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NORTHERN IRELAND

Taxing Times

UK Finance Bill

July 2015

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Foreword

Following the post-election Budget in early July, the Government has now published the requisite Finance Bill. The Bill contains draft legislation for provisions which were held over prior to the May General Election as well as some new measures which were announced in the July Budget.

Eamonn Donaghy
Partner and Head of Tax
KPMG Belfast

As promised in the Government's manifesto, a "tax lock" provision has been included which will prevent the Government from increasing the rates of income tax or the rate of VAT during the current Parliament.

The requisite legislation for changes to the income tax personal allowance and national minimum wage are included in the Bill as is the confirmation that the corporation tax rate will fall to 19 per cent in 2017, 2018 and 2019 and will be reduced to 18 per cent in 2020.

This edition of Taxing Times looks at some of the key issues contained in the Finance Bill including:

- **Inheritance tax** – the extension of the nil rate band for residential properties and changes to the tax charges applicable to trusts.
- **Banking** – the introduction of the new banking levy charge and changes to the definition of "banks".
- **Funds** – changes relating to carried interests and disguised investment management fees.
- **Pensions** – changes to the annual allowance entitlement.
- **Income tax** – changes to the relief for finance costs related to residential property businesses.
- **Investment reliefs** – changes to the Enterprise Investment Scheme, and venture capital trust rules.
- **Corporate debt** – changes to the loan relationship rules for corporates.
- **Corporation tax** – various changes to relief for expenditure on intangible fixed assets, group relief and the CFC charge.
- **Administration and enforcement** – new rules governing the deduction of tax from bank accounts and the obligation to notify taxpayers to improve compliance.

The Finance Bill will pass through Parliament over the next couple of months and is due to receive Royal Assent at the end of September or early October.

In the meantime, should you wish to discuss any of the matters contained in this edition of Taxing Times please do not hesitate to get in touch with either myself or your usual KPMG contact.

Eamonn Donaghy, Partner & Head of Tax

Inheritance Tax

The Finance Bill confirmed the Inheritance Tax (IHT) nil-rate band available for an individual will remain frozen at £325,000 until at least 2021.

Kevin Bell
Partner

However, the Bill introduced a new relief for individuals who die on or after 6 April 2017 in the form of an additional residence nil-rate band when a home is passed on death (but not in respect of lifetime gifts) to direct descendants of the deceased. This measure is intended to reduce the burden of IHT on families and make it easier to pass on the family home without an IHT charge.

The maximum amount of the new residence nil rate band will increase in stages from £100,000 in 2017/18 to £175,000 in 2020/21 per individual, bringing the total nil rate band available for a married couple to claim against their qualifying residence to £1million by 2020/21. Any unused band will be transferable to a spouse or civil partner and if an estate contains more than one qualifying property the personal representatives must nominate a specific property.

The new legislation provides for a restriction to the new relief applying a tapered withdrawal of the increased band for estates valued at more than £2 million. The allowance available will be reduced by £1 for each £2 that the total value of the deceased's estate exceeds £2m.

The provisions governing the extra IHT nil rate band are more complicated than one may have initially expected and not all aspects of the new relief have been incorporated into the Finance Bill. In light of these changes, individuals should consider reviewing wills they currently have in place to ensure they receive the maximum relief available. Additional legislation is expected in Finance Bill 2016 to deal with the benefit of the additional nil rate band for individuals who downsized to a less valuable property or disposed of a residence during their lifetime.

Inheritance Tax on Trusts

Property held in most discretionary trusts can be subject to a 6 per cent IHT charge every ten years on the value of the property exceeding the nil rate band and an exit charge may also arise when property leaves the trust. Finance Bill 2015 will introduce new legislation to change the way in which the IHT ten year charge and exit charges are calculated, to now include additions of property to other settlements on the same day, in order to remove the advantage that enables individuals to mitigate IHT by using multiple trusts. These changes will take effect from the date the Finance Act is passed.

