

# Draft Finance (No. 2) Bill 2017



## Draft Finance (No.2) Bill 2017

The Government has announced today that the Finance (No.2) Bill 2017, which brings back measures deferred from Finance Act 2017, will be introduced into Parliament as soon as possible after the summer recess. The Bill will legislate for all policies that were previously included in the pre-election Finance Bill but which were withdrawn due to the truncated timescale caused by the election.

The Government has published revised draft legislation on seven key areas which contain technical adjustments and additions to the provisions included in the pre-election Finance Bill:

- ▶ Corporate interest restrictions
- ▶ Corporation tax loss relief reform
- ▶ Substantial shareholding exemption reform
- ▶ Anti-hybrid rules
- ▶ The new 'non-dom' regime
- ▶ Inheritance Tax on overseas property representing UK residential property
- ▶ Employment income provided through third parties

The Government has also announced a relaxation of its 'Making Tax Digital' approach, provisions for which will be included in the Finance Bill.

The omission of the draft legislation in other areas does not mean that those measures will not be included in the Finance Bill. The Financial Secretary to the Treasury, Mel Stride, issued a written statement confirming that it is still the Government's intention to introduce the measures that were previously included in the pre-election Finance Bill.

The Bill is expected to receive Royal Assent later in the year and there is still scope for changes to be made in Committee and Report stages once the Bill has been introduced following the summer recess. However the Government has re-confirmed that all policies originally announced to start from April 2017 will be effective from that date, which means that many of the proposed new rules are already in force (even if for accounting purposes the Bill is not yet substantively enacted). This means, for example, that companies subject to quarterly instalment payments ought to have already taken account of these changes and interest could arise if not properly accounted for.

## Business Tax

### Corporate interest deductions

**Summary** From 1 April 2017, the new rules will restrict each group's net corporation tax deductions for interest and other financial payments to 30% of earnings before interest, tax, depreciation and amortisation (EBITDA) that is taxable in the UK, subject to a modified debt cap based upon the worldwide group's net interest expense. An optional group ratio rule, based on the net-interest to EBITDA ratio for the worldwide group, may permit a greater amount to be deducted in some cases, again subject to a modified debt cap. All groups will be able to deduct up to £2mn of net interest expense per annum under the regime. The existing worldwide debt cap rules will be replaced by these rules.

**Changes in the revised clauses** The revised draft clauses include a number of measures which address some of the concerns raised in discussions with HMRC over the last few months, although there are other anomalies that have been discussed which have not been amended in this draft. Some of the key updates that have been made include:

- ▶ Extending the time limits to appoint a reporting company and file an interest restriction return

in the first year so they cannot expire before 31 March 2018 and 30 June 2018 respectively

- ▶ Including previously disallowed amounts that would otherwise have been 'tax-interest' if and when they subsequently become deductible for any reason (eg, under the anti-hybrid rules)
- ▶ Updating the application of the debt cap when using the blended group ratio to prevent excessive limitations
- ▶ Amending the main related party definition so that it is limited to equity interests in an entity and so that a normal commercial loan would not normally make parties related
- ▶ Updating the public infrastructure rules to ensure the grandfathering provisions work as intended, the de minimis rules work in priority to the public infrastructure rules where relevant and decommissioning activities can be qualifying activities

### Corporation tax losses

**Summary** The rules broadly restrict the offset of brought forward losses to 50% of profits arising on or after 1 April 2017, and enable carried forward losses incurred on or after 1 April 2017 to be offset against profits of any description (or group relieved). The new measures are accompanied by a host of anti-avoidance, including extensions to the losses on change of ownership provisions, and a targeted anti-avoidance rule aimed at arrangements looking to circumvent the intended limits of relief.

**Changes in the revised clauses** The revised draft clauses correct some omissions from the original provisions which we have discussed with HMRC. This includes an extension to the provisions allowing trade losses to transfer with an intra-group trade sale to include post-April 2017 trade losses, and to add post-April 2017 non-trading deficits to the list of losses eligible for current year group relief. The effective commencement date for the application to certain losses of the targeted anti-avoidance rule is shifted from 1 April 2017 to 13 July 2017. The revised clauses also contain carve-outs from the effects of the reforms in relation to certain losses arising in the oil & gas and insurance sectors, and in certain corporate rescue situations.

### Substantial Shareholding Exemption

**Summary** With effect for disposals on or after 1 April 2017 certain aspects of the SSE are being reformed. These include the removal of the

investing company/group trading requirement and a relaxation in the substantial shareholding holding period requirement from 12 months within the previous 2 years to 12 months within the previous 6 years. Also, a new exemption is available for investing companies owned by Qualifying Institutional Investors (QIIs). This has no investee company trading requirement and allows the substantial shareholding requirement to be satisfied for investments of less than 10% but costing at least £20mn.

