Tax Representation

ICAEW TAX FACULTY

TAXREP 49/08

Finance Bill 2008: Report Stage Briefing

Parliamentary Briefing submitted by the ICAEW on 27 June 2008 following the completion of the Finance Bill Committee stages and setting out our key concerns in respect of entrepreneurs' relief, the changes to the remittance rules and HMRC's extended information and inspection powers.

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Finance Bill 2008: Report Stage Briefing

1. Clause 7 and Schedule 3, Entrepreneurs' relief

Introduction
Clause 7 and Schedule 3 enact the new 'entrepreneurs' relief' which was announced on 24 January 2008. This relief is based upon the Capital Gains Tax (CGT) retirement rules that were phased out in the beginning of 1999. It provides that gains of up to £1m on the disposal of all or part of a business are taxed at an effective rate of 10% rather than 18%.

Impact on Enterprise Management Incentive (EMI) option holders
We are particularly concerned that the entrepreneurs' relief legislation as drafted will have a detrimental impact on EMI option holders and are concerned that this reflects the change of view by the Government against supporting such initiatives. We believe that EMI option holders should continue to qualify for this new relief from the date that the option is granted was the position for taper relief.

There is continuing concern over the position of EMI option holders and use of EMI to help growing small businesses to recruit or retain employees for good commercial reasons. This is the purpose of EMI as set out in para 4 of Sch 5 ITEPA 2003. The most widely understood benefit of EMI was that business asset taper relief would apply from the date that the option was granted, rather than the exercise date. This was provided for in para 15 of Sch 7D TCGA 1992. There seems no reason why this should also not be the position for entrepreneurs' relief and the amendment proposed at the Committee Stage was for para 15 to be amended to read "for the purposes of claiming entrepreneurs' relief on a disposal of qualifying shares, then in applying s 169I and s169S(3), the shares are treated as if they had been acquired when the original option was granted". Such an amendment would send out a positive signal in terms of the continuing support for EMI by the government, even though it would not greatly extend entitlement to entrepreneurs' relief. The reason for this is that it would still be necessary to achieve the 5% holding for the personal company definition and many EMI options fall short of that level.

Suggested amendment

Schedule 3, pg 133, after para 4, insert

- *Paragraph 15 Sch 7D be amended to read "for the purposes of claiming entrepreneurs' relief on a disposal of qualifying shares, then in applying s 169I and s 169S(3), the shares are treated as if they had been acquired when the original option was granted."*

Section 169K Disposal associated with relevant material disposal (pg 127) & s 169P Associated Disposals, Amount of relief: Special provision for certain associated disposals (pg 130)
The drafting of the legislation in respect of associated disposals in s 169K and s 169P should be clarified. Following the committee debate on this section of the Bill on 13 May 2008, there are two points relating to associated disposals that we would like clarified.

In the debate on 13 May 2008, significant concerns were expressed over the treatment of associated disposals for the purposes of entrepreneurs' relief within the proposed new s 169K and s 169P of TCGA 1992. A particular issue was over the way the just and reasonable apportionments work in s 169P(4) and the position of rent charged on assets prior to 6 April 2008. The Financial Secretary promised further guidance on this point, which would hopefully include some concession on the strict workings of the legislation. In respect of the rent point, a government amendment (No 29) was tabled on 26 June 2008 which restricts the application of s 169P(4) to periods after 6 April 2008. We welcome this amendment.

Further guidance was also promised on the subject of Condition B in s 169K(3) regarding withdrawal from participation in a business in connection with an associated disposal. No guidance has yet been produced.

i) Section169K lays down three conditions, of which condition A is that there is a main disposal qualifying for Entrepreneurs' Relief and condition C is that the property has been in use for the purpose of the business for a 12 month period. However, Condition B is loosely drafted and refers to the associated disposal being 'part of the withdrawal of the individual from participation in the business carried on by the partnership or by the company'. It is not entirely clear what this relates to and it seems to be a retirement requirement of sorts, as well as conflicting with the main drafting of the requirements for a disposal. Its meaning should be clarified.

In response to these concerns and the Committee Debate on 13 May, the Financial Secretary the Rt. Hon Jane Kennedy MP said "I want to think carefully about the hon. Gentleman's remarks, particularly given the importance he attaches to this group of amendments, which is clearly based on his interface with those groups that have been talking to him about their impact". We continue to be concerned about the practical application of ss 169K and 169P.

Suggested amendment:

- *Schedule 3, page 127, delete s 169K(3) and s 169K(5)*

These deletions will require consequential amendments to the rest of s 169K.

ii) Section 169P deals with the restriction of the relief where the associated asset is not used entirely for the purposes of the business throughout the period of the ownership, or only partly used, or where the relief is based on the payment of rent. As noted above the government has now tabled an amendment which deals with the payment of rent before 6 April 2008. However, similar issues still exist in relation to the conditions in s 169P(4)(a), (b) and (c). Therefore, if we take, for example, a farming partnership where the farmland is owned outside of the partnership and where the business is long established, then it would seem to follow that a partner is restricted to his period of ownership of the asset out of the total period of existence of the business even where the asset has always been in business use.

We appreciate that s 169P operates by reference to a just and reasonable apportionment and that in practice HMRC would not seek to restrict relief in this way but we have not seen any guidance and we would pefer that the latter was put beyond doubt.