Inheritance Tax Consultations

Changes to UK Domicile Status

The Government has outlined proposals to change the UK deemed domiciled rules. Currently UK domiciled and resident individuals are taxed on all worldwide income and gains. Non-UK domiciled individuals are able to claim the remittance basis of taxation, which does not tax foreign income and gains if they are not remitted to the UK. To avail of the remittance basis, longer term UK resident but non-UK domiciled individuals pay an annual remittance basis charge.

Currently an individual will be deemed UK domiciled for IHT purposes (only) when they have been resident in the UK for at least 17 of the last 20 tax years. It has been proposed by the Government that from April 2017, if an individual has been resident in the UK for more than 15 of the past 20 tax years they will be deemed UK domiciled for all UK tax purposes. This extends the deemed domicile concept beyond IHT. When an individual is deemed UK domiciled they will therefore not be able to claim the remittance basis in respect of non-UK income and gains.

In addition, from April 2017 an individual who had a UK domicile of origin at birth then left the UK and acquired a domicile of choice elsewhere but subsequently returned to the UK to become UK resident, will no longer be entitled to claim non domicile status.

A consultation document will be issued on these reforms and the legislation is expected to form part of Finance Bill 2016.

Inheritance Tax on UK Residential Property

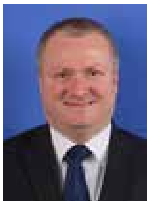
New IHT rules have been proposed for UK residential property held indirectly by non-UK domiciled individuals or excluded property trusts. Currently if a non-UK domiciled individual owns UK residential property through a non-UK company, it will be outside the scope of IHT. This new measure will bring all UK residential property held by foreign domiciled individuals through offshore companies or trusts within the charge to UK IHT. The shares of an offshore company held by non-UK domiciled individuals or their trusts and which holds UK residential property, will no longer be excluded property for UK IHT purposes and IHT charges could therefore arise for the shareholder.

The Government has confirmed they do not intend to change the IHT position in relation to UK assets other than residential property. The reforms will not affect UK domiciled individuals.

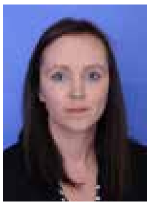
HMRC have acknowledged certain complexities that may arise with the new proposals and they have confirmed they will issue an initial consultation document on the changes. A further consultation document will be issued on the draft legislation which is expected to be included within Finance Bill 2017. The changes are expected to be effective from on or after 6 April 2017.

Pensions

Despite major changes to the taxation of pension contributions and pensions in recent years, the Government has announced a consultation on whether a new system would be introduced where pension contributions are taxed, but the growth in the fund and the final premium are exempt. More details will follow. Certain changes however take effect from April 2015 and April 2016.



Philip Caughey
Director



Kathy Blair
Manager

Reduced annual allowance for high earners

From 6 April 2016, there will be a restriction on the benefits of pension contributions tax relief for individuals with income (including both their own personal and their employer's pension contributions) exceeding £150,000 and threshold income (excluding pension contributions) of more than £110,000.

The new legislation in Finance Bill 2015 restricts the tax relief by means of a tapered reduction of the annual allowance and thus potentially reduces the amount of tax-relieved pension saving an individual can make each year. The allowance is currently £40,000, subject to not exceeding the current lifetime allowance of £1.25 million. The lifetime allowance will reduce from £1.2 million to £1 million from 6 April 2016. It is possible to carry forward unused allowance from the previous three tax years to offset any excess in the current year. The annual allowance will be reduced by £1 for every £2 of the excess over £150,000 to a minimum of £10,000. As a result, individuals earning £210,000 or more (including pension contributions) can receive tax relief on a maximum of £10,000 worth of pension contributions.

The Bill contains anti-avoidance provisions designed to prevent individuals from reducing their income by making pension contributions under salary sacrifice, or flexible remuneration arrangements, made after 8 July 2015.

The annual allowance is measured over pension input periods (PIPs) which do not always match the tax year. Transitional arrangements for the 2015/16 tax year will be introduced to align PIPs with the tax year from 6 April 2016.

