a person has failed to register. The new term "deliberately" is in line with changes made in Schedule 24 to FA 2007 (penalties for incorrect returns) and elsewhere.

100. New sub-paragraph (4A) clarifies that a loss brought about deliberately includes a loss resulting from a deliberate inaccuracy in a document given to HMRC.

101. Paragraph 40(6) amends paragraph 33(5) of Schedule 5 to FA 1996. It extends the period for making an assessment to landfill tax or to associated penalties required by reason of some conduct of a deceased person from 3 to 4 years.

102. Paragraph 41 makes a minor clarifying change to sections 36(2) and (3) of TMA. This is to reflect the fact that sections 36(1) and (1A) of TMA (introduced by paragraph 9(2) of Schedule 39 to FA 2008) replaces "for the purpose" with "in a case".

103. Paragraph 42 omits paragraph 66 of Schedule 39 to FA 2008. This paragraph was a saving so that changes to income tax time limits did not affect PRT. Removing it ensures that the amendments of section 33 of TMA made by Schedule 39 to FA 2008 will have effect for the purposes of PRT.

104. Paragraph 43 makes consequential repeals

BACKGROUND NOTE

105. Schedule 39 to FA 2008 amends, from 1 April 2010 with transitional provision from 1 April 2009, most of the time limits that apply to claims and assessments for income tax, capital gains tax, corporation tax and VAT. The period for making claims is generally set at 4 years. The normal assessing time limit also becomes 4 years. For direct taxes it is 6 years where the loss of tax is brought about carelessly. For all taxes it is 20 years where the loss of tax is brought about deliberately or where there is a failure to notify liability or disclose avoidance arrangements.

106. The provisions of this Schedule make corresponding changes to the limit limits that apply to claims and assessments for insurance premium tax, inheritance tax, stamp duty land tax, petroleum revenue tax, aggregates levy, climate change levy and landfill tax. For some of these there is no requirement to notify liability or disclose avoidance arrangements, and so there is no extended time limit in those circumstances.

SECTION 100 SCHEDULE 52: RECOVERY OF OVERPAID TAX ETC

SUMMARY

1. Section 100 and Schedule 52 change the rules regarding claims for repayment of overpaid income tax, capital gains tax (CGT) and corporation tax (CT). The changes will have effect for claims made on or after 1 April 2010 except for certain transitional cases.

DETAILS OF THE SECTION

2. Section 100 introduces Schedule 52 which amends the existing error or mistake relief legislation and allows HM Treasury to make transitional and other provisions as appropriate.

DETAILS OF THE SCHEDULE

3. Part 1 of the Schedule deals with overpayments of income tax and CGT. It replaces sections 33 and 33A of the Taxes Management Act 1970 (TMA) and introduces new Schedule 1AB to TMA which contains the main provisions. Part 1 amends other sections of TMA and Schedule 1A for error or mistake claims.

4. Paragraph 1 of the new Schedule 1AB provides that a person may make a claim for repayment of an amount they have overpaid by way of income tax or CGT or discharge of an amount that has been over-assessed, subject to restrictions. It also provides that the Commissioners for HM Revenue and Customs (HMRC) are not liable to give relief except under this provision or any other provision relating to income tax or CGT.

5. Paragraph 2 of the new Schedule 1AB sets out cases in which the Commissioners will not be liable to give relief:

- case A is where the alleged overpayment arises from a mistake concerning a claim, election or notice or certain mistakes relating to capital allowances;
- case B is where relief can be obtained by other means;
- case C is where the claimant could have obtained relief by other means when they first knew, or ought reasonably to have known of the overpayment;
- case D is where the grounds of the claim have already been considered by a court or tribunal, or considered by HMRC and settled by agreement between HMRC and the claimant, during the course of an appeal;
- case E is where the claimant knew or ought reasonably to have known the grounds at a time when claimant could have brought the appeal before the tribunal or a court in due course;
- case F is where HMRC have taken proceedings to enforce payment of the amount; and

- cases G and H deal with amounts that were understood to be due under the practice generally prevailing at the time the liability was computed or in the case of PAYE, the practice generally prevailing 12 months after the end of the tax year.

6. Paragraph 3 of the new Schedule 1AB sets a time limit for claims of four years from the period in respect of which the payment or the assessment was made except where the claim arises from a mistake in a return. For mistakes in returns, the time limit runs from the end of the period for which the return was made. Claims are to be made outside a Self Assessment return.

7. Paragraph 4 of the new Schedule 1AB provides that where A is required to pay tax due from B under any enactment, a claim can only be made by B. If A pays an amount that they were not required to pay under a relevant enactment in respect of B, A may claim repayment but HMRC will not be required to pay an amount that has already been repaid to B.

8. Paragraph 5 of the new Schedule 1AB provides that a claim in respect of a mistake in a partnership return must be made by a partner nominated by all the relevant partners.

9. Paragraph 6 of the new Schedule 1AB allows HMRC to make a discovery assessment to recover any related underpayments of income tax, capital gains tax or corporation tax or to make a discovery determination for a related amount where these would otherwise be out of time or barred by section 29(2) of TMA or the CT equivalent. If the assessment or determination depends on these provisions it must be made before the claim is finally determined.

10. Paragraph 7 of the new Schedule 1AB similarly allows HMRC to make a discovery amendment to a partnership statement to recover any related underpayments of income tax, CGT or CT.

11. Paragraph 8 of the new Schedule 1AB extends claims to amounts paid under contract settlements. It allows HMRC to set any repayments against amounts payable under discovery assessments or through partnership amendments related to the claim.

12. Paragraph 5 of the Schedule inserts a new subsection (2B) into section 43A of TMA to provide that a claim is relevant to an amendment or discovery assessment if it relates to the same year of assessment.

13. Paragraph 7 amends Schedule 1A of TMA to ensure that a claim has no effect if it is provided elsewhere that the amount should not be repaid or discharged.

14. Paragraph 10 follows the transitional provisions relating to changes to general claims time limits under Schedule 39 to the Finance Act (FA) 2008. It provides that a longer time limit will apply for claims made before 1 April 2012, by persons other than companies, where the claim relates to a mistake in a return and the notice requiring that return was not given within one year of the end of the tax year.

15. Paragraph 11 provides that section 33 of TMA will continue to apply in its current form for the purposes of petroleum revenue tax.

16. Part 2 deals with overpayments of CT. It amends paragraph 51 of Schedule 18 to FA 1998 and introduces new paragraphs 51A to G.

17. New paragraph 51 of Schedule 18 to FA 1998 provides that a person may make a claim for repayment of an amount they have overpaid by way of CT or discharge of an amount that has been over-assessed, subject to restrictions. It also provides that the Commissioners are not liable to give relief except under this provision or any other provision relating to corporation tax.

18. New paragraph 51A sets out the cases in which the Commissioners will not be liable to give relief:

- case A is where the alleged overpayment arises from a mistake concerning a claim or election or notice or certain mistakes relating to capital allowances;
- case B is where the claimant can obtain relief by other means;
- case C is where the claimant could have obtained relief by another means when they first knew, or ought reasonably to have known of the overpayment;
- case D is where the grounds of the claim have already been considered by a court or tribunal, or considered by HMRC and settled by agreement between HMRC and the claimant, during the course of an appeal.
- case E is where the claimant knew or ought reasonably to have known the grounds at a time when the claimant could have brought the appeal before the tribunal or a court in due course;
- case F is where HMRC have taken proceedings to enforce payment of the amount; and
- case G deals with amounts that were understood to be due under the practice generally prevailing at the time the liability was computed.

19. New paragraph 51B sets a time limit for claims of four years from end of the accounting period in respect of which the payment or the assessment was made except where the claim relates to a mistake in a return. In that case, the time limit runs from the end of the accounting period for which the return was made. Claims are also to be made outside a company tax return.

20. New paragraph 51C provides that where A is required to pay tax on behalf of B under any enactment, a claim can only be made by B.

21. New paragraph 51D provides that a claim in respect of a mistake in a partnership return must be made by a partner nominated by all the relevant partners.

22. New paragraph 51E allows HMRC to make related discovery assessments or determinations where these would otherwise be out of time or prevented by paragraph 42 of Schedule 18 to FA 1998. If the assessment or determination depends on these provisions it must be made before the claim is finally determined.

23. New paragraph 51F similarly extends the circumstances in which an amendment to a partnership statement can be made.

24. New paragraph 51G extends claims to amounts paid under contract settlements. It allows HMRC to set any repayments against amounts payable under discovery assessments or through partnership amendments that are related to the claim.

25. Paragraph 15 of the Schedule inserts a new sub-paragraph (1A) into paragraph 62 of Schedule 18 to FA 1998 to provide that a claim is relevant to an amendment or discovery assessment if it relates to the same accounting period.

26. Paragraph 16 inserts a new sub-paragraph (8) into paragraph 88 of Schedule 18 to FA 1998 so that a company can make a claim where a mistake in its tax return for one accounting period leads to an additional amount being assessed in a later period.

BACKGROUND NOTE

27. Error or mistake relief is intended to provide a final opportunity for taxpayers to reclaim overpaid tax.

28. However, the current rules only apply to tax overpaid on assessments as a result of a relevant mistake in a return. The claim must be made within time limits. On receiving a claim, HMRC determine what amount is just and reasonable to repay and may take into account any liabilities that have not been assessed.

29. Claims under the new rules will apply to all overpayments of tax, ensuring there is a single route to obtain redress and that, as far as possible, disputes are dealt with through the tribunal.

30. A claim will be possible only if no other statutory steps are available to recover an overpayment when a person first becomes aware, or might reasonably be expected be aware, that they have overpaid.

31. The person must also have used any appeal rights that were available and the claim will have to be made within time limits.

32. The new rules also identify who can make a claim in respect of an overpaid amount. They enable the claimant to determine the amount to be repaid, subject to HMRC's right to enquire into the claim. There are detailed rules on how the amount to be repaid should be determined.

33. HMRC will be able to make an assessment to recover any directly related underpayments, rather than restricting the claim to take account of such liabilities.

SECTION 101 SCHEDULE 53: LATE PAYMENT INTEREST ON SUMS DUE TO HMRC

SUMMARY

1. Section 101 sets out the general proposition for applying late payment interest to any sum due under or by virtue of an enactment to HM Revenue & Customs (HMRC) but paid late. Schedule 53 sets out the special provisions concerning the amounts, start date and end dates for charging late payment interest as well as further provisions to clarify the effect of interest on certain reliefs.

DETAILS OF THE SECTION

2. Subsection (1) provides that the section applies to the late payment of any sums which are payable by a person to HMRC. The section is designed to cover those sums due to be paid to HMRC as imposed by statute, while excluding those sums paid to HMRC as an organisation (such as sums paid in respect of the provision of supplies or rent).

3. Subsection (2) provides for the exclusion of amounts of corporation tax and petroleum revenue tax. In addition this subsection provides a power for the Treasury to specify in an order those other payments which will not fall within the scope of this legislation.

4. Subsection (4) sets out the general rule for the late payment interest start date. This general rule is subject to the special provisions that follow.

5. Subsection (5) introduces Schedule 53 which caters for the exceptions where the general rule set out at subsection (4) where special provisions apply.

DETAILS OF THE SCHEDULE

6. Paragraph 1 provides that this provision applies where a person makes a claim to reduce their payments on account due under income tax self assessment and is then due to make a balancing payment. The paragraph is designed to reproduce the effect of the current law set out at section 86(4)-(6) of the Taxes Management Act 1970 (TMA).

7. Paragraph 1(1) provides for the conditions under which paragraph 1 applies.

8. Paragraph 1(2) sets out how to calculate the late payment interest in this situation and how much should be paid as a balancing payment.

9. Paragraph 1(3) sets out how to determine what amount if any is payable by the taxpayer.

10. Paragraph 2 deals with the application of late payment interest where payments on account of income tax are due from a person who is also entitled to a repayment of an overpayment.

11. Paragraph 2(1) states that paragraph 2 applies where payments on account are due from a taxpayer who is also entitled to a repayment of an overpayment.

12. Paragraph 2(2) provides for the amount of late payment interest that can be applied in the situation defined in paragraph 2(1).

13. Paragraph 2(3) sets out how to determine the size of the repayment if any, that is repayable.

14. Paragraphs 3(1) and (2) encompass such alterations to the tax liability after it has been initially established, and provide that the late payment interest start date in such cases is the date that would have applied if the assessment had been complete and accurate and made on time, and the amount had been due and payable as a result of the assessment.

15. Paragraph 3(3) provides further explanation of the words 'an assessment which ought to have been made' as used in this paragraph. This then provides clarity regarding the charging of interest where a person fails to notify HMRC of their liability to tax as required under section 7 of TMA.

16. Paragraph 4 provides the start date for late payment interest in respect of amounts postponed under section 55 of TMA (as specified).

17. Paragraph 5 provides the start date for late payment interest on an overpayment of tax recovered by virtue of an assessment under section 30 of TMA.

18. Paragraph 6 repeats the provisions of section 87A(5) of TMA relating to recovery of company tax credits or interest on such payments. The late payment interest start date on assessments made to recover such payments is the date when the payment of the tax credit or interest was made.

19. Paragraph 7 provides the late payment start dates for certain instalments of inheritance tax made under sections 227 and 229 of the Inheritance Tax Act 1984 (IHTA).

20. Paragraph 8 recreates the effect of section 236(2) of IHTA to ensure that where an amount of inheritance tax is underpaid as a result of an order made under the specified sections that late payment interest will not run until that order is made.

21. Paragraph 9 provides the start date for late payment interest in respect of amounts payable under section 147(4) of IHTA.

22. Paragraph 10 provides the date to start charging late payment interest in cases where VAT has been paid late as a consequence of a trader failing to register with HMRC for VAT purposes.

23. Paragraph 11 provides the date to start charging late payment interest where VAT has been charged on an invoice by a trader who has not registered with HMRC for VAT purposes and is subsequently recovered by HMRC.

24. Paragraph 12 legislates for the concessionary interest treatment currently applied where a taxpayer dies before payment of income tax is due (see Extra-statutory Concession A17).

25. Paragraph 12(1) describes the conditions that must apply for the rule set out in paragraph 12(2) to apply.

26. Paragraph 12(2) provides that such amounts do not carry interest from the date of death until the later of the normal late payment interest start date or the day after the end of the period of 30 days beginning with the grant of probate or letters of administration.

27. Paragraph 13 is designed to replicate the rules regarding the date to which late payment interest runs for those entities falling within the provisions of Chapter 15 of Part 15 of the Income Tax Act 2007 (ITA) (deposit takers, building societies and certain companies liable to deduct tax on behalf of others and pay it over to HMRC). The rules set out in this paragraph replace those currently set out at section 87 of TMA.

