Langdowns DFK Newman & Co.

Emergency Budget Report

22nd June 2010

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1. Introduction

2. Income Tax

2.1 Rates
2.2 Deduction of Tax at Source
2.3 ISA's
2.4 Furnished Holiday Lettings
2.5 Pensions – Compulsory Annuity Purchase
2.6 Pension Annual Allowance
2.7 Pensions – NEST
2.8 Asbestos Trusts
2.9 Tax Repayments to Settlors
2.10 Childcare Payments
2.11 Capital Allowances for Carers
2.12 Employment Related Securities
2.13 MP's Expenses
2.14 Seafarers

3. Capital Gains Tax

3.1 Rates
3.2 Private Residence Relief for Carers

4. Corporation and Business Tax

4.1 Rates
4.2 Capital Allowances Rates
4.3 FYA's for Goods Vehicles
4.4 Capital Distribution
4.5 Worldwide Debt Cap
4.6 R&D Credit
4.7 Oil & Gas
4.8 EMI Schemes
4.9 EIS & VCT Conditions
4.10 Film Tax
4.11 Consortium Relief
4.12 Investment in Funds
4.13 Loan Relationships
4.14 Stock Dividends from REIT's

5. VAT

5.1 Rates
5.2 Thresholds
5.3 Aircraft
5.4 Power Supplies
5.5 Postal Services
5.6 Lennartz

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6 Indirect Taxes

6.1 Insurance Premium Tax Rates

7 Bank Levy

7.1 Bank Levy

8 Compliance

8.1 Interest on Overdue Tax
8.2 Repayments of Tax
8.3 Anti-avoidance
8.4 Compliance Review

1. Introduction

After so much careful preparation, was this really the austerity budget we had been encouraged to look forward to with dread? True, almost everyone will pay more tax but many of the rises were less painful than we had been conditioned to expect.

Every Chancellor likes to have a goal. Today George Osborne set himself the dual aims of eradicating the structural deficit, excluding net investment, by 2015/16 and for net debt to be falling in the same time.

Today's announcements should reduce forecast borrowing by £37bn in 2014/2015. Public sector net debt will peak at 70.3% of GDP in 2013/2014. All this based on rather lower growth rates than had previously been assumed.

The Office for Budget Responsibility's task is to decide whether the Government's tax and spending measures are likely to deliver its fiscal mandate. The OBR believes the Government will meet both targets one year early.

Certainly, the City took the announcement as a credible plan towards dealing with the UK deficit and marked sterling up and bond yields down in reaction.

Key features include: -

- Introduction of new levy on banks to raise £2bn annually
- Rise in the headline capital gains tax rate to 28% with immediate effect, but softened by an equally immediate increase in entrepreneur's relief to £5m
- Rise in the headline rate of VAT to 20% from 4 January, but softened by no extension of the tax base to food, children's clothing or the like
- Rise in the personal income tax allowance, but negatived for higher earners by the freezing of the higher rate thresholds and curtailment of pension reliefs previously announced
- Retention of the favourable treatment of furnished holiday lettings, including for those letting out properties outside the UK (but in the EEA)

In addition, there are promises of further reviews of the operation of the Controlled Foreign Companies rules, the taxation of branch profits and the taxation of non-domiciled individuals.

Altogether a brave Budget, not just for the judgment on whether the revenue-raising measures will choke off growth and prolong recession but also for the reception the coalition partners are likely to receive from their supporters.

2. Income Tax

2.1 Rates

From 6 April 2011, the personal allowance for individuals under 65 will be increased by £1,000 to £7,475. To remove the benefit of this increase from higher rate taxpayers, the basic rate limit will be reduced by approximately £2,500 although the exact amount will not be confirmed until September's Retail Price Index (RPI) is known.

For National Insurance, the threshold at which employers start paying Class 1 NICs will be increased by an additional £21 per week above indexation. Again the exact figure will not be confirmed until the Autumn. This increase is in addition to the previously announced increase in the employee threshold for NICs and the additional 1% increase in NIC rates.

2.2 Deduction of Tax at Source

At present, there is no statutory deadline for the delivery of reports and payment of tax withheld from interest, patent royalties or other annual payments made by individuals and other non-corporate entities.

A more formal system is to be introduced as soon possible after Parliament's summer recess which will be operated by way of Regulation.