Suggested amendment

In order to clarify further the legislation and provide certainty to taxpayers we recommend the following amendment

- On page 130,

  On line 30, after (4) delete the rest of line 30 to the end of line 36 and insert:

  'The conditions referred to in sub section (1) are that during the period of ownership of the individual or from 6 April 2008 if later –

  a) that the assets which (or interests in which) are disposed of have not been in use for the purposes of the business throughout that entire period,

  b) that only part of the assets which (or interest in which) are disposed of are in use for the purposes of business'

2. Clause 23 and Schedule 7, Remittance basis

Background

Our objective
It has been our intention throughout this process to be as practical and helpful as possible. Accordingly, we confine our detailed comments in section 2 to areas where we think that:

- the Government has indicated some sympathy with the points we have raised;
- the latest Finance Bill legislation can be interpreted in a way that is unintended and adversely impacts on taxpayers; or
- the provisions create difficulties for unrepresented taxpayers.

The current legislation contains many traps for taxpayers who may, through lack of knowledge in this complicated area, suffer penal tax consequences as a result of making simple mistakes.

Our concerns
We wish to place on record our concerns that there has been insufficient time:

- to achieve legislation which is fit for purpose; and
- to inform taxpayers adequately of the changes which take effect from 6 April 2008.

We are very concerned that in places the legislation we have currently:

- works in a capricious/unintended manner; and/or
- is either so complicated or so impractical (such as the failure to set a delimitation date for the source ceasing provisions) that taxpayers will not be able to adequately self-assess.

We are also concerned that changes which are unfavourable to the taxpayer (such as the new order of matching in s 809P with respect to mixed funds) are being enacted with effect from 6 April 2008 without due attention being drawn to them.

We understand and respect the Government's policy decisions in this area. Our concerns are not with the underlying policy but with the operation of the tax system and the rights of taxpayers. The remittance basis legislation enacted in Schedule 7 introduces new rules for both the position of individuals (mainly Part 1) and the anti-avoidance provisions for offshore structures (mainly Part 2). Given the complexity of the provisions there has been insufficient time to scrutinise either the initial Finance Bill legislation or the Government amendments. The approach that has been adopted is unreasonable and damaging to the reputation of the UK as a place to invest

The rules for individuals
The Finance Act legislation is to be effective from 6 April 2008 but the final rules are still unknown and there is concern over key issues (see sections 2 and 3 below). It is difficult to understate the significance of the changes and yet guidance cannot be provided to taxpayers until after Royal Assent. Many unrepresented taxpayers will not have fully understood what has changed and will have proceeded largely as before possibly taking actions after 5 April 2008 (such as settling from foreign income UK fund management fees offshore where the portfolio contains mainly UK securities) which without their knowing constituted a remittance.

This uncertainty is likely to result in widespread confusion and non-compliance. We have requested previously that the **remittance rules relating to individuals should be postponed until 6 April 2009** but this has been rejected. If the Government is not willing to postpone the remittance rules, we think that as a minimum these new rules should only apply from the date of Royal Assent, with remittances before that date taxed under the old rules.

Offshore trust legislation
We welcome the transitional provisions contained within the legislation for offshore trust structures and the amendments made during the Finance Bill Committee Stage to extend the meaning of "relevant assets" (though we would welcome clarification that the definition of relevant asset includes a new holding acquired after 6 April 2008 as the result of a re-organisation within s 127 TCGA 1992). However, this area of legislation is highly complex and we think that the timescale to draft legislation has been too short.

We are concerned that there is insufficient time to scrutinise legislation of this complexity and that, despite the best efforts of all involved, complex legislation passed with such haste could contain errors. Furthermore, there are significant differences between the legislation we have now and the details released on Budget Day in "RESIDENCE AND DOMICILE: ALIGNING THE CAPITAL GAINS TAX TREATMENT FOR NON-UK RESIDENT TRUSTS". We appreciate why changes occurred in the course of drafting the actual legislation but would say that taxpayers (and especially unrepresented taxpayers) will be very confused by the whole process and decisions could have been taken on the basis of what was set down rather than what the position actually is.

Whilst we appreciate that Government is not minded to accede to this request we believe that the start date of the legislation in Part 2 of Schedule 7 should be postponed until 6 April 2009. This will allow time to correct any technical errors in the

Finance Bill 2009 and ensure that taxpayers have full knowledge of the changes **before** they become effective.

The way forward
When we have the final legislation, we will be producing a practical report setting down the various areas where there is uncertainty either as to the actual meaning of the legislation or how it will work practically. We hope to work with HMRC officials to address the concerns we will raise in this report. **We would welcome Ministerial commitment to the establishment of a joint review group committee comprising officials from HMRC, the professional bodies and other key stakeholders to review the operation of the legislation. We appreciate that the policy decisions have been taken but are concerned to ensure the legislation works in practice and that the inevitable technical errors can be identified and corrected in Finance Act 2009.** The creation of a review group on the remittance basis legislation would seem to provide an appropriate mechanism through which to do this.

Proposed amendment

Schedule 7, page 156, line 8, at end insert –

"No provision within Part 1 of this schedule shall have effect before Royal Assent. Prior to that date remittances shall be determined under the pre Finance Act 2008 provisions.

No provision within Part 2 of this schedule shall have effect prior to 6 April 2009 and the dates and transitional provisions contained herein shall be changed accordingly."