The Finance Bill sets out the transitional arrangements, under which tax year 2015/16 will be split into two tax years for the purposes of the annual allowance and the calculation of relief due. The legislation ensures that although tax year 2015-16 has been split into two for the purposes of the annual allowance, the period over which unused annual allowance can be carried forward is not reduced and remains at three full tax years.

From 6 April 2016, all PIPs will run from 6 April to 5 April, and the tapered annual allowance will apply. For those high earners remaining in defined benefit or similar hybrid schemes, it is likely that normal rates of accrual will generate an annual allowance charge each year.

Tax on lump sum pensions at death

The Autumn Statement 2014 announced changes to the tax payable on lump sums paid from an individual's pension fund on death. The tax charge had previously been 55 per cent but was reduced to 45 per cent from 6th April 2015. In the Finance Bill the Government has removed the 45 per cent tax charge on certain lump sum death payments made from a registered pension scheme if the individual dies aged 75 or above. From

6 April 2016 income tax will be payable at the marginal rate of tax of the recipient. The 45 per cent tax charge remains payable if the lump sum is made to a non-qualifying person i.e. a person who is not an individual, for example a trust.

The legislation introduced in the Finance Bill allows a taxable lump sum death benefit paid to a trust to be treated as income of the beneficiary who receives it. The beneficiary will be taxed at their marginal rate of income tax on the gross amount of the lump sum and can claim a deduction for the 45 per cent tax charge paid against their own income tax.

If the deceased died under the age of 75 the lump sum death benefits are usually exempt unless they are paid out more than two years after the scheme administrator became aware of the individual's death.

In the event of the pension holder's death over the age of 75 or if the individual died under age 75 and the lump sum is not paid within two years of the scheme administrator becoming aware of the death, the lump sum paid to a qualifying person is taxed on the recipient as pension income and tax will be collected under PAYE when paid from a registered pension scheme.

Dividend Taxation Reform

The Government have confirmed there will be a major reform of the taxation of UK dividends from April 2016. Currently dividends paid by a UK company include a 10 per cent notional tax credit. As a result, if a basic rate taxpayer receives dividend income there will be no income tax liability arising. A higher rate taxpayer pays an effective rate of 25 per cent income tax and an additional rate tax payer pays an effective rate of 30.5 per cent.

Following the reform dividend notional tax credits will be abolished from April 2016 and a new annual dividend tax allowance of £5,000 will be introduced. Dividend income in excess of this exempt amount will be taxed at rates of 7.5 per cent for basic rate taxpayers; 32.5 per cent for higher rate taxpayers and 38.1 per cent for additional rate taxpayers.

The Government has indicated that most individuals in receipt of dividend income will pay the same or less income tax however those with higher incomes receiving substantial dividends will pay more income tax. The introduction of this measure is to counteract tax planning involving companies taking advantage of reducing corporation tax rates and profits are extracted as dividends and not as a salary.

No detailed guidance has yet been published regarding the reform and is not expected until Finance Bill 2016. Additional detail will be required to determine the impact the new legislation will have on UK resident individuals receiving dividend from foreign companies. Foreign dividends currently receive a notional tax credit equivalent to the tax credit UK dividends receive and it would appear likely this credit may also be abolished for foreign dividend income.

Finance Costs Related to Residential Property Business

Paddy Doherty
Director

In the Budget, the Chancellor announced plans to restrict tax relief on certain costs incurred by individual landlords of residential property.

The most well published restriction was in relation to finance costs incurred by individuals in relation to buy to let property. In calculating taxable profits arising in respect of a residential buy to let business, the restriction operates by denying a tax deduction for finances costs. However, the individual taxpayer will be entitled to claim a tax reduction for such costs by reference to the basic rate of income tax.

According to HMRC guidance, it is not just mortgage interest to which the change in tax relief applies. As well as mortgage interest, finance costs include interest on loans to buy furnishings and fees incurred when taking out or repaying mortgages or loans. So the changes also apply to mortgage arrangement, booking and valuation fees.