**Changes in the revised clauses** The only provisions published today relate to the QII exemption, where there has been a minor change to the definition of a qualifying life assurance company. We understand the remaining general changes to the SSE will proceed unaltered, in which respect we note that there appears to be no further clarification by the Government of the impact of partnerships on the SSE, except in relation to the QII exemption, despite this being considered during the consultation.

### Anti-hybrid rules

**Summary:** The UK's new anti-hybrid rules were introduced in Finance Act 2016 and came into force on 1 January 2017 to broadly counteract tax advantages arising from the involvement of hybrid entities or instruments or where there is a company with a permanent establishment which generates a similar advantage. Two measures were announced at Autumn Statement 2016 to have effect from 1 January 2017, covering the:

- ▶ Prevention of a deduction for amortisation from being within the scope of the rules for the purposes of the deduction/no-inclusion provisions (although it will remain in scope for the double deduction provisions)
- ▶ Removal of the requirement to make a formal claim to extend the time period during which temporary mismatches relating to hybrid financial instruments or hybrid transfers can be ignored

**Changes in the revised clauses** The changes noted above have been retained in the draft clauses published today. In addition, the definition of foreign tax will be modified with effect from 13 July 2017. From this date, taxes levied by a state, province or other part of a country or municipal or local body taxes will not be considered to be foreign tax for the purposes of the hybrid rules. As an example, income subject to US state tax but not US

federal tax will not be considered as brought into account as income on which a relevant tax is charged.

## Personal Tax

### Reform of domicile rules

**Summary:** Significant changes to the taxation of non-UK domiciled individuals were announced in the Summer Budget 2015. The changes will take effect from 6 April 2017.

Key changes include the following:

- ▶ Non-UK domiciled individuals who have been resident in the UK in 15 out of the last 20 years and those born in the UK with a UK domicile of origin and who are resident in the UK at any time, will be deemed domiciled in the UK for all taxes.
- ▶ There will be special rules for foreign income and gains arising in offshore trusts established by non-UK domiciled individuals (except those with a UK domicile of origin) prior to becoming deemed domiciled in the UK.
- ▶ Individuals becoming deemed domiciled on 6 April 2017 (except those with a UK domicile of origin) will qualify for rebasing for capital gains tax in respect of assets held personally as at 5 April 2017. The assets must have been non-UK situs assets in the period from 16 March 2016 until disposal or from the date acquired, if later
- ▶ Individuals will be able to separate out amounts held in mixed funds under special rules applying for a two year period beginning on 6 April 2017

**Changes in the revised clauses** The changes to the draft clauses are largely technical to ensure the rules operate as expected. However, there has been some uncertainty regarding whether the rules allowing the cleansing of mixed funds would apply to income and gains arising before 6 April 2008 and the new clauses appear to suggest that they will.

For those looking to take advantage of the transitional provisions in respect of loans to protected settlements and the cleansing of mixed funds, the final dates for action also remain unchanged. This means that the window of opportunity will have been shortened by the period of uncertainty.

## Inheritance tax (IHT) on UK residential property

**Summary** The rules broadly provide that, where UK residential property is held via an interest in a non-UK close company or partnership, that interest will no longer be excluded property and will be subject to UK IHT. Similar rules apply to interests in loans made where the loan is used to finance the acquisition, maintenance or enhancement of UK residential property.

**Changes in the revised clauses** Minor technical changes to some of the anti-avoidance provisions have been made, including changes to the calculation of a person's interest in a close company or partnership for the purpose of the 5% de minimis test, below which the new rules would not apply.

## Employment Taxes

### Tackling disguised remuneration avoidance schemes

**Summary** The new rules amend the existing Part 7A ITEPA 2003 'disguised remuneration' rules which are targeted at scenarios where employment income is provided through third parties. Of the 37 or so pages of provisions originally in the March Finance Bill, only 9 pages were retained in Finance Act 2017, which were aimed at ensuring a charge arises where loans are transferred or released (with measures to mitigate any double taxation) in relation to relevant steps taken on or after 6 April 2017. The remaining provisions expected to be re-introduced into Finance (No.2) Bill 2017 cover:

- ▶ Disguised remuneration loans or quasi-loans made on or after 6 April 1999 that remain outstanding on 5 April 2019
- ▶ The disguised remuneration gateway for close companies
- ▶ Schemes by self-employed persons to avoid income tax and NICs, specifically where trading income is provided through third parties, including loans/quasi-loans made on or after 6 April 1999 and before 6 April 2017 that remain outstanding on 5 April 2019
- ▶ The denial of income tax and corporation tax relief for contributions to disguised remuneration tax avoidance schemes, unless

any associated PAYE/NIC charge is paid within 12 months of the relevant period in relation to remuneration paid on or after 6 April 2017/1 April 2017 as appropriate

**Changes in the revised clauses** The definition of disguised remuneration loans or quasi-loans is widened to include those loans or quasi-loans in currencies other than sterling, loans made in a depreciating currency and repayments in currencies other than the loan currency.