2.3 Individual Savings Accounts (ISAs)

With effect from 6 April 2011, all individuals who invest in ISAs will see limits increased in line with the Retail Prices Index (RPI). From this date all annual increases thereafter will be based on the RPI. In the event that the RPI is negative, the limits will remain unchanged. All RPI calculations will be by reference to the September RPI prior to the start of the tax year.

From 6 April 2010 the annual ISA subscription limits were increased to £10,200, of which £5,100 can be saved in cash. These limits are per individual subscriber. Any subsequent increased limits will enable half to be invested in cash.

From 6 April 2011 the increase due to the RPI will be rounded to the nearest £120. This is to enable individuals who save monthly the ability to calculate their monthly saving more easily.

2.4 Furnished Holiday Lettings

In the 2009 Budget it was announced that there would be changes made to the furnished holiday lettings regime in regard to properties in the European Economic Area (EEA). Owners of properties that fall within the Furnished Holiday Lettings regime qualify for many of the tax benefits available to traders. At the time of the 2009 Budget, a property situated outside the UK did not fall within this regime. Where the property is located in a European Economic Area (EEA) state, this did not appear to comply with European law.

For 2009/10, HMRC have applied the same tax treatment as applies to qualifying UK property to properties located in another EEA state. It was envisaged that this practice would cease from 2010/11 onwards and new rules would be introduced.

However, it has now been announced that the existing rules will continue for 2010/11 and there will be a public consultation with a view to introducing new rules from April 2011. The proposed new rules will ensure that they apply to properties in the EEA as well as the UK, increase the number of days required to be available for letting and actually let and change the way that loss relief is given.

2.5 Pensions – Compulsory Annuity Purchase

The Government has announced that the age at which members of a pension fund must buy an annuity will rise from 75 to 77 with effect from 22 June 2010.

Under current legislation, members with money purchase arrangements who have not bought an annuity by age 75 are subject to strict minimum and maximum income withdrawal limits.

For scheme members who reach 75 on or after 22 June 2010 the above limits will apply from their 77th birthday. In addition, immediately before their 75th birthday, members will be entitled to income withdrawal and a tax free pension commencement lump sum in respect of funds not previously available for income withdrawal.

In the period before the main changes will have effect in 2011/12, tax charges of 35% on lump sum death benefits paid by the scheme will apply if the member dies on or after 22 June 2010 and is aged 75 or over.

The Government has announced that it will shortly consult on the main changes for 2011/12. However, these interim measures enable those reaching 75 to now defer their decision on their pension savings until the new rules have been finalised.

2.6 Pension Annual Allowance

The Government has announced that it is considering restricting pensions tax relief from 6 April 2011, in particular by significantly reducing the annual allowance perhaps to between £30,000 and £45,000. These reformed allowances would replace the changes currently due to come into effect next year.

2.7 Pensions - NEST

The Finance Bill 2010 will legislate to enable the National Employment Savings Trust (NEST) to be registered with HMRC for tax purposes. This measure will treat the NEST as an occupational pension scheme, meaning that members and contributing employers will 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.

2.8 Asbestos Trusts

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

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

2.9 Tax Repayments to Settlors

Settlors are taxable on the income of trusts in which they retain an interest. Where a settlor is liable to income tax at a lower rate than the trustees it can lead to a settlor receiving a tax refund of the tax effectively paid by the trustees.

Previous legislation required a settlor to repay the refund to the trustees where they received it due to an allowance or relief. This requirement will now be extended to require settlors to pay any tax repayment back to the trustees where it relates to trust income that arises on or after 6 April 2010.

The repayments to the trustees will be disregarded for inheritance tax purposes.

2.10 Childcare Payments

Qualifying guardians are individuals who care for one or more children placed with them under a special guardianship order (special guardians) or a residence order (certain kinship carers). They are generally taxed on the income for providing that care under normal trading income rules or the rules for miscellaneous income.

For adult placement carers, HMRC provides simplified income tax arrangements where they can claim a fixed rate of expenses. Until 5 April 2010, special guardians and kinship carers are able to use the simplified tax arrangements, as used by adult placement carers.

From 6 April 2010, qualifying guardians will be exempt from income tax on payments made by a parent or local authority under a special guardianship or residence order.

Where a kinship carer cares for a child who has not been placed with them under a residence order, they will not be qualifying carers for the above. However, they will be entitled to claim the new reliefs for Shared Lives Carers.

Shared lives carers are generally taxed on the income for providing that care under normal trading income rules or the rules for miscellaneous income.

