Linklaters

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UK Tax News.
Issue 30.

Press Releases

Banking Code of Practice on Taxation - HM Treasury, 30 November 2010

HM Treasury has announced that the UK's top 15 banks (which are named in the Press Release) have now all signed up to the Banking Code of Practice on Taxation. As set out in the Press Release, the Code provides that:

> "Banks should have strong governance around tax, which is integrated into their business decision making.

> They should follow the spirit of the law in addition to the letter - this means banks can undertake tax planning to support their business operations, but this should not be used to achieve tax results that are contrary to the intentions of Parliament.

> HMRC and the banks should work together to encourage mutually open and transparent relationships."

Legislation and Guidance

Restriction of Pensions Tax Relief: Response to Queries and Discussion Document - HMRC and HM Treasury, 1 December and 30 November 2010

HMRC has published some additional guidance dealing with questions raised in relation to the reduced annual allowance for tax privileged pensions contributions (from £255,000 to £50,000), that will apply from April 2011.

HM Treasury has also published a discussion document (publicised by way of a Written Ministerial Statement) setting out the options it is considering to assist individuals who exceed the annual allowance and suffer a large tax charge to meet the charge out of pension benefits rather than current income.

See Tax News Issue 26 for further details of the pensions tax relief changes.

Equalisation in Offshore Funds - HMRC, 30 November 2010

HMRC has issued a statement confirming that the Offshore Funds (Tax) Regulations 2009 will be amended to clarify how offshore funds which

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operate equalisation on accumulation units should calculate reported income. Draft legislation will be published by the end of the year.

A number of other issues apparently raised by the industry will also be addressed in early 2011, however no further details are provided at this time.

Autumn Statement, Corporate Tax Roadmap and Associated Consultations - Parliament and HM Treasury, 29 November 2010

The Autumn Statement from the Chancellor of the Exchequer, in response to the Office for Budget Responsibility's Autumn forecast, was given on 29 November 2010.

Although it had been billed as a move away from the Pre-Budget Reports of recent years, George Osborne still used this statement as a platform to launch a number of Government consultations on taxation. These were all published as part of a single document entitled "Corporate Tax Reform: Delivering a More Competitive System" which is intended to form a comprehensive "road-map" of how the Government sees the corporate tax system developing over the next few years (indeed the Government confirms that it does not intend any other significant corporate tax reforms until 2013 other than those discussed in this document).

Click here for a summary of some of the key aspects of the consultations, which relate to the reform of the tax rules on controlled foreign companies, foreign branches and intellectual property.

DOTAS Regulations and Guidance - Parliament and HMRC, 25 and 29 November 2010

Regulations have been made which, from 1 January 2011, will amend the Tax Avoidance Schemes (Prescribed Descriptions of Arrangements) Regulations 2006. The 2006 Regulations set out the "hallmarks" which, if present in a scheme, trigger an obligation to make a disclosure under the disclosure rules. As already announced (see Tax News Issue 26), *inter alia* the amendments will:

> amend the confidentiality and premium fee hallmarks

> remove the off market terms hallmark

Click here for the Explanatory Memorandum.

Revised guidance, reflecting all the changes to be made to the DOTAS regime from 1 January 2011, has been published by HMRC.

Bank Levy - HM Treasury and HMRC, 21 and 24 November 2010

HMRC has published draft legislation dealing with the collection of the bank levy. Although a single "responsible member" will be determined for each

group (either by nomination by the group, a default rule, or HMRC selection), all members of banking and building society groups and all relevant members of non-banking groups, other than securitisation companies, that are within the charge to corporation tax will be jointly and severally liable for the levy. This may result in complications for M&A transactions and structured transactions. The current drafts of the legislation and guidance are below:

> Draft legislation on the collection and management of the Bank Levy

> Explanatory note

> Updated technical note

HM Treasury has also announced that it has reached agreement with France on a mechanism to avoid double taxation, however no details are provided. Discussions with other jurisdictions are continuing.

