

# Budget 2010

## BUDGET NOTES

22 June 2010

Budget Notes contain technical information additional to the press notices issued by HM Treasury with the Budget. They are not the same as press notices, which are primarily used as brief explanations of new policy for the media, but rather contain additional, more detailed information on the changes to tax law announced in the Budget. As such they are designed to assist businesses that may be immediately affected by the changes, and to provide more technical information to those with a specialist interest such as tax consultants and advisers, City financial institutions and local HM Revenue & Customs offices. This information is also published on the Treasury and HM Revenue & Customs internet sites. Contact details for each note were correct at the time of publication. Please refer to HMRC's individual web versions as these are updated as required.

### CONTENTS:

<b>BN</b>	<b>Budget Note</b>	<b>Page</b>
1	The Personal Allowance, Basic Rate Limit and National Insurance Thresholds for 2011-12	5
2	Corporation Tax Main Rates	7
3	Corporation Tax Small Profits Rates	9
4	Capital Allowances: Rate and Annual Investment Allowance Changes	11
5	Zero-Emission Goods Vehicles: 100 Per Cent First-Year Allowances	13
6	Capital Distributions	15
7	Relief for Interest: Amendments to the "Worldwide Debt Cap" Legislation	17
8	Research and Development Tax Relief	19
9	Oil and Gas Fiscal Regime	21
10	Enterprise Management Incentives	25
11	Venture Capital Schemes	27
12	Film Tax Relief: Multi Year Claims	29
13	Changes to the Rules on the Deduction of Income Tax at Source	31
14	Consortium Relief	33
15	Life Insurance Companies: Changes to Tax Rules	35
16	Corporation Tax Avoidance: Authorised Investment Funds	39
17	Loan Relationships: Anti-Avoidance	41
18	UK Real Estate Investment Trusts and Stock Dividends	43
19	Insurance Premium Tax: Increase in the Standard Rate and Higher Rate	45
20	Capital Gains Tax: Rates and Entrepreneurs' Relief	47
21	Indexing Individual Savings Account Limits from 2011	51
22	Transitional Measure Deferring the Effective Requirement to Buy an Annuity to Age 77	53
23	Pensions Taxation: NEST	55

24	Tax Changes for Certain Trusts Compensating Asbestos Victims	57
25	Income Tax Adjustments Between Settlers and Trustees	59
26	Income Tax: Special Guardianship Orders and Residence Orders	61
27	Income Tax Relief for Shared Lives Carers	63
28	Capital Gains Tax: Private Residence Relief and Adult Placement Carers	67
29	Capital Allowances Rules for Qualifying Carers	69
30	Expenses Paid to MPs	71
31	Seafarers' Earnings Deduction: EU and EEA Residents	73
32	Landfill Tax: Criteria for Determining Material to be Subject to the Lower Rate	75
33	Aggregates Levy: Northern Ireland Credit Scheme	77
34	Tobacco Products Duty: Long Cigarettes	79
35	Relief for Overpayments of Stamp Duty Land Tax and Petroleum Revenue Tax	81
36	Interest Harmonisation for Corporation Tax and Petroleum Revenue Tax	83
37	Review of HMRC Powers, Deterrents and Safeguards: Penalties for Late Filing of Returns and Payment of Tax	85
38	Review of HMRC Powers, Deterrents and Safeguards: Excise Modernisation and Compliance Checks	89
39	VAT: Change to Zero-Rating of "Qualifying" Aircraft	93
40	VAT: Place of Supply of Gas, Heat and Cooling	95
41	VAT: Postal Services	97
42	VAT: Lennartz Accounting: Restricting Application and Securing Revenue	99
43	VAT: Change of Standard Rate	101
44	VAT: Change of Standard Rate: Anti-Forestalling Legislation	103
45	VAT Flat Rate Scheme: Changes to the Flat Rate Thresholds and Percentages	105

## **HM REVENUE & CUSTOMS PRESS OFFICE**

Press enquiries: 020 7147 2328 / 0798 (Business Tax Desk)  
020 7147 2318 / 0051/ 2331 (Individuals Desk)  
020 7147 0052 / 0394 (Family & Law Enforcement Desk)  
07860 359544 (Out of hours)

## **GOVERNMENT DEPARTMENT INTERNET SITES**

Further information and all published documents relating to the Budget may be found on the Internet at the following addresses:

HM Treasury: [www.hm-treasury.gov.uk](http://www.hm-treasury.gov.uk)

HM Revenue & Customs: [www.hmrc.gov.uk](http://www.hmrc.gov.uk)



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## THE PERSONAL ALLOWANCE, BASIC RATE LIMIT AND NATIONAL INSURANCE THRESHOLDS FOR 2011-12

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### Who is likely to be affected?

1. Income tax payers, employers, employees and the self employed.

### General description of the measure

2. Legislation will be introduced to provide for the following income tax and National Insurance Contributions (NICs) changes for 2011-12:
  - the personal allowance for those aged under 65 will be increased by £1,000 to £7,475;
  - the basic rate limit will be reduced so that higher rate taxpayers do not benefit from the increase in the personal allowance. The exact figure will be confirmed when September's Retail Prices Index (RPI) is known;
  - the alignment of the Upper Earnings/Profits Limit (UEL/UPL) with the higher rate threshold (the total of the personal allowance for those aged under 65 and the basic rate limit) will be maintained by reducing the UEL/UPL; and
  - the secondary threshold, which is the point at which employers start to pay Class 1 NICs, is to be increased by an extra £21 per week above indexation.

### Operative date

3. These changes will have effect on and after 6 April 2011.

### Current law and proposed revisions

4. Existing legislation requires the Government to increase personal allowances and rate limits by the annual percentage increase to the RPI for the year to September preceding the new tax year. The Government will make the Order to set the relevant amounts for 2011-12 after the relevant percentage is published in October 2010.
5. The Government has announced that for 2011-12 it will over-ride the amounts that will be set in the Order for the personal allowance for those aged under 65 and the basic rate limit. Decisions on other allowances will be made at the appropriate time. The exact amounts of the basic rate limit for 2011-12 will not be known until publication of the RPI for September.

6. The personal allowance provides an amount of tax free income. An individual is liable to basic rate tax on their taxable income up to the basic rate limit. Above the basic rate limit, higher rate tax is payable up to the higher rate limit. Above the higher rate limit, additional rate tax is payable.
7. For National Insurance, the secondary threshold will rise by £21 a week above the level that indexation would reach. The secondary threshold for 2011-12 will not be known until publication of the RPI for September. The secondary threshold change is in addition to the increase in the primary (employee) threshold already planned for 2011-12, and the 1 per cent rise in rates.

### **Further advice**

8. Examples of how these changes affect the amount of tax and NICs that individuals will pay will be published on the HM Revenue & Customs website when the amounts of the basic rate limit and UEL/UPL for 2011-12 are known.
9. If you have any questions about this change in connection with NICs, please contact Hasan Mustafa on 020 7147 2508 (email: [hasan.mustafa@hmrc.gsi.gov.uk](mailto:hasan.mustafa@hmrc.gsi.gov.uk)). If you have any other questions about this change, please contact Paul Thomas on 020 7147 2479 (email: [paul.thomas@hmrc.gsi.gov.uk](mailto:paul.thomas@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## CORPORATION TAX MAIN RATES

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### Who is likely to be affected?

1. Companies with profits above the upper limit (£1.5 million).

### General description of the measure

2. Legislation will be introduced in Finance Bill 2010 to set the main rate of corporation tax (CT) at 27 per cent on and after 1 April 2011.
3. The main rate of CT for companies with profits, arising on and after 1 April 2011, from oil extraction and oil rights in the UK and the UK Continental Shelf ("ring fence profits") will remain at 30 per cent.

### Operative date

4. This change in the main rate of CT will have effect on and after 1 April 2011.

### Current law and proposed revisions

5. Where companies have profits above the upper limit, the whole of those profits are chargeable to the main rate of CT. Section 2 of the Finance Act 2010 set the main rate on and after 1 April 2011 at 28 per cent for companies with profits other than ring fence profits and at 30 per cent for companies with ring fence profits. The main rate of CT needs to be set in advance. This is because companies paying at this rate have to pay some of their CT by in-year instalments.
6. Finance Bill 2010 will reduce the main rate of CT for non-ring fence profits to 27 per cent on and after 1 April 2011. There will be further reductions to 24 per cent by 1 April 2014. The main rate of CT for ring fence profits will remain at 30 per cent.

### Further advice

7. If you have any questions about this change, please contact Andrea Pierce on 020 7147 2591 (email: [andrea.pierce2@hmrc.gsi.gov.uk](mailto:andrea.pierce2@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)



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## CORPORATION TAX SMALL PROFITS RATES

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### Who is likely to be affected?

1. Companies with profits below the lower limit (£300,000).

### General description of the measure

2. Legislation will be introduced in Finance Bill 2011 to set the small profits rate (SPR) of corporation tax (CT) at 20 per cent on and after 1 April 2011.
3. The SPR for companies with profits, arising on and after 1 April 2011, from oil extraction and oil rights in the UK and the UK Continental Shelf ("ring fence profits") will remain at 19 per cent.

### Operative date

4. This change in the SPR will have effect on and after 1 April 2011.

### Current law and proposed revisions

5. Where companies (that are not a closed investment-holding company) have profits below the lower limit, the whole of those profits are chargeable to the SPR of CT. Section 3 of the Finance Act 2010 set the SPR on and after 1 April 2010 at 21 per cent for companies with profits other than ring fence profits and at 19 per cent for companies with ring fence profits.
6. Finance Bill 2011 will reduce the SPR for non-ring fence profits to 20 per cent on and after 1 April 2011. The SPR for ring fence profits will remain at 19 per cent.

### Further advice

7. If you have any questions about this change, please contact Andrea Pierce on 020 7147 2591 (email: [andrea.pierce2@hmrc.gsi.gov.uk](mailto:andrea.pierce2@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)



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## CAPITAL ALLOWANCES: RATE AND ANNUAL INVESTMENT ALLOWANCE CHANGES

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### Who is likely to be affected?

1. Businesses investing in plant and machinery.

### General description of the measure

2. Legislation will be introduced in a future Finance Bill to make the following changes:
  - first, to reduce the rates of writing-down allowances (WDAs) for new and unrelieved expenditure on plant and machinery:
    - from 20 per cent to 18 per cent per annum for expenditure allocated to the main rate pool; and
    - from 10 per cent to 8 per cent per annum for expenditure allocated to the special rate pool; and
  - second, to reduce the maximum amount of the annual investment allowance from the current limit of £100,000 to a new limit of £25,000.

### Operative date

3. The first measure will have effect for the calculation of WDAs for chargeable periods ending on or after 1 April 2012 for businesses within the charge to corporation tax (CT) and on or after 6 April 2012 for businesses within the charge to income tax.
4. The second measure will have effect from April 2012. Details of the transitional arrangements will be published, along with the relevant draft legislation, in good time before the reduction takes effect.

### Current law and proposed revisions

#### WDAs

5. Capital allowances allow business to write off the costs of capital assets, such as plant and machinery, against their taxable income. They take the place of commercial depreciation, which is not allowed for tax. The general rate of plant and machinery WDA is currently 20 per cent per annum on a reducing balance basis. For special rate expenditure the rate of plant and machinery WDA is currently 10 per cent per annum on a reducing balance basis. Special rate expenditure includes expenditure on long-life assets, thermal insulation, integral features and expenditure incurred on or after 1 April 2009 on cars with CO<sub>2</sub> emissions of more than 160g/km.

6. The main rate of WDA will be reduced from 20 per cent to 18 per cent and the special rate from 10 per cent to 8 per cent from 1 April 2012 (CT) or 6 April 2012 (income tax). The rate changes will have effect from a fixed date, so for those businesses where the chargeable period spans the change date hybrid rates will have effect for the whole of that transitional chargeable period.
7. Oil and gas ring fence activities will retain their existing capital allowances treatment.

### Hybrid rates

8. For businesses whose chargeable period spans 1 April (CT) or 6 April (income tax), a hybrid rate will have effect for unrelieved expenditure in any pool, including single asset pools. There will be two hybrid rates:
  - one for any expenditure that qualifies for the current 20 per cent WDA; and
  - the other for any expenditure that qualifies for the current 10 per cent WDA.
9. The hybrid rate will be arrived at by calculating the proportion of a chargeable period falling before the change date and the corresponding proportion falling after the change date. For example, if a company's chargeable period began on 1 January 2012 and ends on 31 December 2012, about one quarter of that period would fall before the date of change (on 1 April 2012) and about three quarters would fall after that date.
  - The calculation of the hybrid rate for the main rate of WDAs would therefore be as follows:

$$\begin{array}{rcl} 91/366 \times 20\% & = & 4.97\% \\ \text{Plus } 275/366 \times 18\% & = & \underline{13.52\%} \end{array}$$

**Therefore, hybrid main rate for transitional period = 18.49%**

(Note: in the context of the last rate change, the legislation contained an explicit rule that, where there would be a figure with more than two decimal places, it is always rounded up in the taxpayer's favour.)

- The calculation of the hybrid rate for the special rate of WDAs would be as follows:

$$\begin{array}{rcl} 91/366 \times 10\% & = & 2.49\% \\ \text{Plus } 275/366 \times 8\% & = & \underline{6.01\%} \end{array}$$

**Therefore, hybrid special rate for transitional period = 8.50%**

### **Further advice**

10. If you have any questions about this change, please email [joy.guthrie@hmrc.gsi.gov.uk](mailto:joy.guthrie@hmrc.gsi.gov.uk) or [malcolm.smith3@hmrc.gsi.gov.uk](mailto:malcolm.smith3@hmrc.gsi.gov.uk) or telephone 020 7147 2610. Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## ZERO-EMISSION GOODS VEHICLES: 100 PER CENT FIRST-YEAR ALLOWANCES

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### Who is likely to be affected?

1. Businesses that purchase new zero-emission goods vehicles.

### General description of the measure

2. This measure will provide a 100 per cent first-year allowance (FYA) for business expenditure on new and unused (not second hand) zero-emission goods vehicles.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. This measure will have effect for a period of five years for expenditure incurred on new zero-emission goods vehicles on or after 1 April 2010 for businesses within the charge to corporation tax (CT) and on or after 6 April 2010 for businesses within the charge to income tax.