Detailed comments

The comments below are set out in our order of priority rather than their position in the legislation. Page and line references given are with respect to the 23 June 2008 Finance Bill as amended in Committee and Finance Bill Committee.

a) Transitional provisions (page 196 of the Bill, para 83)
We understand that government felt it necessary to amend the para 86 transitional provisions to make it clear the exemptions for property acquired by the relevant person before 12 March 2008 only applied to goods and not money. However, we feel that an unintended consequence of the amendments is that there is now concern that any money brought into the UK prior to 6 April 2008 that was not taxed when remitted (possibly as it was the result of a successful source ceasing operation or a successful alienation) could be deemed to be taxable in 2008/09. Given comments made by government and HM Treasury/HMRC officials we feel sure this is not intended. However, given the importance of the issue we feel that it is vital that the legislation be amended to put the issue beyond any doubt.

We also feel that the issue of exporting and re-importing money after 6 April 2008 should be clarified. We have proceeded on the basis that Government does not intend individuals who have imported funds from successful source ceasing exercises prior to 6 April 2008 to be taxed should the funds be exported and then re-imported. The legislation prior to 6 April 2008 allowed the source-ceasing technique so individuals would have had no reason to keep records. Given how mixed the funds could have become during their various transfers into and out of the UK we feel that to seek to impose a tax charge in such situations would be completely impractical.

Proposed amendment

Schedule 7, page 196, line 37, at end insert –

"(2A) Nothing in section 832 of ITTOIA 2005 (as amended by this Schedule) applies in relation to any of an individual's relevant foreign income that:

a) arose in tax year 2007/08 or any earlier tax year; and
b) has been brought to, or received, or used in, the United Kingdom by or for the benefit of any relevant person at any time before 6 April 2008."

b) Meaning of remitted to the United Kingdom (section 809L, page 162 of the Bill)

We are concerned that the interaction between s 809N and s 809L could unintentionally result in a tax liability arising where an individual has gifted foreign income or chargeable gains prior to 6 April 2008.

We are concerned that an individual can be a gift recipient prior to 6 April 2008 and that the use of "used in" and "enjoyed by" in s 809L(4)(a) is sufficient to apply to a situation where the gift occurred prior to 6 April 2008. For example, a gift of say employment income to a trust, from which the settlor is excluded, which uses the funds to purchase a property for the wife prior to 6 April 2008 would be taxed as a remittance on the husband should he continue to use or enjoy the property by residing there with his wife after 5 April 2008. We felt that the intention was not to impose a tax charge with respect to gifts that occurred before 6 April 2008 even if the use or enjoyment occurs after 5 April 2008.

Proposed amendments

To exempt from the charge gifts occurring prior to 6 April 2008 where only use or enjoyment occurs after 5 April 2008:

Schedule 7, page 197, line 42 at end insert -

"85(5A) Where the qualifying property referred to in condition C of section 809L was gifted prior to 6 April 2008 one reads section 809L(4)(a) as follows "is brought to or received in the United Kingdom by a relevant person."

If Government only wishes the exemption to apply where the property was brought to the UK prior to 6 April 2008 and only use or enjoyment occurs after 5 April 2008:

Schedule 7, page 197, line 42 at end insert -

"85(5A) Where the qualifying property referred to in condition C of section 809L was brought to the UK prior to 6 April 2008 one reads section 809L(4)(a) as follows "is brought to or received in the United Kingdom by a relevant person."

c) Relevant foreign income charged on remittance basis (page 188 of the Bill para 53)

We have expressed significant practical concerns with respect to the anti-source ceasing legislation found at para 53 of Schedule 7.

We note the Minister's comments during the Finance Bill Committee debate:

"I appreciate that in some cases people may no longer have all the records to make a full and complete return. In such cases the individual will need to complete their tax return to the best of their ability and to explain their problem in the white space that is available on the tax return for that purpose. If HMRC inquires into the return—[Interruption.] Well, the hon. Gentleman asked what they would have to do. The individual and HMRC will need to work together to establish the correct figure, based on the facts which the individual is declaring. I am confident that such problems can be dealt with pragmatically by HMRC and if problems arise in practice I am sure that they will be brought to my attention."

Whilst appreciating the point the Minister was making, given that the legislation has no delimination date we think that there will be many problems with this legislation unless HMRC takes a light touch approach. In many cases records will not be available, so it will be impossible to establish the correct figure as the taxpayer will not have the information available to set down facts. Clean capital from before UK residence commenced and from gifts from family resident offshore may have been so intermingled with funds from historic source-ceasing exercises that the individual may have no knowledge of how the account that prior to 6 April 2008 was deemed to wholly contain clean capital is broken down.

It appears to us inevitable that problems will arise in practice and that the way in which HMRC will have to adopt the Minister's instructions to be pragmatic is to only go back so far when looking at source ceasing issues. As such we feel that it would clarify matters and ease concern amongst taxpayers if the legislation contained a delimitation date.

Proposed amendment

Schedule 7, page 188, line 36, after "when the income is remitted" insert "where the source ceased after 5 April 2007".

d) Sections 809C Claim for remittance basis by long-term UK resident: nomination of foreign income and gains to which section 809H(2) is to apply (page 156 of the Bill)

We appreciate the fact that Government decided to cap the remittance basis charge at £30,000. However, we are concerned that the way s 809C(4) is drafted suggests that the claim is invalidated if an individual nominates foreign income or gains which result in a relevant tax increase that exceeds £30,000. This is a genuine and serious concern to taxpayers and we would ask that the amendments set down or Government amendments achieving the same objective are enacted to provide comfort on this issue.