Finance (No 2) Bill 2010-2011 - Parliament, 22 November 2010

The Finance (No 2) Bill 2010-2011 (the third Finance Bill of the calendar year) has now passed through the House of Lords (without amendment, as it is a Money Bill and so the Lords has no power to amend it).

Royal Assent is expected on 16 December 2010.

New Tax Transparent Fund Regime - HM Treasury, 22 November 2010

The Financial Secretary to the Treasury, Mark Hoban, has announced that the UK will launch a new authorised fund regime for a tax transparent vehicle. The relevant extract from his speech is below:

“From our consultation work it’s become obvious that there’s a real demand for a tax-transparent vehicle in Britain; the industry were vocal about this - and it was underpinned by convincing evidence, so today I’m pleased to announce that the UK will launch a new authorised fund regime for a tax transparent vehicle. This will help competitive UK firms take advantage of one of the opportunities that UCITS IV presents.

We’ll be working closely with industry to ensure the new vehicle is fit for purpose that it’s both suitable for the pooling of pensions, and for use within the new UCITS IV master/feeder fund structure.”

Stamp Taxes Group Litigation Order - HMRC, 19 November 2010

HMRC has issued a statement confirming that the High Court has granted a group litigation order to provide for the case management of claims relating to the 1.5% stamp duty/SDRT “season ticket” charge, following the decision of the ECJ in Case-569/07 *HSBC Holdings and Vidacos* Nominees. Click here for Linklaters‘ Tax Alert (issued in March 2009), summarising the ECJ decision.

Ministerial Statement Relating to Certain Types of Debt Securities and the Securitisation Regime - Parliament, 19 November 2010

David Gauke has made a written ministerial statement acknowledging that the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) Order 2010 (SI 2010/86) may unintentionally have adverse tax and regulatory consequences. The concern from a tax perspective is that it may have prevented certain securitisation companies from falling within the Securitisation Regulations with effect from February 2010. It was announced that measures will be introduced in the Finance Bill 2011 to ensure that such companies remain within the Securitisation Regulations

Tax Cases

***Executive Benefit Services (UK) Ltd v Revenue & Customs* [2010] UKFTT 550 (TC)**

In this case the First tier Tax Tribunal (John Barton) was required to consider the meaning of the term "associated company" in Section 416 ICTA 1988 (now Section 449 CTA 2010). The issue arose in the context of entitlement to small companies relief under Section 13 ICTA 1988.

The appellant was controlled by an individual that was also a director, shareholder and loan creditor of another company. Although the individual did not have control of the other company by virtue of his shareholding or directorship, the Tribunal found that he did have control by virtue of the loan, and therefore the two companies were associated.

Section 416(2)(c) refers to "such rights as would, in the event of a winding up of the company or in any other circumstances, entitle him to receive the greater part of the assets of the company which would then be available for distribution among the participators". The Tribunal found that a loan owed to a participator has to be regarded as an asset available for distribution for the purposes of this Section, and at the relevant time the loan represented the greater part of the assets of the company. More specifically, the Tribunal found that the repayment of a loan to a participator can be regarded as a "distribution", and that Section 416(2)(c) is not only concerned with the amounts available for distribution in winding up (i.e. amounts available after the company's liabilities have been discharged).

***Houston Cox Interiors Ltd v Revenue & Customs* [2010] UKFTT 510 (TC)**

This was a short decision concerning Section 343 ICTA 1988 (now Chapter 1 of Part 22 CTA 2010). The appellant company acquired the business of a connected company which was suffering serious financial difficulties. The stated consideration was "nil". However, the appellant also made a loan to the transferor company, to enable it to settle its debts (including to HMRC). When

making this loan, the appellant company was aware that it could not be repaid.