### Current law and proposed revisions

5. Capital allowances allow business to deduct the costs of capital assets, such as plant and machinery, against their taxable income. They take the place of commercial depreciation, which is not allowed for tax.
6. Any expenditure not covered by a claim to the annual investment allowance, or a FYA, will be dealt with in the normal capital allowances regime, entering either the main pool or special rate pool, where it will attract writing-down allowances (WDAs) at the appropriate rate.
7. Expenditure incurred on a new (and not second hand) zero-emission goods vehicle will qualify for the new 100 per cent FYA if:
  - the vehicle cannot under any circumstances produce CO<sub>2</sub> emissions when driven;
  - it is of a design primarily suited to the conveyance of goods or burden; and
  - the expenditure is incurred on or after 1 April 2010 and before 1 April 2015 for businesses within the charge to CT and on or after 6 April 2010 and before 6 April 2015 for businesses within the charge to income tax.

8. As with existing FYAs, the general exclusions in section 46 of the Capital Allowances Act 2001 will apply to the new FYA; this includes the exclusion of expenditure on assets for leasing.
9. In order to comply with State aid rules (see *Commission Regulation (EC) No 800/2008, General Block Exemption Regulation*) a number of additional conditions will also apply to the new FYA. In particular, the FYA will not be available to a business:
  - in difficulty for the purposes of the *Community Guidelines on State Aid for Rescuing and Restructuring Firms in Difficulty (2004/C 244/02)*;
  - subject to an outstanding recovery order following a European Commission decision declaring an aid illegal;
  - engaged in the fisheries and aquaculture sectors, as covered by Council Regulation (EC) No 104/2000; or
  - managing waste for other undertakings for the purposes of Directive 2008/98/EC (for example, a waste collector contracting with a local authority, or large retail business, to provide an integrated waste management service).
10. The amount of expenditure that will qualify for the new FYA is limited to €85 million per undertaking over the five year life of the measure. For example, qualifying expenditure by a group of companies would be limited to a maximum of €85 million for the group as a whole over the five year life of the scheme. Similar rules will also apply to the unincorporated.

#### **Further advice**

11. Further details will be published alongside the Finance Bill.
12. This measure was previously announced at Budget 2010 and a version of this note was published as BN42. This note supersedes that version.
13. If you have any questions about this change, please contact Nick Williams on 020 7147 2541 (email: [nicholas.williams@hmrc.gsi.gov.uk](mailto:nicholas.williams@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## CAPITAL DISTRIBUTIONS

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### Who is likely to be affected?

1. UK companies in receipt of distributions.

### General description of the measure

2. This measure will clarify the corporation tax (CT) treatment of certain distributions received by UK companies.
3. Distributions within the definition in Part 23 of the Corporation Tax Act (CTA) 2010 will not be prevented from falling within the distribution exemption regime for companies introduced in Finance Act (FA) 2009 by virtue only of being “of a capital nature”.
4. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

5. The legislation will have retrospective effect, but companies will be able to elect for the legislation not to apply retrospectively.

### Current law and proposed revisions

6. FA 2009 introduced Part 9A of CTA 2009, which extended the scope of exemption from CT for distributions received by UK companies. Distributions other than capital distributions paid by UK resident companies (UK distributions) have been exempt distributions for many years. The legislation in Part 9A extended the exemption to foreign distributions but excluded distributions of a capital nature.
7. Until recently, established practice has been to treat UK distributions as being of an income nature subject only to some specific exceptions. Clarification of the law made by the Income Tax (Trading and Other Income) Act 2005 made this treatment impossible to sustain. This development went unnoticed, and HM Revenue & Customs (HMRC) did not change its practice until after the introduction of the exemption regime in FA 2009.
8. The measure will ensure that distributions within the definition in Part 23 of CTA 2010 will not be prevented from falling within the exemption regime solely because they are of a capital nature.

9. The existing rule that limits the application of the distribution exemption regime to distributions of an income nature will be removed. This change will have effect for all distributions made on or after 1 July 2009.
10. The new legislation will also make clear that distributions made out of reserves arising from a reduction in capital are distributions within the definition in Part 23 of CTA 2010. This change will have full retrospective effect for distributions by UK-resident companies, and will apply to distributions made on or after 1 July 2009 by non-UK resident companies.
11. Recipient companies will be able to opt for the retrospective effects of this legislation not to apply.
12. The definition of distribution in Part 23 of CTA 2010 also applies for certain income tax purposes. In consequence, the clarification (mentioned at paragraph 9 above) in relation to distributions from reserves arising from capital reductions will have effect for income tax purposes where the distributing company is UK-resident. However, the application of this clarification for income tax purposes will only have effect in respect of distributions made on or after 22 June 2010.

### **Further Advice**

13. This measure was previously announced at Budget 2010 and a version of this note was published as BN05. This note supersedes that version.
14. Draft legislation and an accompanying explanatory note have been published today on the HMRC website.
15. If you have any questions about this change, please contact Andrew Page on 020 7147 2673 (email: [andrew.page@hmrc.gsi.gov.uk](mailto:andrew.page@hmrc.gsi.gov.uk)) or Steve Denyer on 020 7147 0330 (email: [stephen.denyer@hmrc.gsi.gov.uk](mailto:stephen.denyer@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## RELIEF FOR INTEREST: AMENDMENTS TO THE “WORLDWIDE DEBT CAP” LEGISLATION

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### Who is likely to be affected?

1. Large groups of companies (but not banking or insurance groups).

### General description of the measure

2. The “worldwide debt cap” was introduced last year to guard against excessive debt funding of UK companies. The legislation, which has now been rewritten into Part 7 of the Taxation (International and Other Provisions) Act 2010, does this by restricting relief for UK financing costs where these exceed the financing costs of the worldwide group.
3. As a result of consultation with businesses and their advisers on the practical application of the debt cap, a number of changes have been identified that either ensure the rules work as originally intended or meet concerns expressed by representatives of particular industries.
4. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

5. The debt cap legislation as a whole applies to periods of account of the worldwide group beginning on or after 1 January 2010, and with one exception, the changes will apply from that date. The exception is the extension of the scope of “relevant assets” and “relevant liabilities” for the gateway test, where groups may elect for the change to apply only prospectively.

### Current law and proposed revisions

6. This measure will make fourteen separate changes. One group of changes ensures that, where a UK figure is being compared with a worldwide figure, the same amount is included in both figures in respect of the same borrowing. The following changes fall within this group:
  - in the “gateway test” (which filters out groups from the main debt cap rules), the UK measure of debt is to be adjusted where a mismatch would otherwise occur;
  - regulation-making powers are included that will enable similar mismatches, arising in connection with the main debt cap rules, to be resolved through secondary legislation; and
  - the mismatch that may arise where borrowing is carried out by a partnership will be corrected.

7. Other proposed amendments specifically affect securitisation companies. Companies within the special corporation tax regime for securitisation companies introduced by Finance Act 2005 will be excluded from the main debt cap rules, including exclusion of their financing expenses when computing the worldwide group's cost of finance (the "available amount"). In addition, there will be a power to make regulations that would allow a company involved in capital market arrangements to transfer any additional tax liability as a result of the debt cap to another company in the group.
8. The other changes that are being made are as follows:
  - the assets and liabilities of companies that are taken into account for the "gateway test" will include long-term arrangements that have the economic effect of loans;
  - a minor expansion of the definition of "financial instrument" when determining whether a financial services group is excluded from the debt cap;
  - preventing groups from allocating a debt cap disallowance to a dual resident investing company;
  - including guarantee fees in the financing income of a company;
  - correcting a drafting error relating to group treasury companies;
  - distributions made by industrial and provident societies will be excluded from the financing expenses of such companies;
  - exclusion of interest paid to a non-departmental public body;
  - clarifying the meaning of "ancillary expenses" in the definition of the available amount; and
  - introducing two restrictions on entities that can be the "ultimate parent" of a group of companies.

#### **Further advice**

9. This measure was previously announced at Budget 2010 and a version of this note was published as BN06. This note supersedes that version.
10. If you have any questions about these changes, please contact Lesley Hamilton on 020 7147 2564 (email: [lesley.hamilton@hmrc.gsi.gov.uk](mailto:lesley.hamilton@hmrc.gsi.gov.uk)) or Sarah Mulkerins on 020 7147 0676 (email [sarah.mulkerins@hmrc.gsi.gov.uk](mailto:sarah.mulkerins@hmrc.gsi.gov.uk)) Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## RESEARCH AND DEVELOPMENT TAX RELIEF

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### Who is likely to be affected?

1. Companies that are small or medium enterprises (SMEs) claiming enhanced tax relief for expenditure on research and development (R&D). For the purpose of the R&D relief, the SME thresholds are higher than those set out by the European Commission (500 employees, annual turnover of €100 million and balance sheet total of €86 million rather than 500, €50 million and €43 million respectively).

### General description of the measure

2. This measure will abolish the condition requiring that any intellectual property deriving from the R&D to which the expenditure is attributable be owned by the company making the claim.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. The change will have effect for any expenditure incurred by a SME company on R&D in an accounting period ending on or after 9 December 2009.

### Current law and proposed revisions

5. The enhanced tax relief for R&D is in Part 13 of the Corporation Tax Act 2009 (CTA). The rules applying to companies which are SMEs are in Chapter 2.
6. Currently, sections 1052 and 1053 of CTA require, among other conditions, that any intellectual property created as a result of the expenditure to which the R&D is attributable is, or will be, vested in the company.
7. Sections 1071 and 1072 of CTA apply the same condition where a company which is a SME applies under the rules for large companies, because the expenditure is excluded from the SME relief by virtue of being subsidised.
8. This condition will be removed.

## **Further advice**

9. This measure was previously announced at the 2009 Pre-Budget Report and a version of this note was published as PBRN06. This note supersedes that version.
10. If you have any questions about this change, please contact Neil Smillie on 020 7147 0864 (email: [neil.smillie@hmrc.gsi.gov.uk](mailto:neil.smillie@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## OIL AND GAS FISCAL REGIME

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### Who is likely to be affected?

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

### General description of the measure

2. Finance Act (FA) 2009 introduced a package of measures to provide support through the UK Oil and Gas fiscal regime for investment in the UK and UKCS. Legislation will be introduced to make further changes to the regime.
3. FA 2009 provided that chargeable gains would not arise in some circumstances where disposal proceeds are reinvested in new oil trade assets and the disposal and acquisition qualify for rollover relief. Finance Bill 2011 will widen the scope of this reinvestment relief so it can apply when proceeds are reinvested in exploration and development expenditure, including drilling costs.
4. One measure will ensure reinvestment relief can apply as intended in a group context, when the company making the reinvestment is not the company making the disposal. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.
5. FA 2009 provided that chargeable gains would not arise on the swap of UK/UKCS licences in some circumstances. Finance Bill 2011 will extend the scope of application of that measure.
6. FA 2009 introduced a field allowance to provide an incentive to invest in new fields. Finance Bill 2011 will extend this to investment in fields that have previously been decommissioned.
7. The field allowance qualifying criteria for an ultra high pressure/high temperature (HPHT) field will be reduced, and the allowance tapered.

### Operative date

8. The extension of reinvestment relief will have effect with retrospective application to disposals made on or after 24 March 2010.
9. The reinvestment relief group change will have effect with retrospective application to disposals made on or after 22 April 2009.

10. The chargeable gains swaps change will have effect for disposals made on or after Budget Day 2011.
11. The extension of the scope of field allowance will have effect with retrospective application to fields whose development is authorised on or after 22 April 2009.
12. The reduction in the qualifying criteria for an HPHT field will be achieved by way of an order to be introduced before 29 July 2010. It will come into force on the day following the one on which the order is made.

## **Current law and proposed revisions**

### Chargeable gains

13. FA 2009 introduced reinvestment relief which provides that no chargeable gain arises in some circumstances where disposal proceeds are reinvested in new oil trade assets and the disposal and acquisition qualify for rollover relief.
14. Certain expenditure on drilling costs and expenditure incurred on other development and exploration activities is not included within the prescribed classes of assets for rollover relief purposes and does not permit a claim for reinvestment relief.
15. The new legislation will include expenditure on exploration and development, including drilling costs, within the classes of assets for which reinvestment relief is available.
16. The reinvestment relief legislation was intended to apply in a group context where the disposal is by one company in a group and the acquisition is by another company in the same group, but a technical oversight prevents the legislation from applying in such circumstances. The legislation will be amended so that it can apply as intended.
17. FA 2009 introduced legislation which provides that no chargeable gains arise on the swap of UK/UKCS licences in some circumstances. The new legislation will address some circumstances in which non-licence consideration is involved.
18. A licence swap agreement usually includes provision for various payments to be made between the parties, which are typically treated as adjustments to the consideration.
19. The existing legislation does not remove the chargeable gains liability that may arise in respect of the receipt of such payments. The new legislation will remove some of these payments from the scope of taxation on chargeable gains.

## Field allowance

20. FA 2009 introduced the field allowance which reduces the profits on which the supplementary charge is payable. The allowance is available for certain new oil fields.
21. The new legislation will extend the scope of the field allowance to fields that have previously been decommissioned but are being redeveloped.
22. One of the classes of qualifying field for which the field allowance is available is a HPHT field, being a field with pressure in excess of 1034 bar (15 kpsi) and temperature in excess of 176.67°C (350°F). The revised thresholds will be pressure in excess of 862 bar (12.5 kpsi) and temperature in excess of 166°C (330°F). The allowance will increase on a straight-line basis from £500 million at 166°C to £800 million at 176.67°C.

## **Further advice**

23. These measures were previously announced at the 2009 Pre-Budget Report and Budget 2010 and versions of this note were published as PBRN03 and BN08. This note supersedes those versions.
24. If you have any questions about these changes please contact either Hugh Hedges on 020 7438 6576 (email: [hugh.hedges@hmrc.gsi.gov.uk](mailto:hugh.hedges@hmrc.gsi.gov.uk)) or Paul Philip on 020 7438 6993 (email: [paul.philip@hmrc.gsi.gov.uk](mailto:paul.philip@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)



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## ENTERPRISE MANAGEMENT INCENTIVES

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### Who is likely to be affected?

1. Companies wishing to offer share options to their employees under Enterprise Management Incentives (EMI).

### General description of the measure

2. This measure will amend the requirement that a company granting qualifying EMI options to its employees must operate “wholly or mainly” in the UK. A company granting EMI options will now be required instead to have a “permanent establishment” in the UK.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. The change will have effect in respect of EMI options granted on or after the date that the legislation receives Royal Assent.