Given the possible ramifications with respect to a claim for foreign tax credit we feel that a taxpayer who makes a mistake and nominates an excessive amount of foreign income/gains or whose return is adjusted so that too much foreign income/gains has been nominated should be informed that they have over-nominated and be entitled to adjust their nomination.

Proposed amendments

Schedule 7, page 156, line 35, leave out "must be" and insert "will be deemed to be".

Schedule 7, page 156, line 42, at end insert-

"Where the relevant tax increase exceeds £30,000 the nomination will be valid but the charge will be capped at £30,000. The individual will be notified that the cap has been enforced and, will have the opportunity to revise the nomination of foreign income and gains. A revised nomination is not necessary for the remittance basis claim to be valid for the tax year."

e) Sections 809Q: remittance of income and gains: transfers from mixed funds (pages 167 to 169 of the Bill)

We explained in our Committee Stage Briefing our concern that the new rules overturn the previous practice as set out in SP5/84 which is more favourable to the taxpayer. We think that it is counter-intuitive and penal to tax previously untaxed income before income that has already suffered tax and there is a risk that taxpayers will not understand the rules.

We note the Minister expressed concern for the position of unrepresented taxpayers during the Finance Bill Committee Debates saying:

> *"The hon. Gentleman makes a fair point. My understanding is that the vast majority of those using the funds would not be in that position; they would be getting good advice. However, I would want to consider whether his point is valid."*

In our experience well advised taxpayers only have mixed fund accounts where the accounts were established before they took proper advice, they have no intentions of making remittances or the accounts are so actively managed by an investment manager that segregation is not commercially viable. Standard advice to clients is to segregate wherever possible as this enables remittances to be made more efficiently. A taxpayer for example would be very badly advised to have mixed in an offshore account:

- UK taxed letting income (£15,000);
- foreign dividend income which suffered 15% withholding tax (£20,000);
- foreign untaxed bank interest (£11,000); and
- pre-arrival capital (£110,000).

An individual who received good advice would have established separate offshore accounts for each source of funds with specially designated interest accounts to receive interest income from the accounts established. If we suppose the individual needed to remit £10,000 the individual would remit funds either from the UK letting income account or the clean capital account and there would be no UK tax liability. In contrast, the unrepresented taxpayer is likely to have just the one account and under s 809Q will be deemed to remit funds from foreign untaxed bank interest thereby incurring a 40% charge (if we assume he or she is a higher rate taxpayer).

We are still of the view that the matching rules should be changed so that matching is undertaken in an order favourable to the taxpayer. Furthermore, rather than imposing a strict matching order which the individual may have insufficient information to support we feel that provided the tax liability is not reduced the individual should be able to nominate the paragraph of foreign income or foreign chargeable gains which has for tax purposed been remitted from the mixed fund account.

Proposed amendments

Schedule 7, page 168, omit lines 27 to 42

After line 26 insert:

"(4) The kinds of income and capital are-

(a) income and gains subject to a UK tax,
(b) employment income subject to a foreign tax,
(c) relevant foreign income subject to a foreign tax,
(d) foreign chargeable gains subject to a foreign tax,
(e) relevant foreign earnings (other than income within paragraph (b)),
(f) foreign specific employment income (other than income within paragraph (b)),
(g) relevant foreign income (other than income within paragraph (c)),
(h) foreign chargeable gains (other than chargeable gains within paragraph (d)), and
(i) income or capital not within another paragraph of this subsection.

Provided it does not result in a lower UK tax liability than if the order shown above is followed an individual may determine which paragraph of income or gains has been remitted from a mixed fund by nomination on his tax return but in default of such a nomination the order is as shown above."

f) Section 809R: composition of mixed fund and section 809Q: anti-avoidance (pages 169 to 170 of the Bill)

Whilst generally we support the use of primary legislation, it must be fit for purpose and proportional to any mischief at which it is aimed.

We are concerned by the drafting with respect to the three sections (809Q, 809R and 809S) dealing with transfers from mixed funds. As we have stated previously prior to 6 April 2008 the mixed fund rules were taken from a mixture of case law and customarily practice. Given that these rules are be held up as comprehensive it would be helpful to have additional clauses to enact the following past HMRC practice (which one assumes is not being overturned). That is that even though a bank (as a matter of banking law) owes only a single debt to its customer (even where the customer has more than one account) for the purposes of the taxes acts the funds will only be deemed to be mixed if they are in the same bank account (*Kneen v Martin 19 TC 33*) and this has not arisen due to banking error (*Duke of Roxburghe's Executors v IRC 20 TC 711*) or because income has been swept in and then swept out again.

We are no entirely clear with respect to the rules where there is a payment out of the offshore account to settle an offshore expense and would welcome clarification as to whether the payment out would be matched to elements within the mixed funds account in the same order as that for a remittance to the UK (that is in line with s 809Q (4)).

We understand the principle that s 809R (Composition of mixed funds) is seeking to enact, namely that where there is a transfer from an offshore account containing mixed funds to another offshore account the funds transferred be treated as containing the same proportion of the different categories of income and capital as the original account from which the funds were transferred. The drafting is complex and the legislation not sufficiently clear.