The appellant sought to make use of the trading losses suffered by the transferor company in relation to the business in previous years pursuant to Section 343(3) ICTA 1988. However, HMRC contended that the appellant's ability to use such trading losses was restricted by Section 343(4) because the "relevant liabilities" of the transferor company (essentially its retained liabilities) exceeded its "relevant assets" (essentially its retained assets and the consideration it received)

The appellant argued that the substance of the transaction was that it gave consideration for the assets, namely the loan that it knew would not be repaid. However, despite the apparent fairness of such a result, the First tier Tax Tribunal (Geraint Jones QC) emphasised that there was no legal transfer of the liabilities, and that the loan was recorded in both companies' accounts. Recharacterising the loan as consideration in these circumstances would be "a bridge too far". It was noted that this result could have been avoided "had proper care been taken" in structuring the transaction.

Barrie Macey v HMRC [2010] UKFTT 533 (TC)

The First tier Tax Tribunal (Michael Tildesley) found that a one-off award of restricted stock units to the appellant was an inducement to become an employee and was in recognition of his future service as an employee (a "golden hello"). Therefore the award constituted employment income within the meaning of Section 62 ITEPA 2003, and was subject to income tax. The appellant's argument that the award should be regarded as compensation for the surrender of a personal asset unconnected with his employment (shares which he was required to forfeit when leaving his previous employment) was rejected. More specifically, the Tribunal found that:

- the value of the shares to be forfeited was used by the appellant as a "bargaining tool" in the course of his remuneration negotiations;
- the employer awarded the restricted stock units as part of the remuneration package;
- the restricted stock units did not entitle the appellant to immediate payment or a guarantee of future payment;
- the vesting and conversion of the restricted stock units into common stock was conditional on satisfactory and continuous employment;
- the reference to the shares to be forfeited in the employment offer letter was simply to fix the number of restricted stock units included in the remuneration package and nothing more.

HMRC v Airtours Holidays Transport Ltd [2010] UKUT 404 (TCC)

This dispute concerned the input VAT recoverability of amounts paid under a tripartite agreement.

Airtours was in financial difficulties, and needed to renew its loans with a number of financial institutions. The financial institutions approached an accountancy firm to provide advice on the Airtours business. Under a tripartite agreement between Airtours, the financial institutions and the accountancy firm, Airtours agreed to pay the accountancy firm its fee, and subsequently sought to recover the input VAT element. This would only be possible if Airtours itself had received a supply of something of value under the agreement.

The Upper Tribunal (John Avery Jones and Charles Hellier) overturned the decision of the First tier Tax Tribunal, finding that the work done by the accountancy firm did not discharge any business obligation of Airtours, and nor did the group receive any *Redrow*-type benefit (i.e. its business was not benefitted by the right to have the accountancy firm's services provided to the financial institutions). The services were provided by the accountancy firm to the financial institutions (who first approached the accountancy firm and contracted with it) and Airtours had simply contracted to pay its fees.

International Developments

The Future of VAT - European Commission, 1 December 2010

The European Commission has launched a broad consultation, entitled "On the future of VAT: Towards a simpler, more robust and efficient VAT system" which covers all aspects of the European VAT system. The primary focus of the consultation is on cross-border intra-EU transactions, however a number of other areas are addressed, and moreover views are invited on "any other issues that might be relevant to the future of VAT."

Perhaps unsurprisingly given the extensive nature of this exercise, the consultation is on a relatively slow timetable, with comments requested by 31 May 2011, which will then lead to the Commission communicating its priorities by the end of 2011.

Minimum VAT Rate of 15% Maintained - EU Council, 26 November 2010

Article 97(1) of Directive 2006/112 (the EU VAT Directive) provided for a minimum standard VAT rate of 15% until 31 December 2010. This minimum rate has now been extended until 31 December 2015, to prevent a growing divergence in VAT rates leading to "structural imbalances" and "distortions of competition".

EU Infringement Proceedings - European Commission, 24 November 2010

The European Commission has issued press releases concerning a number of infringement proceedings in the field of taxation.