The changes will be phased in from 6 April 2017 as follows:

Tax Year	% of costs allowed as tax deduction	% of costs relieved at basic rate of income tax
2017/18	75%	25%
2018/19	50%	50%
2019/20	25%	75%
2020/21 onwards	0%	100%

In practice this tax reduction will be calculated as 20% of the lower of the:

- finance costs not deducted from income in the tax year (25% for 2017 to 2018, 50% for 2018 to 2019, 75% for 2019 to 2020 and 100% thereafter);
- profits of the property business in the tax year; and
- total income (excluding savings income and dividend income) that exceeds the personal allowance and blind person's allowance in the tax year.

Any excess finance costs may be carried forward to following years if the tax reduction has been limited to 20% of the profits of the property business in the tax year.

The rationale behind this change is that the existing income tax relief puts individual landlords investing in a rental property at an advantage compared with ordinary homeowners. The measure is also intended to curb the rapid growth of buy-to-let mortgages.

HMRC estimate that these changes will affect one in five individual landlords.

Another change, is the removal of the 10% wear and tear allowance. Irrespective of whether they have spent money on repairing or replacing furnishings, this currently allows landlords to reduce the amount of tax they pay by deducting the allowance – which is equal to 10% of their annual rental income – from their rental income to arrive at the amount of income on which they pay tax. From 6 April 2016, the notional wear and tear allowance will be replaced by a new relief that only allows landlords to deduct actual costs of repairing or replacing furnishings.

Changes to Enterprise Investment Scheme and Venture Capital Trust Schemes

Jenny Sheridan
Director

Finance Bill 2015 includes a series of amendments to the Enterprise Investment Scheme (EIS) and Venture Capital Trust schemes (VCT) mainly to bring them in line with new EU rules on state aid.

The legislation makes some significant changes to the EIS income tax rules but makes no changes to the EIS Capital Gains deferral relief rules. In relation to the VCT rules, significant amendments have been made to the conditions for VCT approval as well as changes to the rules defining qualifying holdings.

Sunset Clause

Provisions are being introduced to restrict EIS and VCT relief to shares issued before 6 April 2025. There is, however, a provision which allows that date to be amended by Treasury order.

New lifetime limit

A £12 million cap (rather than £15 million cap as indicated in the spring Budget) will be introduced on the total investment a company and its subsidiaries can receive under tax advantaged venture capital schemes (broadly, SEIS, EIS, VCT and Social Investment Tax Relief). This limit will apply at the time of investment **and** for a further period following investment (broadly 3 years for EIS and 5 years for VCT). The purpose of these provisions is to stop an investee company exceeding the total investment limit by using EIS/VCT money for a company or trade that it acquires after it received the relevant EIS/VCT investment.

Age limit

Companies will generally only be eligible to receive EIS or VCT funding if they have made their first commercial sale within the last 7 years. This 7 year rule is stricter than the 12 years announced in the spring Budget. This rule will not apply where the total investment, including the current issue of shares, is at least 50 per cent of the company's average turnover, based on the preceding 5 years.

Prohibition – Existing trades

New rules announced will prohibit EIS and VCT funds from being used for the acquisition of existing businesses in a bid to ensure funds are properly directed to companies that need them to grow and develop. The new legislation prevents the following types of acquisitions from being a qualifying use of money – acquisition of a 51 per cent subsidiary interest, acquisition of a further interest in an existing 51 per cent subsidiary, a trade, intangible assets employed for the purposes of a trade and goodwill employed for the purposes of a trade.

Existing Shareholding Requirement

New provisions will require that individuals who claim EIS relief do not hold any other shares in the company other than founder shares or other risk finance investments (broadly shares subscribed for under EIS, SEIS or SITR).