A far reaching anti-avoidance rule such as that set down at s 809Q appears to us wholly inappropriate in the context of mixed fund accounts. The provision appears to provide HMRC with excessive power to challenge transfers from mixed fund accounts such that the taxpayer will not be confident of their ability to self-assess.

> *Example*
>
> *Mr TF is UK resident but German domiciled. He has an account in Switzerland containing £300,000 which he has accumulated over a number of years from his UK employment bonuses, this means that the whole £300,000 has suffered UK tax. Mr TF received some basic UK tax advice when he first came to the UK and he knew enough to establish a separate income account to receive the interest from the bonus funds.*
>
> *He also had German bank account. He had never intended to remit funds from the German account as he was confident that he earned enough from his UK employment to fund his UK lifestyle and so the German account contained mixed funds.*
>
> *Mr TF wanted to remit the £300,000 from his Swiss account to the UK to acquire a property. However, for family reasons he wanted to retain funds in Switzerland. Accordingly, he transferred £300,000 to the German account and then remitted £300,000 to the UK.*
>
> *Under the matching rules in s 809Q Mr TF should still be seen as remitting the UK employment income and so no additional tax should be payable. It would seem to us quite unfair if the anti-avoidance provisions in s 809S were invoked to deem Mr TF to have remitted income originating from the German account.*

If Government thinks the anti-avoidance provision is necessary we would welcome examples of the mischief it is designed to counter. In our experience it is just ill-advised and unrepresented taxpayers or those who have made a mistake who do not segregate their income rather than taxpayers who are seeking to engage in a sophisticated tax avoidance scheme.

We would suggest that if Government is minded to retain s 809Q, thought is given to copying what was done with the IHT (Double Charge Relief) Regulations 1987. In this case secondary legislation was enacted setting down examples so the primary provisions could be understood and the explanations had statutory authority so could be relied upon by the taxpayer.

Proposed amendments

Schedule 7, page 177, line 37 insert –

> *"(8) "Even though a bank (as a matter of banking law) owes only a single debt to its customer (even where the customer has more than one account) for the purposes of the taxes acts the funds will only be deemed to be mixed if they are in the same bank account and this has not arisen due to banking error (Duke of Roxburghe's Executors v IRC 20 TC 711) or because income has been swept in and then swept out again."*

Schedule 7, page 169, omit lines 40 to 45

Schedule 7, page 170, omit lines 1 to 13

g) Paragraph 127 Rebasing election (page 213 of the Bill) - the need to make an election

As set down in our Finance Bill Committee Briefing our overriding concern is that not all taxpayers may benefit from the rebasing election as trustees may not make the election in time. This will particularly be the case for unrepresented taxpayers who will not have advisers to liaise/educate offshore trustees on their behalf. The Minister indicated during the Finance Bill Committee Debates that she would reconsider the issues as she did not want unrepresented taxpayers to lose out.

It is important to understand that just because an individual is a beneficiary of an offshore trust does not mean that they have access to specialist UK tax advice. Furthermore, offshore trustees (who have to make the election) will not necessarily be up to speed with the changes as quickly as one might think.

Prior to 6 April 2008 offshore trustees did not necessarily need much knowledge of the UK tax system. Provided income was segregated from capital and cleared out of the structure through offshore payments to foreign domiciled beneficiaries on an annual basis the trustees had no need to further concern themselves with UK tax. The period during which an election can be made is quite limited and could easily be missed where trustees have not sought specialist advice in time. Events that took place prior to 6 April 2008 (such as an interest free loan provided by the trust or allowing free use of UK accommodation owned by the trust) can, if they continue after 5 April 2008, give rise to deemed capital payments in 2008/09 and the need for an election to be made by 31 January 2010. Since the trustees will have done nothing active in 2008/09 they may not realise they have made a capital payment and not appreciate the need for advice and action.

It is important to remember that, even where the beneficiary does have access to advice and so knows that the trustees should be making an election, the trustees cannot be compelled to seek specialist advice or to complete the election (which means having contact with an overseas tax authority when there is no need to and may be something the trustees have no interest in doing).

The above demonstrates that where the trustees have to make an election, foreign domiciled beneficiaries may forfeit entitlement to the rebasing provision through no fault of their own. For this reason, we propose a system in which the trustees have to opt out. This would be predicated on the fact that the rebasing provisions in themselves do not involve the trustees in having to provide any information to HMRC. The provisions are only relevant to determining a UK tax liability where there is both a capital payment to a UK resident foreign domiciliary, which is matched to a capital gain with respect to a disposal occurring after 5 April 2008, and the payment is remitted to the UK.

Accordingly, whilst a valuation of all relevant trust assets would have to be obtained and the information retained, it would only be used to calculate the foreign domiciliary's tax liability in the year the capital payment is remitted and HMRC would have the normal powers to enquire into that tax return should they wish to. Prior to the tax year during which the remittance is made there would be no UK tax impact and we can see no reason why additional information need be provided to HMRC.

Should the trustees wish to opt out of the rebasing provisions a document containing the name of the trust, the fact the election is being made, the name of the trustee signing the election and the date and signature would seem to us sufficient.