> Belgium, treatment of pension savings contributions (IP/10/1559);

> Denmark, the Netherlands and Spain, exit tax rules (IP/10/1565). A reasoned opinion was sent to these countries in March 2010, concerning tax charge levied by them on the unrealised capital gains of a business changing its residence, moving its permanent establishment or transferring its assets outside of the jurisdiction. The Commission has now decided to take the next step of referring the countries to the ECJ;

> France, electricity taxation (IP/10/1575);

> Ireland, VAT on horses and greyhounds (IP/10/1576);

> Spain, fiscal representatives (IP/10/1569);

> Belgium, discriminatory treatment of certain income from capital (IP/10/1563);

> Spain, VAT on medical items (IP/10/1572).

Press Stories

Big banks meet tax code deadline - Financial Times, 1 December 2010

The biggest banks operating in Britain have met a Treasury deadline to sign up to a code of conduct designed to curb tax avoidance…

Only four of the 15 banks on Mr Osborne's list had signed the code…which he described as "unacceptable". Privately, however, bankers said that they had been unaware of any deadline before the chancellor's announcement.

Many banks, particularly US institutions, had been reluctant to sign up to an extra-statutory code because of uncertainty over its implications.

Patent tax break is poorly targeted, says IFS - Financial Times, 1 December 2010

George Osborne's decision to go ahead with a £1.1bn tax break for patent income came under fire from the Institute for Fiscal Studies, the independent think-tank, which described it as poorly targeted and expensive.

"Our analysis suggests that the policy will lead to a large reduction in UK tax receipts from the income derived from patents, is poorly targeted at promoting research, will add complexity to the tax system, and it is far from clear that any additional research resulting from the policy will take place in the UK," the IFS said on Tuesday.

According to the institute, a small group of companies would benefit the most from the policy... It warned that the Britain's success in attracting patents might be swiftly eroded if other countries followed suit, saying the resulting tax competition “could amount to governments engaging in a race to the bottom in which related government revenues fall”…

Tax advisers defended the government's plans, saying they would stop companies shifting patents out of Britain into low-tax jurisdictions that put the country at risk of losing out on the development work required for the later stages of innovation…

Scotland to be handed £12bn of fiscal powers in draft bill - Financial Times, 1 December 2010

Scotland will see the largest transfer of fiscal power from London since the creation of the union, according to Michael Moore, the Scottish secretary, under draft legislation published on Tuesday.

Proposals in the Scotland bill will see the devolved government receive new financial powers worth £12bn, handing Holyrood control of a third of its budget…

…powers to be devolved include stamp duty and landfill tax - although plans to hand over powers on the aggregates levy and aviation tax have been put on hold.

The bill's most controversial proposal is that the basic and higher rates of income tax should be reduced by 10p in Scotland, with the block grant received by the Holyrood government cut accordingly. This shortfall would force MSPs to take responsibility for revenue-raising as well as spending, by deciding whether to set the Scottish rate of income tax above, below or in line with UK rates…

Corporate tax reform found lacking - Financial Times, 30 November 2010

Far-reaching changes described by George Osborne as “the most significant programme of corporate tax reforms for a generation” may be insufficient to stop some of Britain's biggest multinationals from moving their headquarters offshore, a leading tax expert said.

The Treasury has issued a 94-page “corporate roadmap”, designed to send a “signal loud and clear that Britain is open for business” by modernising “outdated and complex rules for controlled foreign companies [CFCs]”…

The Institute of Directors welcomed the document, particularly on interest deductibility, but said it lacked “real ambition”. The Chartered Institute of Taxation hailed reform “with a sense of urgency”. Will Morris, European tax policy director at the multi-national GE, said: “This is another very positive step.”

The proposals focus on “pragmatic” approaches to protecting the UK tax base, while targeting profits that had been artificially diverted overseas, in an effort not to catch commercial offshore operations in the UK tax net.

The Treasury steered away from curbing interest deductibility, even though the ability to offset interest costs relating to foreign profits against companies' UK tax bills had been seriously considered as a way to protect revenues when the CFC regime was relaxed...