28. Paragraph 13(1) explains that this provision applies where tax was not paid when due by a deposit-taker, building societies and certain companies but was subsequently discharged or repaid because it was collected by deduction at source in a later period.

29. Paragraph 14 deals with acceptance of property in lieu of payment of inheritance tax. This paragraph states that late payment interest running in such cases will cease from the date when the property is valued.

30. Paragraph 15 restates elements of section 91 of TMA and provides that, where certain conditions are met, adjustments will be made to the amount of late payment interest payable, and if necessary, such sums will be repaid.

31. Paragraph 15(1) provides that, where certain conditions are met, adjustments will be made to the amount of late payment interest payable, and if necessary, such sums will be repaid.

32. Paragraphs 15(2) and (3) set out the conditions referred to in paragraph 15(1). These are that the interest must have arisen on sums due under income tax self assessment and that relief from tax has to be given by discharge.

33. Paragraph 16 permits a person receiving relief from tax by repayment of income tax to require it to be treated as a discharge of a qualifying charge to tax.

34. Paragraph 16(3) states that the repayment cannot be treated as a discharge of any assessment made after the relief was given, or as reducing without reducing to nil the tax charged in more than one assessment.

BACKGROUND NOTE

35. Section 101 is designed to apply a simple and consistent interest charge to late payments across all taxes and duties. Late payment interest will apply, for the majority of payments due to HMRC and made late, from the payment due date until the date that payment is received. The interest charged will be simple interest, and will not generally be deductible in computing profits or income.

36. The section sets out a general proposition for applying late payment interest to any sum due to HMRC but paid late. The formulation follows that used at section 127(1) of the Finance Act 2008 designed to facilitate recovery action for sums owed to HMRC.

37. Both corporation tax and petroleum revenue tax are excluded from the Finance Act 2009 legislation which does not currently accommodate either tax. The intention is to introduce parallel legislation for both taxes in Finance Act 2010.

38. This Schedule sets out the exceptions to the general rules set out in the section and how interest will operate in particular situations. These provisions cater for particular regime-specific rules. Although the aim is to harmonise the application of interest across taxes, some rules of this kind are necessary given the different structure and operation of the various taxes.

39. Part 1 of this Schedule sets out the amounts to which late payment interest will apply in particular circumstances. The first two paragraphs deal with claims to incorrectly reduce the payments on account due under the income tax self assessment system.

40. Part 2 sets out the situations where the late payment interest start date does not coincide with the date that the tax for the period or on the transaction is due for payment. The main situation where this applies is when a tax charge changes after it has been initially established, either due to amendment, correction or by some other method. The other situation where the late payment interest start date does not coincide with the date that the tax is due for payment is where HMRC brings tax into charge, usually by making an assessment where one has not already been made.

41. Part 3 sets out the situations where the late payment interest end date does not coincide with the date that the tax for the period or on the transaction is due for payment.

42. Part 4 restates elements of section 91 of TMA, defining how interest is to be treated in circumstances where the taxpayer qualifies for a relief. As well as defining the conditions that must be met for the taxpayer to qualify, the legislation sets out how any overpayments of late payment interest are to be repaid to the taxpayer.

SECTION 102 SCHEDULE 54: REPAYMENT INTEREST ON SUMS TO BE PAID BY HMRC

SUMMARY

1. Section 102 is designed to apply repayment interest on a simple and consistent basis to all overpayments of tax and Schedule 54 sets out some special rules regarding amounts carrying repayment interest.

DETAILS OF THE SECTION

2. Subsection (1) provides that the section applies to any sums which are payable to a person by HM Revenue & Customs (HMRC) under or by virtue of an enactment. The section is designed to cover those sums due to be paid by HMRC as imposed by statute, while excluding those sums paid by HMRC as an organisation (such as sums paid in respect of the provision of supplies or rent).

3. Subsection (2) provides that both corporation tax and petroleum revenue tax are excluded from this section. In addition, this subsection provides a power for HM Treasury to specify in an order those other repayments which will not fall within the scope of this legislation.

4. Subsection (3) states that amounts provided for by this section will carry interest at the 'repayment interest rate' from the 'start date' until the date HMRC make the payment or repayment.

5. Subsection (4) introduces Schedule 54.

6. Subsection (5) provides that repayment interest does not apply in circumstances whereby an amount is payable as a result of a court judgement or an order of a court.

7. Subsection (6) provides that repayment interest will not apply on repayment interest itself so maintaining the current position of repaying simple interest.

DETAILS OF THE SCHEDULE

8. Paragraph 1 states that this part sets out the general rule for determining the repayment interest start date, and that this rule is subject to the provisions of Part 2 of this Schedule.

9. Paragraph 2 state that where an amount has been paid to HMRC, the repayment interest start date is the later of the date when the amount now being repaid was paid to HMRC and the date the payment became due and payable where an amount has been paid in connection with a liability and is now to be repaid.

10. Paragraph 5 provides that for amounts not previously paid to HMRC but that are payable by HMRC as the result of a return being filed or a claim being made, the repayment interest start date is the later of the filing date for the return or the date the claim was required to be made (if any), or the date the return or claim was filed or made.

11. Paragraph 6 restates section 824(3)(b) of the Income and Corporation Taxes Act 1988 (ICTA) by providing that the repayment interest start date for repayments of income tax deducted at source for a year of assessment is 31 January next following that year.

12. Paragraph 7 sets the repayment interest start date at 31 January next following the year that is the later year in relation to the claim for certain claims to carry back loss relief and for the averaging of profits of farmers.

13. Paragraph 8 concerns the application of repayment interest in prescribed Mortgage Interest Relief at Source (MIRAS) cases and replaces section 824(3)(aa)(i) of ICTA.

14. Paragraph 9 concerns the application of repayment interest to repayments made as a result of a claim under section 228 of the Income Tax Act 1952 and is designed to replace section 824(2A) of ICTA.

15. Paragraph 10 recreates the effect of section 236(2) of the Inheritance Act 1984 (IHTA) to provide that where an amount of inheritance tax is overpaid as a result of an order made under the specified sections that repayment interest will run from when that order was made.

16. Paragraph 11 provides the repayment interest start date to be used where a claim is made under the prescribed sections.

17. Paragraph 12 provides the repayment interest start date where an amount is repayable under section 147(2) of IHTA.

18. Paragraph 13 is designed to replace section 824(4) of ICTA in so far as attributing repayment made in respect of income tax.

19. Paragraph 13(2) sets out how the repayment should be attributed to payments of tax.

20. Paragraph 13(3) sets out how the repayment should be attributed to instalment payments of income tax.

21. Paragraph 14 replaces section 824(4A) of ICTA and explains the meaning of income tax deducted at source for the purpose of this Schedule.

BACKGROUND NOTE

22. Section 102 is designed to apply repayment interest on a simple and consistent basis to all overpayments of tax. The section sets out the general rules for applying repayment interest on sums to be repaid by HMRC 'under or by virtue of an enactment'.

23. Both corporation tax and petroleum revenue tax are excluded from the Finance Act 2009 legislation which does not currently accommodate either tax. The intention is to introduce parallel legislation for both taxes in the Finance Act 2010.

24. Schedule 54 sets out the exceptions to the general rules set out in the section regarding repayment interest and covers how repayment interest will operate in particular situations. The provisions cover particular regime-specific rules. Although the aim is to harmonise the application of interest across taxes, some rules of this kind are necessary given the different structure and operation of the various taxes.

25. Part 1 of the Schedule sets out the general rule for applying late payment interest.

26. Part 2 sets out the specific rules to apply where the repayment interest start date does not follow the general rule.

27. Part 3 sets out how any repayment is to be apportioned for specific taxes and in specific circumstances. It goes on to give the definition for income tax deducted at source.

SECTION 103: RATES OF INTEREST

SUMMARY

1. Section 103 provides that the late payment and repayment rates of interest shall be specified in regulations made by HM Treasury.

DETAILS OF THE SECTION

2. Subsection (1) and (2) provide that the late payment and repayment interest rates will be set by regulations made by HM Treasury.

3. Subsection (3) provides a broad power to make regulations to set interest rates.

BACKGROUND NOTE

4. This section provides for regulations to be made that would establish a regime with a single rate of interest applied by HM Revenue & Customs (HMRC) on overpayments across all taxes, duties and penalties (other than repayments made as part of the corporation tax quarterly instalment payments regime). The regulations would also provide for a single rate of interest to apply late payments across all taxes, duties and penalties (other than payments made as part of the corporation tax quarterly instalment payments regime).

5. The section also provides the power to arrive at the prevailing rates of interest using formulae. The proposal is for HMRC to calculate interest by reference to the Bank of England base rate. Any rate changes would be made 13 working days after the Bank of England's Monetary Policy Committee make changes to the base rate.

6. This section also provides the power for regulations to be made that set different rates for different taxes, if appropriate. HMRC intends to apply separate rates to the corporation tax quarterly instalment payments regime.

SECTION 104: INTEREST: SUPPLEMENTARY

SUMMARY

1. Section 104 sets out the definition of the terms used in sections 100-102 and their associated Schedules and how the legislation would come into force.

DETAILS OF THE SECTION

2. Subsection (1) defines a number of terms used in these sections and Schedules.

3. Subsection (2) provides the definition for the date when an amount becomes due and payable.

4. Subsection (3) and (4) provide that the legislation will come into force on a day or days appointed by HM Treasury in an order made by them and that different commencement days may be used for different provisions or for different purposes.

5. Subsections (5) and (6) provide that HM Treasury may by order make any consequential, transitional and incidental changes to interest legislation as necessary. This may cover amendments necessary to ensure that the legislation is correctly implemented and provides continuity of cover for interest and includes a power to amend any primary or secondary legislation.

6. Subsection (8) specifies which orders and regulations are to be provided by statutory instrument.

7. Subsection (9) requires that any Statutory Instrument so made may be subject to annulment by the House of Commons (the negative procedure).

BACKGROUND NOTE

8. This section provides the full definition of all terms quoted throughout the legislation. In addition the section provides for any amendments, repeals or general changes which may need to be made, prescribing how and in which manner such changes can be made.

9. This section provides for the commencement of the new harmonised interest regimes by a series of orders over time, so providing for a phased introduction. This is particularly relevant for those taxes where interest is not currently applied. This will allow time to ensure that clear guidance is available for taxpayers and their advisors and that HM Revenue & Customs' staff are trained in the new rules so that effective advice can be given to taxpayers.

10. The section also provides for a definition of the process for introducing any orders and how and when any orders would be introduced or annulled.

SECTION 105: MISCELLANEOUS AMENDMENTS

SUMMARY

1. Section 105 sets out amendments to current legislation on interest charged and paid by HM Revenue & Customs (HMRC). The section provides the due date for income tax charged where relief under the Enterprise Investment Scheme (EIS) is withdrawn from a taxpayer. The section provides that the rate of interest paid on repayments of estate duty, capital transfer tax and inheritance tax (IHT) is the same as the rate paid for other taxes. It also clarifies the link between interest on repayments of IHT and the interest rate setting legislation in section 178 of the Finance Act (FA) 1989. Finally the section makes changes to existing interest rate setting provisions so that in future interest rates can change automatically.

DETAILS OF THE SECTION

2. Subsections (1) to (3) make amendments to section 239 of the Income Tax Act 2007 so that when relief under the EIS is withdrawn from the taxpayer, the due date for any income tax charged as a result is in line with the general date for income tax under section 59B of the Taxes Management Act 1970.

3. Subsection (4)(a) makes amendments to section 48(1) of FA 1975 so that the interest paid on repayments of estate duty will be paid at the applicable rate under section 178 of FA 1989.

4. Subsection (4)(b) makes amendments to section 235(1) of the Inheritance Tax Act 1984 so that the interest paid on repayments of IHT and capital transfer tax will be paid at the applicable rate prescribed under section 178 of FA 1989.

5. Subsection (5)(a) makes amendments to section 178(2) of FA 1989 so that the rate for interest paid on Estate Duty repayments is directly linked to the rate setting legislation.

6. Subsection (5)(b) makes amendments to section 178(2) of FA 1989 so that the rate for interest paid on IHT and its predecessor capital transfer tax is directly linked to the interest rate setting legislation.

7. Subsection (6) removes the requirement for HMRC to set interest rates by order for those taxes where interest is currently charged.

BACKGROUND NOTE

8. The EIS is designed to help smaller higher-risk trading companies to raise finance by offering a range of tax reliefs to investors who purchase new shares in those companies.

9. Subsections (1) to (3) remove an anomaly where the due dates for interest on any income tax due when relief under the EIS is withdrawn differed from the due date for income tax self assessment. Removing this anomaly is a step towards harmonising when interest becomes due across taxes.

10. Subsections (4) and (5) are designed to bring IHT, capital transfer tax and estate duty in line with all other taxes where HMRC charge and pay interest so that the new harmonised interest rates can be applied across all taxes.

11. Subsection (6) removes the requirement for HMRC to change interest rates by Order. This enables HMRC to set interest rates in line with changes announced by the Bank of England, offering greater transparency.

SECTION 106 AND SCHEDULE 55: PENALTIES FOR FAILURE TO MAKE RETURNS ETC

SUMMARY

1. Section 106 and Schedule 55 create a new penalty regime for late filing of tax returns for income tax, corporation tax (CT), Pay as you Earn (PAYE), National Insurance Contributions (NICs), the Construction Industry Scheme (CIS), stamp duty land tax (SDLT), stamp duty reserve tax (SDRT), inheritance tax (IHT), pension schemes and petroleum revenue tax (PRT). Taxpayers have a right of appeal against all penalties and no penalty can be charged if a taxpayer has a reasonable excuse for their failure. The section provides for the Schedule or parts of the Schedule to be bought into force by Treasury order.

DETAILS OF THE SECTION

2. Subsection (3) allows different provisions of the Schedule to be brought into force at different times.

3. Subsection (8) provides that a statutory instrument, which contains an order under subsection (4), which includes provision to amend or repeal primary legislation, is subject to the negative procedure (meaning the instrument takes effect on a specified future date but is subject to annulment in pursuance of a resolution of the House of Commons).

DETAILS OF THE SCHEDULE

4. Paragraph 1 specifies in a Table all the returns or documents required to be made or delivered by a person which, if not made or delivered to HM Revenue & Customs (HMRC) on or before the filing date, would result in that person being liable to a penalty.

5. Paragraph 1(3) provides for more than one penalty to be charged in respect of the same failure. Each penalty can be applied and pursued in isolation and a person has a right of appeal against each of them.

Amount of penalty: occasional returns and annual returns

6. Paragraph 2 details the returns to which an annual or occasional penalty applies.

7. Paragraph 3 provides that a failure to submit a return listed in paragraph 2 results in P becoming liable to a penalty of £100.