Proposed amendments

To make the rebasing election automatic:

Schedule 7, page 213:

- *Line 18, delete "made an election under this sub-paragraph" and insert "have not opted out from the provisions within this paragraph".*
- *Line 20 delete "An election under sub-paragraph (1)" and insert "An election to opt out from the provisions within this paragraph".*
- *Line 20 after "on or before the" insert "anniversary of the"*
- *Line 37, delete (1) and replace with (2).*
- *After line 39 insert:*

> *"(6A) The only information that need be provided in the course of making the election is the name of the trust and the name of the trustee making the election."*

Time limit and disclosure

If the above amendments to make the rebasing election automatic are not accepted:

On page 213:

- *Line 20 after "on or before the" insert "anniversary of the"*

- *After line 39 insert:*

> *"(6A) The information that under sub-paragraph (6) can be required by Her Majesty's Revenue and Customs when specifying how an election under sub-paragraph (1) is made cannot exceed the name of the trust and the name of the trustee making the election."*

h) Paragraph 127 Rebasing election page 214 of the Bill the meaning of relevant asset

We welcome the extensions made to the rebasing election as a result of the Government amendments. We suggest below an amendment to clarify the situation where there is a re-organisation under the provisions of s 127 TCGA 1992. An example illustrates our concern:

> *Example*
>
> *The X Offshore Settlement has held a 20% share in UK Trading Ltd since 1990. The shares were worth £4 million immediately before 6 April 2008. On 17 May 2008 the company was acquired by Big Plc in a share for share exchange such that the provisions of s 127 TCGA 1992 were in point and there was no disposal for CGT purposes. The X Offshore Settlement sells its shares in Big Plc on 25 October 2009 for £5 million.*
>
> *We would welcome clarification that the provisions of s 127 TCGA 1992 mean that the holding in Big plc is identified with the original holding in UK Trading Ltd such that sub-paras 127(10)(b) or (11)(b) and (c) of Schedule 7 are deemed to have been met and relief under para 127 of Schedule 7 would be available should the trust make a capital payment to a foreign domiciliary who remits funds to the UK.*

Proposed amendment

Schedule 7, page 214, after line 17 insert-

"(c) For the avoidance of doubt where after 6 April 2008 a re-organisation has taken place which meets the conditions in s 127 TCGA 1992 the new holding (or part of that holding) is a relevant asset if the condition in sub-paragraph (10)(b) or the conditions in sub-paragraph 11 (b) and (c) would be met were the references there to the asset to be read as references to the new asset or the original asset,

i) Aligning the rules for foreign employment income, relevant foreign income and foreign gains

The Government has taken the opportunity with this legislation to align and widen the remittance definitions for foreign employment income, relevant foreign income and foreign gains. Whilst not commenting on the policy decision to align the rules such that the definition of a remittance has been made much stricter, adopting a common definition is a welcome simplification.

A common definition will be particularly helpful for unrepresented taxpayers. However, the benefit of this common definition has been undermined as the exempt property rules in s 809X only apply where imported goods are purchased out of relevant foreign income. Unrepresented taxpayers are likely to assume that since the common definition of a remittance will apply to foreign income and gains, then the exemptions will also apply to all foreign income and gains and that not having them apply in this manner is unnecessarily complicated.

In the interests of fairness and simplicity we think that the rules should be changed to take account of this issue, although we appreciate that the change will make the position more beneficial than that prior to 6 April 2008. If Government is concerned about the impact on the tax take, we propose a monetary limit for single items imported under the personal use rule. It seems to us illogical that an individual can import a £1 million diamond ring purchased out of relevant foreign income without incurring a tax charge but not a £100 watch purchased out of foreign employment income.

Equally we believe that the provisions at paragraph 90 with respect to exempting the payment of interest on offshore mortgages taken out prior to 12 March 2008 should be applicable to payment from foreign income or gains (though in this case it is our understanding that this was the case prior to 6 April 2008).

Proposed amendments

Schedule 7, Page 171:

Line 33, leave out "that derive from relevant foreign income"

Line 36, leave out "that derives from relevant foreign income"

Schedule 7, Page 198

Line 31, delete "Relevant foreign income" and replace with "Foreign income and foreign chargeable gains."

j) Paragraph 90 (page 186), grandfathering of interest payments for offshore mortgages (pages 198 to 199 of the Bill)

We appreciate that the Minister is not minded to extend the provisions to all pre 12 March 2008 offshore mortgages or to mortgages where funds were used to acquire both an interest in the property and finance enhancement work. We also appreciate that the Minister is not minded currently to remove or modify the conditions set down in para 90(3). We feel that there is a significant issue for the unrepresented taxpayer who may unwittingly take out a further loan and by so doing forfeit entitlement to any relief. We request the Minister to consider again the position of the unrepresented taxpayer and whether it is fair that a minor variation to the loan terms of taking out additional loan funds secured on the property should result in all relief being lost.

We do believe that the Minister was minded to allow relief for straight forward re-mortgaging situations where the re-mortgage took place prior to 12 March 2008. However, we feel there is a problem with the legislation as one of the conditions is that the funds should have been received in the UK prior to 6 April 2008. It is our understanding that where there are two offshore mortgage providers it would be unlikely for the funds to be received in the UK. Rather, it would be likely that the new mortgage provider would transfer the funds straight to the original mortgage provider.

Proposed amendments

Schedule 7, page 198, delete line 38.

