Clients&FriendsMemo

UK Budget 2012 – Key Tax Measures

22 March 2012

The Chancellor of the Exchequer's third budget, held on 21 March 2012, might well be remembered in future years for a balancing act (at least in a taxation context) between stimulus and incentive on the one hand, and austerity and anti-avoidance on the other. A number of the Chancellor's provisions focused on enterprise incentives and were accompanied by an additional 1 per cent. reduction in the main rate of UK corporation tax from April 2012. While these announcements will be welcomed, they were balanced against a very tough message on tax avoidance – particularly in the areas of stamp duty land tax planning and income tax avoidance. Foremost among the Budget statements on combating tax avoidance was the announcement that the Government will proceed with the introduction of a general anti-avoidance rule ("**GAAR**"), consulting in the summer of 2012 on draft legislation based on the recommendations of the Aaronson Report published in November 2011 with a view to introducing legislation in Finance Bill 2013.

In this memorandum we have set out the details of a number of key changes in legislation and practice that we expect to be of interest to Cadwalader's clients and friends. These developments are briefly addressed in our "speed read" section which summarises the key points, each of which is expanded in the lengthier commentaries which follow.

Speed Read

Corporate Tax Competitiveness: reduction in main UK corporation tax rate by an additional 1 per cent. from April 2012. No further change to draft controlled foreign companies legislation or draft patent box legislation announced in Budget 2012.

Stamp Duty Land Tax ("**SDLT**"): increase in rate of SDLT to 7 per cent. on consideration paid for acquisition of residential properties over £2 million, applicable where effective date of transaction is on or after 22 March 2012. Other wide ranging SDLT anti-avoidance provisions announced.

General Anti-Avoidance Rule: announcement of consultation on GAAR in summer 2012, with legislation to follow in Finance Bill 2013.

Disclosure of Tax Avoidance Schemes: formal consultation announced on extending DOTAS hallmarks.

Other anti-avoidance provisions: raft of anti-avoidance measures announced including provisions relating to life insurance policies and corporate settlor-interested trusts.

Plant and Machinery: two targeted anti-avoidance measures to be introduced (and one anti-avoidance measure to be refined) to prevent continued perceived tax avoidance in relation to capital allowances and the sheltering of deferred tax profits in lessor companies.

Financial institutions: measures include an increase in the rate of the bank levy from 1 January 2013, anticipated draft regulations concerning the introduction of a tax transparent fund regime in summer 2012, a regulation making power under which the tax treatment of regulatory capital instruments will be determined and provisions to ensure that listed debtor companies remain eligible for group relief despite issuing certain convertible loans.

Insurance: a new targeted anti-avoidance rule to be introduced to prevent avoidance using the transitional measures under the new Solvency II tax regime for life insurance companies and claims equalisation relief to be abolished with reserves being brought into tax over a six year period.

Enterprise: a number of measures have been announced in relation to seed enterprise investment schemes, enterprise investments schemes, venture capital trusts and enterprise management incentives to both simplify and relax the requirements relating to these tax advantaged schemes and increase the tax benefits available.

Corporate Tax Competitiveness

The Government has announced that the main rate of UK corporation tax will be reduced by an additional 1 per cent. from April 2012. This will result in the main corporation tax rate falling by 2 per cent. from 26 per cent to 24 per cent. in April 2012, to 23 per cent. in April 2013 and to 22 per cent in April 2014. In consequence, HM Treasury have stated that the UK will have the lowest main corporation tax rate in the G7, and the fourth lowest in the G20. The reductions in the main corporation tax rate are part of a co-ordinated strategy to improve UK tax competitiveness, particularly when placed alongside other tax attractive jurisdictions in the EU such as Ireland and the Netherlands. Other key components of the UK Government's strategy of increasing tax competitiveness are the extensive reform of the UK controlled foreign companies ("**CFC**") legislation and the introduction of a UK "patent box". Both measures will be introduced in Finance Bill 2012, due to be published on 29 March 2012.