The new rules will replace the simplified rules and create a new set of rules for qualifying shared lives carers, which will encompass shared lives carers and will be based on the rules for foster carers.

A new tax free allowance will be available for 2010/11 and will be available per household and consist of a £10,000 fixed annual amount, plus other amounts depending on the duration of stay and age of the person being cared for.

For 2010/11 only, the qualifying shared lives carers can choose between the simplified rules for adult placements carers or the new annual allowances. These rules only relate to income from the provision of shared lives care or foster care, it will not affect the taxation of the carer's other income.

2.11 Capital Allowances for Carers

There are special capital allowances rules for carers which enable capital expenditure to be written off against their taxable business profits at prescribed rates. This only applies where the carer chooses to tax their income on normal business rules, rather than the other methods allowed. Carers are allowed to adopt whichever set of rules applies each year.

To correct technical anomalies in these rules, and to ensure they operate as intended, the Finance Bill will include corrections to clarify the position where a carer changes their taxation method and set out rules for capital allowances when starting or ceasing to be taxed under the business rules.

The clarified legislation will have effect from the date of Royal Assent.

2.12 Employment Related Securities

A consultation is to be undertaken during this year with a view to ensuring that employment income from employment-related securities is subject to income tax and national insurance. The consultation will look particularly at shares and securities where geared growth arrangements are used.

2.13 MP's Expenses

Legislation will be introduced into the Finance Bill 2010 to address the Income Tax and NIC consequences of the new expenses scheme for MPs which has been administered by the Independent Parliamentary Standards Authority (IPSA) since 6 May 2010.

These changes are required as the current wording of the exemptions reflects the fact that these were made under a resolution of the House of Commons, therefore amendment is required as these expenses are now determined and paid by IPSA.

The legislative changes will apply to and exempt the following expenses:

- Personal Additional Accommodation Expenditure – paid to MPs in respect of additional expenses incurred as a result of staying overnight away from their main residence as a result of their Parliamentary duties.
- Costs of certain visits to EU institutions or to Parliaments of other EU members.
- Previously given as a concession, travel expenses incurred on Parliamentary duties will now be included in the legislation.
- Spouse travel will be exempt; however this will be reimbursed only in more restricted circumstances than previously.
- Evening meals purchased and eaten by MPs on the Parliamentary estate when the House of Commons is sitting late.

In addition, regulations will also be introduced to ensure that the NIC treatment of these expenses mirrors the tax treatment.

2.14 Seafarers

With effect from 6 April 2011, seafarers from the EU and European Economic Area (EEA) will also be able to claim the seafarers' earnings deduction (SED) from UK tax on their earnings as a seafarer. One of the current qualifying conditions is that the claimant must be ordinarily resident in the UK and this condition will be extended to EU or EEA residents.

SED can provide 100% tax relief from earnings carried out as a seafarer wholly or partly outside the UK during an eligible period.

3. Capital Gains Tax

3.1 Rates

The rate of capital gains tax (CGT) for individuals will increase to 28% for gains, or any parts of gains, which taken together with the individual's income for the year exceed the upper limit for payment of basic rate income tax (higher rate taxpayers).

The rate of CGT will remain at 18% for individuals whose total income and gains are less than the upper limit for payment of basic rate income tax (basic rate taxpayers).

The rate of CGT for trustees and personal representatives will increase to 28%.

The effective rate of CGT for gains qualifying for entrepreneurs' relief remains at 10% but the lifetime limit is increased to £5million.

Both the rate changes and the change to the entrepreneur's relief limit take effect for gains arising on or after 23 June 2010. Gains arising before this date are not included when comparing total income and gains for the tax year with the basic rate income tax band.

3.2 Private Residence Relief for Carers

Under current rules, where part of a person's main residence is used exclusively for the purposes of a trade, business or vocation, Private Residence Relief is not available on that part so that a tax charge may arise when the property is sold.

Effective for disposals on or after 9 December 2009, there will be no such restriction of relief where a person cares for an adult under a local authority adult placement scheme.

4. Corporation and Business Tax

4.1 Rates

The main rate of Corporation Tax will reduce from the current rate of 28 % to 27% on 1 April 2011.

There will be further reductions of 1% per annum so that the main rate will be 24% by 1 April 2014.

The threshold for the main rate remains at £1,500,000.

The Small Companies Rate will reduce from the current rate of 21% to 20% on 1 April 2011.

The threshold for the small companies' rate remains at £300,000.