Schedule 7, page 199. delete line 5.

Schedule 7, page 199, insert after "the money" the words "or directed that the money be used".

k) Section 809W: Consideration for certain services (page 171 of the Bill)

As stated in our prior representations and briefings we have concerns generally with the operation of the extended remittance basis rules with respect to services.

We welcome the fact that this exemption applies to all foreign income and gains.

Extent of the exemption

Further to the Minister's explanation during the Finance Bill Committee debate, we understand the reasoning for introducing this exemption and realise that it is designed to be specific and targeted. However, though the amendment is a response to direct concerns expressed by the financial services industry, we feel that the exemption can (and should) apply to services other than banking and investment management services. The Minister said that:

> "*The hon. Gentleman asked whether the fees exemption would apply to individuals who used a UK-based firm to advise on completing US returns. That could be within the terms of the exemption. However, it would depend on the details of the individual case. I am not deliberately trying to avoid the question; it genuinely will depend on the individual circumstances when the work is considered."*

The explanatory notes state that "Accountancy fees for preparing non-UK tax returns would also be covered providing the majority of the accountancy service relates to non UK property." Please confirm whether UK tax advice pertaining to a foreign domiciliary's UK tax exposure with respect to overseas property would also be considered to be within the exemption? We feel strongly that such advice represents a service which should be covered by the exemption.

We would ask the Minister to consider the position of all service providers in the UK and that this exemption should be worded as broadly as possible to enable fair competition with foreign providers. Accordingly, the exemption should be amended to cover services relating not just to wholly or mainly to property situated outside the UK but also to or employment or trading activities carried on outside the UK.

Why must payment take place overseas?

On a practical level, the stipulation that the payment must be to an overseas account seems a strange condition as it will force UK service providers to have overseas bank accounts whether they would otherwise wish to or not. It adds a complexity and administrative burden that is unwarranted. International money laundering requirements make opening a bank account in a foreign country especially burdensome. It seems especially odd in the context that HMRC are currently engaged in a major exercise to identify UK residents with overseas bank accounts, so encouraging the growth of such accounts will put an extra burden not only onto taxpayers but also onto HMRC.

Travel services

There was speculation that travel services would be covered by the exemption but during the Finance Bill Committee debate the Minister stated that travel would not come within this exemption. Whilst this clarification is welcome to the extent that it removes uncertainty, we are disappointed with the decision as we think it is wrong. It would seem that any payment from offshore income or gains with respect to inward or outward travel to or from the UK will be caught by s 809L and be a remittance. Furthermore, it would appear that the whole cost of the travel service would be deemed a remittance rather than just a proportionate part. We fear this could have a severe impact on the UK as a world renowned transport hub. We had thought that Government had some sympathy for these concerns, and would welcome a clarification of the thinking behind this decision. There appears to us to be a real danger that foreign domiciliaries rather than flying long haul from the UK will take short haul trips out of the UK (to say Dublin or Paris) and go on from there.

Broader effect on UK investment

We are concerned that the legislation at present acts as an incentive for relevant persons such as offshore trusts and companies to disinvest in the UK so that they can come within the terms of the exemption as their assets will be wholly or mainly sited overseas. Where the service is provided to and enjoyed by a non UK resident person, the exemption should apply even if all the trust property is situated in the UK.

Proposed amendments

Schedule 7, page 171, delete lines 16 to 17 and insert-

“(3) Condition A is that the relevant UK service:

(a) relates wholly or mainly to property situated outside the United Kingdom or employment or trading activities carried on outside the United Kingdom;
(b) relates wholly or mainly to travel outside the United Kingdom; or
(c) where the service is provided to and enjoyed by a non UK resident relevant person.

Schedule 7, page 171, delete lines 18 to 21 and insert-

"(4) Condition B is that the whole of the relevant consideration is paid by way or one or more direct payments to the UK service provider or a nominee of the UK service provider."

General Comments

We have produced various representations on the changes as well as Parliamentary briefings. Detailed comments on the changes formed part of our comprehensive Finance Bill Representation which cam be viewed at http://www.icaew.com/index.cfm?route=157680.

Whilst we welcome the fact that some of our concerns have been addressed many of the points we raised have not been. We appreciate the legislation will be passed without further significant amendments but, as stated on page 2 of this briefing, would welcome continued dialogue on practical issues to ensure the legislation achieves the Government's policy aims whilst operating practically and fairly for all taxpayers.

In particular, we would welcome a Ministerial commitment to adopting a pragmatic approach to evaluating the operation of these provisions and, if election time limits or certain provisions are found to be impractical, a commitment to introducing legislation in the Finance Act 2009 to provide practical solutions so that the regime works in the best interest of taxpayers whilst still meeting the Government's policy objectives.

3. Clause 108 and Schedule 36, Information and inspection powers

Paragraph 29, *Right to appeal against taxpayer notice*

We believe that paragraph 29(2) should be amended to provide the taxpayer with the right of appeal against a notice to provide any information or produce any document that forms part of the taxpayer's statutory records. In the Finance Bill Committee debate, the Financial Secretary to the Treasury said, "A right of appeal against a statutory right is inappropriate and would be unworkable in practice. For example, what could the right of appeal be" (column 618). The Minister then said, "If a taxpayer is required to keep the records, it is reasonable that they should be asked to provide them and to show them to HMRC" (column 618).