The new CFC rules will apply to relevant CFC accounting periods beginning on or after 1 January 2013, with companies being able to elect into the patent box regime for accounting periods beginning on or after 1 April 2013.

No new announcements regarding the draft CFC or patent box legislation were made in Budget 2012. Detailed consultation responses and policy update documents were published by the Government regarding the changes to the CFC regime in December 2011 and in both January and February 2012, with a consultation response document for the patent box being published in December 2011.

Stamp Duty Land Tax

In recent years, HMRC have increasingly focused efforts in combating the avoidance of SDLT through a number of approaches. In June 2010, HMRC published "Spotlight 10" featuring SDLT avoidance and asserted that the general SDLT anti-avoidance rule in FA 2003 s.75A could be used to prevent SDLT avoidance schemes seeking to depress or avoid SDLT on the full consideration paid for a property. HMRC stated that such "contrived" arrangements would be "actively challenged, through the courts where appropriate". While the first litigation concerning a sub-sale into a partnership in *DV3 RS Limited Partnership v HMRC*[1] was decided in favour of the taxpayer, HMRC have appealed the decision of the First Tier Tribunal and other litigation is understood to be on-going.

In addition, provisions were introduced in Finance Act ("**FA**") 2011 to prevent schemes exploiting alternative finance relief or property exchanges which were focused on mitigating SDLT. In a tax planning environment in which it was increasingly challenging to mitigate SDLT on a direct property purchase, a number of buyers have explored using companies, unit trusts and other vehicles to acquire property. A number of these structures appear to have been used to effect residential property transactions for non-domiciliaries with an eye to both SDLT and capital gains tax mitigation, with the buyer generally being asked to pay a higher purchase price to reflect lower SDLT costs.

In a corporate context, the use of property holding companies to mitigate corporate chargeable gains and SDLT does not appear to be viewed in a wholly pejorative light.[2] However, the Government's approach, at least as regards SDLT avoidance regarding residential property, appears to have hardened. In Budget 2012, the Government has announced a number of measures designed "to ensure that individuals and companies pay a fair share of tax on residential property transactions". These are:

- to introduce a new 15 per cent. rate of SDLT to be applied to the chargeable consideration for the acquisition of residential properties over £2 million purchased by "non-natural persons", including companies, collective investment schemes and partnerships in which the non-natural person is a partner. The new rate will take effect where the effective date of the land transaction is 21 March 2012 or later and the person(s) acquiring the property are among the non-natural persons to whom the provision applies. This change is intended by

1 *DV3 RS Limited Partnership v HMRC* [2011] UKFTT 138.

2 See HMRC Stamp Duty Land Tax Manual paragraph 23040 in the context of the group relief anti-avoidance provision in FA 2003, paragraph 2(4) Schedule 7.

the Government to "stop or reduce the number of properties that will enter such complex ownership structures" through the "enveloping" of residential property. Owing to the anti-avoidance focus of the measure and immediate effect, no forestalling legislation is to be introduced.

- that the Government will consult on the introduction of an annual charge on residential properties valued at over £2 million owned by non-natural persons. The Government has announced its intention of enacting legislation in this regard in Finance Bill 2013 for commencement in April 2013.
- to extend the capital gains tax regime to gains on the disposal of UK residential property and shares (or interests in such property) by non-resident, non-natural persons with effect from April 2013. Consultation on the extension of the capital gains tax regime in this manner has also been announced by the Government.

Complementing these changes, the Government has announced an increase in the rate of SDLT on the chargeable consideration paid on the acquisition of residential properties over £2 million to 7 per cent. This change of SDLT rate is applicable from 22 March 2012, with transitional provisions ensuring that contracts entered into before 22 March 2012 but completed on or after that date will be charged at the previous SDLT rate applicable for such properties.