### Current law and proposed revisions

5. Paragraphs 13 to 15 of Schedule 5 to the Income Tax (Earnings and Pensions) Act 2003 require that, in the case of a single company granting EMI options to its employees, that company must carry on a trade “wholly or mainly” in the UK or, in the case of a parent company, at least one company in the group must be carrying on a “qualifying trade” (within the meaning of the legislation) “wholly or mainly” in the UK.
6. To ensure EMI complies with EU State aid guidelines, the present rule will be amended. In future, a company wishing to grant EMI options must have a “permanent establishment” in the UK. Alternatively in the case of a parent company, at least one company in the group that is carrying on a “qualifying trade” within the meaning of the legislation must have a “permanent establishment” in the UK.
7. “Permanent establishment” has the same meaning as in Chapter 2 of Part 24 of the Corporation Tax Act 2010.

### Further advice

8. This measure was previously announced at Budget 2010 and a version of this note was published as BN13. This note supersedes that version.

9. If you have any questions about this change, please contact Andrew Ellis on 020 7147 2658 (email: [shareschemes@hmrc.gsi.gov.uk](mailto:shareschemes@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## VENTURE CAPITAL SCHEMES

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### Who is likely to be affected?

1. Investors under the Enterprise Investment Scheme (EIS) and Venture Capital Trust (VCT) schemes; companies receiving investment under the schemes; and VCTs themselves.

### General description of the measure

2. This measure will make the final four changes to the EIS and VCT schemes agreed with the European Commission as a condition for their approval by the Commission as approved State aids.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. The changes generally will have effect on and after a date to be appointed, with the exception of the eligible shares changes for VCTs, which will not affect monies raised by the VCT before that date.

### Current law and proposed revisions

#### VCTs only

5. The current legislation at section 274 of the Income Tax Act 2007 (ITA) requires the shares making up a VCT's ordinary share capital to be included in the official UK list throughout the relevant accounting period. This will be replaced with a requirement that the shares instead be admitted for trading on any EU regulated market. The effect is that VCTs will be able to be listed on markets throughout the EU/European Economic Area (EEA). The European Commission publishes a list of all regulated markets in the Official Journal of the European Union at least annually, and the list of regulated markets is also available on its website.
6. The current legislation at section 274 of ITA requires that at least 30 per cent of the VCT's qualifying holdings is represented throughout the relevant accounting period by holdings of eligible shares. Section 285(3) of ITA defines "eligible shares" for this purpose. The new legislation will increase the eligible shares holdings requirement to 70 per cent, but will also change the definition of "eligible shares" to allow VCTs to include shares which may carry certain preferential rights to dividends.

## EIS and VCTs

7. The new legislation will exclude shares in a company from qualifying for the purposes of the EIS or VCT legislation if it is reasonable to assume that the company would be treated as an “enterprise in difficulty” for the purposes of the European Commission’s Rescue and Restructuring Guidelines, published in the Official Journal at OJ C 2004/C 244/02, at section 2.1.
8. The current legislation, at sections 179 (for EIS) and 291 (for VCTs) of ITA requires that there is a qualifying trade carried on wholly or mainly in the UK. For shares issued on or after the commencement date of the legislation, the requirement will be that the company issuing the shares must simply have a permanent establishment in the UK.
9. “Permanent establishment” will be defined based on Article 5 of the Organisation for Economic Co-operation and Development (OECD) Model Tax Convention on Income and Capital.
10. Regulations will be made to update Statutory Instrument 2004/2199 to reflect the new conditions concerning eligible shares.

### **Further advice**

11. This measure was previously announced at Budget 2010 and a version of this note was published as BN12. This note supersedes that version.
12. If you have any questions about this change, please contact Kathryn Robertson on 020 7147 2589 (email: [kathryn.robertson@hmrc.gsi.gov.uk](mailto:kathryn.robertson@hmrc.gsi.gov.uk)), David Harris on 020 7147 2562 (email: [david.harris@hmrc.gsi.gov.uk](mailto:david.harris@hmrc.gsi.gov.uk)) or Des Ryan on 020 7147 0818 (email: [des.ryan@hmrc.gsi.gov.uk](mailto:des.ryan@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## FILM TAX RELIEF: MULTI YEAR CLAIMS

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### Who is likely to be affected?

1. Film production companies making films whose production spans two or more accounting periods and which have some overseas expenditure.

### General description of the measure

2. This measure will correct an unintended anomaly affecting the amount of tax credit claimable where films are produced over more than one accounting period.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. The measure has effect for accounting periods ending on or after 9 December 2009 and will be treated for those periods as always having had effect.

### Current law and proposed revisions

5. In any accounting period after the first period, the loss surrenderable for tax credit is currently the lesser of the available qualifying expenditure (cumulative qualifying expenditure to date, less any previously surrendered amount), and the loss incurred in that period.
6. HM Revenue & Customs has become aware of a quirk in the legislation where there is an increased UK spend in the second or later periods. The unintended effect of this is to restrict the amount of tax credit claimable.
7. The proposed revision will adjust the way the amount surrenderable for tax credit is calculated. The calculation will become the lesser of:
  - the available qualifying expenditure; and
  - the loss for the period, plus any unsurrendered loss brought forward.

### Further advice

8. This measure was previously announced at the 2009 Pre-Budget Report and a version of this note was published as PBRN07. This note supersedes that version.

9. If you have any questions about this change, please contact Des Ryan on 020 7147 0818 (email: [des.ryan@hmrc.gsi.gov.uk](mailto:des.ryan@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## CHANGES TO THE RULES ON THE DEDUCTION OF INCOME TAX AT SOURCE

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### Who is likely to be affected?

1. Individuals and other non-corporates that make payments of interest, patent royalties or other annual payments which require tax to be deducted at source. Companies making these payments are unaffected.

### General description of the measure

2. Following consultation with affected parties, this measure will provide the Commissioners for Her Majesty's Revenue and Customs with a power to amend the rules relating to the time and manner in which persons need to report and remit the income tax deducted from certain payments.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. The measure will have effect on and after the date that the legislation receives Royal Assent.

### Current law and proposed revisions

5. Currently, the rules setting out when and how a person must report income tax deducted at source from certain payments are set out in primary legislation.
6. The legislation provides that where a person other than a company makes a payment of a type contained within section 963 of the Income Tax Act 2007 from which income tax is required to be deducted, they are required to deliver an account of that payment to an officer of HM Revenue & Customs (HMRC) without delay. An officer of HMRC may make an assessment of the tax due on the person making the payment.
7. This change will provide HMRC with a power to make regulations to amend when and how a person should report income tax deducted from certain payments.

## **Further advice**

8. If you have any questions about this change, please contact Nicky Rass on 020 7147 2802 (email: [nicola.rass@hmrc.gsi.gov.uk](mailto:nicola.rass@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## CONSORTIUM RELIEF

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### Who is likely to be affected?

1. Companies who are members of corporate consortia.

### General description of the measure

2. This measure will amend the “link company” aspects of consortium relief and add a further test to the rules which determine the amount of a consortium’s losses that may be claimed by its members.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. The changes to the legislation have effect for accounting periods commencing on or after the date that the legislation is published.

### Current law and proposed revisions

5. Consortium relief rules allow, in certain circumstances, a member of a consortium to transfer its share of the consortium’s unused losses to another member of its group. This is commonly known as the “link company rule” and the member that makes the transfer is known as the “link company”. Under current rules, the link company must be UK resident. This measure extends the rules to allow any company established within the European Economic Area to be a link company.
6. Currently, the maximum amount of losses that may be claimed from a consortium company is determined by the lowest result from three tests:
  - i. the percentage of ordinary share capital held;
  - ii. the percentage of profits to which the company is entitled; and
  - iii. the percentage of assets to which the company would be entitled on a winding up.This measure adds an additional test based on the proportion of voting rights and the extent of control the member holds in the consortium.

### Further advice

7. If you have any questions about this change, please contact Chris Thomas on 020 7147 0114 (email: [christopher.thomas1@hmrc.gsi.gov.uk](mailto:christopher.thomas1@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)



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## LIFE INSURANCE COMPANIES: CHANGES TO TAX RULES

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### Who is likely to be affected?

1. Life insurance companies which transfer assets to the equivalent of a non-profit fund of a non-European Economic Area (EEA) company.
2. Life insurance companies which transfer UK business to an EEA (but non-UK) resident company, and which subsequently carry on that UK business through a branch of that EEA company.
3. Companies carrying on life insurance business which defer recognition of profits from business arising in a non-profit fund and which dispose of such non-profit business by way of a transfer of business.

### General description of the measure

4. The Government intends to consult informally with industry on modifications to the rules which govern transfers of life insurance business to ensure that an unintended tax charge does not arise when a UK life insurance company transfers long term insurance business to a non-EEA overseas company. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.
5. Regulations will be introduced to ensure a consistent basis of taxation when life insurance business ceases to be carried on in the UK through a UK company, and starts to be carried on through a UK branch of a company resident elsewhere in the EEA.
6. A measure was introduced in Finance Act (FA) 2010 to prevent manipulation to avoid tax on previously unrecognised profits. As announced on 24 March 2010, an anti-avoidance rule will be introduced in Finance Bill 2010 to ensure that the new measure will be effective in cases where life insurance business is transferred to another company.

### Operative date

7. The rules governing transfers of business will be modified for transfers of business taking place after 22 June 2010.
8. It is intended that regulations governing the taxation of overseas life insurance companies will have effect for periods of account beginning on or after 1 January 2011.

9. In accordance with the previous announcement, the new anti-avoidance rule will apply to transfers of business on or after 24 March 2010.

## **Current law and proposed revisions**

### Rules which govern transfers of life insurance business

10. When life insurance business is transferred from the long term insurance fund (LTIF) of one company to that of another, the rules operate to ensure that the transfer is effectively tax neutral. However, where assets transferred do not arrive in the LTIF of the transferee company (because, for example, they are transferred directly into the shareholders' fund) tax may be lost. Because of this, a tax charge arises on the fair value of any assets which are transferred, but which do not become assets of the LTIF of an insurance company or insurance special purpose vehicle.
11. For the purposes of these rules, a non-EEA overseas insurance company will not meet the definition of an "insurance company", so a tax charge will arise on the fair value of all assets transferred, even if those assets are transferred to match insurance liabilities transferred.
12. Proposals to modify the rules to ensure that any tax charge is appropriate will be informally discussed with industry, prior to the introduction of the legislation.

### Rules governing the taxation of overseas life insurance companies

13. A UK regulated life insurance entity is taxed on the basis of its return to the Financial Services Authority (FSA). A non-UK regulated overseas entity is taxed on the basis of its financial statements. These bases are significantly different, so that on changing from one to the other expenses may be allowed twice and income may not be taxed at all. In addition income may be inappropriately apportioned between classes of business.
14. Regulations will be made under powers conferred on HM Treasury by section 156 of FA 2003 to ensure that where UK business is transferred from a UK regulated entity to an EEA regulated entity, the UK branch will be taxed on the basis of the return made to the overseas regulator, provided that it is equivalent to an FSA return.
15. This is an interim measure, as UK branches will move to an accounts basis on a Solvency II timescale, along with all UK life insurance companies.

### Anti-avoidance rule

16. The investment return arising in a non-participating fund of a life company is apportioned between classes of business in accordance with section 432C of the Income and Corporation Taxes Act 1988 (ICTA). A company can choose which year that return is recognised for tax purposes. It was therefore possible for companies to manipulate apportionments, so profits (which actually arose in one class of business) were allocated to another class when they were recognised in a future

year, with the result that they were not taxed, or were taxed at a lower rate. FA 2010 introduced section 432CA of ICTA to prevent this manipulation.

17. Section 432CA operates when profits in a non-participating fund, previously unrecognised, are ultimately recognised and emerge for tax purposes. It has the effect of ensuring that, when the profit emerges, it is apportioned not on the basis of the current year mix of liabilities under section 432C, but on the basis of a prior year apportionment fraction.
18. However, if part or all of the unrecognised profits are effectively transferred to another life company by way of a transfer of business involving an excess of assets over liabilities, the profit will ultimately emerge in the new company. That new company may have (and always have had) a section 432C fraction which results in little or no tax arising. Section 432CA would not have any effect because prior year apportionment fractions would be in line with that for the year in which the profit emerged.
19. The anti-avoidance rule now being introduced will create a tax charge on the transferring company in respect of any excess in the fair value of assets transferred over the amount brought into account as a business transfer-out for the period of account in which the transfer occurred, or, if an actual period or deemed period of account ended immediately before the transfer, the period of account ending immediately before the transfer. The rule will only impact where one of the purposes of the transfer was to avoid tax.
20. Where such a tax charge arises in the transferring company, there will be provision for relief in the transferee company to ensure that no amounts are taxed twice.

#### **Further advice**

21. A Technical Note on the form of the anti-avoidance rule was published on 24 March 2010. HM Revenue & Customs intends to consult further with the industry to ensure that the legislation finally enacted is effective and targeted.
22. It is intended that draft regulations relating to the taxation of overseas life insurance companies will be published for consultation with industry on their final form over the summer.
23. If you have any questions about these changes, please contact Carol Johnson on 020 7147 0517 (email [carol.johnson@hmrc.gsi.gov.uk](mailto:carol.johnson@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)



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## **CORPORATION TAX AVOIDANCE: AUTHORISED INVESTMENT FUNDS**

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### **Who is likely to be affected?**

1. Corporate investors in authorised investment funds (AIFs).

### **General description of the measure**

2. This measure will ensure that a corporate investor cannot make use of an AIF to create a credit for UK tax where no UK tax has been paid.

### **Operative date**

3. This measure has effect on and after 22 June 2010.

### **Current law and proposed revisions**

4. The tax regulations applicable to AIFs (the AIF regulations) “stream” any dividend distribution made by an AIF and paid to a corporate investor. This means that any part of the distribution derived from taxable income of the AIF is treated as an annual payment with an associated deemed tax credit. This normally ensures the correct rate of corporation tax is paid by the investor after taking into account tax in the AIF. The two amendments to the AIF regulations described below prevent the artificial creation, inflation or repayment of the deemed tax attached to an annual payment.
5. The first amendment restricts the corporation tax deduction given for interest distributions so that the deduction is reduced to the extent that the distribution is derived from dividends exempt from corporation tax.
6. The second amendment ensures that where foreign tax is suffered by an AIF then the deemed tax credit in the hands of the corporate investor (including another AIF) is treated as a foreign tax credit for all tax purposes (and that a proportionate part of the income is treated as foreign income).

### **Further advice**

7. If you have any questions about this change, please contact John Buckeridge on 020 7147 2560 (email: [john.buckeridge@hmrc.gsi.gov.uk](mailto:john.buckeridge@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)



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## LOAN RELATIONSHIPS: ANTI-AVOIDANCE

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### Who is likely to be affected?

1. Large companies involved in avoidance of corporation tax involving derecognition of income from loan relationships and derivative contracts.