8. Paragraph 4(1) sets out the conditions for charging daily penalties where the delay in filing a return is prolonged.

9. Paragraph 4(2) provides for a penalty of £10 for each day that the failure to submit a return continues for a period of up to 90 days beginning with the date specified in the notice under paragraph 4(1).

10. Paragraph 4(3) provides for the date specified in the notice from which the penalty is payable to be earlier than the date on which the notice is given. This is because HMRC will be unaware of certain returns for taxes such as SDLT and IHT until they are received. The date specified in the notice may not be earlier than the end of the period of three months after the filing date.

11. Paragraph 5(1) provides for a penalty to be payable if a return is still outstanding six months after the filing date and there would have been a liability to tax shown in the return.

12. Paragraph 5(2) provides for that penalty to be the greater of £300 or 5 per cent of the liability to tax shown in the return.

13. Paragraph 6(1) provides for a penalty to be payable if a return is still outstanding 12 months after the filing date and there would have been a liability to tax shown in the return.

14. Paragraph 6(2) provides for the details of a penalty to be payable where, by failing to make the return, a person withholds information which would enable or assist HMRC to assess the person's liability to tax:

15. Paragraph 6(3) states that in any other case, the penalty is to be the greater of £300 or 5 per cent of the liability shown in the return.

Amount of penalty: CIS returns

16. Paragraph 7 states that the following paragraphs, which provide for a penalty, apply only for CIS returns.

17. Paragraph 8 provides for a penalty of £100 if the taxpayer fails to submit a return by the due date.

18. Paragraph 9 provides for a penalty of £200 if the failure continues after the end of a period of two months beginning with the penalty date.

19. Paragraph 10 provides for a penalty of the greater of £300 or 5 per cent of the liability to make payments which would have been shown on the return if the failure continues after the end of the period of six months beginning with the penalty date and there would have been a liability to make payments to HMRC shown in the return in question.

20. Paragraph 11 provides for an additional penalty if the failure continues after the end of the period of 12 months beginning with the penalty date and there would have been a liability to make payments to HMRC shown in the return in question.

21. Paragraph 11(2) provides for higher penalties where by failing to make the return, the taxpayer withholds information, which would enable or assist HMRC to assess the amount of CIS deductions that the taxpayer is liable to pay.

22. Paragraph 11(5) states that in any other case, the penalty, if the failure continues after the end of the period of 12 months beginning with the penalty date, is the greater of £300 or 5 per cent of the liability to make payments which would have been shown on the return in question.

23. Paragraph 13 provides for fixed-sum penalties arising from late filing a CIS return to be capped to £3,000 where the person has failed to make a first CIS return by the due date.

Reductions for disclosure

24. Paragraphs 14 and 15 provide details of reductions for disclosure in penalties under paragraphs 6, 11(3) or 11(4) where the taxpayer discloses relevant information, which has been withheld by a failure to make a return.

25. Paragraph 14(2) defines what is meant by disclosure of relevant information. It sets out three distinct elements, all of which are required for the maximum reduction: admission – telling HMRC that information has been withheld; taking active steps – giving HMRC reasonable help in assessing any tax unpaid as a result of the information being withheld; and access – allowing HMRC access to records to check the extent of any liability.

26. Paragraph 14(3) sets out two types of disclosure: unprompted – where the taxpayer has no reason to believe that HMRC have discovered or are about to discover the relevant information; prompted – all other disclosures.

27. Paragraph 14(4) defines the quality of disclosure in terms of timing (how promptly the disclosure was made), nature (the level of evidence provided and degree of access to test the disclosure) and extent (how complete the disclosure may be).

28. Paragraph 15 describes how the penalties must be reduced, depending upon the quality of the disclosure.

29. Paragraph 15(5) states that HMRC must not reduce the penalty under this paragraph to below the minimum amount set under paragraph 14.

Special reduction

30. Paragraph 16(1) gives HMRC a power to reduce any penalty under the Schedule including the minimum amount penalty where they think it right because of special circumstances.

Interaction with other penalties and late payment surcharges

31. Paragraph 17 sets out to what penalties HMRC should charge if a taxpayer is liable to more than one penalty which is determined by reference to the same tax liability (which could for example include late payment surcharges, penalties for incorrect returns etc), subject to some exclusions set out in paragraph 18(2). Paragraph 18 states that where a taxpayer is liable to a penalty under this Schedule, it is to be reduced by the amount of any other penalty incurred by P that is determined by reference to the same tax liability.

32. Paragraph 17(3) states that tax-geared penalties under this schedule may not exceed 100 per cent of the relevant liability to tax.

Assessment

33. Paragraph 18 sets out the mechanisms by which HMRC must assess, notify and enforce penalties which are to follow the same procedures as for assessments to tax. All penalties must be paid before the end of the period of 30 days beginning with the day on which the notification of the penalty is issued.

34. Paragraph 19 states that the assessment of any penalty under this Schedule must be made on or before the later of two dates. The first date is the last day of the two year period beginning with the filing date. The second date is the last day of the period of 12 months beginning with the end of the appeal period for the assessment of the amount of tax shown on the return, or, where there is no such assessment, the date on which the amount of tax is ascertained.

Appeal

35. Paragraph 20 provides appeal rights against decisions by HMRC to impose a penalty and of the amount of the penalty.

36. Paragraph 21(2) provides that a person is not required to pay a penalty before an appeal against the assessment of the penalty is determined.

37. Paragraph 22(3) provides that, if the tribunal substitutes its decision for HMRC's, then it may rely on paragraph 17 (special reduction) to the same extent as HMRC or to a different extent to HMRC only if the tribunal thinks HMRC's decision in relation to paragraph 17 is flawed. Flawed is defined in paragraph 23(4) as meaning in light of the principles applicable in proceedings for judicial review.

Reasonable excuse

38. Paragraph 23(1) provides that no penalty arises in relation to any failure under this Schedule if the person satisfies HMRC or (on appeal) the tribunal that there is a reasonable excuse for the failure.

39. Paragraph 23(2) contains provisions about what is precluded from being a reasonable excuse.

Determination of penalty geared to tax liability where no return made

40. Paragraph 24(1) provides that a liability to tax that would have been shown in a return means an amount that, if a complete and accurate return had been delivered on the filing date would have been shown as due or payable by the taxpayer.

BACKGROUND NOTE

41. These provisions bring in an aligned system of deterrents and safeguards for failing to comply with some filing obligations, with a view to incorporating the remaining filing obligations next year for the taxes and duties administered by HMRC. Implementation will be staged over the next few years, and the provisions will be brought into effect by Treasury Orders. Necessary repeals of and amendments to legislation will be given effect through the order when appropriate.

42. This measure was the subject of initial consultation in June 2008 and further consultation in November 2008, when draft legislation was also published. A response document together with a final Impact Assessment was published in April 2009.

SECTION 107 AND SCHEDULE 56: PENALTY FOR FAILURE TO MAKE PAYMENTS ON TIME

SUMMARY

1. Section 107 and Schedule 56 create a new penalty regime for late payment of the following taxes: income tax, corporation tax (CT), Pay as you Earn (PAYE), National Insurance Contributions (NICs) the Construction Industry Scheme (CIS), stamp duty land tax (SDLT), stamp duty reserve tax (SDRT), inheritance tax (IHT), pension schemes and petroleum revenue tax. Taxpayers have a right of appeal against all penalties and no penalty can be charged if a taxpayer has a reasonable excuse for their failure. The Schedule provides that if a taxpayer enters into a time to pay arrangement with HM Revenue & Customs (HMRC), any late payment penalties that they would become liable to after the agreement is reached will be removed if the taxpayer meets the terms of the agreement. The section provides for the Schedule or parts of the Schedule to be brought into force by Treasury order.

DETAILS OF THE SECTION

2. Subsection (3) allows different provisions of the Schedule to be brought into force at different times.

3. Subsection (8) provides that a statutory instrument, which contains an order under subsection (4), which includes provision to amend or repeal primary legislation, is subject to the negative procedure (meaning the instrument takes effect on a specified future date but is subject to annulment in pursuance of a resolution of the House of Commons).

DETAILS OF THE SCHEDULE

Penalty for failure to pay tax

4. Paragraph 1(1) introduces the Table setting out the amounts of tax to which the new penalty provisions apply and the date after which the penalty will be incurred. The Table defines the penalty date both for principal amounts of tax and amounts that might become due as the result of an assessment or determination of an amount of tax by HMRC, or by a correction to a return by HMRC or a taxpayer. It states that if a taxpayer fails to pay an amount of tax in column 3 of the Table by the date specified in column 4 of the Table, the taxpayer will be liable to a penalty under the Schedule.

5. Paragraph 1(3) states that a person may be liable to more than one penalty in the Schedule.

Amount of penalty for failure to pay annual or occasional amounts

6. Paragraph 3(1) defines the taxes to which this penalty model applies by referring to items in the Table.

7. Paragraph 3(2) provides that a person is liable to a penalty of 5 per cent of the amount of tax unpaid. This penalty is incurred if a taxpayer fails to pay the tax in full by the date provided for in column 4 of the Table. This date is normally 30 days after the due date for the tax.

8. Paragraph 3(3) states that any person who has tax unpaid five months after the penalty date is liable to an additional penalty of 5 per cent of the remaining unpaid tax.

9. Paragraph 3(4) states that any person who has tax unpaid eleven months after the penalty date is liable to an additional penalty of 5 per cent of the remaining unpaid tax.

10. Paragraph 4(1) applies the provisions of this paragraph to CT, whether payable under the Quarterly Instalment Payments scheme or not. Separate provisions are required for CT as the penalty dates are different. The first penalty date for CT is the day after the filing date for the CT return rather than the day after the due date for the tax, which is usually three months earlier.

11. Paragraph 4(2) states that any person who has tax unpaid the day after the filing date for CT is liable to a penalty of 5 per cent of the amount unpaid.

12. Paragraph 4(3) states that any person who has tax unpaid three months after the penalty date is liable to an additional penalty of 5 per cent of the remaining unpaid tax.

13. Paragraph 4(4) states that any person who has tax unpaid nine months after the penalty date is liable to an additional penalty of 5 per cent of the remaining unpaid tax.

Amount of penalty for failure to pay PAYE & CIS amounts

14. Paragraph 5 applies paragraphs 6 to 8 (the penalty structure) to payments of tax under the PAYE or CIS regulations, except where HMRC has allowed or directed that the relevant period last six months (or more).

15. Paragraph 6(1) provides that a person is liable to a penalty of an amount determined by reference to the number of defaults of payments made of the same tax during the tax year. A default is defined in paragraph 6(2) as a failure to pay an amount of tax in full by the due date.

16. Paragraph 6(3) states that the first failure to pay an amount of tax due by its due date during a tax year does not count as a default.

17. Paragraph 6(4) provides that, where a person has one, two, or three defaults in a tax year, the taxpayer is liable to a penalty of 1 per cent of the total amount of those defaults.

18. Paragraph 6(5) provides that, where a person has four, five or six defaults in a tax year, a penalty of 2 per cent of the total of the defaults arises.

19. Paragraph 7 provides for a penalty of 5 per cent of the unpaid tax where the tax is unpaid six months after the penalty date.

20. Paragraph 8 provides for a penalty of an additional 5 per cent of the unpaid tax where the tax is unpaid 12 months after the penalty date.

Special reduction

21. Paragraph 9(1) provides for a reduction in penalty where there are special circumstances.

Suspension of penalty during currency of agreement for deferred payment

22. Paragraph 10(1) sets out the circumstances in which this paragraph will apply.

23. Paragraph 10(2) removes liability for penalties under this Schedule from the date a request for deferral is received until the end of the deferral period.

24. Paragraph 10(3) provides that if the taxpayer breaks the agreement (as defined in sub-paragraph 4) and HMRC serves a notice specifying to which penalties they would become liable, they become liable to that penalty from the date of the notice. This provision effectively enables HMRC on issue of a notice to reinstate a liability that has been removed under paragraph 10(2).

25. Paragraph 10(5) applies the paragraph if the agreement between HMRC and the taxpayer is varied. This means that if an agreement is extended, paragraph 10(2) applies to remove any liability to a penalty for the extended agreement period.

Assessment

26. Paragraph 11 sets out the mechanisms whereby HMRC can assess, notify and enforce penalties, which are to follow the same procedures as for assessments to tax.

27. Paragraphs 11(4) and (5) allow HMRC to make supplementary assessments where an earlier assessment was made by reference to an underestimate of the amount of tax or for PAYE and CIS penalties, if a taxpayer makes additional defaults in year.

28. Paragraph 12 sets the time limit by which an assessment of any penalty must be made.

29. Paragraph 12(1) states that the assessment must be made on or before the later of two dates. The first date is the last day of the period of two years beginning with the date specified in column 4 of the Table. The second date is the last day of the period of 12 months beginning with the end of the appeal period for the assessment of the amount of tax in respect of which the penalty is assessed, or if there is no such assessment the date on which the amount of tax is ascertained.

Appeal

30. Paragraph 13 provides appeal rights against decisions by HMRC to impose a penalty and of the amount of the penalty.

31. Paragraph 14 (2) states that sub-paragraph (1) does not operate to require a taxpayer to pay any penalty before an appeal against the assessment of the penalty is determined.

32. Paragraph 15 (3) provides that, if the tribunal substitutes its decision for HMRC's, then it may rely on paragraph 9 (special reduction) to the same extent as HMRC, or to a different extent to HMRC only if the tribunal thinks HMRC's decision in relation to paragraph 9 is flawed. Flawed is defined in paragraph 15(4) as meaning in light of the principles applicable in proceedings for judicial review.

Reasonable excuse

33. Paragraph 16(1) provides that no penalty arises in relation to any failure under this Schedule if the person satisfied HMRC or (on appeal) tribunal that there is a reasonable excuse for the failure.

34. Paragraph 16(2) contains provisions about what is precluded from being a reasonable excuse.

BACKGROUND NOTE

35. These provisions bring in an aligned system of deterrents and safeguards for failing to comply with some tax payment obligations, with a view to incorporating the remaining tax payment obligations next year for the taxes and duties administered by HMRC. Implementation will be staged over the next few years, and the provisions will be brought into effect by Treasury Orders. Necessary repeals of and amendments to legislation will be given effect through the order when appropriate.

36. This measure was the subject of initial consultation in June 2008 and further consultation in November 2008, when draft legislation was also published. A response document together with a final Impact Assessment was published in April 2009.

SECTION 108: SUSPENSION OF PENALTIES DURING CURRENCY OF AGREEMENT FOR DEFERRED PAYMENT

SUMMARY

1. Section 108 provides that taxpayers who enter into agreements with HM Revenue & Customs (HMRC) to defer payment of taxes are not liable to certain surcharges or penalties that would otherwise be due because of late payment. The section includes a power to impose the surcharge or penalty if the taxpayer does not keep to the terms of the agreement. The change becomes effective for deferral agreements reached on or after 24 November 2008.