Alongside measures designed to prevent SDLT mitigation regarding residential property, the Government has also announced measures to "put beyond doubt" that an SDLT avoidance scheme involving the sub-sale rules and an option to purchase land is ineffective. Under the scheme, the purchaser of an interest in land, at the same time as completing the purchase, grants an option to purchase that interest in land to a third party. The rationale of the scheme is to avoid SDLT on the purchaser's acquisition and to avoid SDLT on the option which remains unexercised. The view of HMRC is that the grant or assignment of an option is not a "transfer of rights" within FA 2003 s45, and that, accordingly, the grant or assignment of the option does not result in the completion of the original contract being disregarded. Nevertheless, draft legislation has been published by HMRC making it clear that the reference in FA 2003 s45(1)(b) to an assignment, subsale or other transaction does not include the grant or assignment of an option. The legislative change will be effective on or after 21 March 2012. The Government has also announced that it will consult on a wider approach to addressing SDLT sub-sale avoidance.

The package of anti-avoidance measures relating to SDLT may be considered to be indicative of a hardening attitude to avoidance generally by the Government. In view of the Government's view that SDLT avoidance schemes continue to be "widely marketed", it was perhaps unsurprising that the ambit of the GAAR (on which see further below) is to be widened to include SDLT. In addition, the Chancellor left no room for doubt in his speech about the Government's determination to eradicate SDLT avoidance in the residential property sector:

> "*Let me make this clear to people. If you buy a property in Britain that is used for residential purposes, then we will expect stamp duty to be paid. That is the clear intention of Parliament. I will not hesitate to move swiftly, without notice and retrospectively if inappropriate ways around these new rules are found. People have been warned*".[3]

Notwithstanding the clear political capital to be obtained by the Government through being seen, very visibly, to be closing down perceived SDLT avoidance structures, it is likely that a detailed analysis of offshore corporate holding structures for UK residential property will result in a variety of non-tax reasons for the establishment of such structures (such as, for example, asset preservation and to enable the widest possible range of potential buyers).

Although shareholders and participants in non-natural holders of UK residential property may wish to unwind such structures before the introduction of the annual charge in April 2013, the introduction of the new SDLT rate of 7 per cent. is likely to make it very challenging to achieve such an unwind without tax costs. Even if suitable methods of unwinding such structures can be located which do not involve significant tax costs, consideration will inevitably need to be given to the risk of such methods being targeted by retrospective tax legislation.

A General Anti-Avoidance Rule, and other anti-avoidance measures

The Government has announced that it will legislate to introduce a GAAR in the UK in Finance Bill 2013. A consultation will take place in the summer of 2012 on the content of the GAAR. However, given that the Government has confirmed in the Budget 2012 press releases that it "accepts the recommendation of the Aaronson Report published on 11 November 2011 that a GAAR targeted at artificial tax avoidance schemes would improve the UK's ability to tackle tax avoidance whilst maintaining the attractiveness of the UK economy as a location for genuine business investment", it seems at least likely that the consultation will echo the approach adopted in the Aaronson Report. It is notable that the scope of the GAAR will be extended to encompass SDLT, although the interaction between the GAAR and the general anti-avoidance rules in the SDLT legislation, FA 2003 s 75A, is unclear at this time.

Following the informal consultation in 2011 on extending the "hallmarks" in the Disclosure of Tax Avoidance Schemes ("DOTAS") regime in FA 2004, the Government has announced that it will engage in a formal consultation in the summer of 2012 on extending the hallmarks. The informal HMRC consultation in June 2011 contemplated possible changes for employment income schemes disclosures, offshore schemes relying on their effect on "less than transparent arrangements in offshore territories" and loss schemes aimed at individuals. The stated intention of the extension of the hallmarks in the 2012 consultation is to capture avoidance schemes which are not currently notifiable, with a view to the publication of draft regulations later in 2012.