### General description of the measure

2. Legislation will be introduced in Finance Bill 2010 to tackle avoidance schemes that have been notified to HM Revenue & Customs under the avoidance disclosure rules. In such schemes the profits arising to a company from a financial asset are said to fall out of account for tax purposes as a result of the 'derecognition' of a loan or derivative.

### Operative date

3. The legislation has effect for credits and debits arising on or after 22 June 2010.

### Current law and proposed revisions

4. A company's taxable profits and losses from its loan relationships and derivative contracts are normally based on the amounts shown in accounts drawn up in accordance with generally accepted accounting practice. In certain circumstances, where accounting practice allows or requires a loan or derivative or its associated cash flows to be 'derecognised', the tax rules override the accounting practice and require the profits and losses to be computed as if the asset in question had been fully recognised.
5. The measure will extend the circumstances in which amounts are to be fully recognised for tax purposes, to cases where derecognition arises as a result of the acquisition or variation of a capital interest in a company, partnership or trust, or where derecognition is triggered by an event that occurs in a later accounting period to that in which the derecognition takes place.

### Further advice

6. A Technical Note is to be issued in early July 2010 setting out proposals for generic legislation to tackle avoidance schemes involving derecognition of loan relationships and derivative contracts.
7. Any further changes to the legislation on derecognition will be made in Finance Bill 2011, with effect from a date to be announced.

8. If you have any questions about this change, please contact Tony Sadler on 020 7147 2608 (email: [tony.sadler@hmrc.gsi.gov.uk](mailto:tony.sadler@hmrc.gsi.gov.uk)) or Richard Rogers on 020 7147 2625 (email: [richard.rogers@hmrc.gsi.gov.uk](mailto:richard.rogers@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## UK REAL ESTATE INVESTMENT TRUSTS AND STOCK DIVIDENDS

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### Who is likely to be affected?

1. UK Real Estate Investment Trusts (REITs) and shareholders in UK-REITs.

### General description of the measure

2. This measure will allow UK-REITs to issue stock dividends in lieu of cash dividends in meeting the requirement to distribute 90 per cent of the profits from the property rental business of the REIT.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. The measure will have effect for property income distributions made on or after the date that the legislation receives Royal Assent.

### Current law and proposed revisions

5. The UK-REIT legislation was introduced in Part 4 of the Finance Act 2006. This legislation has been rewritten, as part of the Tax Law Rewrite Programme, to Part 12 of the Corporation Tax Act 2010 with effect from 1 April 2010.
6. A UK-REIT is a qualifying group or company with a property rental business that elects to join the UK-REITs regime. The principal benefit of joining the regime is that the profits and gains arising from the property rental business are exempt from corporation tax.
7. The UK-REITs legislation requires that a UK-REIT distributes, for each accounting period, 90 per cent of the profits from its property rental business by way of a dividend. This is known as the distribution requirement. The distribution itself is known as a property income distribution.
8. In the hands of the shareholders a property income distribution is taxed as though it was income from property. This is to give investors a return similar to investing in property directly and assists in making the regime cost neutral to the Exchequer.

9. Currently stock dividends do not count as property income distributions and so are not able to be used by UK-REITs to meet the distribution requirement.
10. A change to primary legislation will be made to allow UK-REITs to issue stock dividends in lieu of cash dividends for the purpose of the distribution requirement.
11. The recipients of stock dividends paid to meet the distribution requirement will be taxed in the same way as the recipients of property income distributions paid in cash. Where REITs currently deduct income tax from property income distributions issued by way of cash dividends, they will do so for property income distributions issued by way of stock dividends.

**Further advice**

12. This measure was previously announced at Budget 2010 and a version of this note was published as BN22. This note supersedes that version.
13. If you have any questions about this change, please contact Tony Linehan on 020 7147 0527 (email: [tony.linehan@hmrc.gsi.gov.uk](mailto:tony.linehan@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## **INSURANCE PREMIUM TAX: INCREASE IN THE STANDARD RATE AND HIGHER RATE**

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### **Who is likely to be affected?**

1. Insurers who receive premiums under taxable insurance contracts, and some intermediaries responsible for collecting taxable premiums.

### **General description of the measure**

2. The standard rate of insurance premium tax (IPT) applies to most general insurance, including property, motor and medical insurance. Life assurance and other long term insurance products are exempt from IPT.
3. The higher rate of IPT applies to travel insurance and to certain insurance (e.g. extended warranties) sold alongside motor vehicles and some consumer goods. It was introduced at 17.5 per cent in 1997 to stop VAT avoidance through 'value-shifting' between goods (subject to VAT at 17.5 per cent) and related insurance.
4. Legislation will be introduced in Finance Bill 2010 to provide for an increase in the standard rate of IPT from 5 per cent to 6 per cent and an increase in the higher rate of IPT from 17.5 per cent to 20 per cent in line with the increase in the standard rate of VAT.

### **Operative date**

5. There will be a lead-in period of just over six months before the increase has effect. The new standard rate and higher rate will have effect for premiums received or written by an insurer on or after 4 January 2011. Please see paragraphs 7 and 8 below.

### **Current law and proposed revisions**

6. IPT is charged as an inclusive amount within premiums received under taxable insurance contracts. Section 51 of the Finance Act 1994 provides the current higher rate of IPT as 17.5 per cent, and the standard rate of IPT as 5 per cent. Finance Bill 2010 will increase the standard rate of IPT to 6 per cent and increase the higher rate of IPT to 20 per cent.
7. For insurers using the cash receipt method to account for IPT, the new rates will have effect for premiums received under taxable insurance contracts on or after 4 January 2011.

8. For insurers who account for IPT using the special accounting scheme the new rates will have effect for premiums that are written into their records as due to them on or after 4 January 2011.
9. There are already special measures in place to prevent tax avoidance in relation to the period between the announcement of a rate change and the date the rate increase takes effect.

**Further advice**

10. If you have any questions about this change, please contact the VAT Helpline on 0845 010 9000. Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk), and about IPT rate rises in section 14 of the Public Notice IPT1.

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## CAPITAL GAINS TAX: RATES AND ENTREPRENEURS' RELIEF

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### Who is likely to be affected?

1. Individuals, trustees and personal representatives of deceased persons who pay capital gains tax (CGT).

### General description of the measure

2. Legislation will be included in Finance Bill 2010 to introduce a new rate of CGT of 28 per cent. For individuals, the rate of CGT remains 18 per cent where total taxable gains and income are less than the upper limit of the income tax basic rate band. The 28 per cent rate applies to gains (or any parts of gains) above that limit. For trustees and personal representatives of deceased persons, the rate is increased to 28 per cent (previously 18 per cent).
3. The rate of CGT for gains qualifying for entrepreneurs' relief remains 10 per cent. The lifetime limit on gains qualifying for entrepreneurs' relief is increased from £2 million to £5 million.
4. The annual exempt amount (AEA) for 2010-11 remains at the level set previously, £10,100.

### Operative date

5. The new rates of CGT and lifetime limit for entrepreneurs' relief have effect on and after 23 June 2010.

### Current law and proposed revisions

#### Rates of CGT

6. At present section 4 of the Taxation of Chargeable Gains Act 1992 (TCGA) provides that net gains chargeable to CGT (after deduction of reliefs, losses and the CGT AEA) are taxed at 18 per cent.
7. Finance Bill 2010 will include provision to change the rates of CGT for gains arising on or after 23 June 2010.
8. For individuals, where their total taxable income and gains after all allowable deductions (including losses, the income tax personal allowance and the CGT AEA) are less than the upper limit of the basic rate income tax band (£37,400 for 2010-11), the rate of CGT will be 18 per cent. For gains (and any parts of gains) above that limit the rate will be 28 per cent. For trustees and personal representatives of deceased persons, the rate

will be 28 per cent. Where entrepreneurs' relief applies for individuals or trustees the rate remains 10 per cent (see below).

9. Gains arising in 2010-11, but before 23 June 2010, will continue to be liable to CGT at 18 per cent and will not be taken into account in determining the rate (or rates) at which gains of individuals arising on or after 23 June 2010 should be charged.
10. Certain CGT reliefs allow gains on disposal of an asset to be deferred until some time after the disposal. For instance, a gain can be reinvested in shares under the Enterprise Investment Scheme (EIS) and, subject to conditions, can be deferred until the EIS shares are disposed of. The CGT rate(s) on a gain deferred in this way will be the rate(s) at the time the deferral ends and the gain becomes liable to tax. Gains on disposals before 23 June 2010 which are deferred until 23 June 2010 or later will therefore be liable to CGT at the 18 or 28 per cent rates, in the same way as gains arising on disposals on or after that date.
11. In working out the CGT payable, taxpayers will be able to deduct losses and the AEA in the way which minimises the tax due.

#### Example 1

In 2010-11 X's taxable income, after all allowable deductions and the personal allowance, is £27,400. The upper limit of the income tax basic rate band is £37,400. X sells an asset in May 2010 and realises a chargeable gain of £17,000. In November 2010 X sells another asset, realising a chargeable gain £25,100. X has no allowable losses to set against these gains, and the AEA for 2010-11 is £10,100. Neither of the gains qualifies for entrepreneurs' relief.

X's taxable income is £10,000 less than the upper limit of the basic rate band (£37,400 - £27,400). X sets the AEA against the later gain (because part of that gain is liable to tax at the higher CGT rate), leaving £15,000 taxable (£25,100 - £10,100). The first £10,000 of the £15,000 is taxed at 18 per cent and the remaining £5,000 is taxed at 28 per cent. The £17,000 chargeable gain X realised in May 2010 before the change of rates on 23 June 2010 is taxable at the old 18 per cent rate.

12. For trustees and personal representatives of deceased persons, the CGT rate will be 28 per cent for gains arising on or after 23 June 2010, except where entrepreneurs' relief applies (see below).

## Entrepreneurs' relief – rate of CGT and lifetime limit on relief

13. Subject to satisfying certain conditions, including the lifetime limit of £2 million, gains on disposals of entrepreneurial businesses by individuals and certain trustees qualify for entrepreneurs' relief (Chapter 3 of Part 5 of TCGA). Currently entrepreneurs' relief reduces qualifying gains by 4/9 and the remaining 5/9 are then charged at the single 18 per cent rate. This results in qualifying gains being taxed at an effective rate of 10 per cent.
14. The changes to CGT rates from 23 June 2010 would mean the 4/9 reduction no longer achieved an effective rate of 10 per cent. Finance Bill 2010 will therefore include provision to charge gains on disposals that qualify for entrepreneurs' relief on or after 23 June 2010 at a 10 per cent rate. The previous 4/9 reduction will cease to apply from that date.
15. The amount of an individual's gains that can qualify for entrepreneurs' relief is subject to a lifetime limit of £2 million (£1 million for disposals before 6 April 2010). For trustees, the £2 million limit is that of the beneficiary of the settlement who meets the conditions for the trustees to claim the relief.
16. Finance Bill 2010 will include provision to increase that limit to £5 million from 23 June 2010.
17. Where individuals or trustees make qualifying gains above the previous £2 million limit before 23 June 2010 (£1 million limit before 6 April 2010), no additional relief will be allowed for the excess above the old limit. But if they make further qualifying gains on or after 23 June 2010, they will be able to claim relief on up to a further £3 million of those additional gains (or up to £4 million where the earlier £1 million limit applied), giving relief on accumulated qualifying gains up to the new limit of £5 million. In determining at what rate(s) an individual should be charged to CGT on any other gains, those gains qualifying for entrepreneurs' relief are set against any unused basic rate band before non-qualifying gains.

### Example 2

Y has previously used £1 million of their lifetime entrepreneurs' relief limit. In 2010-11 Y's taxable income, after all allowable deductions and the personal allowance, is £17,400. The upper limit of the income tax basic rate band is £37,400. In May 2010 Y realises a chargeable gain of £3 million on the disposal of a business. In December 2010 Y sells another business, realising further chargeable gains of £7 million. Both disposals qualify for entrepreneurs' relief (subject to the lifetime limits). Y has no allowable losses to set against these gains, and the AEA for 2010-11 is £10,100.

The £3 million gain realised in May 2010 is subject to the £2 million lifetime limit for entrepreneurs' relief (for qualifying disposals from 6 April 2010), of which Y has previously used £1 million. The gain is reduced by 4/9 of £1 million and the remainder charged to CGT at the single rate of 18 per cent. The increase in the lifetime limit from 23 June 2010 means

that £3 million of the £7 million gain from December is chargeable at the 10 per cent rate of CGT. Y's taxable income is £20,000 below the basic rate band (£37,400 – £17,400). But the £3 million of the gain charged at 10 per cent is taken into account in priority to other gains in determining whether total income and gains exceed the basic rate band. So the remaining £4 million gains, less the AEA, are charged at the higher rate of 28 per cent.

### **Further advice**

18. If you have any questions about these changes, please contact the capital gains tax team by email at [capitalgains.taxteam@hmrc.gsi.gov.uk](mailto:capitalgains.taxteam@hmrc.gsi.gov.uk) or by telephone on 020 7147 0127. Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## INDEXING INDIVIDUAL SAVINGS ACCOUNT LIMITS FROM 2011

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### Who is likely to be affected?

1. All individuals who invest in Individual Savings Accounts (ISAs).

### General description of the measure

2. From 6 April 2011 the ISA limits will be increased in line with the Retail Prices Index (RPI) on an annual basis.

### Operative date

3. Indexation of the ISA limits for the tax year 2011-12 will have effect on and after 6 April 2011. Indexation of the ISA limits for subsequent tax years will have effect on and after 6 April of each year.

### Current law and proposed revisions

4. Under the powers in section 694 of the Income Tax (Trading and Other Income) Act 2005 (ITTOIA), *The Individual Savings Account Regulations 1998 (Statutory Instrument 1998/No 1870 as amended)* provide the rules and regulations for the ISA scheme.
5. From 6 April 2010 the annual ISA subscription limits were increased for all savers, to £10,200, of which £5,100 can be saved in cash.
6. From 6 April 2011 the annual ISA subscription limits will be linked to the RPI. They will be rounded to a convenient multiple of 120 so that individuals who save monthly will be able to calculate their monthly savings more easily.
7. The new limits will be calculated by reference to the RPI for the September before the start of the following tax year, and HM Revenue & Customs will announce the new limits each year in advance of the start of the new tax year in which they will apply.
8. In the event that the RPI is negative, the ISA limits would remain unchanged.
9. As is the case now, following indexation, the cash ISA limit will be half the value of the stocks and shares ISA limit.
10. The ISA regulations will be amended by Statutory Instrument to reflect these changes.