Interaction with SEIS

Firstly, the previous requirement that at least 70 per cent of SEIS funds raised must be spent before EIS/VCT funding can be raised will be removed for qualifying investments made after 6 April 2015. This should facilitate greater interaction between the schemes which allow companies to go straight to market to raise entire financing requirement from both schemes, although SEIS and EIS shares still cannot be issued on the same day.

Secondly, EIS relief will no longer be clawed back if the company buys back or redeems shares held by SEIS investors who will lose their SEIS relief as a result of the buy back or redemption of their shares. This change takes effect in relation to any buy-back or redemption after 6 April 2014.

Knowledge Intensive Companies

The Finance Bill provisions reflect the following increased limits for Knowledge Intensive Companies to provide additional support to companies likely to particularly struggle to access finance:

Lifetime limit £20 million
(£12 million for other companies)

Age limit 10 years
(7 years for other companies)

Employee limit 500
(250 for other companies)

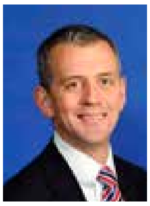
Knowledge Intensive Companies are specifically defined within the new legislation but broadly have relatively high research and development/ innovation spend (at least 10-15 per cent of operating costs) and meet either an 'innovation' condition involving the creation of IP or a 'skilled employee' condition involving highly skilled staff who have attained higher education qualifications.

Effective Date

The changes will take effect for investments made on or after Royal Assent, except for the changes to the interaction with SEIS which are effective from the dates noted above.

Corporate Debt

Changes to the Loan Relationship Rules for Corporates



Eamonn Donaghy
Partner

The taxation of corporate debt is dealt with under the "loan relationship" rules which were first introduced in 1996. Whilst these rules were rewritten into the Corporation Tax Act of 2009, they were not fundamentally changed. The main concept of the loan relationship rules is to derive the taxable profits and losses of corporate debt from the accounting treatment of such debt. However despite this, there is a lot of complexity in the rules especially around debt held within corporate groups or between connected parties. On top of this, there has been a significant number of changes which have been introduced mainly to counteract tax avoidance with respect to corporate debt and as a result the current legislation has become much more complex and unwieldy.

In the 2013 Budget, the Chancellor announced a review of the tax law governing both corporate debt and derivatives. The aim of this review was to both simplify the existing legislation and to take account of upcoming changes to accounting treatment which were being introduced by new UK GAAP and amendments to IFRS.

Following a detailed consultation process new legislation is being introduced in the current Finance Bill which is aimed at reducing the existing complexity and provide additional protection against tax avoidance whilst at the same time remaining true to the concept of taxable profits being based on accounting profits.

The new legislation will take effect from 1 January 2016. However the new rules that deal with corporate rescue and anti-avoidance will take effect from the date of Royal Assent which is expected to take place in late September or early October.

Turning to the main changes contained within the Finance Bill:

Accounting treatment

New rules are being introduced which will clarify the relationship between the tax treatment of loan relationships and the accounting treatment of loan relationships. The new rules confirm that an amount will only be taxable if it is based on amounts recognised in the accounts as items of profit or loss. However the new rules make it clear that this will include amounts that were previously recognised in other comprehensive income and which were subsequently transferred to profit or loss. There are also new rules dealing with the profits and losses from loan relationships which are capitalised in the carrying value of an asset or liability.

Debt release

New rules have been introduced dealing with the tax treatment of debt releases. A new provision will apply which will exempt a credit arising from the release of a debt where there is a material risk that within 12 months of release the debtor company will be unable to pay its debts. This rule will be in addition to the existing relief applicable for debt for equity swaps. A similar relief will apply to debt reorganisations which result in an accounting profit arising. Such profit will not be taxable if there is a material risk that within 12 months the debtor will be unable to pay its debts. There are also changes to the rules dealing with impairment of connected party debts which amends the rules on deemed releases when a connected party acquires a debt at a discount. The deemed release will not be taxable if there is a material risk that the company will not be able to pay its debts.