DETAILS OF THE SECTION

2. Subsection (1) sets out the circumstances in which the section will apply.

3. Subsection (2) removes liability for the penalties and surcharges listed in subsection (5) from the date a request for deferral is received until the end of the deferral period.

4. Subsection (3) provides for HMRC to impose the suspended penalty on service of a notice, if the terms of the deferral agreement are breached.

5. Subsection (4) sets out the ways in which a deferral agreement can be breached.

6. Subsection (5) sets out the penalties and surcharges to which this section applies.

7. Subsection (6) provides that where a deferral agreement is varied by agreement between HMRC and the taxpayer, this section applies to any agreement as varied.

8. Subsections (7), (8) and (9) provide that HM Treasury may by Order add or remove taxes and penalties from subsection (5) by negative resolution statutory instrument in the House of Commons.

BACKGROUND NOTE

9. In many of the taxes administered by HMRC, failure to make a payment in full by the date it is due can result in the taxpayer becoming liable to a late payment penalty or surcharge. This is to encourage taxpayers to fulfil their obligations and to reassure those who pay on time that they are not disadvantaged by those who do not. The way in which such penalties and surcharges work varies for different taxes.

10. In the Pre-Budget Report of November 2008, a new Business Support Package was announced. As part of this package, it was announced that HMRC would not impose penalties or surcharges for late payments of tax in cases where the taxpayer approached them to discuss payment problems before the penalty or surcharge became due and an agreement to defer payment was reached.

11. HMRC have operated this system since November 2008 using their administrative powers. This section is intended to remove liability for penalties and surcharges for late payment of taxes when the taxpayer makes representations to HMRC to pay the tax over an extended period. These representations must be made before the penalty or surcharge becomes due and an agreement to pay over time must be reached.

12. If the taxpayer enters into an agreement to defer payment of an amount of tax, but then does not meet all of the terms of the agreement or make all of the agreed payments, the section permits HMRC to impose the penalty suspended under the arrangement, at their discretion.

13. The section is effective for tax deferral agreements reached on or after 24 November 2008.

SECTION 109 AND SCHEDULE 57: AMENDMENTS RELATING TO PENALTIES

SUMMARY

1. Section 109 and Schedule 57 make amendments to the provisions in Schedule 24 to Finance Act (FA) 2007 (penalties for errors) and Schedule 41 to FA 2008 (penalties for failure to notify and certain other wrongdoing). It also makes certain related changes.

DETAILS OF THE SECTION

2. The section introduces the Schedule. There is no requirement for an order to appoint a day for commencement.

DETAILS OF THE SCHEDULE

3. Paragraph 2 clarifies that the term under-assessment includes a reference to under-determination.

4. Paragraph 3 provides that only relief under section 419 of the Income and Corporation Taxes Act 1988 that is deferred under section 419(4A) of that section is to be ignored for the purposes of calculating "potential lost revenue".

5. Paragraph 5 provides that references to assessment in Part 3 of Schedule 24 to FA 2007 are references to a determination for the purposes of inheritance tax and stamp duty reserve tax.

6. Paragraph 6 provides that it is not necessary for a person to pay the penalty under Schedule 24 to FA 2007 in order for an appeal to be heard.

7. Paragraph 7 clarifies the definition of an officer of the company for the purposes of attributing liability for a penalty.

8. Paragraph 11 provides that it is not necessary for a person to pay the penalty under Schedule 41 to FA 2008 in order for an appeal to be heard.

9. Paragraph 12 clarifies the definition of an officer of the company for the purposes of attributing liability for a penalty.

10. Paragraph 13 disapplies the assessment provisions of the Taxes Management Act 1970 in relation to certain penalty provisions contained within Finance Acts 2007, 2008 and 2009.

BACKGROUND NOTE

11. This section and Schedule make certain necessary changes to provisions in previous Finance Acts to clarify the application of various penalty provisions.

SECTION 110 AND SCHEDULE 58: RECOVERY OF DEBTS UNDER PAYE REGULATIONS

SUMMARY

1. Section 110 and Schedule 58 provide for the Commissioners for HM Revenue & Customs (HMRC) to make regulations to collect debts owed to HMRC through the Pay as You Earn (PAYE) system.

DETAILS OF THE SCHEDULE

2. Paragraph (1) provides that section 684 of the Income Tax (Earnings and Pensions Act 2003 (ITEPA) is amended. Section 684 of ITEPA allows the Commissioners for HMRC to make regulations for the assessment, collection and recovery of tax under PAYE.

3. Paragraph (3) amends section 684 of ITEPA to allow the Commissioners to make regulations for deductions in respect of specified relevant debts, the circumstances in which deductions may be made and the time that any deductions are treated as paid.

4. Paragraph (4) provides that no more than £2,000 may be deducted in any year without the employee's consent. This amount may be changed by Treasury order.

5. Paragraph (6) provides that section 684 of ITEPA is amended to insert new subsections (7AA) and (7AB). New subsection (7AA) defines a relevant debt as a sum payable under or by virtue of an enactment other than an excluded debt, or one payable under a contract settlement. "Under or by virtue of an enactment" brings in those debts arising from taxes, duties etc imposed by statute. "Contract settlements" are contractual agreements made in connection with a person's liability, usually as the result of an enquiry covering a number of years.

6. New subsection (7AB) defines terms and expressions used in new subsection (7AA). The definition of "excluded debts" preserves the Commissioners' existing powers to make regulation for the collection of income tax or capital gains tax through PAYE in section 684 of ITEPA and for the collection of tax credits through PAYE in section 29(5) of the Tax Credits Act 2002.

7. Paragraph 10 allows the necessary consequential changes to ITEPA and other enactments to be made by Treasury order.

BACKGROUND NOTE

8. This section and Schedule give HMRC the power to collect small debts through the PAYE system, allowing debtors to spread payments and reducing HMRC's costs. Small debts account for a large proportion of the volume of tax debts but a small proportion of their value.

9. HMRC's aim is to secure immediate payment of debts in full or, where this is not possible, to set up a Time to Pay arrangement to reschedule the debt. If neither of these options are feasible, HMRC would consider collecting smaller debts through PAYE as one of a number of remedies available to it as a creditor. If the debtor did not want to pay in this way, HMRC would expect them to make other arrangements for payment. If no such arrangements were forthcoming, HMRC would have the ability to collect debts in this way at its option.

10. The right to object to collecting underpayments of income tax and capital gains tax under Self Assessment, where the due date had not already passed, would not be disturbed. The right to object to collecting tax credit overpayments in this way would also not be disturbed. A taxpayer would, as now, be able to appeal against their tax code. The existing safeguards, limiting the amount that may be collected in this way through the PAYE system and protecting the level of the taxpayer's income, would be preserved.

11. This measure was the subject of initial consultation in June 2007 and further consultation in December 2008 (*Payments, Repayments and Debt: the Next Stage*). A response document together with a final Impact Assessment was published in April 2009

SECTION 111: MANAGED PAYMENT PLANS

SUMMARY

1. Section 111 provides for HM Revenue & Customs (HMRC) to introduce managed payment plans.

2. Under these voluntary plans, taxpayers may pay income tax or corporation tax due under Self Assessment by instalments balanced equally before and after the normal due dates. While in the plan, taxpayers are protected from the interest and penalty consequences on payments made after the normal due date. The section applies throughout the United Kingdom.

DETAILS OF THE SECTION

3. Subsection (1) provides that managed payment plans are available in respect of income tax or corporation tax payments that must be made under Self Assessment. These are payments on account of income tax payable in accordance with section 59A of the Taxes Management Act 1970 (TMA); payments of income tax and capital gains tax payable in accordance with section 59B of TMA; and payments of corporation tax payable in accordance with section 59D of TMA. The scope of section 59D of TMA excludes those large companies which are subject to the quarterly instalment payment scheme.

4. Subsection (2) provides that a number of conditions must be satisfied prior to entering into a managed payment plan. Subsection (2)(c) allows the Commissioners for HMRC to apply further conditions.

5. Subsection (3) provides that managed payment plans are not available to companies which have entered into a group payment arrangement.

6. Subsection (4) provides that so long as the taxpayer pays the instalments in accordance with the plan, each instalment is treated as having been paid on the normal due date. This means that there will be no late payment interest or penalties on those agreed instalments that are paid after the normal due date.

7. Subsection (5) provides that if the taxpayer fails to pay an agreed instalment, those payments made up to the date of failure are still treated as paid on the normal due date. Later payments are outside the scope of the section and, from the date of the failure, will attract late payment interest and penalties as appropriate. Late payment interest will run from the normal due date and late payment penalties will run from the penalty date.

8. Subsection (6) provides that companies that do not pay the agreed instalments still benefit from credit interest, but only where the failure arises before the normal due date.

9. Subsection (7) provides that an officer of Revenue and Customs may notify the payer that payments made after the due date will not result in a penalty.

10. Subsection (8) provides that instalments paid before the due date are balanced by instalments paid afterwards if their time values as defined in subsection (10) are equal, or approximately equal.

11. Subsection (9) provides that the time value of instalments paid before and after the due date are aggregated for this purpose.

12. Subsection (10) provides that the time value of any particular instalment is the product of its amount and the period in days before or after the due date.

BACKGROUND NOTE

13. Some taxpayers find it difficult to pay their tax liabilities, particularly those with annual or twice yearly payment dates. Consultation and research have indicated that small businesses in particular would like a more flexible system that allows them to make smaller and more frequent tax payments than at present, which could help them better manage their cash flow.

14. HMRC supports those in temporary financial difficulty once a sum has become due through its Business Payment Support Service. It also offers a range of methods for payment in advance, including income tax budget payment plans and certificates of tax deposit.

15. Managed payment plans would allow taxpayers to spread their payments either side of the normal due date for payment of the tax, so long as those made in arrears are balanced by those made in advance. Entry to the plan will be voluntary.

16. While in the plan, taxpayers will not have to pay interest and penalties on instalments made after the normal due date. If they fail to make the agreed payments they fall out of the plan and the normal consequences for late payment will follow for the amounts unpaid at the date of the failure. However, taxpayers who fail to make the payments, but who remain in contact with HMRC about their debt, may be relieved from penalties that would otherwise arise. This is in line with HMRC's Time to Pay arrangements to reschedule debt.

17. While it is expected that the details of any managed payment plan will be set out in the terms under which they are made available, HMRC may if appropriate specify these in regulations.

18. This measure was the subject of initial consultation in June 2007 and further consultation in December 2008 (*Payments, Repayments and Debt: the Next Stage.*) Draft legislation was published for consultation in January 2009, and a response document and a final Impact Assessment in April 2009.

SECTION 112: CUSTOMS AND ENFORCEMENT POWERS: MOVEMENTS BETWEEN MEMBER STATES

SUMMARY

1. Section 112 amends section 4 of the Finance (No. 2) Act (F(No.2)A) 1992 to ensure that, in appropriate circumstances, officers of HM Revenue & Customs (HMRC) can use their powers to check whether or not a movement is between Member States. It will also make a textual change to clarify the circumstances in which officers can use their powers to conduct selective and proportionate checks on EU travellers for drugs and other prohibited goods.

DETAILS OF THE SECTION

2. Subsections (2) and (3) insert a new subsection 1A into section 4 of F(No.2)A 1992, which allows the exercise of powers in order to ascertain whether a movement is in fact between Member States.

3. Subsection (4) makes a drafting amendment to subsection (2) to clarify that the precondition for exercising powers for purposes listed in subsections 2(a) to (c) is where it is necessary to exercise such a power.

BACKGROUND NOTE

4. Section 4 of F(No.2)A 1992 limits the use of certain powers in the Customs and Excise Management Act 1979 (CEMA) in relation to movements between Member States. But the section provides two exceptions to that limitation. The first is where there are reasonable grounds for believing that the movement in question is not in fact between Member States. The second is where it is necessary to exercise the power for purposes connected with the collection of Community customs duties or the enforcement of any import prohibition or restriction.

5. The effect of this amendment is that an officer of HMRC will no longer need reasonable grounds for believing that a passenger has come from outside the EU in order to exercise the specified customs powers. This is necessary because at large international airports passengers from several flights mix airside before reaching customs. The amendment will permit officers to conduct limited checks such as questioning the traveller and inspecting their travel documents in order to ascertain whether they are EU travellers or not.

6. Another effect of this section is to amend the drafting of section 4 to clarify that officers do not need reasonable grounds for believing that it is necessary to exercise the relevant CEMA power before being able to do so for purposes connected with the collection of Community customs duties or the enforcement of any import prohibition or restriction. The section will now provide that the powers can be exercised where it is necessary to do so, as opposed to where there are reasonable grounds for believing that it is necessary to do so.

7. All checks on EU travellers are carried out in a selective and proportionate manner, and therefore will not interfere with an EU passenger's free movement rights.

SECTION 113: VAT EXEMPTION FOR GAMING PARTICIPATION FEES

SUMMARY

1. Section 113 amends Group 4 of Schedule 9 to the Value Added Tax Act 1994 to exempt from VAT all participation fees for playing bingo and other games of chance for a prize. The section also makes consequential repeals.

DETAILS OF THE SECTION

2. Subsection (2) removes Note (1)(b) to Group 4, which was the basis of taxation for participation fees.

3. Subsection (3) removes Notes (5) to (11) from Group 4. These notes are now unnecessary, because they listed various categories of exceptions to the taxation of participation fees.

4. Subsection (4) revokes the Value Added Tax (Betting, Gaming and Lotteries) Order 2007 (S.I. 2007/2163). This Order updated the law on participation fees in the light of the Gambling Act 2005.

5. Subsection (5) removes sections 19(3)(b) and 26E(2) of the Betting and Gaming Duties Act 1981, and section 11(9)(a) of the Finance Act 1997. These sections are now unnecessary as they required the VAT element of participation fees to be ignored for the purposes of calculating bingo duty, remote gaming duty and gaming duty respectively.

BACKGROUND NOTE

6. Gambling is in principle exempt from VAT under EU law, although Member States have discretion as to the scope of the exemption they apply. In the UK, betting, gaming and lotteries are generally exempt from VAT under Group 4 of Schedule 9 to the VAT Act. However, Note 1(b) to Group 4 excluded from the exemption "the granting of a right to play a game of chance for a prize unless the playing of the game is excepted from this paragraph by Note (5)". This in effect taxed participation fees for playing bingo and other games of chance, apart from certain exceptions for remote gaming and various categories of small scale gaming specifically listed in the law. (Participation fees are charges that a gaming operator makes to customers for participating in gaming. They may take the form of a fixed fee or a percentage of any stakes kept by the operator.)