3 Budget speech of the Chancellor of the Exchequer, 21 March 2012.

In addition to general announcements regarding the proposals for a GAAR and the consultation on the extension of DOTAS hallmarks, a number of avoidance scheme and arrangements are the subject of proposals and legislative changes in the Budget:

- *Cap on unlimited tax reliefs* – The Government has announced that income tax reliefs, other than those with a statutory limit such as pension contributions or investments in enterprise investment schemes, are to be capped for individuals at £50,000 or 25 per cent. of income, whichever is greater, in an single tax year. It is intended that the capping will have effect from 6 April 2013, with draft legislation being published for consultation later in 2012. The proposal is indicative of the Government's determination to counteract perceived tax avoidance, and it will be interesting to see how this proposal dovetails with the extension of the DOTAS hallmarks in the area of loss schemes used by individuals. Particular focus will also fall on the method by which the £50,000 cap will be calculated in order to ensure trading losses arising in genuine, commercial businesses are not affected adversely.

- *Income tax avoidance regarding life insurance policies* – Finance Bill 2012 will include legislation to amend the legislation in the Income Tax (Trading and Other Income) Act 2005 ("ITTOIA 2005") regarding the taxation of life insurance policies, life annuity contracts and capital redemption policies. The changes are focused on the computation of chargeable event gains which may be liable to income tax.

  There are two main changes. First, the legislative change will ensure that interdependent and "connected" policies , where the value of benefits payable from one policy is dependent on the premiums paid into another policy, are treated as one single policy for the purposes of the chargeable event gains regime. Second, the legislation will "put beyond doubt" that the calculation of a chargeable event gain under a life insurance policy will permit the deduction of earlier gains in the life of that policy only to the extent that the earlier gains are attributable to one of the persons taxable under the chargeable event gain regime. HMRC's concern in this regard appears to have been that schemes have been designed to crystallise earlier (deductible) gains at a time when no taxpayer would bear tax on that earlier gain (owing to, for example, the non-residence of the person to whom the earlier gain was attributable).

  The changes will apply to policies issued on or after 21 March 2012 and to policies issued before 21 March 2012 where certain events occur on or after this date.

- *Income tax avoidance regarding corporate settlor-interested trusts* – Draft legislation has been produced by the Government for inclusion in Finance Bill 2012 to amend the settlements legislation in Part 5, Chapter 5 of ITTOIA 2005, thereby closing down a tax avoidance arrangement involving corporate settlors. ITTOIA 2005, s 624(1) provides that income which arises under a settlement is treated for income tax purposes "as the income of the settlor and of the settlor alone" if it arises during the life of the settlor and from property in which the settlor has an interest. The wording of the legislation has been exploited by corporate settlors of "interest in possession" trusts (in which such a corporate settlor would retain an interest) claiming to avoid income tax at higher or additional rates which would otherwise be due on dividends paid by a subsidiary of the corporate settlor. In this regard, very broadly, the corporate settlor could serve as a tax shelter for an individual beneficiary who would themselves be taxed on such income at higher or additional rates of income tax. The proposed amendments published by HMRC provide that ITTOIA 2005, s 624(1) will not apply from 21 March 2012 to income arising from a settlement which originates from any settlor which was not an individual. A corporate settlor which is interested in a such a settlement will not, therefore, be treated as receiving income from that settlement for the purposes of ITTOIA 2005, s 624(1).

Plant and Machinery

Further changes have been announced to the capital allowances regime to close perceived loopholes and counter tax avoidance as well as to refine changes which have already been included in the draft Finance Bill 2012.

Changes to capital allowances anti-avoidance rules

The capital allowances regime contains certain targeted anti-avoidance rules ("**TAARs**") which apply in relation to sales, hire purchases and assignments of hire-purchase contracts relating to plant and machinery where the transaction is between connected parties, is entered into where to sole or main benefit is the obtaining of an allowance or where the transaction is a sale and lease-back transaction.

Where these circumstances arise, first year allowances and annual investment allowances may be denied and the amount of the allowance claimed by the buyer (recognised for the purposes of the legislation) may be restricted.

An exception to the denial or restriction of allowances applies in cases where there is a sale or hire purchase contract (but not an assignment of the hire-purchase contract) in relation to plant and machinery which is purchased directly from the supplier or manufacturer.