Anti-avoidance

New rules are being introduced that will act as a Targeted Anti-Avoidance Rule (TAAR). Some existing avoidance legislation is removed to make way for the new anti-avoidance measures. The new rules are aimed at counteracting "loan related tax advantages" arising from "relevant avoidance arrangements" by way of a just and reasonable adjustment to the resultant debits or credits. The legislation confirms that arrangements that are aimed at obtaining a tax advantage which can reasonably be assumed to have been intended under the loan relationship legislation will not be excluded by the new rules. There is also a non-exhaustive list of examples of transactions that are unlikely to be excluded from the anti-avoidance rules. Once again, these examples will only be relevant if it is reasonable to assume that the result in question was not the anticipated outcome when the relevant provisions were enacted.

All in all, whilst the loan relationship legislation remains complex, the amendments resulting from the Finance Bill should both simplify and clarify the existing rules. The extension of the corporate rescue reliefs are a welcome addition to the tax code. However as with all anti-avoidance legislation, an element of uncertainty will still be applicable with respect to complex transactions and whether they fall within the new anti-avoidance rules.

Corporation Tax

David Nelson
Partner

Intangible assets

Back in 2002 the Government introduced a special tax regime for intangible assets which broadly facilitated corporation tax relief for the amortisation or impairment of goodwill and other qualifying intangible assets. At the time, this was a welcome addition to the UK corporation tax system and one which the Government claimed was designed "to enhance the position of the UK as an attractive environment in which and from which to do business". In the Autumn Statement 2014, the Chancellor announced several changes to this tax regime to prevent perceived tax avoidance. These changes were largely designed to prevent corporation tax deductions being claimed for goodwill on the incorporation of businesses (something which arguably the original rules did not intend). However in a surprising and unexpected move, the Chancellor has now introduced measures in Finance Bill 2015 to eliminate tax relief for purchased goodwill altogether as from 8 July 2015. As the announcement was hidden away towards the bottom of the list of Budget changes on the relevant GOV.UK webpage many Budget commentaries missed it for this reason.

From 8 July 2015 a company acquiring a business (via trade and assets rather than via shares) will no longer be able to claim corporation tax relief as it writes down the value of "purchased goodwill" or associated "customer related intangibles" such as customer lists as well as unregistered trademarks. Some relief may still be available if and when the goodwill is sold at a loss, but in another surprising twist, the Chancellor has included measures in Finance Bill 2015 to ensure that such a loss will be treated as a 'non-trading debit' for tax purposes thus eliminating the existing potential for relief as a 'trading loss' against future trading profits. Non-trading losses can only be group relieved or carried forward for use against future non-trading profits or gains; with the result that the change could mean many such losses remain unutilised.

The good news is that those companies who have acquired goodwill or intangible assets before 8 July 2015 (or who are under an unconditional contract to do so at that date) will be able to continue to claim corporation tax relief for their amortisation and impairment. And just to be clear, tax relief will still be available for other intangible assets which are not goodwill or customer related intangibles as defined – e.g. for purchased trademarks, patents, and other forms of registered intangible assets.

So why, all of a sudden, do we have a complete Government u-turn on tax policy when it comes to goodwill, especially when the Autumn Statement 2014 measures would have prevented much of the perceived tax avoidance? The answer is not clear but the Budget announcement gives the following explanation "The current rules allow corporation tax profits to be reduced following a merger or acquisition of business assets and can distort commercial practices and lead to manipulation and avoidance. Removing the relief brings the UK regime in line with other major economies, reduces distortion and levels the playing field for merger and acquisition transactions" (which is presumably a reference to share acquisitions where no tax relief is available for the cost of acquiring shares). But weren't the 2002 rules specifically designed to enhance the UK's attractiveness for businesses compared to other countries, and wasn't a large part of this attractiveness due precisely to the availability of tax relief for goodwill? However, with the removal of tax relief for purchased goodwill, there will no longer be the irreconcilable tension between vendors wishing to sell shares (to obtain entrepreneurs relief?) but purchasers wishing to buy assets (to obtain tax relief for goodwill?). To this extent at least, the Chancellor's surprise move may achieve its objective.