7. The effect of the amendments in this section is to exempt from VAT all participation fees for gaming.

SECTION 114: GAMING DUTY

SUMMARY

1. Section 114 makes provision for gaming duty to be extended to apply to equal chance gaming, subject to specified exceptions. It also removes the requirement to list individual games for the purposes of gaming duty and gives the Treasury powers to add or remove specified games from the scope of gaming duty by order.

DETAILS OF THE SECTION

2. Subsection (3) substitutes a new definition of dutiable gaming in section 10(2) of the Finance Act (FA) 1997.

3. Subsection (4) exempts from duty any gaming which takes place in accordance with Article 77 of the Betting, Gaming, Lotteries and Amusements (Northern Ireland) Order 1985 (gaming for prizes on bingo club premises).

4. Subsection (5) inserts a new subsection (3AA) into section 10 of FA 1997 which exempts gaming in respect of which bingo duty or lottery duty is chargeable or would be chargeable but for an express exception.

5. Subsection (6) ensures all non-commercial equal chance gaming permitted under section 300 of the Gambling Act 2005 is exempted.

6. Subsection (7) exempts equal chance gaming which takes place in accordance with section 269 of the Gambling Act 2005 or to which Article 128 of the Betting, Gaming, Lotteries and Amusements (Northern Ireland) Order 1985 applies.

7. Subsection (8) amends section 10(5) to give the Treasury powers to provide that any specified game is or is not a casino game or equal chance gaming for the purposes of gaming duty.

8. Subsection (9) provides that a reference made to a game in an order made under section 10(5) shall be taken to include a reference to any game which is essentially similar to that game.

9. Subsections (10), (11) and (12) set out the legislative process by which Treasury orders to include or exclude specified games from the scope of gaming duty shall be made.

10. Subsections (13), (14) and (15) insert definitions of ‘casino games’ and ‘equal chance gaming’ into section 15(3).

11. Subsection (16) removes redundant references to gaming duty in section 11 of Finance Act 2002 and paragraph 17(4) of Schedule 25 to Finance Act 2007.

BACKGROUND NOTE

12. Gaming duty currently applies to gaming by way of the non-equal chance games specified in section 10(2) of FA 2007 and games that are essentially similar. This section has the effect of extending the scope of dutiable gaming to include equal chance gaming (games where players play against each other rather than against the house e.g. poker). It also replaces the current list of dutiable non-equal chance casino games with a generic description of such games, which removes the requirement for secondary legislation whenever new games are introduced.

13. The section also gives the Treasury powers to add or remove specified casino games or equal chance gaming from the scope of gaming duty by order.

SECTION 115: REMOTE BINGO ETC

SUMMARY

1. Section 115 makes provision for remote gaming duty to be charged on the provision of facilities for remote bingo and removes the playing of remote bingo, other than premises-based licensed bingo, from the scope of bingo duty. These changes will apply to games of bingo starting on or after 1 July 2009.

DETAILS OF THE SECTION

2. Subsection (2) of the section amends section 17 of the Betting and Gaming Duties Act 1981 (BGDA), which sets out the charge to bingo duty, by inserting a new subsection (2A) so that bingo duty is not charged on the playing of bingo if it is not licensed bingo and remote gaming duty is charged on the provision of facilities for playing it.

3. Subsection (3) amends section 26H (exemptions to remote gaming duty) by inserting a new subsection (2A) so that the provision of facilities for remote bingo, other than licensed bingo, is not exempted from remote gaming duty.

BACKGROUND NOTE

4. Bingo duty is currently chargeable on the playing of bingo in the UK, unless specifically exempted, and applies to any version of the game of bingo, whatever name it is called.

5. Remote gaming duty is chargeable on the provision of facilities for remote gaming (i.e. gaming in which players participate by the use of digital communication media such as the internet, interactive TV or telephone) but excludes any gaming which is charged with, or specifically excluded from another gambling duty. It therefore excludes remote bingo played in the UK, which falls within the scope of bingo duty.

6. The effect of the current legislation is that the duty treatment of remote bingo varies according to where the bingo is played. In addition, remote bingo played in the UK in a domestic environment is exempted from bingo duty under the provisions of Part 1 of Schedule 3 to BGDA so in practice is not chargeable with either bingo duty or remote gaming duty.

7. The section removes these inconsistencies in the treatment of remote bingo by bringing all remote bingo, except licensed bingo, within the scope of remote gaming duty. Licensed bingo refers to bingo played on licensed premises within the meaning of section 20C(2).

SECTION 116: MEANING OF "GAMING MACHINE" AND "GAMING"

SUMMARY

1. Section 116 provides for the definition of "gaming machine" and "gaming" for the purposes of the Betting and Gaming Duties Act 1981 to be set out in that Act.

DETAILS OF THE SECTION

2. Subsection (3) substitutes the meaning of "gaming machine" contained in section 25(1A) of the Betting and Gaming Duties Act 1981 (BGDA) and introduces new subsections (1A) and (1B).

3. New subsection (1A) provides that such machines which can be used for purposes other than gambling may be covered by the definition of a gaming machine, as well as those designed or adapted for the purposes.

4. New subsection (1B) excludes from the definition of gaming machine those machines that are designed or adapted to bet on future real events, for playing bingo on which bingo duty is or would be charged but for specific duty exemptions, or for playing a real game of chance on which gaming duty is or would be charged but for specific gaming exemptions.

5. Subsection (5) amends section 25 of BGDA by inserting new subsections (5) and (6).

6. New subsection 5(a) provides that a reference to gambling is to gaming or betting.

7. New subsection (5)(b) provides that "machine" includes a machine powered mechanically, by electricity, or by both means.

8. New subsection (5)(c) provides that a reference to a machine being designed or adapted for a purpose includes any alterations made to a machine which can reasonably lead it to be expected to be used for that purpose.

9. New subsection (5)(d) provides that the installation of computer software on a machine constitutes being adapted.

10. New subsection (5)(e) provides that "real" means non-virtual.

11. New subsection (5)(f) provides that "game of chance" includes a game that involves both an element of chance and an element of skill, a game that involves an element of chance that can be eliminated by superlative skill and a game that is presented as involving an element of chance, but does not include a sport.

12. New subsection 5(g) provides that a reference to bingo includes any version of that game, regardless of what it is called.

13. New subsection (6) provides that the definition of gaming machine in section 25 of BGDA may be amended by Treasury order.

14. Subsection (6) of the section provides for the amendment of section 33(1) of BGDA (interpretation).

15. Subsection (6)(a) provides that in section 33(1) of BGDA, the definition of "gaming" is amended to remove the reference to the Value Added Tax Act 1994.

16. Subsection (6)(b) introduces a new subsection (1A) into section 33 of BGDA.

17. New subsection (1A)(a) provides that a reference to game of chance in subsection (1) when used in relation to gaming includes a game that involves both an element of chance and an element of skill, a game that involves an element of chance that can be eliminated by superlative skill and a game that is presented as involving an element of chance, but does not include a sport.

18. New subsection (1A)(b) provides that a reference to playing a game of chance in subsection (1) means participation in a game of chance whether or not there are other participants in the game and whether or not a computer generates images or data taken to represent the actions of other participants in the game.

19. New subsection (1A)(c) provides that a reference to prize does not include the opportunity to play the game again.

BACKGROUND NOTE

20. There are two elements to this section; the first concerns the definition of gaming machine, the second the definition of gaming. At present both expressions are defined for the purposes of BGDA by reference to definitions contained in the Value Added Tax Act 1994 which in turn rely to a substantial degree on social legislation contained in the Gambling Act 2005.

21. This section amends sections 25 and 33 of BGDA so that they include their own statutory definition of "gaming machine" and "gaming" without the need to cross refer to the VAT legislation.

22. The changes are being made to simplify and clarify the betting and gaming duties legislation.

SECTION 117: CLIMATE CHANGE LEVY: TAXABLE COMMODITIES INELIGIBLE FOR REDUCED-RATE SUPPLY

SUMMARY

1. Section 117 enables entitlement to claim the climate change levy (CCL) reduced rate to be restricted, by specifying in certificates given under the climate change agreement (CCA) scheme that certain taxable commodities will be ineligible for reduced rate supply.

DETAILS OF THE SECTION

2. Subsection (1) provides for Schedule 6 to the Finance Act (FA) 2000 to be amended.

3. Subsection (2) inserts new sub-paragraphs in paragraph 44 of Schedule 6 to FA 2000:

   - New sub-paragraph (2A) provides for the Secretary of State (in practice, for the Department of Energy and Climate Change) to:

     - give a new certificate or vary an existing certificate to make one or more taxable commodities ineligible for the reduced rate of climate change levy under the climate change agreement scheme; and

     - vary an existing certificate to allow such taxable commodities to be eligible for the reduced rate.

   - New sub-paragraph (2B) provides that a facility is not entitled to the reduced-rate on a taxable commodity if the commodity is described within a certificate as being ineligible for reduced-rate supply; and

   - New sub-paragraph (2C) provides that the Secretary of State can only include such provision in a certificate with the consent of HM Treasury and if the provision is in line with the stated EC State aid rules.

4. Subsection (3) makes consequential amendments to Schedule 6 to FA 2000.

BACKGROUND NOTE

5. CCL was introduced in 2001 and is a UK wide tax on the use of electricity, gas, solid fuel and liquefied gases used for fuel purposes by business and the public sector.

6. The purpose of the CCL is to encourage the efficient use of energy and the use of renewable energy, in order to help meet the UK's international and domestic targets for cutting emissions of greenhouse gases.

7. CCAs were introduced alongside the levy in recognition of the levy's impact on the competitiveness of energy-intensive sectors of industry. They are voluntary agreements made between the Department of Energy and Climate Change and sector associations and their members. The agreements entitle participating facilities to pay a reduced rate of levy in return for meeting challenging targets for improving energy efficiency or reducing emissions.

8. The CCA scheme is a State Aid. Under new Community Guidelines on State Aid for Environmental Protection issued in 2008, where beneficiaries of aids in the form of tax reductions pay less than the relevant Community minimum tax levels, they must satisfy the European Commission that the aid is necessary and proportionate. The CCL reduced rates for gas and solid fuel are below the minimum rates given out in the Energy Products Directive (Dir 2003/96 EC). Denying sectors that do not satisfy the necessity and proportionality tests entitlement to claim the reduced rate on those particular taxable commodities will ensure compliance with the State aid rules and enable the sectors to join the CCA scheme, though such sectors will be able to benefit from the reduced rate only on supplies of electricity and liquefied petroleum gases.

SECTION 118 SCHEDULE 59: REMOVAL OF REDUCED RATE WHERE TARGETS ARE NOT MET

SUMMARY

1. Section 118 provides for Schedule 59, which amends Schedule 6 to the Finance Act (FA) 2000, to provide for HM Revenue & Customs (HMRC) to recover climate change levy (CCL) where a facility in the climate change agreements (CCA) scheme does not meet the targets it has agreed with the Department of Energy and Climate Change (DECC). The recovery mechanism applies to certification periods under the CCA scheme beginning on or after 1 April 2009.

DETAILS OF THE SECTION

2. Subsection (1) introduces Schedule 59, and subsection (2) provides that the amendments made by the Schedule have effect where the certification period (under the CCA scheme) begins on or after 1 April 2009.

DETAILS OF THE SCHEDULE

3. Paragraph 1 inserts a new paragraph 45B into Schedule 6 to FA 2000 to provide:

- that the new paragraph applies to a facility in a CCA (sub-paragraph (1));
- for the Secretary of State (in practice, for DECC) to issue a certificate in cases of unsatisfactory performance against targets agreed by a facility signing a CCA (sub-paragraph (2));
- that the certificate must specify the facility, agreement, certification period, the target(s) and the progress made by the facility towards the target(s) (sub-paragraph (3));
- that, where a certificate is issued, taxable supplies are treated as not being reduced-rate supplies and an amount is payable as levy on the supplies (sub-paragraph (4));
- for calculating the amount payable on the taxable supplies (sub-paragraph (5));
- that the certificate must be sent to the Commissioners for HMRC and the operator of the facility (sub-paragraph (6));
- that a certificate may be issued after the end of the certification period (sub-paragraph (7));
- that the facility operator must not be required to pay the levy due under new paragraph 45B before the certificate is issued (sub-paragraph (8));
- that the levy due under the paragraph is additional to levy already due on the supply (sub-paragraph (9)); and
- for definitions of terms used in the new paragraph (sub-paragraph (10)).

4. Paragraphs 2 to 9 make consequential amendments to Schedule 6 to FA 2000.

BACKGROUND NOTE

5. CCL was introduced in 2001 and is a UK wide tax on the use of electricity, gas, solid fuel and liquefied gases used for fuel purposes by business and the public sector.

6. The purpose of the CCL is to encourage the efficient use of energy and the use of renewable energy, in order to help meet the UK's international and domestic targets for cutting emissions of greenhouse gases.

7. CCAs were introduced alongside the levy in recognition of the levy's impact on the competitiveness of energy-intensive sectors of industry. They are voluntary agreements made between the DECC and sector associations and their members. The agreements entitle participating facilities to pay a reduced rate of levy in return for meeting challenging targets for improving energy efficiency or reducing emissions.

8. The CCA scheme is a State Aid. A condition of the State Aid approval for the scheme in 2001 was that, for the last two years of the 10 year approval (1 April 2009 to 31 March 2011), the UK must introduce a mechanism to recover tax from facilities that fail to meet their targets during the period proportional to the extent that the targets were missed.

SECTION 119 SCHEDULE 60: LANDFILL TAX: PRESCRIBED LANDFILL SITE ACTIVITIES

SUMMARY

1. Section 119 provides for Schedule 60 which will enable HM Treasury to prescribe by order that a landfill site activity is subject to landfill tax, remove the power to make regulations to provide that landfill tax is not payable in respect of the temporary holding of material for certain purposes in designated areas and remove the exemption from landfill tax for site restoration. The Schedule will also provide that HM Revenue & Customs (HMRC) has access to information on the temporary holding of material at a landfill site and site restoration and enable the landfill tax return form to be prescribed in guidance rather than regulations.

DETAILS OF THE SCHEDULE

2. Paragraph 2 inserts a new section 65A into Finance Act (FA) 1996. The new section makes a number of provisions, including that:

- HM Treasury may prescribe by order that an activity on a landfill site is subject to landfill tax;
- an order may make any provision which HM Treasury thinks necessary or expedient in connection with the prescribing of landfill site activities;
- an order may prescribe a landfill site activity by reference to conditions; and
- an order may amend or otherwise modify part 3 of FA 1996 or any other enactment relating to landfill tax, apart from the rate at which landfill tax is charged.