It was unveiled in Finance Bill 2012 that this exception would now only apply to restrictions in the amount of the allowance which may be claimed by the buyer (and no longer to the denial of first year allowances and annual investment allowances) for times on or after 12 August 2011. Additionally, the sole or main benefit standard for one of the three TAARs is to be replaced by a purpose test which will apply the denial and restriction where the main or one of the main purposes of the transaction is to enable a person to obtain a tax advantage. The legislation then operates to cancel the tax advantage.

The exception for purchases and hire-purchases from suppliers and manufacturers was to be modified so that it prevented the denial of first year allowances and annual investment allowances for times on or after 1 April 2012 and 6 April 2012 (as applicable) provided that the transaction (or scheme of which the transaction is part) does not have an avoidance purpose. This modification will now apply with effect from 12 August 2012.

Sale of lessor companies

The tax regime relating to the sale of lessor companies will also be tightened. Currently, when a qualifying change of ownership of a company in the business of leasing plant and machinery occurs, deferred tax profits of the lessor company are brought within the charge of corporation tax. This is intended to prevent purchaser groups being able to utilise the capital allowances of purchased lessor companies to shelter group profits.

Under the tonnage tax rules the profits of lessor companies are not calculated by reference to the usual corporation tax provisions and it is possible to move within the tonnage tax regime without a qualifying change of ownership occurring. The legislation will be amended so that deferred tax profits will also be brought within the charge to corporation tax immediately before a lessor company or transferred lessor trade falls within the charge to tonnage tax.

Additional amendments will also be made to prevent the carry back of losses from an accounting period following a change in ownership from being carried back against the profits brought into account under the rules.

Long funding leases

Capital allowances may be claimed by lessees under long-funding leases. Long funding leases are “funding leases” of more than seven years duration (or, subject to certain conditions, leases of more than five years duration which are not finance leases). A funding lease is a lease which is a finance lease for accounting purposes, a lease under which the present value of the minimum lease payments is 80 per cent of the fair value of the machinery or a lease with a term which is more than 65 per cent. of the remaining useful economic life of the plant and machinery.

When there is a disposal event under the legislation, the disposal value is calculated under a statutory formula which limits the lessee’s total capital allowances to payments made under the lease (excluding finance charges where relief is given separately as a trading expense) less any rebates received.

The Government will now widen the scope of rebates brought within the disposal value formula to include all payments in connection with the lease, or any arrangement connected to the lease, that have not otherwise been brought into account for tax purposes and which are payable for the benefit, directly or indirectly, of the lessee or a connected person. Under the current rules it would seem only “payments” are captured by the formula, however under the new provision “payment” will be taken to include anything of money’s worth regardless of the timing of the “payment”.

Financial institutions

This has been a relatively unspectacular Budget from the perspective of financial institutions generally. However, there are a few announcements of note.

Bank levy

The bank levy, which will rise to 0.088 per cent. with effect from 1 January 2012 (with chargeable equity and long term chargeable liabilities levied at 0.044 per cent.), will now rise again to 0.105 per cent. from 1 January 2013 (and 0.0525 per cent.). The Government's policy behind the increase is that the levy should raise at least £2.5 billion annually, which suggests that the bank levy could rise further if receipts fall below £2.5 billion per year in the future. However, as the Chancellor of the Exchequer announced, at least part of the rationale behind the increase is to protect the Government from any allegation that next year's headline corporation tax cut to 22 per cent. (also announced in the Budget) will benefit the banks. The effect of these two measures on banking institutions may therefore broadly be expected to cancel out one another.

Deduction of tax at source from interest and interest-like returns

A consultation has been announced in relation to the income taxation of interest and interest-like returns with possible legislation to be included in Finance Bill 2013. The consultation will be of interest to financial institutions as they may include changes to the rules concerning the deduction of tax at source from interest and other payments, which can be particularly problematic in some cross-border financing arrangements. The consultation appears to be driven by broad policy considerations, not specific concerns, and could therefore amount to greater importance than the brief mention of this measure in the Budget releases suggests.