Other corporation tax measures

Apart from the changes to intangible assets and to loan relationships (covered by the previous article herein), most of the other corporation tax measures in Finance Bill 2015 are relatively minor and of limited application; they include:

- Restrictions to prevent universities and charities from claiming the Research and Development Expenditure Credit (RDEC) as from 1 August 2015
- Minor changes to the Controlled Foreign Companies (CFC) regime to prevent CFC charges being reduced or eliminated by UK loss offsets after 8 July 2015
- Changes to impose market value adjustments on trading stock not sold in the course of trading or on cessation, and on the transfer of intangible assets to related parties, on or after 8 July 2015
- Relaxation of consortium relief rules to ensure the link company no longer needs to be in the UK or in the EEA for accounting periods commencing on or after 10 December 2014
- Changes to tighten the rules for designated currency elections by investment companies for accounting period commencing on or after 1 January 2016.

Administration and Enforcement

In 2013-14, around 90 per cent of total tax revenue was paid on time, with 10 per cent remaining unpaid at the due date. This 10 per cent equated to approximately £50 billion, and so it is perhaps understandable that the Treasury are introducing new rules to facilitate more direct action against taxpayers who refuse to settle their debts on time.

Mark Hood
Director

The Finance Bill is introducing new provisions to allow HMRC to enforce payment of outstanding debts by way of collection direct from a taxpayer's (i.e. the debtor) bank and building society accounts. The process is known as the Direct Recovery of Debts (DRD).

As such action effectively bypasses the taxpayer, there are a number of safeguards which will be built into the legislation in order to protect the taxpayer's position in various circumstances.

The DRD process will apply to a "relevant sum", where such a sum is at least £1,000 and is either an established debt (broadly, a debt for which there is no further right of appeal) or is due under the Accelerated Payment Legislation introduced in FA 2014.

HMRC must also be satisfied that the debtor is aware that the sum is due and payable – this will be achieved by way of a face-to-face visit. The debtor must also have been identified as being not vulnerable.

Where a debtor is to be brought within the DRD mechanism, HMRC will issue an "information notice" to deposit-takers (i.e. banks and building societies), if it appears that the debtor holds one or more accounts with such institutions. The information notice requires the deposit-taker to provide HMRC with prescribed information about accounts held by the debtor. Subsequent to this, HMRC will issue a "hold notice" to the deposit taker, which will set out the relevant sum in respect of which the notice has effect, together with a "safeguarded amount" and the order of priority of accounts subject to the notice (joint accounts being given lower priority).

The safeguarded amount will generally be a minimum of £5,000 and must continue to be available to the debtor whilst the hold is in place. If there is money left in the accounts above the safeguarded amount, a hold is placed on this credit balance up to the amount of the relevant sum (i.e. the debt due to HMRC). The deposit taker must then inform HMRC, who must then provide a copy of the hold notice to the debtor.

A debtor can raise an objection to the hold notice within a period of 30 days. There are a number of potential grounds for objection, including that the hold notice will cause exceptional hardship to the debtor or an interested third party. HMRC must deal with objections within 30 days. If the objection is not upheld by HMRC, the debtor can subsequently appeal to the County Court (again within a period of 30 days from the day on which the debtor was given notice by HMRC of the outcome of the objection) on the grounds that the hold notice is causing undue hardship.

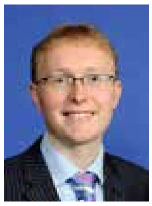
If the Court rejects the appeal, or in cases where there is no longer any possibility of objections or appeals to the hold notice, HMRC can issue a "deduction notice" to the deposit taker, which will require the deposit taker to deduct and pay a qualifying amount (which will be an amount not exceeding the held amount) by a specified date. The legislation will also include provisions for penalties to be issued to deposit takers if they fail to comply with either an information notice, a hold notice or a deduction notice.