3. Paragraph 3 inserts new subsections (7) (ca) and (cb) into section 71 of FA 1996 to provide that an order relating to the prescribing of landfill site activities, or an order amending part 3 of the FA 1996 or any other enactment relating to landfill tax, shall be laid before the House of Commons and, unless approved within 28 days, shall cease to have effect.

4. Paragraph 4 provides for the omission of section 62 of FA 1996 which confers the power to make regulations to provide that landfill tax is not payable in respect of the temporary holding of material for certain purposes in designated areas.

5. Paragraph 7 inserts a new paragraph 1A in Schedule 5 to FA 1996. It provides for Commissioners' of HMRC regulations that may make provision about giving information about material on a landfill site (or part of a landfill site) to HMRC. Regulations may require, or authorise HMRC to require, the designation of part of a landfill site as an "information area", that certain material is deposited in an information area and make provision about information relating to what is done with material.

6. Paragraph 9 inserts a new paragraph 2A in Schedule 5. It provides for regulations that may require the keeping of records relating to material at a landfill site (or part of a landfill site), including records about what is done with that material.

7. Paragraph 10 provides for the omission of section 43C of FA 1996 which provides for the exemption from landfill tax of material used for site restoration.

8. Paragraph 11 inserts a new paragraph 1B into part 1 of Schedule 5 of FA 1996. It provides that a landfill site operator must supply HMRC with certain information before commencing site restoration.

9. Paragraph 12 amends section 49 of FA 1996 so that the landfill tax return form shall be prescribed in such form as the Commissioners determine (and not necessarily by regulation).

10. Paragraph 13 provides that:

- paragraph 10 (repeal of section 43C) comes into force on 1 September 2009;
- paragraph 11 (information about site restoration) has effect in relation to the restoration of landfill sites commencing on or after 1 September 2009; and
- regulations made under section 62 of FA 1996 (which is repealed by paragraph 4) and the repealed part of section 49 of FA 1996 (see paragraph 12) will remain in force until they are revoked. The power to revoke any such regulations by statutory instrument is retained.

BACKGROUND NOTE

11. Landfill tax was introduced on 1 October 1996. It encourages waste producers and the waste management industry to switch to more sustainable alternatives to landfilling waste.

12. The provisions in Finance Act 2009 follow the judgment of the Court of Appeal in Commissioners for *Her Majesty's Revenue and Customs – v- Waste Recycling Group Limited [2008] EWCA Civ 849* ("the WRG case"). The judgment has significant implications for what is considered to be a taxable disposal of waste.

13. HM Treasury is taking powers to prescribe by order that an activity on a landfill site is subject to landfill tax in order to address the situation, in the light of the WRG case, that uses of waste on a landfill site are not taxable. The order will be published in draft during the Public Bill Committee stage.

14. Following the WRG case, it is clear that the temporary holding of waste on a landfill site for certain purposes and the use of material for site restoration are not, in any case, taxable. The current provisions in legislation, that tax is not payable in these situations, are therefore being removed as they are no longer necessary and their retention would create confusion.

15. In order to establish whether or not a taxable disposal of waste has taken place, HMRC will have a continued need for information about the temporary holding of waste at a landfill site and site restoration. Finance Act 2009 provides that HMRC will continue to have appropriate access to this information.

16. The Commissioners' regulations provided for in the Schedule will be published in draft during Public Bill Committee.

17. The removal of the requirement that the landfill tax return form is prescribed in regulations is a matter of administrative convenience which will bring landfill tax in line with the other environmental taxes (aggregates levy and climate change levy).

18. The Schedule will come into effect on the date that Finance Act 2009 receives Royal Assent, save for paragraphs 10 and 11 which will come into effect on 1 September 2009. The associated secondary legislation provided for in the Schedule will come into effect on 1 September 2009.

SECTION 120: REQUIREMENT TO DESTROY REGISTRATION DOCUMENTS WHICH ARE REPLACED

SUMMARY

1. Section 120 amends Section 22(1) of the Vehicle Excise and Registration Act 1994 (VERA) and introduces a new subsection which allows the Secretary of State for Transport to make Regulations compelling the registered keeper of a vehicle to destroy an existing Vehicle Registration Certificate (V5C) once they have received an amended or updated document.

DETAILS OF THE SECTION

2. The subsection introduces the amendments made to VERA by the section and inserts a new Section 22(1)(ha) into VERA which allows the Secretary of State for Transport to make Regulations requiring the destruction of a V5C where a new one is issued in place of it.

BACKGROUND NOTE

3. Registered keepers of vehicles are issued with a V5C registration document by the Driver and Vehicle Licensing Agency (DVLA). The V5C contains vehicle information as well as the name and address of the person recorded as the registered keeper. Keepers are legally obliged to notify DVLA if any of the details on the V5C change. The only method currently available to motorists to notify such changes is to post the current V5C to DVLA. DVLA records the changes and issues a new V5C.

4. DVLA plans to increase the amount of services it offers electronically, in line with the general policy of modernising Government. This section will give DVLA the scope to develop a system for electronic notifications of changes in driver and vehicle details. Once these are in place motorists will be able to destroy a superseded V5C instead of having to return it to DVLA.

5. DVLA plans to consult with all interested parties, including the police, before the relevant regulations (The Road Vehicles (Registration and Licensing) Regulations 2002) are amended.

SECTION 121: HYDROCARBON OIL DUTIES: MINOR AMENDMENTS

SUMMARY

1. Section 121 makes two minor drafting amendments to the Hydrocarbon Oil Duties Act 1979 (HODA).

DETAILS OF THE SECTION

2. Subsection (2) removes an unnecessary reference in section 11(1) of HODA.

3. Subsection (3) corrects the wording of section 14D(2) of HODA so that there is a clear distinction between the conduct that attracts a civil penalty and conduct that is a criminal offence in relation to the supply of rebated biodiesel or bioblend for a prohibited use.

BACKGROUND NOTE

4. Finance Act 2008 introduced section 14D (penalties for misuse of rebated biodiesel or bioblend) of HODA. The section amends this section so that there is a clear distinction between the conduct that attracts a civil penalty and conduct that is a criminal offence in relation to the supply of rebated biodiesel or bioblend for a prohibited use, and it removes an unnecessary reference in section 11(1) of HODA.

SECTION 122: EXTENSION OF AGRICULTURAL PROPERTY AND WOODLANDS RELIEF FOR EEA LAND

SUMMARY

1. Section 122 provides that the existing inheritance tax reliefs for agricultural property and woodlands are extended to property in the European Economic Area (EEA) when an event chargeable to inheritance tax (IHT) occurs. Property qualifying for this extended IHT relief will also qualify for capital gains tax (CGT) hold-over relief.

2. The extension of agricultural property relief (APR) and woodlands relief (WR) also applies where IHT was due or paid on or after 23 April 2003. CGT hold-over relief in respect of disposals of agricultural property located in a qualifying EEA state in the past will also be possible.

DETAILS OF THE SECTION

3. Subsection (2) amends subsection (3) of section 115 of the Inheritance Tax Act 1984 (IHTA) to ensure relief continues to be limited to the agricultural value of agricultural property. Existing provisions limit relief by establishing agricultural value with reference to an assumed "perpetual covenant" that would prevent property being used for anything other than agricultural purposes under the terms of the Act. The amendment provides that an equivalent restriction must apply when establishing the agricultural value of the property (and therefore relief) outside the UK, Channel Islands and the Isle of Man. This is to ensure that relief is given on the same terms for property in other EEA states where the reference to a "perpetual covenant" may not have meaning.

4. Subsection (3) amends subsection (5) of section 115 of IHTA. The existing subsection allows relief in respect of agricultural property located in the UK, Channel Islands and the Isle of Man. Subsection (3) extends this so that relief is also applied to agricultural property located in states other than the UK, provided that the state in question is an EEA state (as defined by the Interpretation Act 1978) when a transfer of value under the terms of IHTA occurs. This change has a consequential effect on section 165 of the Taxation of Chargeable Gains Act 1992 (TCGA) as applied by virtue of paragraphs 1 and 3 of Schedule 7 to TCGA. The change to IHTA means that property which qualifies for APR under this section will also qualify for business asset 'hold over' relief where it is farmed by a person other than the owner (property farmed by the owner already qualifies for hold-over relief regardless of where it is situated).

5. Subsection (4) inserts a new subsection (7A) into section 116 of IHTA. This ensures that, where agricultural relief for property is dependent on provisions that are specific to (or have meaning only in respect of) the law of the UK, the relevant UK legislation is to be taken to refer to equivalent provisions in other EEA states. The amendment enables existing references to rights and obligations that are specific to the law of the UK to operate in the context of the law of a foreign jurisdiction.

6. Subsection (5) amends subsection (1) of section 125 of IHTA, removing the words "in the United Kingdom". The amendment removes the existing geographical restriction on the location of property qualifying for woodlands relief in accordance with section 125.

7. Subsection (6) introduces a new subsection (1A) into section 125 IHTA. This applies woodlands relief to land located in the UK or other EEA state at the time of the death of the person whose estate is chargeable to IHT.

8. Subsection (7) provides that the extension of relief against inheritance tax for qualifying agricultural and woodland property will take effect for transfers of value where tax would have been payable on or after 22 April 2009 and for similar events before that date where IHT on such property was due or paid on or after 23 April 2003.

9. Subsection (8) provides that IHT paid on or after 23 April 2003, together with any interest that was charged on such IHT, on property newly qualifying as agricultural and woodland property under this section, is repayable provided a claim for repayment is made. Such repayments (including interest) will attract interest under an existing IHTA provision. The deadline for making a claim to repayment will be six years after the date on which a qualifying payment was made (this is the normal time limit for claiming repayments of overpaid IHT) or, if later, 21 April 2010.

10. Subsection (9) provides that, in the case of property becoming entitled to relief as a result of this section, an election to obtain woodlands relief can be made within two years of the date of death giving rise to the IHT charge or, if later, 21 April 2010. Claims for repayment of IHT will be possible where IHT paid falls within the previous subsection.

BACKGROUND NOTE

11. Agricultural property relief (APR) is set out at sections 115 to 124C of IHTA. The relief reduces, either entirely or partially, the agricultural value of agricultural property for the purposes of calculating a charge to IHT.

12. Agricultural property includes:

- agricultural land or pasture;
- farmhouses, cottages or buildings that are used for agricultural purposes and are proportionate in size to the nature and size of the farming activity;
- woodland and buildings used for intensive rearing of livestock or fish;
- growing crops transferred with the land;
- stud farms that are breeding and rearing horses, and the land that the horses graze on;

- short rotation coppice – trees that are planted and harvested at least every ten years;

- land that is actively not being farmed to help preserve the countryside and habitat for wild animals and birds under the Habitat Scheme;

- the value of land where the value includes the benefit of a milk quota; and

- some agricultural shares and securities.

13. APR is normally given at a rate of 100 per cent of the agricultural value of land. However property rented out since before 1 September 1995 usually only qualifies for relief at a rate of 50 per cent of the agricultural value.

14. Prior to 22 April 2009, for agricultural property to qualify for APR, it must have been located in the UK, the Channel Islands or the Isle of Man. The extension of APR to property in any EEA state will have effect for all occasions on or after 22 April 2009 chargeable to IHT. This extension will also have effect for earlier chargeable occasions where IHT in respect of the occasion was due or paid on or after 23 April 2003. The amendments ensure that relief will apply in respect of qualifying property located in either the UK, Channel Islands or Isle of Man or in an EEA state when a transfer of value under the terms of IHTA occurs.

15. The existing statutory regime for APR contains certain eligibility conditions for relief; for example, there is a minimum length of time for which the property must be owned. This section extends APR to qualifying property in other EEA states but otherwise leaves APR unchanged. So the existing qualifications for relief will continue to apply to agricultural property on and after the date of extension.

16. Where APR is dependent on terms and restrictions which have meaning in the UK, this section ensures that property in newly included EEA states will only qualify for relief to the extent that equivalent terms and restrictions are applied. For example APR at 100 per cent is dependent on the transferor having vacant possession of the land in question, or the right to obtain it within 12 months of the transferor. This new provision will ensure that the relief will work satisfactorily in other EEA states where a right to obtain something equivalent to vacant possession exists.

17. Extension of APR under this section applies (but is not solely restricted) to relief against any chargeable events associated with settled property (i.e. property placed into a trust). Thus the extension will apply to periodic or exit charges associated with such settlements arising on or after 22 April 2009 and to similar charges arising before that date where the IHT was due or paid on or after 23 April 2003.

18. Extension of agricultural relief under this section also applies (but is not solely restricted) to transfers of value which are, or are treated as being, Potentially Exempt Transfers (PETs) under section 3A of IHTA (provided those PETs result in an IHT being due or paid on or after 23 April 2003 and are in respect of qualifying property).

19. This section also extends the availability of existing relief against IHT for trees or underwood comprised in estates (woodlands relief).

20. Woodlands relief (WR) gives relief, providing an election is made by the person liable for the IHT that would otherwise be due, by excluding the full value of trees or underwood on qualifying land from the calculation of the death estate for IHT purposes. When the timber is sold an IHT liability may then arise on the original beneficiaries.

21. WR could only previously apply in respect of trees or underwood growing on land located in the UK. This section extends the relief to trees or underwood growing on land located in other qualifying EEA states. The amendments restrict the extension of relief to circumstances where the land in question is located in a qualifying EEA state at the time of death. The relief is otherwise left unchanged.

22. Business asset hold-over relief allows deferral of a capital gains tax charge (on a gift or sale at undervalue of a business asset) until the asset is disposed of by the recipient. Claims for hold-over relief are possible in respect of agricultural property that is not farmed by the person claiming the relief.

23. This section will have the effect of extending, from 22 April 2009, hold-over relief to agricultural property in other qualifying EEA states. Other conditions for the relief are unchanged.

24. Hold-over relief in respect of disposals of agricultural property located in a qualifying EEA state in the past will also become eligible for relief. Claims in respect of gifts or sales at undervalue on or after 23 April 2003 will be possible within existing statutory provisions for claims and amended returns. The time limit for claiming hold over relief is five years from 31 January following the tax year to which the claim relates. Claims to relief in respect of the tax year 2003-04 can therefore be made until 31 January 2010.

SECTION 123 AND SCHEDULE 61: ALTERNATIVE FINANCE INVESTMENT BONDS

SUMMARY

1. Section 123 and Schedule 61 facilitate the issue of alternative finance investment bonds based on real property. They ensure that disposals and acquisitions of real property in connection with such bonds do not incur liabilities to stamp duty land tax (SDLT) or tax in respect of chargeable gains and entitlements to capital allowances are preserved. They have effect from the date of Royal Assent.

DETAILS OF THE SECTION

2. Section 123 provides for Schedule 61 to have effect in relation to relief from taxation of chargeable gains, SDLT, and capital allowances in connection with alternative finance investment bonds.