Cable threatens banks with tax on bonuses - The Independent, 29 November 2010

Business Secretary Vince Cable warns today that the Government will tax bankers' bonuses as a “last resort” if voluntary restraint and other “sanctions” failed to end what he calls “a very damaging bonus culture”…

At a series of meetings at the Treasury with the Chancellor and the Business Secretary leaders of the major banks have been asked to show “self-restraint”...

Mr Cable's intervention raises the stakes within the Cabinet over the issue of bank bonuses. Critics have seized on the chancellor, George Osborne's apparent willingness to water down proposed new rules on public disclosure of bonus packages of more than £1m. Mr Osborne has said these should only be made public if agreement can be reached across the European Union - which will take many months...

Irish give and take on tax proves the big draw - Financial Times, 27 November 2010

Low corporate rate is only part of the story for companies fleeing UK levy on foreign profit…

“So what first attracted you to 12.5 per cent corporate tax rate Ireland?”

Certainly the Irish government thinks it knows how companies that have chosen to locate activities in the Republic would answer. Dublin is determined that whatever pain is inflicted in the national recovery plan, that low headline rate is a part of Ireland's “international brand” to be protected no matter what.

The rate remained unscathed this week, though Dublin is under pressure from France, Germany and elsewhere to raise it. While an increase would affect Ireland's international competitiveness, it would be less of a concern for the British companies that moved there than a straight comparison of corporate tax rates would suggest.

The reason is that their decisions to change corporate structure were not down to the headline rate alone…

The CFC regime is an issue particularly for groups that can choose widely where they place operations...

VAT increase Ireland the latest to fall for charms of dream tax - The Times, 26 November 2010

And then there were four. Ireland's decision this week to raise VAT from 21 per cent to 23 per cent by 2014 has established the beginnings of a firm trend.

Beleaguered Portugal is raising its standard rate from 21 per cent to 23 per cent in January. At the same time Poland goes from 22 per cent to 23 per cent and Britain, of course, raises from 17.5 per cent to 20 per cent. “Other countries will now follow,” predicts John Whiting, tax policy director at the Chartered Institute of Taxation.

With most EU nations facing big fiscal deficits and under pressure from bond investors to tighten policy, the temptation to take more from the VAT tap will be irresistible…

EU member nations are free to set their standard VAT rate anywhere in the range of 15-25 per cent, but the trend has been upwards as nations attempt to close their deficits…

Taxes on business ease to promote growth - Financial Times, 19 November 2010

Governments around the world are lightening the fiscal burden on business in spite of big structural deficits, according to a World Bank study…

The study found governments were reluctant to raise taxes on business to avoid stifling recovery. “The economic and financial crisis has caused fiscal constraints for many economies, yet many are still choosing to lower tax rates on businesses,” it said.

The report also warned that economies with the top rankings for ease of payment did not necessarily provide the best models for other countries to follow.

The survey focused on small and medium-sized companies, measuring the cost and administrative burden of taxes for a fictional flower pot manufacturer with five owners and 60 employees. On average, such a company pays nearly half of its commercial profit in taxes, spends seven weeks dealing with its tax affairs and makes a tax payment every 12 days.

The research found that paying taxes is easiest for businesses in high-income economies that had the lowest tax cost and administrative burdens and the greater use of electronic interface with tax authorities. It said that developing countries could increase growth and revenues by reducing profit taxes.

Tax system adds to burden on small business - Financial Times, 19 November 2010

Britain's tax system has slipped from 11th to 16th place over five years in an international ranking of tax effectiveness by the World Bank, a development likely to reinforce the government's drive to increase the UK's competitiveness.

The UK's fall down the league table resulted from increased tax bills on small and medium-sized businesses and an extra administration burden resulting from changes to value added tax rates. The UK had fallen behind some countries on electronic filing, the survey said…

The UK government has promised to simplify the tax system, cut tax rates and reform its regime for foreign profits. David Gauke, exchequer secretary, highlighted concern about the tax system this week, citing a CBI description of it as a "ball and chain round the ankle of the UK economy".

He said: "We need to break these shackles. Our tax system was once viewed as an asset. And it needs to be an asset again."…

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