According to the Treasury, the DRD rules should affect only a small minority of taxpayers who still refuse to pay what they owe, despite having the money to do so. It is presumably HMRC's view that the introduction of this new legislation will change taxpayers' behaviour so that they pay all due amounts to HMRC on time, rather than being subject to the hold and deduction notices which HMRC will be able to issue.

Further measures will also be introduced to support the Government's offshore evasion strategy, under which financial intermediaries and tax advisers will be obliged to notify clients about various matters including the Common Reporting Standard (under which the UK will begin to receive information on offshore accounts and financial assets from 2017), together with the penalties for evasion and the opportunity to disclose previous evasion to HMRC. This can be seen as widening the ambit of the current requirements to disclose tax avoidance schemes and is something which tax advisers will need to carefully focus on in the coming months.

Financial Services Tax

Reflecting the focus of the UK Financial Services Industry, the main FS related measures impacted Banks and Investment Managers.



Ian Lockington
Partner

Main measures for Banks – Bank Levy and profits surcharge

- In a move away from recent practice, and perhaps due to some UK headquartered banks indicating that scale of the Bank Levy charges, and regular unannounced increases were prompting them to look at leaving the UK the Chancellor announced that he will reduce the full bank levy rate from 0.21% to 0.18% in 2016, 0.17% in 2017, 0.16% in 2018, 0.15% in 2019, 0.14% in 2020 and 0.10% in 2021. As the rate was only raised to 0.21% via the March 2015 Budget this seems to be swift action to retain the UK's competitive position in Financial Services. In addition, it was announced that the Government will also legislate in this Parliament to change the tax base of assets subject to the Bank Levy to UK operations from 1 January 2021.
- An 8% surcharge is to be levied on the profits of banking companies (defined as for the loss restriction rules) from 1 January 2016, to the extent these exceed a group allowance of £25 million.

  The legislation effectively creates a corporation tax ring fence regime for banking companies, as the surrender of group relief from non-banking companies is ignored for the purposes of the surcharge, as are pre 1 January 2016 losses (including capital losses) carried forward in banking companies. Finally a targeted anti-avoidance rule (TAAR) attacks arrangements designed to effectively move significant parts of the profits of banking companies outside the scope of the surcharge. This means that groups carrying on identical activities may be very differently affected by the regime, depending on how those activities are split between legal entities. The concern of those groups on the losing end of such comparisons is the extent to which the TAAR will limit attempts to re-level the playing field through restructuring.

  Also of significance is the fact that the surcharge will be taken into account for the purposes of determining whether there is an 'effective tax mismatch' – potentially drawing intra-UK provisions between banking and non-banking companies within the scope of the DPT regime.

Main Measures for Investment Managers – carried interest

The Finance Bill seeks to end what is commonly known within the private equity industry as 'base cost shift' (see below) in respect to carried interest – so increasing the UK capital gains tax paid on carried interest. The definition of carried interest is wide-ranging and the changes may also affect participants in investment structures that have adopted a partnership model similar to the private equity industry. Broadly, 'base cost shift' describes the effect of carried interest holders historically sharing the base cost of fund investments. As they did not suffer the original cost they often benefitted from having a taxable gain lower than their economic gain. The new rules put an end to what has been a long standing and accepted tax treatment of carried interest. In addition, the rules provide that carried interest should only be treated as a foreign chargeable gain to the extent that the carry recipient performs his/her services outside of the UK. This is likely to be a significant change for some carry recipients who are currently taxable on the remittance basis.

The rules operate so that, going forward, where carried interest arises due to the disposal of an underlying fund asset, carry recipients will be taxed on a gain equal to their proceeds received. Where carry arises in any other circumstance, the proceeds will be taxed as a capital gain and the carry recipients will also be taxed on their underlying allocation of profits, with measures to allow for relief for double taxation. The carry recipients also get relief for amounts paid for their carry or assessed as an employment benefit when the carry was awarded to them. The rules affect amounts arising on or after 8 July 2015. Applying the new rules is likely to be complicated and HMRC guidance will be important.

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