We believe there needs to be further clarification on this issue. Firstly, the statutory requirement is to keep "records". Whilst a document is capable of being a "record" it is not clear to taxpayers how "any information" can be a "record" and thus form part of the taxpayer's statutory records. Secondly, and more importantly, the right of appeal could be that the taxpayer does not believe that a particular document forms part of their statutory records. We do not dispute that if a taxpayer is required to keep a record it is reasonable that they should be required to produce it to HMRC. A First-Tier Tribunal would order the production of such records so it would be pointless to appeal (particularly bearing in mind that the tribunal will have power to impose costs where it considers that a taxpayer's conduct has been vexatious). It is highly unlikely that a taxpayer would incur the costs of mounting a hopeless appeal to the tribunal "to delay HMRC's compliance work".

However, there are very many records where it is likely to be unclear whether or not something is part of a taxpayer's statutory records. The Financial Secretary told the

Committee that a diary "would be a statutory record only if it were a business appointment diary, such as a hairdresser might keep" (column 618). We doubt that anyone would dispute that the appointment diary of a hairdresser's salon is a statutory record. Its sole purpose is to record customers' appointments. It is the diary of the salon, not of an individual hairdresser. However most taxpayers do not keep separate business and personal diaries and it is often impractical to do so. Unlike the hairdresser's appointment diary, the purpose of such a diary is to remind the individual of what he intends to do at a particular time and to ensure that his appointments do not clash. A taxpayer may not think that their diary forms part of their business records. However, some HMRC Officers would disagree.

It is surely reasonable that a taxpayer should be able to ask the tribunal to decide whether or not their personal appointment diary which happens also to include business appointments, would form part of their statutory records. It is not reasonable that a taxpayer should be expected to decide for themselves that they do not and then have to defend themselves against the imposition of a penalty of £300 plus a further £60 a day for every day between the imposition of the £300 penalty and the Tribunal Service being able to arrange a hearing of any appeal against the initial £300 penalty. It should be remembered that the Financial Secretary thought the suggestion that the daily penalty should not start to accrue until after the tribunal had ruled on the £300 penalty was unreasonable (column 624/625).

Proposed amendments

Page 388:
- *Leave out lines 22 to 24*
- *Leave out lines 32 to 34*

Paragraph 10, Power to inspect business premises etc
We are proposing amendments to the government's amendment 221 set out in column 603 of the Committee's proceedings. This provides that the power to inspect business premises does not include the power to inspect any part of the premises "that is used solely as a dwelling".

The Financial Secretary told the Committee, "The hon. Member for Dundee, East gave a good example of an individual musician. I hope to reassure him that it would be very unlikely that these powers of inspection would apply in that sort of example. A fair question would need to be asked: what business activity would take place that it would be reasonable for HMRC to inspect in that individual's home? It is unlikely that part of the home would be used just for business".

The Minister's last sentence highlights the main issue. On the assumption that she is right that it is unlikely that part of the home would be used "just for business", the government's amendments lets out virtually nothing. It enables HMRC to inspect the entire dwelling house, because it is only those unlikely bits that it excludes. What Stewart Hosie MP said was "I am concerned that someone might take a booking for a band for a wedding on a house phone … and that would negate the family home's being used solely as a dwelling". This point is correct. For example, the musician might sometimes take the phone call on the extension in his bedroom and sometimes on the extension in his living room and sometimes on the extension in his dedicated music room. That would give HMRC power to inspect the bedroom and the living room as the fact that he takes business calls in such rooms prevents them being a part of the premises that is used solely as a dwelling. Whilst the Minister is clearly right in questioning whether it would be reasonable for HMRC to inspect the bedroom, that is hardly a safeguard to the taxpayer who refuses access to the bedroom and in doing so risks the penalty under paragraph 37(1)(b) of £300 plus £60 a day until he gets a hearing before the tribunal to challenge the reasonableness.

Proposed amendments

- *Page 382, line 37, leave out "solely" and insert "in whole or in part".*
- *Page 383, line 23, leave out "solely" and insert "in whole or in part".*

Paragraph 10, Carrying out inspections

We are proposing an amendment to government amendment 222 (set out in column 587 of the Committee proceedings) which provides that where HMRC wishes to inspect premises they must either agree a time with the occupier or give at least 7 days notice or be authorised to do so by an authorised Officer. The provision for agreement with the occupier is meaningless if the Officer can simply give 7 days notice instead of seeking to reach an agreement. The amendment triggers a notice period only if the Officer has sought to reach agreement and the taxpayer has refused to co-operate. It also extends the notice period from 7 to 14 days because it is not unusual for people to take two weeks holiday, so a 7-day notice given during the holiday period would in reality be no notice at all. The requirement to seek to reach agreement is not overridden where an inspection is authorised by an authorised Officer so the extension of the period from 7 to 14 days would not affect HMRC's ability to combat fraud.

Proposed amendment

Page 383, line 29

- *delete from "If sub-paragraph 2" to "the inspection" and insert "If sub-paragraph 2(b) applies or the occupier does not agree a time and sub-paragraph 2 is satisfied, at any reasonable time.*

(2) This sub-paragraph is satisfied if –

a) the occupier of the premises has been given at least 14 days notice of the time of the inspection".

Further information

Please do contact the ICAEW if you require any further information:

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