Changes have already been included in Finance Bill 2012 in relation to withholding of income tax from interest paid on qualifying time deposits.[4] With effect from 6 April 2012, deposit takers will be required to withhold income tax at the basic rate from interest on qualifying time deposits. Interest on qualifying time deposits made prior to 6 April 2012 may still be paid without deduction of tax.

Foreign currency assets and corporate chargeable gains

A consultation has also been announced with a view to allowing companies with a non-Sterling functional currency to compute their chargeable gains and losses in their functional currency. Legislation may then be included in Finance Bill 2013 to achieve this.

4 A qualifying time deposit is a deposit consisting of a loan of at least £50,000, the terms of which require its repayment within 5 years, where the right repayment cannot be transferred and where partial withdrawals or additions cannot be made.

Basel III and treatment of regulatory capital

Unfortunately, uncertainty remains regarding the tax treatment of regulatory capital instruments issued by banking institutions in accordance with the Basel III accord and the fourth EU Capital Requirements Directive. The Government has announced that a regulation making power will be included in Finance Bill 2012 and regulations governing the tax treatment of regulatory capital instruments will be made to take effect upon commencement of the Capital Requirements Directive.

Tax transparent funds

Legislation will be introduced to give effect to tax transparent funds in summer 2012 with draft regulations (to be made under powers included in Finance Bill 2012) to be published in relation to the tax treatment of UK investors' holdings and the applicability of stamp taxes. The capital gains rules applying to mergers and reconstructions of collective investment schemes will also be rewritten with a view to simplifying the CIS regime across the board, including for tax transparent funds.

Corporation tax grouping legislation and convertible debt

Currently, creditors whose loans carry a right of conversion into the shares of an unconnected debtor company are treated as holding equity capital in the debtor company. This treatment can affect the debtor company's eligibility for group relief. In the current financial climate, with historically low interest rates, a lender may prefer to lend on terms which allow it to convert the loan into shares in the debtor company, thereby potentially improving the lender's return above the interest rate on the loan where the share value of the debtor rises over the term of the loan.

To avoid such arrangements risking the de-grouping of the debtor company, the Government has announced a proposal that loans carrying rights of conversion into an unconnected company listed on a recognised stock exchange are to be treated as "normal commercial loans" for the purposes of the loan relationships regime. Such "normal commercial loans" would not affect the availability of group relief to the debtor company. As the definition of "normal commercial loan" is used elsewhere in the Taxes Acts, such as identifying whether a loan is a "qualifying corporate bond", any amendment will need to be drafted to avoid any unintended consequences elsewhere in the Taxes Acts. The convertible loans should, on conversion into debtor company shares, be treated as new consideration in the debtor company. The change will be introduced in Finance Bill 2012, and will have effect for transactions where the relevant day falls on or after 21 March 2012.

Insurance

Targeted anti-avoidance rule for transitional arrangements to new Solvency II life insurance company regime

The tax regime for life insurance companies is set to change substantially as a result of the commencement of the Solvency II regime on 1 January 2014 and transitional rules will be needed in relation to the streaming of certain carry-forward losses and the smoothing of mismatches arising from the move to an accounts basis of taxation. Following consultation, the Government has published a new TAAR to prevent the securing of a tax advantage using the transitional provisions for the new life regime (which will apply from 21 March 2012 to prevent forestalling). The TAAR operates by cancelling the tax advantage. Helpfully, a statutory clearance procedure will also be available with HMRC expressing a willingness to discuss uncertainties with life insurers prior to enactment.

Claims equalisation reserves ("CERs")

Currently, general insurers are required to maintain CERs, which are made tax effective by reference to the regulatory requirement. Since these requirements will be superseded by the introduction of Solvency II, the relief will no longer be tax effective.