## **Further advice**

11. This measure was previously announced at Budget 2010 and a version of this note was published as BN28. This note supersedes that version.
12. If you have any questions about this change, please contact Stephen Lig on 020 7147 2827 (email: [steve.lig@hmrc.gsi.gov.uk](mailto:steve.lig@hmrc.gsi.gov.uk)). Information is also available from the Individual Savings Account (ISA) Helpline on 0845 604 1701. Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## TRANSITIONAL MEASURE DEFERRING THE EFFECTIVE REQUIREMENT TO BUY AN ANNUITY TO AGE 77

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### Who is likely to be affected?

1. Members of registered pension schemes and their dependants, particularly those members approaching age 75; registered pension schemes and their administrators, annuity providers and personal representatives of deceased pension scheme members.

### General description of the measure

2. The Government has announced that it will end the effective requirement to use a pension fund to buy an annuity by age 75 with effect from 2011-12.
3. Pending implementation of the necessary changes, legislation will be introduced in Finance Bill 2010 to increase to 77 the age by which members of registered pension schemes have to buy an annuity or otherwise secure a pension income. This change will also apply for the purposes of the inheritance tax (IHT) charges that specifically apply to pension scheme members aged 75 and over.

### Operative date

4. The increase in the age by which the member must secure an income has effect on and after 22 June 2010. This change will also apply for IHT purposes to members, who die on or after that date. In both cases the change applies only to individuals, who have not yet reached age 75 before 22 June 2010.

### Current law and proposed revisions

5. For scheme members with money purchase arrangements who have not yet bought an annuity by age 75, the income withdrawals they may make become subject to strict minimum and maximum limits from age 75. Also, if such a member dies after reaching age 75 and any of the fund is not used to pay either pensions to dependants or a charitable donation, it is subject to tax charges up to 70 per cent. Specific IHT charges also apply to certain pension scheme members who die on or after their 75<sup>th</sup> birthday.
6. For scheme members with money purchase arrangements who have not yet bought an annuity and reach age 75 on or after 22 June 2010:
  - the strict minimum and maximum limits on income withdrawals will apply from their 77<sup>th</sup> instead of their 75<sup>th</sup> birthday;
  - immediately before their 75<sup>th</sup> birthday they will become entitled to

income withdrawal and a tax free pension commencement lump sum in respect of those funds not previously made available for income withdrawal; and

- in the interim period before the main changes have effect in 2011-12, there will be tax charges of 35 per cent on lump sum death benefits paid by the scheme if they die on or after 22 June 2010 and aged 75 or over. The specific IHT death charges on pension scheme members, who are in drawdown and are aged 75 or over when they die, will not apply in these circumstances. Previously there could have been tax charges up to 82 per cent of the value of the drawdown fund.

7. These interim changes enable those reaching age 75 on or after 22 June 2010 to defer their decision on what to do with their pension savings until after the new rules are finalised next year.

#### **Further advice**

8. The Government has announced that it will consult shortly on the detail of the changes being introduced in 2011-12.
9. If you have any questions about this change to pension tax rules, please contact Stephen Webb on 020 7147 2872 (email: [stephen.t.webb@hmrc.gsi.gov.uk](mailto:stephen.t.webb@hmrc.gsi.gov.uk)). For questions about this change to IHT rules please contact Simon Galloway on 020 7147 2776 (email: [simon.galloway@hmrc.gsi.gov.uk](mailto:simon.galloway@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## PENSIONS TAXATION: NEST

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### Who is likely to be affected?

1. The National Employment Savings Trust (NEST), its future members and contributing employers.

### General description of the measure

2. This measure will enable NEST (the pension scheme provided for under section 67 of the Pensions Act 2008) to be registered with HM Revenue & Customs (HMRC) for tax purposes.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. The amendment to enable NEST to be registered will have effect on and after the date the legislation receives Royal Assent.

### Current law and proposed revisions

5. The current pensions tax rules mean that NEST would not be able to be registered. A pension scheme can be registered for tax purposes only if it is an occupational pension scheme, a public service pension scheme, or a pension scheme established by a person with permissions to establish a personal pension scheme or stakeholder pension scheme.
6. The change will allow NEST to be treated as an occupational pension scheme for the purposes of Part 4 of the Finance Act 2004. An application could then be made to HMRC for NEST to be a registered pension scheme. This would mean that members of NEST and contributing employers would be able to benefit from the tax reliefs available to registered pension schemes on contributions and investment growth and to be subject to the same tax rules as other tax-registered pension schemes.

### Further advice

7. This measure was previously announced at Budget 2010 and a version of this note was published as BN35. This note supersedes that version.

8. If you have any questions about this change, please contact Beverley Davies on 020 7147 2869 (email: [beverley.davies@hmrc.gsi.gov.uk](mailto:beverley.davies@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## TAX CHANGES FOR CERTAIN TRUSTS COMPENSATING ASBESTOS VICTIMS

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### Who is likely to be affected?

1. Trustees of certain trusts that have been specifically set up as part of an arrangement made by a company with its creditors to pay compensation to asbestos victims.

### General description of the measure

2. This measure will exempt trustees of certain trusts from capital gains tax (CGT), inheritance tax (IHT) and income tax. The trusts that will benefit are those set up on or before 23 March 2010 as part of an arrangement made by a company with its creditors and specifically to pay compensation to, or in respect of, individuals with asbestos related conditions.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. This measure will have effect on and after 6 April 2006.

### Current law and proposed revisions

5. Trustees are subject to IHT charges every 10 years on the value of property held in trust above the IHT nil rate band (currently £325,000) and also on certain payments made out of the trust. Trustees are also liable to income tax on income arising to the trust, and CGT on disposals of certain trust assets.
6. This measure provides for exemptions from the IHT, CGT and income tax charges on the trustees of certain trusts that have been set up as part of an arrangement made by a company with its creditors. For the exemptions to apply, the trust must also be specifically for the purpose of paying compensation to, or in respect of, individuals with asbestos related conditions. This will apply to trusts set up on or before 23 March 2010.

### Further advice

7. This measure was previously announced at Budget 2010 and a version of this note was published as BN29. This note supersedes that version.

8. If you have any questions about this change, please contact Guy Leiser on 020 7147 2775 (email: [guy.leiser@hmrc.gsi.gov.uk](mailto:guy.leiser@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## INCOME TAX ADJUSTMENTS BETWEEN SETTLORS AND TRUSTEES

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### Who is likely to be affected?

1. Individuals who are taxed on the income of a trust they have set up (a settlor-interested trust).

### General description of the measure

2. Settlers (people who set up a trust) may receive repayments of tax on trust income if they are liable to income tax at a lower rate than the trustees. This measure will require settlers to pay any such repayments of tax they receive to the trustees. The result of this will be that these payments to trustees will be disregarded for inheritance tax purposes.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. The measure will have effect for repayments relating to trust income that arises on or after 6 April 2010.

### Current law and proposed revisions

5. Section 646 of the Income Tax (Trading and Other Income) Act 2005 requires settlers to pay over to trustees repayments of tax in respect of an "allowance or relief" in relation to trust income.
6. This will be extended to all repayments of tax received by settlers in relation to trust income.

### Further advice

7. This measure was previously announced at Budget 2010 and a version of this note was published as BN30. This note supersedes that version.
8. If you have any questions about this change, please contact Alan McGuinness on 020 7147 2766 (email: [alan.mcguinness@hmrc.gsi.gov.uk](mailto:alan.mcguinness@hmrc.gsi.gov.uk)) Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)



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## INCOME TAX: SPECIAL GUARDIANSHIP ORDERS AND RESIDENCE ORDERS

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### Who is likely to be affected?

1. Individuals who care for one or more children placed with them under:
  - a special guardianship order (i.e. special guardians); or
  - a residence order, where that individual is not the children's parent or step parent (e.g. certain kinship carers).

### General description of the measure

2. This measure will mean that payments to qualifying guardians will be exempt from income tax.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. This change will have effect for payments received on or after 6 April 2010.

### Current law and proposed revisions

5. Income from providing care is normally taxed under the trading income rules, or the rules for miscellaneous income.
6. HM Revenue & Customs (HMRC) provide simplified income tax arrangements for certain carers, known as the simplified arrangements for adult placement carers. These arrangements allow the carer to claim a fixed rate of expenses when computing their taxable profits from providing care. The fixed rate of expenses are:
  - £400 a week for the first child placed with the carer;
  - £250 a week for the second placed with the carer; and
  - a further £250 a week for the third placed with the carer.
7. Until 5 April 2010, special guardians and kinship carers are able to use the simplified arrangements described above to compute their taxable profits.
8. From 6 April 2010, qualifying guardians will be exempt from income tax on any qualifying payments they receive.

9. Qualifying guardians are individuals who care for one or more children placed with them under:
  - a special guardianship order; or
  - a residence order, where the individual is not the child's parent or step parent.
  
10. Qualifying payments are payments:
  - by the child's parents or payments by, or on behalf of, the local authority;
  - to a qualifying guardian; and
  - which are made in relation to a special guardianship order or a residence order.
  
11. Kinship carers who are providing care to a child who has not been placed with them under a residence order will not be considered a qualifying guardian for the purposes of this income tax exemption. However, they will be entitled to claim the new income tax relief for shared lives carers.

#### **Further advice**

12. This measure was previously announced at Budget 2010 and a version of this note was published as BN37. This note supersedes that version.
  
13. For further information on the new income tax relief for shared lives carers, please see BN27: Income Tax Relief for Shared Lives Carers.
  
14. If you have any questions about this change, please contact Jenni Rich on 020 7147 0686 (email: [jenni.rich@hmrc.gsi.gov.uk](mailto:jenni.rich@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## INCOME TAX RELIEF FOR SHARED LIVES CARERS

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### Who is likely to be affected?

1. Shared lives carers, including adult placement carers, staying put carers and certain kinship carers.

### General description of the measure

2. This measure will allow qualifying shared lives carers to claim the same income tax relief as foster carers. The new relief will be known as the qualifying care relief.
3. Qualifying shared lives carers will be entitled to claim a tax free allowance. Those whose shared lives earnings are less than the tax free allowance will not be taxed on their income from providing shared lives care. Those whose shared lives earnings are more than the tax free allowance have the option to choose a simplified method for calculating their profits.
4. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

5. This change will have effect on and after 6 April 2010.

### Current law and proposed revisions

6. Income from providing shared lives care is normally taxed under the trading income rules, or the rules for miscellaneous income.
7. HM Revenue & Customs (HMRC) provide simplified income tax arrangements for shared lives carers, known as the simplified arrangements for adult placement carers. These include a fixed rate of expenses (depending on the number of placements and the type of care provided e.g. day care), and a tax exemption for respite carers providing up to 182 days care a year. The new relief will replace the simplified arrangements for adult placement carers.
8. The new tax free allowance will be available to shared lives carers from 2010-11. For the tax year 2010-11 only, shared lives carers can choose between the current simplified arrangements for adult placement carers and the new tax free allowance. The simplified arrangements will then be withdrawn from 2011-12.

9. Qualifying shared lives carers:
- provide accommodation, care and support for up to three individuals who have been placed with them under a local authority shared lives placement scheme; and
  - share their home and family life with the individuals placed with them under the shared lives scheme.
10. Qualifying shared lives carers may provide a maximum of three shared lives placements at any one time, but they may care for a number of different individuals during the tax year. Foster children are not counted as shared lives placements for this purpose. Siblings placed together in the same household will be counted as one shared lives placement for this purpose only.
11. The new relief will be based on the existing foster care relief (Part 7 of Chapter 2 of the Income Tax (Trading and Other Income) Act 2005).
12. Qualifying shared lives carers, whose total receipts from providing care do not exceed the tax-free allowance for the year, will be exempt from income tax on their income from providing shared lives care.
13. Qualifying shared lives carers, whose total receipts from providing care exceed the tax free allowance for the year, will be able to choose to pay tax on:
- their total receipts from providing care less the tax free allowance; or
  - their actual profits computed using the normal tax rules for businesses.
14. The tax free allowance will be available per household, and consists of:
- £10,000 fixed amount per tax year;
  - £200 per week (or part week), per placement aged under 11; and
  - £250 per week (or part week), per placement aged 11 or over.
15. Where there is more than one carer in the household, the household may provide care to a maximum of three shared lives placements, and the allowance will be shared equally between the carers.
16. Where a carer is both a foster carer and a shared lives carer, the household will only be entitled to claim one £10,000 fixed amount per year. The carer will pool their caring income and reliefs so that:
- if their total income from providing foster care and shared lives care is less than their total foster care and shared lives care tax free allowance, then they will not be taxed on their income from providing care; or
  - if their total income from providing foster care and shared lives care is more than their total foster care and shared lives care tax free allowance, they will be able to choose to pay tax on:
    - their total foster care and shared lives care receipts less their total tax free allowance; or
    - their actual profits computed using the normal tax rules for businesses.

### Example

For the tax year 2011-12, Sarah is paid £35,000 to foster three children aged 7, 10 and 13. She is also paid £15,000 to provide shared lives care to one young adult.

Sarah's total tax free allowance for the year will be £56,800, which is made up of:

- £10,000 fixed annual amount for the tax year;
- £10,400 = £200 x 52 for fostering the 7 year old child;
- £10,400 = £200 x 52 for fostering the 10 year old child;
- £13,000 = £250 x 52 for fostering the 13 year old child; and
- £13,000 = £250 x 52 for caring for the young adult.

Sarah's total caring income is £50,000, this is less than her total tax free allowance and so she will not pay income tax on her caring income.

17. The tax free allowance will only apply to income obtained from the provision of shared lives care or foster care. It will not affect the tax treatment of income received from other sources.
18. Special guardians, and kinship carers providing care to a child who has been placed with them under a residence order, will not be considered a qualifying carer for the purposes of this income tax relief. However, they will be entitled to claim the new income tax exemption for payments to qualifying guardians. For further information about that tax exemption, please see Budget Note 26: Income Tax: Special Guardianship Orders and Residence Orders.

### **Further advice**

19. This measure was previously announced at the 2009 Pre-Budget Report and a version of this note was published as PBRN22. This note supersedes that version.
20. For further information about the simplified arrangements for adult placement carers, please see Business Income Manual 52750, which can be accessed via the HMRC website.
21. A change is also being made to the capital gains treatment of adult placement carers. For further information please see BN28: Capital Gains Tax: Private Residence Relief and Adult Placement Carers.
22. If you have any questions about this change, please contact Jenni Rich on 020 7147 0686 (email: [jenni.rich@hmrc.gsi.gov.uk](mailto:jenni.rich@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)



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## CAPITAL GAINS TAX: PRIVATE RESIDENCE RELIEF AND ADULT PLACEMENT CARERS

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### Who is likely to be affected?