DETAILS OF THE SCHEDULE

3. Paragraph 1(1) of the Schedule provides that terms used in the Schedule have the same meaning as in section 48A of the Finance Act (FA) 2005, which deals with alternative finance investment bonds. This sub-paragraph also explains that references in the Schedule to "prescribed evidence" mean evidence prescribed in regulations made by HM Revenue & Customs (HMRC). It also defines a qualifying interest as "a major interest in land". The only exclusion is a lease of 21 years or less.

4. Paragraph 1(2) provides that, unless it is clear from the context that this is not the case, any expressions used in the Schedule which are also used in Part 4 of FA 2003 (which deals with SDLT) shall have the same meanings in both places.

5. Paragraph 2 provides an exemption from SDLT for alternative finance investment bonds by ensuring the tax treatment of the bonds is the same as that provided within section 48B(2) of FA 2005 for income tax and capital gains tax (CGT).

6. Paragraph 3(1) states that the tax treatment of alternative finance investment bonds provided at paragraph 2 is not available where a bond-holder, or a group of connected bond-holders, acquires control of the underlying asset.

7. Paragraph 3(2) explains the circumstances in which it may be possible for a single bond-holder, or a group of connected bond-holders, to acquire control of the underlying asset.

8. Paragraph 4 provides two exclusions from paragraph 3.

9. Paragraph 4(2) provides the first exclusion, which applies where, at the time the rights under the bond were acquired, a bond-holder, or all of a group of connected bond-holders, did not know or had no reason to suspect that the bonds enabled the exercise of the rights of management and control of the bond assets and, having subsequently become aware of the rights attached to the bonds, the bond-holder(s) transferred sufficient bonds, as soon as reasonably possible so that they could no longer exercise such control.

10. Paragraph 4(3) provides for the second exclusion which is available for persons acting as underwriters of the bond issuance providing they do not exercise control and management of the bond asset.

11. Paragraph 5(1) introduces 7 conditions (conditions A to G) for the application of paragraphs 6 to 18 of the Schedule to provide relief from SDLT and tax on chargeable gains and to determine the treatment for capital allowances purposes. This sub-paragraph also provides that paragraphs 20 and 22 of the Schedule can prevent these reliefs even if all 7 conditions are satisfied.

12. Sub-paragraph (2) provides condition A. This is that a person ("P") transfers a qualifying interest in land to another person ("Q") and P and Q agree that at a later time (when Q ceases to hold that interest as a bond asset in relation to an alternative finance investment bond of which Q is the issuer) Q will transfer that interest to P. The transfer of the qualifying interest to Q is described in the Schedule as "the first transaction".

13. Sub-paragraph (3) provides condition B. This is that Q acts as bond issuer in relation to an alternative finance investment bond, and holds the interest in land as a bond asset.

14. Sub-paragraph (4)(a) provides condition C. This is that Q and P enter into a "leaseback agreement" to generate income and gains for the alternative investment bond.

15. Sub-paragraph (4)(b) provides that HM Treasury may, by regulations extend the scope of condition C to include financing structures other than those involving a sale and leaseback.

16. Sub-paragraph (5) explains what is meant by "leaseback agreement" in condition C. This is that Q grants P a lease or sublease out of the interest acquired in the first transaction. The sub-paragraph includes provision to ensure that the equivalent transactions under Scottish land law also constitute a leaseback agreement.

17. Sub-paragraph (6) provides condition D. That is that, the bond issuer (Q) is required to provide prescribed evidence that a satisfactory legal charge has been entered on the Land Register. The evidence needs to be provided to HMRC within 120 days of the first transaction. "Prescribed evidence" is evidence prescribed by regulation made by HMRC.

18. Sub-paragraph (7) provides rules relating to the charge over the land referred to in sub-paragraph 6.

19. Sub-paragraph (8)(a) provides that the amount of the charge is to include the amount of SDLT that would be due on the market value of the transfer of the interest at the date of the transfer.

20. Sub-paragraph (8)(b) provides that the charge also includes any interest and penalties that would be payable if the tax has been due (but not paid) on the first transaction.

21. Sub-paragraph (9) provides condition E. This is that, over the life of the alternative finance investment bond, Q receives payments of capital of at least 60 per cent of the value of the interest in land at the time of the first transaction. The purpose of condition D is to ensure that the main use of the interest in land is as a bond asset.

22. Sub-paragraph (10) provides condition F. This is that throughout the life of the alternative finance investment bond Q holds the interest in land as a bond asset.

23. Sub-paragraph (11) provides condition G. This is that at the termination of the bond, when the interest in land ceases to be a bond asset, the interest is transferred to P by Q (this transfer is described as "the second transaction"), and that the second transaction takes place no later than 10 years after the first transaction. This effectively puts a term of 10 years on the alternative finance investment bond.

24. Sub-paragraph (12) provides that the period of 10 years referred to in condition G can be altered by Treasury regulation.

Stamp duty land tax: first transaction

25. Paragraph 6(1) sets out the requirements for relief from SDLT on the first transaction. These are that the interest acquired is of land in the UK and that each of the conditions A to C are met within 30 days of the date of the transfer of interest in land from P to Q.

26. Paragraph 6(2) provides that where the requirements in this paragraph are satisfied the first transfer from P to Q is exempt from SDLT.

27. Paragraph 6(3) provides that the relief is subject to conditions relating to asset substitution at paragraph 18.

28. Paragraph 6(4) provides that relief on the first transaction is also subject to the provisions of paragraph 20 which provides that relief on the first transaction is not available where a bond-holder, or group of connected bond-holders, acquires control of the underlying asset.

29. Paragraph 7 details the circumstances where the relief on the first transaction will be withdrawn.

30. Paragraph 7(1)(a) provides for the first circumstance, where the asset is returned to P but the requirement to issue bonds to the value of 60 per cent of the asset is not satisfied and the asset is not held as a bond asset until the termination of the bond.

31. Paragraph 7(1)(b) provides that the relief is also withdrawn where a period of ten years has elapsed since the first transaction without conditions E and F having been satisfied.

32. Paragraph 7(1)(c) provides that relief is also withdrawn if at any time it becomes evident that any of conditions E to G cannot or will not be fulfilled.

33. Paragraph 7(2) provides that relief is also withdrawn where Q fails to provide prescribed evidence to HMRC that they have registered a charge within 120 days of the transaction (see above).

34. Paragraph 7(3) provides that if any of the circumstances set out in paragraphs 7(1) and (2) apply then the first transaction is no longer exempt from SDLT.

35. Paragraph 7(4) provides that the amount of SDLT chargeable is the tax that would have been charged on the market value of the interest transferred and paragraph 7(5) provides the time from which interest is due in respect of that amount.

36. Paragraph 7(6) provides that Q is also required to deliver a further land transaction return within 30 days of the date on which the relief is withdrawn.

37. Paragraph 7(7) provides that the return must include a self-assessment of the amount chargeable to tax in respect of the first transaction.

38. Paragraph 7(9) provides that the requirements of Schedule 10 to FA 2003 and section 76 of that Act are modified for the purposes of this Schedule with the transaction being the event which triggered withdrawal of the relief and the effective date of transaction being the date of the withdrawal of the relief.

Stamp duty land tax: second transaction

39. Paragraph 8 provides relief from SDLT on the transfer of the land asset from Q back to P.

40. Paragraph 8(1) provides that the transfer of the land back to P is exempt if conditions A to G have been met and all the provisions of Part 4 of FA 2003 relating to the first transaction have been complied with.

41. Paragraph 8(2) provides that the relief is subject to conditions relating to asset substitution in paragraph 18.

42. Paragraph 8(3) provides that relief is not available in respect of the second transaction if paragraph 20 applies because a bond-holder or group of connected bond-holders acquires control of the underlying asset.

43. Paragraph 9 provides that if following the transfer of the land asset back from Q to P, Q provides prescribed evidence that conditions A to C and E to G have been met then the land ceases to be subject to a charge.

Taxation of capital gains

44. Paragraph 10 provides relief from charges under the Taxation of Chargeable Gains Act 1992 (TCGA) in respect of the first transaction and any leaseback agreement between Q and P, provided that certain of the conditions in paragraph 5 are satisfied.

45. Paragraph 10(1) states that the paragraph applies if conditions A to C in paragraph 5 (see paragraphs 12 to 16 above) are all satisfied within 30 days of the effective date of the first transaction. This condition is the same as that in paragraph 6(1)(b) in respect of SDLT.

46. Paragraph 10(2) provides the relief in respect of the first transaction. The first transaction is not treated for the purposes of the TCGA as a disposal by P or an acquisition by Q. In general, tax is charged under TCGA only if chargeable gains arise on the disposal of assets, so the provision that there is no disposal prevents a charge from arising.

47. Paragraph 10(3) similarly provides that if condition C is satisfied by Q and P entering into a leaseback agreement, the granting of a lease or sub-lease in the leaseback agreement is not regarded for TCGA purposes as a disposal of an interest in the land by Q or an acquisition by P.

48. Paragraph 10(4) provides that sub-paragraphs (2) and (3) are subject to paragraph 11, which provides for withdrawal of the relief if any of conditions D to G are not met.

49. Paragraph 10(5) provides that, if the interest in land ceases to be the bond asset but is replaced by an interest in other land, paragraph 10 is subject to paragraph 18, and sub-paragraph (6) provides that paragraph 10 is also subject to paragraph 20 (see paragraphs 93 to 95 below).

50. Paragraph 11 effectively withdraws the special treatment provided by paragraph 10, if any of conditions D to G are not satisfied.

51. Paragraph 11(1) provides three circumstances in which the paragraph applies. These are that:

- Q transfers the interest in land back to P without conditions E and F having been met;
- the period specified in condition G (under paragraph 5(11)(b) this is currently 10 years, but can be changed by regulations) expires without both condition E and condition F being satisfied; or
- it becomes clear at any time that one or more of conditions E to G cannot or will not be satisfied.

52. Paragraph 11(2) provides for the paragraph to have effect in one other circumstance. This is that the interest in land that is the subject of the first transaction is an interest in land in the UK, but Q fails to provide evidence of a charge over the land as required by Condition D.

53. Paragraph 11(3) provides that where paragraph 11 has effect, the disregards for TCGA purposes of the first transaction and the grant of the lease or sub-lease do not apply. The effect of this is that these transactions can constitute disposals and acquisitions for TCGA purposes, so that chargeable gains or losses may arise. Any gains or losses are computed as they would be if the transactions had not been disregarded.

54. Paragraph 11(4) provides that any chargeable gains or losses that result from the application of sub-paragraph (3) do not arise for tax purposes at the time of the actual transactions (the first transaction, or the grant by Q to P of the lease or sub-lease). The exact time when they arise is determined by the conditions that result in the application of sub-paragraph (3):

- where sub-paragraph (3) applies because the interest in land is transferred from Q to P without one or both of conditions E or F being satisfied, the chargeable gain or loss arises immediately before the transfer of the interest from Q to P;

- where sub-paragraph (3) applies by virtue of either of the conditions in the second and third bullets of paragraph 51 of this note, the chargeable gain or loss arises at the time mentioned in the relevant condition; and

- where sub-paragraph (3) applies by virtue of the failure to provide evidence of a charge over land located in the UK, the chargeable gain or loss arises at the expiry of the time allowed under condition D.

55. Paragraph 12 provides relief from tax under TCGA in respect of the second transaction.

56. Paragraph 12(1) provides that the second transaction is not regarded for TCGA purposes as a disposal by Q and an acquisition by P if:

- conditions A to C and E to G are satisfied; and

- if the relevant land is in the UK, condition D is also met.

Capital allowances

57. Paragraph 13(1) explains that paragraphs 14 to 17 set out the treatment of alternative finance investment bonds for the purposes of the capital allowances legislation.

58. Paragraph 14 sets out the treatment for capital allowances purposes of plant and machinery or industrial buildings used for alternative finance investment bonds.

59. Sub-paragraph (1) provides that paragraph 14 applies to transactions falling within the conditions A to C set out in paragraph 5.

60. Sub-paragraph (2) provides that paragraph 14 only applies to assets that are either plant or machinery or an industrial building (or part of an industrial building).

61. Sub-paragraph (3)(a) provides that the expenditure by Q on acquiring the asset is not capital expenditure for the purposes of CAA.

62. Sub-paragraph (3)(b) provides that, for the purposes of CAA, Q is not treated as becoming the owner of the asset, instead P is to be regarded as continuing to be the owner of the asset.

63. Sub-paragraphs (4) and (5) provide that the treatment of the assets for the purposes of CAA is not affected by the leaseback agreement entered into by Q and P nor by the second transaction.

64. Paragraph 15 provides rules for the case where the asset held for the purposes of the bond is lost or destroyed.

65. Sub-paragraph (2) states that the first condition is that the asset is plant or machinery that was part of the subject matter of the first transaction.

66. Sub-paragraph (3) states that the second condition is that, whilst the asset is held as a bond asset, it is either permanently lost or ceases to exist.

67. Sub-paragraph (4) provides that if the conditions are met then for the purposes of CAA there is a disposal event for P in the period in which the loss occurs or the asset ceases to exist.

68. Sub-paragraph (5) sets out the disposal value that P is required to bring into account for the purposes of CAA.

69. Paragraph 16 sets out the treatment for the purposes of CAA where Q retains the asset, but no longer holds it as a bond asset.

70. Sub-paragraph (2) states that the first condition is that the asset is plant or machinery, or an industrial building (or part of an industrial building), that was part of the subject matter of the first transaction.

71. Sub-paragraph (3) states that the second condition is that Q retains the asset after ceasing to hold the asset as a bond asset.

72. Sub-paragraph (4) states that where the conditions are satisfied, Q is treated for the purposes of CAA as becoming the owner of the asset and P is treated as ceasing to be the owner of the asset.

73. Sub-paragraph (5) states that in the chargeable period for P in which Q ceases to hold the asset as a bond asset, P is treated as having disposed of the asset.

74. Sub-paragraph (6)(a) states that P is required to bring into account as the disposal value, the market value of the plant or machinery at the time of the transfer.

75. Sub-paragraph (6)(b) states that P is treated as receiving as the proceeds of the balancing event, for the purposes of industrial buildings allowances, the market value of the asset.

76. Paragraph 17 sets out the treatment for the purposes of CAA where Q transfers the asset to a third person.

77. Sub-paragraph (2) states that the first condition is that the asset is plant or machinery, or an industrial building (or part of an industrial building), that was part of the subject matter of the first transaction.

78. Sub-paragraph (3) states that the second condition is that Q transfers the asset to any other person than P.

79. Sub-paragraph (4) states that at the time that Q transfers the asset, the other person is treated for the purposes of CAA as becoming the owner of the asset and P is treated as ceasing to be the owner of the asset.