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

4.2 Capital Allowances Rates

Reductions in the rates of capital allowances have been announced in the Budget.

For chargeable periods ending on or after 1 April 2012 (companies) and 6 April 2012 (unincorporated businesses) there will be:

- An annual writing down allowance of 18% (previously 20%) per annum for qualifying plant & machinery expenditure in the general pool; and
- An annual writing down allowance of 8% (previously 10%) per annum for qualifying expenditure in the special rate pool.

In addition, from 1 April 2012, the Annual Investment Allowance (AIA) will be significantly reduced from £100,000 to £25,000.

The AIA is an important tax relief enabling companies to fully write off for tax purposes qualifying capital expenditure on plant and machinery up to the AIA limit. Taxpayers should consider accelerating their programmes of capital expenditure to take advantage of the existing AIA of £100,000 before April 2012 though transitional measures, yet to be announced, may include anti-forestalling moves.

4.3 FYA's for Goods Vehicles

The Chancellor has announced that, for a period of five years starting on or after 1 April 2010 (for companies) and 6 April 2010 (for unincorporated businesses) a 100% First Year Allowance (FYA) will be available for expenditure on new (not second-hand) zero emission goods vehicles.

A qualifying zero-emission goods vehicle is one that:

- cannot under any circumstances produce CO2 emissions when driven; and
- is of a design primarily suited to the conveyance of goods or burden

There are a number of restrictions in order to comply with European State Aid rules.

Additionally, the amount of expenditure that will qualify for the new FYA is limited to €85m per undertaking (including a group of companies) over the five year period.

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4.4 Capital Distribution

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

The treatment of capital distributions will therefore be clarified to enable HMRC to revert to its previous policy where only specified distributions will be regarded as capital. This change, which was announced in March but not then implemented, will have retrospective effect and cover all distributions made on or after 1 July 2009, unless companies elect for this not to apply.

4.5 Worldwide Debt Cap

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

There are 14 separate proposed changes, the main ones are:

- The UK measure of debt in the "gateway test" will be adjusted if a mismatch would occur otherwise
- Where a group includes securitisation companies then the financing costs of the group as a whole are calculated excluding the securitisation companies.
- Long-term arrangements which give rise to an interest-like return are to be taken into account when calculating the cap even if they do not have the legal form of loans
- Stopping a disallowance being allocated to a dual resident company (though any disallowance can be allocated to another group member)
- Including guarantee fees in financing income
- Introducing two restrictions on entities that can be the ultimate parent of a group of companies for debt cap purposes

4.6 R&D Credit

The requirement for SMEs to own intellectual property created as a result of R&D expenditure prior to claiming R&D Tax Relief has been abolished. This applied where SMEs claimed under either the SME scheme or under the Large Company scheme.

Any SME with an accounting period ending on or after 9 December 2009 can claim R&D Tax Relief under the SME scheme whether or not they own the intellectual property.

The measure was previously announced in the Pre-Budget Report by the previous Government. The Coalition Government has announced that there will be further consultation on R&D Tax Reliefs as set out in the March 2010 Dyson report "Ingenious Britain: Making the UK the leading high tech exporter in Europe".

4.7 Oil & Gas

Finance Act 2009 introduced measures to provide fiscal support for investment in the UK or the UK Continental Shelf ("UKCS"). Further measures were announced in the March 2010 Budget and additional measures have now been announced, the most important of which are forms of rollover relief

- With effect from 22 April 2009, reinvestment relief will be permitted on a group basis so the companies reinvesting and realising the gain need not be identical
- With effect from 24 March 2010, expenditure eligible for reinvestment relief is extended to include exploration and development expenditure, including drilling costs

- The scope of the chargeable gains exemption for gains on the swap of UK/UKCS licences is to be extended to include non-licence consideration and will apply to disposals made on or after Budget Day 2011.

Additionally, the field allowance will be extended to include investment in fields that have previously been decommissioned and whose redevelopment is authorised on or after 22 April 2009 and the field allowance thresholds for qualification as ultra high pressure/high temperature fields will be reduced.

4.8 EMI Schemes

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

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

This change will apply to options granted on or after the date that the legislation receives Royal Assent.

4.9 EIS & VCT Conditions

It has been confirmed that four changes have been agreed with the European Commission to widen the scope of the Enterprise Investment Scheme ("EIS") and the Venture Capital Trust ("VCT") scheme. The effective date will be a date to be introduced as soon as possible after the summer recess, except for the change relating to the definition of eligible shares for VCT's which will not affect monies raised prior to that date.