1. Individuals who set aside part of their house exclusively for use under a local authority adult placement scheme.

### General description of the measure

2. This measure will ensure that entitlement to private residence relief (PRR) is preserved where an adult placement carer uses part of their home exclusively for the purposes of their business as a carer.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. The measure will have effect for disposals on or after 9 December 2009.

### Current law and proposed revisions

5. Private residence relief (PRR) is not available on any part of a house which is used exclusively for the purposes of a trade, business, profession or vocation (section 224(1) and (2) of the Taxation of Chargeable Gains Act 1992 (TCGA)). On disposing of the house the appropriate proportion of the gain relating to the part occupied as the only or main residence is eligible for PRR.
6. Where a person cares for an adult under a local authority placement scheme, their contract with the local authority may require them to set aside one or more rooms exclusively for the use of the adult in care. In such a case, section 224 of TCGA may prevent PRR being available on that part of the property.
7. The legislation will remove this possible restriction on PRR. The fact that part of the home is occupied by the adult in care will not prevent PRR being available on that part, which can therefore be treated as part of the carer's only or main residence, eligible for PRR.

### Further advice

8. This measure was previously announced at the 2009 Pre-Budget Report and a version of this note was published as PBRN16. This note supersedes that version.

9. Draft legislation and an explanatory note for this change were published on 9 December 2009 on the HM Revenue & Customs website.
10. A new income tax relief for qualifying shared lives carers is also being introduced from 6 April 2010. For further information please see BN27: Income Tax Relief for Shared Lives Carers.
11. If you have any questions about this change, please contact the capital gains tax team by email at [capitalgains.taxteam@hmrc.gsi.gov.uk](mailto:capitalgains.taxteam@hmrc.gsi.gov.uk), or by telephone on 020 7147 0127. Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## CAPITAL ALLOWANCES RULES FOR QUALIFYING CARERS

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### Who is likely to be affected?

1. Foster carers and shared lives carers.

### General description of the measure

2. This measure will correct technical anomalies in the special capital allowances rules for foster carers, to ensure that the rules operate as intended when individuals start, or finish, qualifying or electing for foster-care relief. The amended legislation will also apply to shared lives carers when the special rules are also extended to them.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. The changes apply to chargeable periods ending on or after the date that the legislation receives Royal Assent.

### Current law and proposed revisions

5. Capital allowances allow certain types of capital expenditure to be written-off against taxable business profits at prescribed rates. When the business is permanently discontinued, a balancing allowance or charge is normally made, to ensure that the business has received allowances equal to actual economic depreciation, as measured by the disposal value of the assets at that time.
6. There are two forms of foster-care relief. A foster carer can earn a certain amount (the individual's limit) from providing care before the income is charged to income tax. Alternatively, if the carer's income is more than their individual limit they may choose to pay tax on:
  - their qualifying care income less their individual limit; or
  - their actual profits computed using the normal tax rules for businesses (including capital allowances).
7. So carers are entitled to claim capital allowances only where their profits are computed using the normal tax rules for businesses. And it is possible for an individual to be entitled to claim capital allowances in one year, but not in the next (and vice versa).

8. Existing special rules in section 825 of the Income Tax (Trading and Other Income) Act 2005 are intended to ensure that there will not be a balancing adjustment when a foster carer moves from claiming capital allowances to qualifying for, or electing for, foster care relief or qualifying-care relief.
9. These rules are also intended to ensure that, if in a subsequent year the individual is again able to claim capital allowances on the same assets, then the appropriate relief is available.
10. However, there could be anomalous results in some circumstances where individuals begin or stop qualifying, or electing, for foster-care or qualifying-care relief. For example, where a foster carer has previously claimed capital allowances the special rules do not apply if the carer does not have unrelieved capital expenditure when they start qualifying, or electing, for foster-care relief.
11. The new legislation will ensure that the special rules apply as intended in all circumstances where an individual begins to claim or qualify for foster-care or qualifying-care relief and has previously claimed capital allowances in respect of their caring trade.
12. The new legislation will also amend the special rules so that if an individual's foster-care or qualifying-care relief ends and the ordinary capital allowances rules start to apply again, then they will be treated as having acquired assets they already own for the smaller of:
  - (a) the market value of the asset; or
  - (b) the unrelieved expenditure that was in the capital allowances pool at the end of the last chargeable period for which they were entitled to claim capital allowances.

#### **Further advice**

13. For further information on the new income tax relief for shared lives carers please see BN27: Income Tax Relief for Shared Lives Carers.
14. If you have any questions about these changes, please contact Sue Pennicott on 020 7147 2610 (email: [sue.pennicott@hmrc.gsi.gov.uk](mailto:sue.pennicott@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## EXPENSES PAID TO MPs

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### Who is likely to be affected?

1. Members of Parliament (MPs).

### General description of the measure

2. The Independent Parliamentary Standards Authority (IPSA) has developed a new scheme under which MPs have been paid their expenses since the Parliamentary election on 6 May 2010.
3. Legislation will be introduced in Finance Bill 2010 to amend the Income Tax (Earnings and Pensions) Act 2003 (ITEPA) to address the tax and National Insurance Contributions (NICs) consequences of the new expenses scheme for MPs. It will consolidate existing tax and NICs treatments following the introduction of the Parliamentary Standards Act 2009 and the provision in that Act for expenses to be administered by IPSA rather than the House Authorities. Full details will be given in guidance to MPs.

### Operative date

4. The legislation will have retrospective effect on and after 7 May 2010.

### Current law and proposed revisions

5. Section 292 of ITEPA exempts from income tax the Personal Additional Accommodation Expenditure (PAAE) that was paid to MPs in respect of additional expenses necessarily incurred in staying overnight away from their only or main home for the purpose of performing their Parliamentary duties prior to the 6 May 2010 Parliamentary election. The current wording of the exemption reflects the fact that payments of PAAE were made under a resolution of the House of Commons. However, following the election, expenses are now determined and paid by IPSA under its new scheme in accordance with the Parliamentary Standards Act 2009. An amendment to ITEPA is needed to reflect this.
6. Section 294 of ITEPA exempts from tax expenses paid to MPs to cover the costs of certain visits to EU institutions or to the Parliaments of other EU members. Like section 292, the exemption is tied to payments that are made in accordance with a resolution of the House of Commons. Again, these payments are now made by IPSA under its scheme and an amendment to ITEPA is needed to reflect this. The amendment also extends the exemption to cover travel to the national Parliaments of Council of Europe member states.

7. To recognise the requirement of MPs of having to carry out their duties in both their constituencies and Westminster, the rules which allow tax relief for expenses incurred on work-related travel have, under a long standing concession, been extended to allow relief for all journeys on Parliamentary business.
8. Without this, in some circumstances expenses reimbursed to MPs for travel between their constituency and Westminster would be taxable. This concessionary treatment will be ended from 7 May 2010 and instead this measure will introduce a statutory exemption for certain travel expenses paid or reimbursed to MPs by IPSA as expenses necessarily incurred in the performance of MPs' Parliamentary functions. Full details will be given in guidance to MPs.
9. Prior to 7 May 2010 MPs were reimbursed the cost of specific travel by spouses and, by concession, no liability to income tax arose. The IPSA scheme will continue to reimburse some spouse travel, but in more restricted circumstances, and a provision will be introduced to allow the tax-free treatment of these payments.
10. The costs of evening meals purchased by MPs and eaten on the Parliamentary estate when the House of Commons is sitting late were previously covered under the PAAE and so not subject to tax under ITEPA. Under the IPSA scheme, payments in respect of such meals are dealt with separately. A new provision is therefore being introduced to exempt from tax the cost of these meals reimbursed under IPSA's scheme to maintain the previous tax treatment.
11. Regulations which will be made under existing powers will also be introduced to ensure that the treatment of NICs will mirror that for tax.

#### **Further advice**

12. If you have any questions about this change, please contact Paul Harris on 020 7147 2528 (email: [pa.harris@hmrc.gsi.gov.uk](mailto:pa.harris@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## SEAFARERS' EARNINGS DEDUCTION: EU AND EEA RESIDENTS

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### Who is likely to be affected?

1. EU and European Economic Area (EEA) residents who pay UK tax on their earnings as a seafarer. Broadly speaking, a seafarer is a person who works on a ship.

### General description of the measure

2. This measure will extend the seafarers' earnings deduction (SED) to EU and EEA seafarers.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. The measure will have effect on and after 6 April 2011.

### Current law and proposed revisions

5. SED can provide 100 per cent tax relief from the earnings for carrying out duties as a seafarer wholly or partly outside the UK during an eligible period.
6. One of the current qualifying conditions for SED is that the claimant must be ordinarily resident in the UK.
7. This condition will be extended so that seafarers who are EU or EEA residents can claim SED on their earnings as a seafarer that are liable to UK income tax. There are no other changes to the rules for SED.

### Further advice

8. This measure was previously announced at the 2009 Pre-Budget Report and a version of this note was published as PBRN23. This note supersedes that version.
9. If you have any questions about this change, please contact Graham Lewis on 0121 712 8604 (email: [graham.lewis@hmrc.gsi.gov.uk](mailto:graham.lewis@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)



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## LANDFILL TAX: CRITERIA FOR DETERMINING MATERIAL TO BE SUBJECT TO THE LOWER RATE

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### Who is likely to be affected?

1. Businesses registered for landfill tax.

### General description of the measure

2. This measure will provide:
  - for the publication and review of criteria for determining the lower rate of landfill tax; and
  - that HM Treasury will have regard to these criteria when listing in an Order the materials that qualify for the lower rate.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. The measure will have effect on and after the date that the legislation receives Royal Assent. The current Treasury Order listing lower rated wastes is not affected by the changes as long as disposals are made, or treated as made, before 1 April 2011.
5. Any changes required to the current Treasury Order as a result of the new primary legislation would come into force on 1 April 2011.

### Current law and proposed revisions

6. Under the current rules in section 42(4) of the Finance Act 1996, HM Treasury must have regard to whether material being landfilled is commonly described as inactive or inert when deciding whether or not to include it in an Order that lists the materials that qualify for the lower rate of tax. The Landfill Tax (Qualifying Material) Order 1996 lists the qualifying wastes.
7. The measure will replace section 42(4) with new provisions that specify that the Commissioners for Her Majesty's Revenue and Customs must publish the criteria that HM Treasury will have regard to when determining what material is lower rated, and will publish revised criteria when necessary. HM Treasury will take account of these criteria when listing in an Order the materials that qualify for the lower rate of tax, for any disposals made, or treated as made, on or after 1 April 2011.

8. Any amendments to the current Landfill Tax (Qualifying Material) Order 1996 needed as a result of changes to primary legislation would be introduced in a new Treasury Order.

**Further advice**

9. This measure was previously announced at Budget 2010 and a version of this note was published as BN54. This note supersedes that version.
10. If you have any questions about these changes, please contact the Excise and Customs Helpline on 0845 010 9000. Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## AGGREGATES LEVY: NORTHERN IRELAND CREDIT SCHEME

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### Who is likely to be affected?

1. Those commercially exploiting taxable aggregate in Northern Ireland.

### General description of the measure

2. This measure will allow for the extension of the Northern Ireland aggregates levy credit scheme for a further ten years. The scheme grants an 80 per cent tax credit to aggregate producers in Northern Ireland who meet certain conditions.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. The primary, enabling legislation will have effect on and after the date that it receives Royal Assent. Regulations will be laid at a later date following State aid approval for an extension of the scheme.

### Current law and proposed revisions

5. Under section 30A of the Finance Act 2001, the Commissioners for Her Majesty's Revenue and Customs may make regulations providing for a tax credit where a charge to aggregates levy has arisen on a quantity of aggregate which has been subject to commercial exploitation in Northern Ireland during a period ending 31 March 2011. Section 30A(2)(b) will be amended so that the period to which such regulations may apply ends on 31 March 2021.
6. Under regulation 3(1) of the Aggregates Levy (Northern Ireland Tax Credit) Regulations 2004, a tax credit may only be granted on aggregate commercially exploited before 1 April 2011. Subject to EU Commission State aid approval, new regulations will be laid amending regulation 3(1) to extend this date to 1 April 2021.

### Further advice

7. This measure was previously announced at Budget 2010 and a version of this note was published as BN57. This note supersedes that version.

8. If you have any questions about this change, please contact the Excise and Customs Helpline on 0845 010 9000. Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## TOBACCO PRODUCTS DUTY: LONG CIGARETTES

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### Who is likely to be affected?

1. Manufacturers and importers of cigarettes.

### General description of the measure

2. This measure will change the basis of tobacco products duty calculation in the case of long cigarettes i.e. those longer than 8 cm excluding any filter.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. The change will have effect on and after 1 January 2011.

### Current law and proposed revisions

5. The current law is section 4 of the Tobacco Products Duty Act 1979. This details how tax is to be calculated on long cigarettes and when they are to be deemed as more than one cigarette.
6. The measure will amend this legislation so that, in the case of cigarettes longer than 8 cm (excluding any filter), each additional 3 cm (or part thereof) is treated as an additional cigarette for the purposes of specific duty calculation. For example a cigarette of 12 cm would be treated as three cigarettes.
7. The measure will ensure UK legislation remains aligned with European Directive 95/59 which has been amended to prevent tax avoidance.

### Further advice

8. If you have any questions about this change, please contact the Excise and Customs Helpline on 0845 010 9000. Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)



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## RELIEF FOR OVERPAYMENTS OF STAMP DUTY LAND TAX AND PETROLEUM REVENUE TAX

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### Who is likely to be affected?

1. Those who pay stamp duty land tax (SDLT) and participators in oil fields who are liable to petroleum revenue tax (PRT).

### General description of the measure

2. This measure will amend the SDLT and PRT error or mistake relief rules. This follows similar changes to the income tax, capital gains tax and corporation tax rules in the Finance Act (FA) 2009. The changes will provide a means of reclaiming overpayments where there is no other statutory route. They will ensure there is a comprehensive statutory scheme of remedies in such cases.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. To allow a transitional period in which claims can be made under the old rules, the measure will have effect on and after 1 April 2011.

### Current law and proposed revisions

5. Paragraph 34 of Schedule 10 to FA 2003 provides relief in cases where a person has overpaid tax under an assessment to SDLT that is excessive due to a mistake in a land transaction return.
6. Part 1 of Schedule 2 to the Oil Taxation Act 1975 and section 33 of the Taxes Management Act 1970 provide relief where a participator in an oil field pays tax under an assessment to PRT which is excessive due to a mistake in a return.
7. The time limit for claiming repayments under both provisions is currently six years. From 1 April 2011 they must be claimed within four years.
8. No repayment is given where the return followed the general practice at the time it was made, or where the mistake is governed by another statutory claim.
9. The measure will remove the requirement that the overpayment must be the result of a mistake in a return and that it must be made under an assessment.