80. Sub-paragraph (5) states that in the chargeable period for P in which Q ceases to hold the asset as a bond asset, P is treated as having a disposal event in respect of plant or machinery or a balancing event in respect of an industrial building (or part of an industrial building).

81. Sub-paragraph (6)(a) states that P is required to bring into account as the disposal value, the market value of the plant or machinery at the time of the transfer.

82. Sub-paragraph (6)(b) states that P is treated as receiving as the proceeds of the balancing event, for the purposes of industrial buildings allowances, the market value of the asset.

Supplementary

83. This section of the Schedule explains:

- the conditions that need to be satisfied for the relief to remain available if an asset is substituted; and
- the circumstances in which relief may be denied where a bond-holder, or a group of connected bond-holders, acquires control of the asset.

84. Paragraph 18 provides rules for the case where the interest in land that was subject of the first transaction ceases to be a bond asset (before the termination of the bond) and is replaced as bond asset by an interest in other land. These rules allow such a substitution of bond assets to take place without disturbing the reliefs under paragraphs 6 to 17.

85. Sub-paragraph (1) lists the circumstances in which the paragraph applies. These are that:

- conditions A to C and G are met in relation to an interest in land (described as "the original land"), so that the interest in land is transferred from Q to P (condition G) at some time after conditions A to C have been satisfied;
- the interest in land ceases to be held by Q as a bond asset and hence is transferred by Q to P before the termination of the life of the bond;
- P and Q enter into further arrangements that fall within paragraph 5(2) (condition A) in relation to an interest in other land (described as "the replacement land"); and
- the value of the replacement land when transferred from P to Q is at least as great as the value of the interest in the original land at the time of the first transaction.

86. Sub-paragraph (2) provides modifications to the application of paragraphs 6 to 17 to the original land and the replacement land. The purpose of these modifications is that the replacement land is able to become the bond asset in place of the original land, without disturbing the effects of paragraphs 6 to 17 in relation to the relevant alternative finance investment bond arrangements. The modifications in respect of the original land are in sub-paragraph (3), and those in respect of the replacement land in sub-paragraph (4).

87. Sub-paragraph (3) provides that condition F (the requirement that Q should hold the original land as a bond asset throughout the life of the bond) need not be met in relation to the original land, provided that conditions A, B, C, F and G (taking account of the modifications made by sub-paragraph (4)) are met in relation to the replacement land.

88. Sub-paragraph (4) provides that following the substitution of the replacement land for the original land:

- condition E continues to apply by reference to the value of the original land at the time of the first transaction relating to that land (so that the amount of capital that Q must receive to satisfy condition E is unchanged by the substitution of land); and
- the ten year time limit for condition G continues to apply by reference to the first transaction relating to the original land.

89. Sub-paragraph (5) provides that, if the replacement land is in the UK, the charge on the original land will be discharged when, Q provides HMRC with the prescribed evidence that the original land has been returned to P and a charge has been registered in relation to the replacement land,.

90. Sub-paragraph (6) provides that, if the replacement land is not in the UK, the charge on the original land will be discharged when Q provides HMRC with the prescribed evidence that all of conditions A to C are met for the replacement land and that the original land had been returned to the original owner.

91. Sub-paragraph (7) provides for the rules in relation to asset substitution to apply where there is more than one substitution of land during the lifetime of a bond.

92. Paragraph 19 provides that, where a charge on the land is discharged because the land has ceased to be a bond asset, either at the expiration of the bond with all of conditions A to G having been met, or because of a substitution of land to which paragraph 18 applies, HMRC must take the necessary action to remove the charge from the land register. This must be done within 30 days of Q providing the prescribed evidence that enables the charge to be removed.

93. Paragraph 20 provides rules for the situation where a bond-holder, or a group of connected bond-holders, acquires control of the bond assets. The circumstances in which the paragraph applies are the same as for paragraphs 3 and 4 of the Schedule.

94. Sub-paragraph (2) explains what is meant by a single bond-holder, or a group of connected bond-holders, acquiring control of the underlying asset. This happens if:

- the rights of bond-holders under an alternative finance investment bond include rights of control and management over the bond; and
- a bond-holder, or a group of connected bond-holders, acquires sufficient rights to enable them to exercise management and control over the bond assets, regardless of any other bond-holders.

95. Sub-paragraph (3) provides that:

- if a bond-holder, or the group, acquires control before the termination of 30 days from the first transaction, no relief for SDLT or TCGA purposes is available in relation to the arrangements; and
- if a bond-holder, or the group, acquires control after that period of 30 days, and conditions A to C have been met within that 30 day period, paragraphs 8 and 12 apply to withdraw the reliefs under paragraph 6 (for SDLT purposes) and 11 (for TCGA purposes) respectively.

96. Paragraph 21(2) provides that where, at the time the rights under the bond were acquired, a bond-holder, or all of a group of connected bond-holders, did not know or had no reason to suspect that the bonds enabled the exercise of the rights of management and control of the bond assets and, having subsequently become aware of the rights attached to the bonds, the bond-holder(s) transferred sufficient bonds, as soon as reasonably possible so that they could no longer exercise such control.

97. Paragraph 21(3) provides for the second exclusion for persons acting as underwriters of the bond issuance providing they do not exercise the right of control and management of the bond asset.

98. Paragraph 22 is an anti-avoidance provision. It provides that the reliefs under paragraphs 6 to 12 (extended where appropriate by paragraph 18 in relation to substitutions of land) are not available unless the arrangements:

- are entered into for genuine commercial reasons; and
- are not part of arrangements whose main purpose, or one of whose main purposes, is the avoidance of liability to any of a number of taxes (which are listed in paragraph 22(2)).

99. Paragraph 23 provides rules in relation to regulations that can be made under provisions of this Schedule.

Consequential changes

100. Paragraph 25 inserts new section 73C into FA 2003. This provides a cross-reference to this Schedule.

101. Paragraph 26 inserts new subsection (5A) into section 86 of FA 2003 (payment of tax) ensuring that tax is payable where the land ceases to qualify for relief in respect of alternative finance investment bonds.

102. Paragraph 27(2) amends section 48B of FA 2005 (alternative finance investment bonds) to replace references to 'any tax other than the Corporation Tax Acts' in subsection (2) and (3) with references to income tax or CGT.

103. Paragraph 27(3) inserts new subsection (9) into section 48B of FA 2003 which refers to this Schedule.

104. Paragraph 28 repeals paragraph 651(a) of Schedule 1 to the Corporation Tax Act 2009.

105. Paragraph 29 provides the commencement provision for the Schedule. Sub-paragraph (1) provides that the amendments to section 48B of FA 2005 made by paragraphs 2 to 4 and 27, and the amendment to FA 2003 made by paragraphs 25, have effect from the date of Royal Assent.

106. Sub-paragraph (2) of paragraph 29 provides that the rest of the Schedule has effect where the first transaction (as explained in paragraph 5(2), takes place on or after the date of Royal Assent.

BACKGROUND NOTE

107. The Government has already introduced legislation enabling the provision of alternative methods for individuals or business to finance a property purchase, deposit money in a bank and borrow money from a financial institution. The focus has now moved to the issue of alternative finance investment bonds based on real property.

108. Interests in land or property as the underlying asset may often back bonds. In a normal securitisation, the investor does not have a direct ownership in the underlying asset but merely an interest-bearing certificate. With alternative finance investment bonds, however, the investors own part of the underlying asset. This necessary change in ownership of the underlying asset may involve SDLT, tax on capital gains and capital allowances issues.

109. To provide similar tax outcomes for alternative finance products to their equivalent conventional finance products, no SDLT or tax on capital gains should be charged when the land is sold to the issuer of the alternative finance bonds and no SDLT or tax on capital gains charged on the sale back of the property to the originator at the end of the bond term. In addition the position of alternative finance bond-holders will be clarified to ensure that SDLT does not arise on the acquisition or transfer of an alternative finance bond certificate. The originator should also be able to claim any CAs on the asset during the term of the bond.

110. These new provisions address certain tax barriers to ensure that the cost of issuing an asset based alternative finance investment bond is equivalent to conventional equivalent financial product.

SECTION 124: MUTUAL SOCIETIES: TAX CONSEQUENCES OF TRANSFERS OF BUSINESS ETC

SUMMARY

1. Section 124 introduces a power to make provisions by regulations governing the tax consequences of transfers of business or engagements by mutual societies.

DETAILS OF THE SECTION

2. Subsection (1) sets out the scope of the power.

3. Subsection (3) provides that regulations made under this power may in particular make provision about a number of particular areas as identified in subsections (a) to (h) including reliefs, exemptions and countering avoidance.

4. Subsection (4) provides that the regulations may modify enactments and instruments relating to tax; make any incidental, consequential, supplemental or transitional provisions that may be required including different provisions for different cases or different purposes.

5. Subsection (5) allows for such regulations to have unlimited retrospective effect subject to the condition that they do not increase any person's liability to tax.

BACKGROUND NOTE

6. The Building Societies (Funding) and Mutual Societies (Transfers) Act 2007 ("the 2007 Act") received Royal Assent on 23 October 2007. Its aim is to help the mutual sector to expand and flourish as an alternative model to other legal forms such as proprietary companies by making it easier for a mutual society to transfer its business to a subsidiary company of another mutual society.

7. Initial discussions with the mutual society sector ahead of implementation of the 2007 Act identified a number of tax issues that might act as a barrier to transfers under that Act and to transfers under pre-existing continuing rules.

8. This section introduces a power for HM Treasury to make, by way of regulations, provisions for the tax consequences of transfers of business or engagements ensuring, as far as possible, equivalent tax treatment for all such transfers and countering potential avoidance.

SECTION 125: NATIONAL SAVINGS: SURPLUS FUNDS

SUMMARY

1. This section requires the Commissioners for the Reduction of the National Debt ("the Commissioners") to pay to the Consolidated Fund surplus sums held by them by virtue of their investments under section 17 of the National Savings Bank Act 1971 ("the 1971 Act").

2. The section also gives a power to the Treasury to repeal or amend any enactment, by order, where the amendment is required as a consequence of the closure of ordinary accounts or the transfer of the surplus to the Consolidated Fund.

DETAILS OF THE SECTION

3. Subsection (1)(a) requires the Director of Savings and the Commissioners to prepare a statement showing the amount of the surplus held by the Commissioners.

4. Subsection (1)(b) requires the Commissioners to transfer the surplus to the Consolidated Fund.

5. Subsection (2) describes the surplus which must be transferred by the Commissioners to the Consolidated Fund ("the relevant surplus") and specifies the sums which may be deducted from the relevant surplus before the transfer is made. Subsection (2)(a) allows sums expended by the Director of Savings in relation to the surplus to be deducted from the relevant surplus; subsection (2)(b) allows the Commissioners' expenses in managing the surplus to be deducted from the relevant surplus; and subsection (2)(c) provides that any sums which may be transferred to the Consolidated Fund under section 20 of the 1971 Act shall not form part of the relevant surplus.

6. Subsection (3)(a) provides that sums expended by the Director of Savings in relation to the surplus must be paid into the Consolidated Fund.

7. Subsection (3)(b) allows the Commissioners to retain sums representing their expenses in relation to the surplus.

8. Subsection (4) requires the Director of Savings and the Commissioners to present the statement under subsection (1) to the Comptroller and Auditor General who must audit the statement and report to Parliament accordingly.

9. Subsection (5) allows the Treasury, by order, to repeal or amend the legislation on ordinary accounts where the repeal or amendment is considered necessary or expedient in consequence of the closure of ordinary accounts or in consequence of the transfer of surplus moneys to the Consolidated Fund.

10. Subsection (6) requires an order under subsection (5) to be made by statutory instrument.

11. Subsection (7) provides that an order under subsection (5) must be laid in draft before, and approved by a resolution of, the House of Commons before it is made.

12. Subsection (8)(a) provides that references to sums expended or expenses incurred in connection with ordinary accounts includes sums expended or expenses incurred in connection with any amounts held by the Commissioners by virtue of their investments under section 17 of the 1971 Act.

13. Subsection (8)(b) ensures that the expressions used in the section have the same meaning as in the 1971 Act.

14. Subsection (9) provides that the "1971 Act" means the National Savings Bank Act 1971 and an "enactment" (at subsection (5)) includes both an enactment in the 1971 Act and subordinate legislation.

BACKGROUND NOTE

15. The National Savings Bank Ordinary Account was launched in 1861. In accordance with the provisions of sections 17 to 20 of the 1971 Act, the balance of ordinary accounts in the National Savings Bank was transferred to the Commissioners who, in turn, were required to invest the funds transferred to them in accordance with those provisions. Interest on the investments held by the Commissioners met the operational running costs of the ordinary account as well as the interest paid to depositors.

16. When the ordinary account was closed to transactions in 2004, moneys remained unclaimed in some accounts. In 2008, for security and operational reasons, any balances remaining were transferred to a new 'NS&I Residual Account'. The associated funds in respect of these accounts were transferred to the National Loans Fund.

17. All that now remains in the management of the Commissioners in respect of ordinary accounts is a surplus of moneys which represent sums set aside in the past to offset possible depreciation in the value of investments held by them (in accordance with section 20 of the 1971 Act) or sums which represent an increase in the capital value of their investments. The increase in the capital value occurred because the market value of gilt-edged investments held by the Commissioners rose as yields reduced in the 1990s and early 2000s, thereby increasing the value of older gilts. The 1971 Act makes no provision for how such a surplus must be managed.

18. This section requires the Commissioners to pay to the Consolidated Fund surplus sums held by them by virtue of their investments under section 17 of the 1971 Act and makes provision for the manner in which such a surplus must be calculated, transferred and accounted for

19. The section also allows the Treasury to repeal or amend, by order, statutory provisions relating to ordinary accounts which are no longer necessary.

HANSARD REFERENCES

The following table sets out the dates and Hansard references for each stage of the Act's passage through Parliament.

Stage	*Date*	*Hansard Reference*
House of Commons		
Presentation & First Reading	28 April 2009	Vol 491 Column 837
Second Reading	6 May 2009	Vol 492 Column 178 – 317
Whole House Committee	13 –12 May 2009	Vol 492 Column 687- 828 863- 986
Public Bill Committee	19, 21 May and 2,9,11,16,18,23,25 June 2009	Hansard – Finance Bill 2009 Public Bill Committee
Report	7,8 July 2009	Vol 495 Column 844 – 963 992 – 1071
Third Reading	8 July 2009	Vol 495 Column 1071 – 1075
House of Lords		
First Reading	8 July 2009	Vol 712 Column 756
Second Reading	20 July 2009	Vol 712 Column 1451 – 1500
Third Reading	20 July 2009	Vol 712 Column 1500 – 1506
Royal Assent	21 July 2009	Vol 712 Column 1580

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