In Budget 2011, the Government had stated that it was minded to legislate to continue the relief, albeit provided that the industry gave a "robust justification" for the retention of CER relief. However, the Government has now decided to repeal the rules relating to CERs and tax the release of CERs in equal amounts over a six-year transitional period (with an election available to the insurer to subject the balance of the CER to tax during that period). The new rules will also apply to the release of similar reserves maintained by Lloyds members.

Enterprise

Several measures have been announced to increase the attractiveness of investment and incentive schemes associated with entrepreneurial activity.

EIS and VCT simplification

Certain restrictions affecting the enterprise investment scheme ("EIS") and venture capital trusts ("VCTs") will be relaxed with effect in relation to shares issued on or after 6 April 2012 and 1 April 2012, respectively.

In relation to EIS schemes, an individual investor is not eligible for income tax relief where he or she possesses or is entitled to acquire more than 30 per cent. of the loan capital and issued share capital of the company. Finance Bill 2012 will now amend the EIS legislation to disregard loan capital held by the individual for the purposes of this connection test.

Currently shares only qualify under EIS if they carry no preferential right to dividends and no right of redemption (and, unless they are bonus shares, they must be subscribed for wholly in cash and fully paid up on issue). Preference shares will now be permitted where the amount and date of payment of any dividend is not discretionary and the dividends are not cumulative. The £500 investment limit will also be removed.

Currently, there is a "maximum qualifying investment requirement" which provides that up to £1 million may be invested in a company as part of the VCT's qualifying holdings. This £1 million limit will now be removed. However, it appears that, for VCT investments in companies in partnership, the £1 million limit will remain so that the partnership as a whole will not receive more than £1 million by way of investment.

EIS and VCT investment limits

While changes have already been included in Finance Bill 2012 in relation to the investment limits applying to investors in EIS and VCTs, a number of the limits will be relaxed further in relation to the requirements applying to the EIS or VCT investee company.

The limit on the number of employees, currently standing at fewer than 50, will be increased to fewer than 250. The gross assets threshold (applying to the EIS or VCT company), currently £7 million prior to the relevant share issue and £8 million after, will be more than doubled to £15 million and £16 million, respectively. Similarly, the annual investment limit in respect of investments in EIS or VCT companies will rise from £2 million to £5 million.[5]

Subject to EU state aid approval, these changes will take effect from 6 April 2012. State aid approval has already been given to raise the limit on the amount an investor may invest in an EIS from £500,000 to £1 million.

Seed Enterprise Investment Schemes ("SEIS")

The draft legislation in Finance Bill 2012 providing for the embryonic seed enterprise investment scheme, designed to provide incentives to invest in small unquoted trading companies, will be subject to some further changes. SEIS companies will now be able to hold subsidiaries. The two year time limit within which the investment must be made will now run from commencement of trade rather than time of incorporation. The maximum employee limit of 24 and gross asset limit of £200,000 will now be calculated without reference to related entities. Investors may now include previous employees.

Enterprise Management Incentive

Enterprise management incentive ("EMI") schemes offer a means of incentivising key employees of small trading companies and need not be open to all employees (as with other prominent

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[5] Although, note that this was originally intended to be £10 million in the draft Finance Bill 2012 published on 6 December 2011.

employee share schemes, such as share incentive plans). EMI schemes operate through the grant of share options to selected employees without an income tax charge arising. Currently, the limit on the value of shares over which options may granted is £120,000 in a three year period. However, the limit will increase to £250,000 (subject to state aid approval) from a time to be appointed by statutory instrument.

Further changes may also be included in Finance Bill 2013 (again, subject to state aid approval) to bring shares acquired under an EMI scheme within the scope of entrepreneur's relief and the further advantage of a 10 per cent. effective rate of tax. The rules are also anticipated to change so as to extend access to EMI schemes to academics employed by companies operating the schemes.

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Please feel free to contact any of the following Cadwalader lawyers if you have any questions about this memorandum.

Adam Blakemore	+44 (0) 20 7170 8697	adam.blakemore@cwt.com
Oliver Iliffe	+44 (0) 20 7170 8536	oliver.iliffe@cwt.com