10. The measure will also provide that HM Revenue & Customs (HMRC) are not liable to repay an amount except as provided by the measure or by another provision of the Taxes Acts.
11. The current restrictions on the right of appeal will be removed, allowing an appeal to the courts on the same grounds as appeals against other matters.

**Further advice**

12. This measure was previously announced at Budget 2010 and a version of this note was published as BN65. This note supersedes that version.
13. A Technical Note for the SDLT part of the measure, including draft legislation, was published on 6 January 2010 and is available on the HMRC website.
14. If you have any questions about this change, please contact Nick Mosley on 0151 703 8986 (email: [nick.mosley@hmrc.gsi.gov.uk](mailto:nick.mosley@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## INTEREST HARMONISATION FOR CORPORATION TAX AND PETROLEUM REVENUE TAX

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### Who is likely to be affected?

1. Taxpayers that make late payments to HM Revenue & Customs (HMRC) or receive repayments from HMRC of corporation tax (CT) or petroleum revenue tax (PRT).

### General description of the measure

2. This measure will bring CT and PRT within the harmonised interest regime introduced in the Finance Act (FA) 2009. The harmonised interest regime will apply to all late payments and repayments of taxes and duties administered by HMRC.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. Implementation of interest harmonisation requires changes to a number of HMRC internal systems and is to be phased in over a number of years. The new provisions will be brought into effect by Treasury Orders which will specify the dates from which they have effect.

### Current law and proposed revisions

5. The current primary legislation applying interest to CT is in section 87A of the Taxes Management Act 1970 and in section 826 of the Income and Corporation Taxes Act 1988. The current primary legislation applying interest to PRT is in Schedule 2 to the Oil Taxation Act 1975. The harmonised regime is contained in sections 101 to 105 of FA 2009 and this legislation is being amended to encompass CT and PRT.
6. The current rules on interest have evolved over time with additions and adaptations applied as each major tax has been reviewed or each new tax or duty has been introduced. As such, there are a number of different rules applying for interest across the taxes and duties. For some taxes, interest is charged as soon as payment is late; for others it is only charged where under-declarations are assessed, and for some liabilities there is no late payment interest charged at all. In addition, where repayment interest currently applies it may be called a supplement, credit interest or statutory interest.

7. The new harmonised interest provisions replace the current range of differing regimes with a single legislative framework for interest chargeable on late payments and payable on repayments which will apply to all taxes and duties administered by HMRC. Interest will be charged from the date the tax or duty was due to be paid to HMRC until the date it is paid. HMRC will pay interest on repayments from the date the tax or duty was due to be paid or, if later, the date the payment was actually received, to the date the repayment is made.
8. The interest descriptors particular to the current Acts for each tax and duty will be simplified and unified for all taxes and duties to become late payment interest and repayment interest. The rules for Quarterly Instalment Payments remain unchanged and do not form part of the harmonised rules that will apply to CT. This treatment reflects the particular nature of these payments and responds to representations made during earlier consultation.
9. Customs duties are subject to EU Regulation and as such are outside the scope of the harmonised interest regime.
10. Although administered by HMRC, tax credits and child benefits are not taxes and as such are not covered by this harmonised regime.

#### **Further advice**

11. This measure was previously announced at Budget 2010 and a version of this note was published as BN66. This note supersedes that version.
12. This measure was the subject of consultation in June 2008, November 2008 and December 2009. A summary of the responses to the December 2009 consultation *Interest – Working Towards a Harmonised Regime* was published on the HMRC website in March 2010.
13. The Review of HMRC's Powers, Deterrents and Safeguards website will provide updates on the implementation timetable for each tax and duty.
14. If you have any questions about this change, please contact Don Morley on 020 7147 2407 (email: [don.morley@hmrc.gsi.gov.uk](mailto:don.morley@hmrc.gsi.gov.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## **REVIEW OF HMRC POWERS, DETERRENTS AND SAFEGUARDS: PENALTIES FOR LATE FILING OF RETURNS AND PAYMENT OF TAX**

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### **Who is likely to be affected?**

1. Taxpayers who do not file their tax returns on time or pay their tax liabilities in full and on time for:
  - VAT and insurance premium tax;
  - aggregates levy, climate change levy and landfill tax;
  - air passenger duty, alcoholic liquor duties, tobacco products duty, hydrocarbon oil duties, general betting duty, pool betting duty, bingo duty, lottery duty, gaming duty and remote gaming duty; and
  - other excise duties.
2. This measure will not have effect for tax credits.

### **General description of the measure**

3. This measure will complete the reform of the penalty regimes for late filing of tax returns and late payment of tax. The reform began when legislation for certain taxes was enacted in the Finance Act (FA) 2009 including income tax, corporation tax, inheritance tax and other direct taxes.
4. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### **Operative date**

5. Implementation of new penalties for late filing and late payment requires changes to HM Revenue & Customs' (HMRC) internal systems and processes and is to be staged over a number of years. This will also allow for the substantial education and preparatory period that will be necessary for both taxpayers and their agents. The new provisions will be brought into effect by Treasury Orders which will specify the dates from which they have effect.

### **Current law and proposed revisions**

6. The new regimes will replace the current variety of penalties and will treat late payment of tax and late filed returns separately. The legislation creates penalty models which reflect the more frequent filing and paying obligations for these taxes and duties compared to the direct tax penalty models enacted last year.

7. The late filing and late payment penalty models are broadly similar. These are designed to encourage filing and payment by the correct dates by introducing an escalating series of penalties depending upon the number of failures within a set penalty period. Further penalties will arise if there is a prolonged delay in filing returns or paying the tax due.
8. The new penalties will include a right of appeal against penalty decisions if the taxpayer has a reasonable excuse for the lateness. Late payment penalties may also be avoided where taxpayers have agreed a time to pay arrangement with HMRC.
9. The legislation enacted in FA 2009 included those taxes where the obligation to file or pay is either annual or occasional. It also made specific provision for the filing of Construction Industry Scheme returns and payment to HMRC of deductions collected through the Pay As You Earn (PAYE) system. This measure introduces further penalty models with common features, based upon the underlying principles of influencing behaviour, effectiveness and fairness.
10. The key elements of the new penalty models are as follows:

#### Penalties for late filing returns (quarterly)

- A £100 penalty immediately after the due date for filing (whether or not the tax has been paid);
- the failure also starts a penalty period, which is set for a year;
- if there are further failures within the penalty period, then the fixed penalty escalates by £100 for each of those subsequent failures, up to a maximum of £400 per failure. The penalty period is also extended to the first anniversary of the latest failure;
- if any of the failures are prolonged, then additional penalties of 5 per cent of the tax on the relevant return are charged at six and 12 months from the date of the failure; and
- if, by failing to make the return, the taxpayer is deliberately withholding information to prevent HMRC from correctly assessing the liability to tax, then penalties of up to 100 per cent of the tax on the return may be chargeable.

#### Penalties for late filing returns (monthly)

- This is a very similar structure to the quarterly model above, except that the fixed penalties are £100 for the first six failures in any penalty period, and then £200 for any subsequent failures.

#### Penalties for late payments (quarterly)

- Where a taxpayer first pays late, although there is no penalty, it does start a penalty period, which is set for a period of a year;
- any further failures within that period will attract a penalty of 2 per cent of the unpaid tax, as well as extending the penalty period to the first anniversary of the latest failure;
- a third failure within the period will attract a penalty of 3 per cent, with

- further failures attracting a maximum of 4 per cent; and
- if any of the failures are prolonged, then additional penalties of 5 per cent of the unpaid tax are charged at six and 12 months from the date of the failure.

#### Penalties for late payment (monthly)

- This is a very similar structure to the quarterly model above, except that, after the first failure, the tax-geared penalties are 1 per cent for the next three failures in any penalty period, 2 per cent of the next three failures, etc. up to a maximum of 4 per cent per failure.
11. There are special provisions to deal with circumstances where taxpayers may change from a monthly to a quarterly return, or where exceptional payment obligations may arise.

#### **Further advice**

12. This measure was previously announced at Budget 2010 and a version of this note was published as BN67. This note supersedes that version.
13. This measure has been the subject of three separate consultations: *Meeting the obligations to file returns and pay tax on time* was published in November 2008, building upon an initial consultation published with the same title in June 2008. Draft legislation was then exposed for public comment on 9 December 2009. A summary of responses was published on 25 March 2010.
14. The Impact Assessment relating to this measure was published on the HMRC website on 14 April 2009.
15. If you have any questions about this change, please contact David Lewis on 020 7147 2403 (email: [david.e.lewis@hmrc.gsi.go.uk](mailto:david.e.lewis@hmrc.gsi.go.uk)). Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)



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## REVIEW OF HMRC POWERS, DETERRENTS AND SAFEGUARDS: EXCISE MODERNISATION AND COMPLIANCE CHECKS

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### Who is likely to be affected?

1. Businesses and individuals involved with excise duties on alcohol, tobacco, energy products, gambling duties and air passenger duty.

### General description of the measure

2. This measure will update the compliance checking framework for excise duties, including:
  - modernising information and inspection powers; and
  - aligning the record-keeping rules and the time limits for assessments and claims with changes made to other taxes and duties.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. Time limits for making assessments and claims need a transitional period and are not expected to become fully operative before 1 April 2012.
5. Treasury Orders will bring the changes into effect and specify the operative date. The record-keeping changes and amendments to information and inspection powers are expected to have effect from 1 April 2011.

### Current law and proposed revisions

#### Record-keeping

6. The current legislation in the Customs and Excise Management Act 1979 (CEMA) on excise record-keeping is now slightly out of step with the other taxes. This will be changed so that the high-level rules for record-keeping are aligned across all taxes and duties. It will not change the detailed rules on what information needs to be kept.

7. The existing information and inspection powers in CEMA will be updated, as in the table below:

<b>Existing Power</b>	<b>Elements of proposal that are new, aligned or unchanged</b>
To enter premises of revenue traders	A new element that would permit inspection of documents.
To enter premises of those thought to be acting as revenue traders	A new power to inspect documents is included.
To enter premises used by a revenue trader	Clarification that the existing powers include the power to enter premises used by a revenue trader, even if those premises are owned by another.
To make unannounced visits	No change.
Prohibition of inspection of wholly private premises	This is current practice but is now made explicit.
Application for a warrant to search (section 161A)	The power exists but would be extended to search for documents required to accompany the goods.
Information from those who may hold relevant information	This is new and would allow HM Revenue & Customs (HMRC) to seek information from other parties such as banks. Safeguards would be a formal notice requirement, pre-authorised by a tribunal.

#### Time limits

8. As time limits across other taxes and duties have been aligned in recent years, excise is now out of step. The standard time limit for making claims and assessments will be increased from three to four years. The extended 20 year time limit for deliberate underpayment of excise duty will be retained but the terminology used to describe the behaviours subject to it will be aligned with recent penalties legislation.

#### **Further advice**

9. This measure was previously announced at Budget 2010 and a version of this note was published as BN69. This note supersedes that version.
10. This measure was the subject of consultations published in July and December 2009. Draft legislation was published in January 2010, together with a summary of responses and a final Impact Assessment. The Impact Assessment has been republished today on the HMRC website.
11. The proposals in the July 2009 consultation document for modernising some aspects of the excise administrative regime will be taken forward separately.

12. If you have any questions about this change, please send an email to [powers.review-of-hmrc@hmrc.gsi.gov.uk](mailto:powers.review-of-hmrc@hmrc.gsi.gov.uk) or contact Maria Richards on 020 7147 3223. Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)



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## VAT: CHANGE TO ZERO-RATING OF “QUALIFYING” AIRCRAFT

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### Who is likely to be affected?

1. Suppliers of aircraft; suppliers of parts and services for aircraft; and aircraft operators.

### General description of the measure

2. This measure will change the definition of aircraft that can be supplied at the zero rate from one based on weight and usage to one based on the status of the customer. Supplies of aircraft will be zero-rated only where used by airlines operating for reward primarily on international routes.
3. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

4. The change will have effect for all supplies made on or after 1 January 2011.

### Current law and proposed revisions

5. Schedule 8 to the VAT Act 1994 provides that supplies may be zero-rated where the aircraft is of a weight of not less than 8,000kg and is not designed or adapted for recreation or pleasure use.
6. This will be amended to make the changes as set out above.
7. The change aligns the domestic definition of qualifying aircraft with that in Article 148 of the Principal VAT Directive.
8. There is no change to the treatment of supplies of aircraft to State institutions.

### Further advice

9. This measure was previously announced at Budget 2010 and a version of this note was published as BN46. This note supersedes that version.
10. Notice 744C Ships and Aircraft will be updated to provide full details of the changes and how they will apply in practice.

11. If you have any questions about this change, please contact the VAT Helpline on 0845 010 9000. Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## VAT: PLACE OF SUPPLY OF GAS, HEAT AND COOLING

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### Who is likely to be affected?

1. Suppliers, importers and VAT registered recipients of natural gas, heat and cooling. Also providers and VAT registered recipients of services comprising access to, and use of, natural gas and heat and cooling distribution networks.

### General description of the measure

2. This measure will implement changes to the application of VAT to supplies of natural gas and of heat and cooling. Under existing arrangements gas supplied via the natural gas distribution system is treated as supplied where either a wholesale customer is established or the natural gas is consumed. UK customers registered for VAT are required to account for VAT on the supplies of natural gas they receive from suppliers established abroad as a reverse charge. There are currently no rules which specifically govern the application of VAT to supplies of heat and cooling.
3. The existing rules which also include electricity, are to be amended so as to:
  - extend their scope to cover supplies in all categories of natural gas pipeline;
  - limit their scope to supplies involving natural gas pipelines located in the EU or linked to such pipelines; and
  - extend the relief from VAT at importation to all natural gas imported via a network (including liquefied natural gas by tanker).
4. The amended rules (above) will be extended to apply to heat and cooling supplied through networks.
5. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

6. The measure has effect on and after 1 January 2011.

## **Current law and proposed revisions**

7. Amendments will be made to the following provisions of the VAT Act 1994:
  - section 9A(5) - to amend the definition of “relevant goods” for the purposes of applying the reverse charge mechanism through which VAT is accounted for under the place of supply arrangements; and
  - paragraph 3 of Schedule 4 - to add “other cooling” as a category of goods.
8. Further amendments to reflect these changes will be made via secondary legislation.