## Making Tax Digital

**Summary** The Bill will introduce new digital record-keeping and reporting requirements for businesses within the charge to income tax.

### Changes in the revised clauses

The original measures were subject to significant concern and the Government has now confirmed a new timetable such that:

- ▶ only businesses with a turnover above the VAT threshold (currently £85,000) will be required to keep digital records, and only for VAT purposes initially
- ▶ they will now only need to do so from April 2019
- ▶ businesses will not be required to keep digital records, or to update HMRC quarterly, for other taxes until at least 2020
- ▶ Making Tax Digital will be available on a voluntary basis for the smallest businesses, and for other taxes.

## Other measures expected to be re-introduced in Finance (No. 2) Bill

The following measures are expected to be included in Finance (No.2) Bill 2017, although no update has been provided. The dates shown in brackets are the expected commencement dates.

### Corporate Tax

- ▶ Amendments to the patent box to address cost-sharing arrangements (1 April 2017)
- ▶ Northern Ireland Corporation Tax - expansion of definition of Northern Ireland company (Possibly 1 April 2018)
- ▶ The new museums and galleries relief (1 April 2017)
- ▶ Tax relief for contributions to grassroots sport (1 April 2017)
- ▶ Petroleum Revenue Tax (PRT) - elections for oil fields to become non-taxable (23 November 2016)
- ▶ Taxing all profits arising on/after 8 March 2017 from trading in or developing land in the UK regardless of contract date (8 March 2017)
- ▶ Appropriations to trading stock - denying a market value election where an allowable loss would arise (8 March 2017)
- ▶ First-year allowances for electric charging points (23 November 2016)
- ▶ Simplification of capital allowance claims for investors in co-ownership authorised contractual schemes (1 April 2017)

### Personal Tax

- ▶ Valuation of benefit rule - new provisions introducing valuation rules for benefits received from trustees in respect of loans, moveable property and land (6 April 2017)
- ▶ Business investment relief - proposed amendments to extend the scope of the relief (6 April 2017)
- ▶ Life insurance policies - provisions to allow affected parties to make an application for

disproportionate gains to be recalculated on a just and reasonable basis (Royal Assent)

- ▶ Dividend allowance reduction from £5,000 to £2,000 (6 April 2018)
- ▶ Changes to the taxation of carry to reduce the risk of double taxation (8 July 2015)
- ▶ Reduction in the money purchase annual allowance from £10,000 to £4,000 for individuals who have already accessed pension benefits (6 April 2017)
- ▶ Amendments to Social Investment Tax Relief (6 April 2017)
- ▶ Changes to tax-advantaged venture capital schemes to provide additional clarity and flexibility (5 December 2016 for EIS and SEIS changes, 6 April 2017 for VCT changes)
- ▶ The £1,000 trading and property income allowances (6 April 2017)
- ▶ Personal portfolio bonds - provisions to allow the extension of permitted investments by statutory instrument (Royal Assent)

### Employment Taxes

- ▶ Further amendments to the tax treatment of termination payments - (6 April 2018)
- ▶ Company car tax percentage for ultra-low emission vehicles (6 April 2020)
- ▶ 'Making good' on benefits-in-kind not accounted for in real time through Pay As You Earn (6 April 2017)
- ▶ Enabling of automated PAYE settlement agreements (6 April 2018)

### Indirect Taxes and Stamp Taxes

- ▶ A new 30% penalty regime in relation to VAT 'knew or should have known' fraud (Royal Assent)
- ▶ A new Fulfilment House Due Diligence Scheme for certain fulfilment houses/online marketplaces that offer goods to UK (April 2018)

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- ▶ Potential introduction of a 'split payment mechanism' for overseas businesses selling goods online to UK customers
- ▶ Transfer of primary responsibility for disclosure of VAT avoidance schemes to promoters, and broadened application to other indirect taxes (1 September 2017)
- ▶ Increased gaming duty bands (1 April 2017)
- ▶ Certain freeplays made chargeable to remote gaming duty (accounting periods beginning on or after 1 August 2017)
- ▶ Changes to the rates of air passenger duty (1 April 2018)
- ▶ Changes to what constitutes a taxable disposal for landfill tax purposes (Royal Assent)
- ▶ A licensing scheme for owners and lessees of tobacco manufacturing machinery (1 April 2018)
- ▶ Extension of customs enforcement powers (Royal Assent)

## Tax Administration

- ▶ Introduction of partial closure notices (Royal Assent)
- ▶ Changes to penalties for errors in taxpayers' documents (TBC 2017)
- ▶ New penalty for 'enablers' of tax avoidance arrangements (Royal Assent)
- ▶ Requirement to correct for taxpayers with undeclared past UK tax liabilities in respect of offshore interests (6 April 2017)
- ▶ Money Service Businesses introduced as a new category of data-holder from whom HMRC may require bulk data. (Royal Assent)

## Further information

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