The changes affecting both EIS and VCT are:

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

Changes affecting only VCTs are:

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

4.10 Film Tax

As previously announced in the 2009 Pre-Budget Report, legislation will be introduced in a Finance Bill after the summer recess to correct an unintended anomaly affecting the amount of tax credit claimable where films are produced over more than one accounting period. The following measure will have effect for accounting periods ending on or after 9 December 2009.

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.

This will overcome a quirk in the legislation that restricts the available tax credit in an unintended way.

4.11 Consortium Relief

Consortium relief is available to corporate members of a consortium together owning an interest of 75% or more in consortium-owned company. Losses arising in a consortium-owned company can be surrendered to the consortium corporate members in proportion to their interests in the consortium-owned company.

In addition, a consortium corporate member ("link company") can also pass on these losses to another company in its own group under the normal group relief rules. The current legislation does not allow the relief to be passed on where the link company is not resident in the UK.

Legislation will be introduced where, for accounting periods commencing on or after the publication of the legislation, the link company can be any company established within the European Economic Area.

4.12 Investment in Funds

An anti-avoidance measure will be introduced from 22 June 2010 to ensure that a corporate investor cannot make use of an authorised investment fund to create a credit for UK tax where no UK tax has been paid.

The intention behind the tax regulations dealing with distributions from such funds is that they should be fiscally transparent so that the nature of their receipts is passed on to corporate investors. It has proved possible to circumvent this intention so the following amendments are proposed:

- No corporation tax deduction will be given for interest distributions to the extent that the distribution is derived from dividends exempt from corporation tax, and

- Where a distribution derives from foreign income, the deemed tax credit in the hands of the corporate investor is treated as a foreign tax credit for all tax purposes (and a proportionate part of the income is treated as foreign income).

4.13 Loan Relationships

Legislation is to be introduced in the Finance Bill 2010 to counter avoidance by large companies relating to derecognition of income from loan relationships and derivative contracts.

The legislation will widen the circumstances where profits from loan relationships and derivative contracts are recognised for tax purposes even though they have not been recognised for accounts purposes. Two particular circumstances are envisaged – where the derecognition arises from a variation of a capital interest in a company, and where it occurs because of an event in a subsequent accounting period.

The legislation will affect debits or credits arising on or after 22 June 2010 and a technical note is to be issued in July 2010 setting out the proposals for generic legislation to tackle avoidance schemes.

4.14 Stock Dividends from REIT's

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

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

Recipients of stock dividends paid will be taxed in the same way as they are in relation to cash dividends.

5. VAT

5.1 Rates

The standard rate of VAT will rise to 20% on 4 January 2011. The new VAT fraction for working out the VAT in a VAT inclusive price will be 1/6. This rate increase will be accompanied by anti-avoidance legislation to prevent businesses attempting to subvert the rate change by pre-invoicing customers at the current rate for supplies to be made after 4 January 2010. The anti-avoidance legislation will apply in certain circumstances where the customer cannot recover all the VAT; in particular where the supplier and the customer are connected or the value of the supply exceeds £100,000.

5.2 Thresholds

The VAT Flat Rate Scheme percentages have been recalculated to reflect the higher VAT rate applicable from 1 January 2010. The tax inclusive exit threshold has been increased to £230,000

5.3 Aircraft

The VAT definition of a qualifying aircraft eligible for zero rating will change with effect from 1 January 2011 from one based on weight and usage to one based on the status of the customer. Aircraft zero rating will be restricted to airlines operating aircraft primarily on international routes.

5.4 Power Supplies

From 1 January 2011 the place of supply of gas, cooling and heating will change. The existing reverse charge accounted for by VAT registered customers of overseas gas suppliers is extended to cover all categories of natural gas, heat and cooling. The scope of the measure will be limited to supplies involving natural gas pipelines located in the EU.

5.5 Postal Services

With effect from 31 January 2011 the Royal Mail will start to charge standard rate VAT on certain services that are not provided under its universal service obligation. The change will apply to services that are ‘freely negotiated’ and as such will not cover most stamped or franked mail. It will cover services provided by Parcelforce.

5.6 Lennartz

Following changes to European law, the rules that apply to Lennartz VAT accounting are being changed. Lennartz arrangements allow upfront recovery of VAT incurred on purchases of non-business goods (with a later output tax charge) as an alternative to an initial apportionment.