## **Further advice**

9. This measure was previously announced at Budget 2010 and a version of this note was published as BN47. This note supersedes that version.
10. If you have any questions about this change, please contact the VAT Helpline on 0845 010 9000. Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## VAT: POSTAL SERVICES

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### Who is likely to be affected?

1. The only business directly affected by the changes is Royal Mail Holdings PLC, the universal service provider (USP) of public postal services in the UK. Some customers of Royal Mail purchasing the relevant services will also be affected, as they will now have to pay VAT.
2. Social mail, including stamped mail, remains exempt from VAT so private individuals should largely be unaffected.

### General description of the measure

3. This measure will apply VAT at the standard rate to certain postal services provided by the USP.
4. The zero-rating for passenger transport services will also be updated to reflect the status of the provider of a passenger transport service made in conjunction with its postal services.
5. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

6. The measure will have effect for supplies made on and after 31 January 2011.

### Current law and proposed revisions

7. Currently, a VAT exemption applies to the conveyance of postal packets, and services connected to the conveyance of postal packets, by the Post Office company, including any wholly owned subsidiary of the Post Office company. In practice, this means Royal Mail (including Parcelforce).
8. The VAT exemption under Group 3 of Schedule 9 to the VAT Act 1994 (VATA) will be amended to restrict the scope of the exemption to supplies of public postal services and incidental goods made by a USP. The exemption will only apply to supplies of services made under a licence duty, including those where - pursuant to a licence duty - the USP allows private postal operators access to its postal facilities.

9. Supplies of services that a USP is not required to make under a licence duty (such as those made by Parcelforce), and services provided on terms and conditions that have been freely negotiated, will in future be subject to the standard rate of VAT.
10. Zero-rating applies to the transport of passengers by the Post Office company (i.e. Royal Mail), including any wholly owned subsidiary of the Post Office company. The provision has historically only been used for rural bus services - known as the "Postbus" - that Royal Mail provides in conjunction with its postal delivery services, although it also applies to other modes of transport, such as aircraft and ships. Item 4(b) of Group 8 of Schedule 8 to VATA will be amended to zero rate passenger transport provided by a USP. There is no change to the scope of the zero-rating.

#### **Further advice**

11. This measure was previously announced at Budget 2010 and a version of this note was published as BN48. This note supersedes that version.
12. Further guidance on the scope of the exemption was published in the Technical Note (VAT – Postal Services) issued on 24 March 2010. VAT Notices 700 *The VAT Guide*, 700/24 *Postage and delivery charges* and 744A *Passenger transport* will be updated to reflect the amendments.
13. If you have any questions about these changes, please contact the VAT Helpline on 0845 010 9000. Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## VAT: LENNARTZ ACCOUNTING: RESTRICTING APPLICATION AND SECURING REVENUE

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### Who is likely to be affected?

1. Taxpayers buying land, property, boats and aircraft which are to be used for both business and private purposes, as well as taxpayers already using Lennartz accounting arrangements for any assets.

### General description of the measure

2. This measure will implement changes to the recovery of VAT for immovable property, boats and aircraft, implementing changes to EC VAT law made by the Technical Directive (Council Directive 2009/162/EU).
3. Revenue protection legislation will also be introduced to ensure that existing Lennartz accounting users continue to pay the VAT due under the accounting mechanism.
4. The legislation relating to recovery of VAT on directors' accommodation will then be redundant, as the implementation of the Technical Directive and related European case law will ensure that there is no entitlement to any VAT recovery on the private use of directors' accommodation. This legislation will be removed.
5. The Government will legislate for this measure in a Finance Bill to be introduced as soon as possible after the summer recess.

### Operative date

6. The changes to implement the Technical Directive and repeal the legislation relating to directors' accommodation will have effect on and after 1 January 2011. The revenue protection legislation will be treated as having always had effect.

### Current law and proposed revisions

7. Under existing arrangements, VAT on immovable property, boats and aircraft is recoverable upfront and in full on both the business and private use of the asset (subject to any partial exemption restriction). VAT is then payable over subsequent years in respect of the private use of the asset. This is known as "Lennartz" accounting. The changes introduced by this measure will ensure that VAT recovery is restricted only to the business use of the asset, excluding any private use by the taxpayer or the taxpayer's staff. Changes to the capital goods scheme will also be introduced so that it will take account of changes in private use over subsequent years.

8. Until a change in policy arising from a European Court of Justice (ECJ) decision, many taxpayers were incorrectly permitted to use Lennartz accounting (see Revenue and Customs Brief 02/10). The revenue protection legislation introduced by this measure ensures that where such taxpayers choose not to unravel these arrangements, they have a statutory obligation to continue to account for the VAT due under the arrangements. The legislation will ensure that this position is treated as having always had effect.
9. Amendments will be made to the VAT Act 1994 (VATA) to:
  - provide a distinction between business input tax and non-business VAT;
  - ensure that for certain assets specified in the new legislation, VAT cannot be recovered in respect of private use or purposes other than those of a business from 1 January 2011;
  - provide a power to make regulations to treat non-business VAT as input tax;
  - provide enabling powers to introduce further regulations; and
  - ensure that VAT is not recoverable in respect of private use of directors' accommodation.
10. Legislation will be introduced to ensure output tax continues to be paid where a credit was allowed in respect of a supply falling under paragraph 5(4) of Schedule 4 to VATA and to provide the detailed circumstances where this will apply as well as definitions. The legislation will be treated as having always had effect.
11. Amendments to regulations will be made as a result of these changes in due course and will amend the capital goods scheme to take into account changes in business/private use of an asset and other related matters.

#### **Further advice**

12. This measure was previously announced at Budget 2010 and a version of this note was published as BN50. This note supersedes that version.
13. If you have any questions about this change, please contact the VAT Helpline on 0845 010 9000. Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## VAT: CHANGE OF STANDARD RATE

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### Who is likely to be affected?

1. All VAT registered businesses.

### General description of the measure

2. Legislation will be introduced in Finance Bill 2010 to increase the standard rate of VAT from 17.5 per cent to 20 per cent.

### Operative date

3. The 20 per cent rate will have effect for any supply made on or after 4 January 2011 and any acquisition or importation taking place on or after that date.

### Current law and proposed revisions

4. Section 2 of the VAT Act 1994 specifies the standard rate of VAT to be charged on the supply of goods or services, the acquisition of goods from another Member State and the importation of goods from outside Member States. This measure amends the standard rate to 20 per cent with effect from 4 January 2011.
5. Zero-rated supplies, such as basic foodstuffs, children's clothing and books; exempt supplies, such as education and health; and supplies subject to VAT at the 5 per cent reduced rate, such as domestic fuel and power, are not affected by this change.

### Further advice

6. Detailed guidance for businesses on implementing this change has been published today on the HM Revenue & Customs website.
7. Anti-forestalling legislation and changes to the VAT flat rate scheme will also be introduced as a result of this measure – see BN44 and 45 respectively for further details of these changes. Changes to the Payment on Account regime thresholds will be made at a later date to maintain the status quo of the scheme.
8. If you have any questions about this change, please contact the VAT Helpline on 0845 010 9000. Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)



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## VAT: CHANGE OF STANDARD RATE: ANTI-FORESTALLING LEGISLATION

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### Who is likely to be affected?

1. VAT registered businesses unable to recover the VAT they incur and their suppliers, who enter into schemes or arrangements to avoid the effect of the increase in the standard rate of VAT to 20 per cent.

### General description of the measure

2. Legislation will be introduced in Finance Bill 2010 to counter arrangements that purport to apply the 17.5 per cent VAT rate to goods or services to be delivered or performed on or after 4 January 2011.
3. The measure provides that in certain circumstances a supplementary charge to VAT of 2.5 per cent will be due on supplies of goods or services on which VAT of 17.5 per cent has been declared.
4. The legislation has been targeted on artificial arrangements and is unlikely to affect suppliers conducting their business as they normally do when no VAT rate increase is anticipated.

### Operative date

5. The scope of the legislation will be announced by the Exchequer Secretary to the Treasury in a Written Ministerial Statement on 22 June 2010. The legislation will have effect for transactions on and after that date.

### Current law and proposed revisions

6. Forestalling occurs when arrangements are put in place for a VAT invoice to be issued by a supplier or payment received by a supplier before the rate increase, where goods are not due to be delivered or services to be performed, until on or after the date that the rate increases to 20 per cent. The grant of a right or similar option may also be used for forestalling.
7. The legislation applies to standard-rated goods and services. It prevents forestalling by introducing a supplementary charge to VAT on the supply of goods or services where the customer cannot recover all the VAT on the supply, and one or more of the following conditions are met:
  - the supplier and customer are connected parties;
  - the value of the supply (and any related supplies made under the same scheme) exceeds £100,000. But this does not apply if the prepayment or issuing an advance VAT invoice is normal commercial practice;
  - the supplier or someone connected to the supplier funds a prepayment for the goods or services; or

- an advance VAT invoice is issued where payment is not due in full within six months (except hire purchase invoices issued in accordance with normal commercial practice).

The supplementary charge to VAT is due on 4 January 2011 and must be accounted for on the supplier's VAT return covering that date.

8. Similar provisions prevent the use of the grant of standard-rated rights or similar options as an avoidance mechanism. They cover cases where before the rate increase the customer is granted the right to receive goods and services after the rate increase, either free or at a discount, and the customer cannot recover all the VAT on the right or option.
9. The supplementary charge to VAT on rights and options applies if one or more of the following conditions are met:
  - the grantor and the customer are connected parties;
  - the consideration for the right or option (and any related supplies made under the same scheme) exceeds £100,000. But this does not apply if the right or option is normal commercial practice; or
  - the supplier or someone connected to the supplier funds the payment for the right or option.The charge becomes due on the date that the option is first exercised on or after 4 January 2011.
10. The charge does not apply to prepaid or invoiced rentals of land, buildings or other assets, if the period concerned is a year or less, and the prepayment or the issuing of an advance invoice is normal commercial practice.
11. Suppliers may adjust the amount payable under contracts with customers for any supplementary charges, unless the contracts say otherwise.
12. The anti-forestalling legislation is contained in a Schedule to Finance Bill 2010 and does not amend the VAT Act 1994.

### **Further advice**

13. Guidance for businesses has been published today on the HM Revenue & Customs website. Further details of the change to the standard rate of VAT are contained in BN43.
14. If you have any questions about this change, please contact the VAT Helpline on 0845 010 9000. Information about Budget measures is Available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

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## VAT FLAT RATE SCHEME: CHANGES TO THE FLAT RATE THRESHOLDS AND PERCENTAGES

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### Who is likely to be affected?

1. Small businesses that currently use, or are considering using, the VAT flat rate scheme.

### General description of the measure

2. This measure recalculates percentages used in the flat rate scheme to reflect the increase in the standard rate of VAT to 20 per cent. The table below shows the new flat rates.
3. The VAT inclusive thresholds applicable to the scheme have also been recalculated to reflect the increase in the standard rate of VAT to 20 per cent.

### Operative date

4. The recalculated flat rate percentages will have effect on and after 4 January 2011 until further notice. The recalculated thresholds will also have effect on and after 4 January 2011 until further notice.

### Current law and proposed revisions

5. The VAT flat rate scheme was introduced in 2002 with the objective of simplifying VAT for businesses with an annual turnover up to £150,000, tax exclusive. That threshold remains unchanged.
6. Currently, a business has to leave the scheme if either its tax inclusive annual flat rate turnover exceeds £225,000 or, on a forward look, its tax inclusive turnover in the next 30 days can reasonably be expected to exceed £225,000. As a result of the increase in the standard rate of VAT to 20 per cent, both of these exit thresholds will be increased to £230,000 to maintain the same effect.
7. However, if a business using the flat rate scheme exceeds the annual exit threshold as a result of a one off transaction but, in the subsequent year, expects its tax inclusive annual flat rate turnover to be less than £187,500, it may remain in the scheme with the agreement of HM Revenue & Customs (HMRC). As a consequence of the increase in the VAT standard rate to 20 per cent this threshold will be increased to £191,500 to maintain the same effect.

8. Membership of the flat rate scheme is optional and businesses wishing to leave it may do so at any time. HMRC also has the discretion to agree a retrospective leaving date and intends to apply this discretion sympathetically where a business takes the view that, as a result of these changes, it no longer wants to use the scheme.
9. These changes come into force on 4 January 2011 and require amendments to secondary legislation which will be made later in the year.

### Further advice

10. Further details of the change to the standard rate of VAT are contained in BN43.
11. If you have any questions about this change, please contact the VAT Helpline on 0845 010 9000. Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)

Category of business	Appropriate percentage
Accountancy or book-keeping	14.5
Advertising	11
Agricultural services	11
Any other activity not listed elsewhere	12
Architect, civil and structural engineer or surveyor	14.5
Boarding or care of animals	12
Business services that are not listed elsewhere	12
Catering services including restaurants and takeaways	12.5
Computer and IT consultancy or data processing	14.5
Computer repair services	10.5
Dealing in waste or scrap	10.5
Entertainment or journalism	12.5
Estate agency or property management services	12
Farming or agriculture that is not listed elsewhere	6.5
Film, radio, television or video production	13
Financial services	13.5
Forestry or fishing	10.5
General building or construction services*	9.5
Hairdressing or other beauty treatment services	13
Hiring or renting goods	9.5
Hotel or accommodation	10.5
Investigation or security	12
Labour-only building or construction services*	14.5

Laundry or dry-cleaning services	12
Lawyer or legal services	14.5
Library, archive, museum or other cultural activity	9.5
Management consultancy	14
Manufacturing fabricated metal products	10.5
Manufacturing food	9
Manufacturing that is not listed elsewhere	9.5
Manufacturing yarn, textiles or clothing	9
Membership organisation	8
Mining or quarrying	10
Packaging	9
Photography	11
Post offices	5
Printing	8.5
Publishing	11
Pubs	6.5
Real estate activity not listed elsewhere	14
Repairing personal or household goods	10
Repairing vehicles	8.5
Retailing food, confectionary, tobacco, newspapers or children's clothing	4
Retailing pharmaceuticals, medical goods, cosmetics or toiletries	8
Retailing that is not listed elsewhere	7.5
Retailing vehicles or fuel	6.5
Secretarial services	13
Social work	11
Sport or recreation	8.5
Transport or storage, including couriers, freight, removals and taxis	10
Travel agency	10.5
Veterinary medicine	11
Wholesaling agricultural products	8
Wholesaling food	7.5
Wholesaling that is not listed elsewhere	8.5

\*"Labour-only building or construction services" means building or construction services where the value of materials supplied is less than 10 per cent of relevant turnover from such services; any other building or construction services are "general building or construction services".