From January 2010 charities and similar organisations were prevented from using Lennartz. The budget announces legislation to prevent avoidance if taxpayers decide to unravel existing arrangements following this change.

From 1 January 2011 Lennartz accounting will be further restricted and not permitted for immovable property, boats and aircraft. Changes to the VAT Capital Goods Scheme will be introduced so that subsequent changes to the business/non business use of an asset are included.

6. Indirect Taxes

6.1 Insurance Premium Tax Rates

The Insurance Premium Tax (IPT) rates are being increased from 4 January 2011. The standard rate which applies to most insurance will rise to 6% and the higher rate which applies to warranties provided with goods will rise to 20%.

7. Bank Levy

7.1 Bank Levy

With effect from 1 January 2011, a new levy will be introduced on banks and building societies. Currently proposed at an initial 0.4% rate, it will be based on the consolidated balance sheet position less deduction for Tier 1 capital, insured retail deposits and certain other prudential assets.

The Government proposes extensive consultation on the detail of this levy before implementation.

8. Compliance

8.1 Interest on Overdue Tax

Legislation is to be included in a Finance Bill introduced as soon as possible after the summer recess to bring interest on late payments of corporation tax and petroleum revenue tax into the harmonised interest regime introduced in Finance Act 2009.

These provisions are to be phased in over a number of years and will be brought into effect by Treasury Orders specifying the date.

8.2 Repayments of Tax

Legislation is to be included in a Finance Bill introduced as soon as possible after the summer recess to amend stamp duty land tax and petroleum revenue tax error or mistake relief rules so that overpayments can be claimed where there is no other statutory route.

This measure will come into effect for claims made on or after 1 April 2011 and will reduce the current six year time limit to four years. However, repayments will not made where the return followed the general practice at the time it was made or the mistake is governed by another statutory claim.

8.3 Anti-avoidance

The Government is to examine the following:

- The introduction of a general anti-avoidance rule (GAAR) as a strengthened, backstop defence against tax avoidance that exploits loopholes in the specific applicable legislation and is not within the scope of a targeted anti-avoidance rule (TAAR).
- Consultation on bringing Inheritance Tax on trusts within the Disclosure of Tax Avoidance Schemes (DOTAS) regime.
- Further changes to the rules on Stamp Duty Land Tax (SDLT) for high value property transactions.

The Government has also confirmed that Employer Financed Retirement Benefit Schemes (EFRBS) will be within the scope of legislation, to be introduced from April 2011, to tackle arrangements using trusts and other vehicles to reward employees whilst avoiding, deferring or reducing employment tax liabilities.

8.4 Compliance Review

Penalties for late filing of returns and late payment of taxes and duties for indirect taxes, with the exception of tax credits, assessed on a monthly and quarterly basis are to be reformed to bring them closer to the penalty models which apply for direct taxes.

The first penalty for failure to file a quarterly return will be £100, and a 12 month penalty period will start. Further failures within the penalty period will result in the penalty escalating by £100 for each failure, up to a maximum of £400, and the penalty period being extended by a further quarter. Additional penalties of 5% of the tax due are charged 6 and 12 months after the failure.

There will not be a penalty for the first late quarterly payment, but a penalty period of 12 months will commence. A second failure within the period will attract a 2% penalty, a third failure a 3% penalty and subsequent failures a 4% penalty, and the penalty period will be extended each time. Additional penalties of 5% of the tax due are charged 6 and 12 months after the failure.

Penalties for monthly failures follow a similar pattern, except that the penalties for failure to file returns are £100 for the first 6 failures and £200 thereafter, and the penalties for late

payment are 1% for the second, third and fourth failures, 2% for the next three failures, etc. up to a maximum of 4% per failure.

The new penalties will be introduced over a period by Treasury Orders which will specify the dates from which they will apply.

The compliance checking framework for excise duties including alcohol, tobacco, gambling and air passenger duty is to be updated, including:

- Modernising information and inspection powers; and
- Aligning record-keeping rules and time limits for assessments & claims with other taxes and duties.

Information and inspection powers will be amended to allow the inspection of documents, to confirm that premises used by a trader but not owned by them may be entered and to allow information to be sought from relevant third parties, for example a bank.

The high level rules on record keeping will be aligned across all taxes, and the standard time limit for making claims and assessments will be increased to four years in line with other taxes and duties.

Treasury orders will be used to make these changes operative and specify the dates from which they apply.