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UK Budget 2015: Key Implications for Alternative Asset Managers

In a speech crammed full of digs aimed at opposition parties (and the French), the UK’s Chancellor of the Exchequer delivered his final pre-election Budget this afternoon.

We have summarised below those announcements that we feel may be of particular relevance to alternative asset managers.

Disguised investment management fees

Today’s Budget confirms that legislation will, as announced in December 2014, be introduced in Finance Bill 2015 to ensure that all sums that arise to investment fund managers for their services are charged to income tax.

This measure will affect sums that arise to managers who have entered into arrangements involving partnerships or other transparent vehicles. The new rules are not, however, intended to catch sums linked to performance (e.g., “carried interest”). In addition, returns that are exclusively from investments by partners are not intended to be in scope.

Her Majesty’s Revenue & Customs (“HMRC”) states that, following consultation, the legislation has been revised to:

- better reflect industry practice on performance-related returns (i.e., what should fall within the term “carried interest”)
- restrict the charge on non-UK residents to UK duties
- ensure that the rules apply to investment trust managers.

Despite the forecasts accompanying the Budget suggesting that HMRC expects to receive negligible amounts from this measure in 2015/16, changes will take effect in respect of sums arising on or after 6 April 2015 irrespective of when the fund was set up or the arrangements were entered into.

Draft legislation, showing how HMRC intends to effect the above, is awaited on 24 March 2015.

Capital gains tax — entrepreneurs’ relief, joint ventures and partnerships

Budget 2015 announced that legislation will be introduced in Finance Bill 2015 to prevent claims to Entrepreneurs’ Relief (“ER”) in respect of gains on shares in certain companies that:

- invest in joint venture companies or
- are members of partnerships.
Legislation will be introduced in Finance Bill 2015 to amend the relevant UK rules so that, for ER purposes, the definitions of a “trading company” and “the holding company of a trading group” do not take account of activities:

- carried on by joint venture companies in which a company is invested or
- of partnerships of which a company is a member.

The new rule will deny ER where the company invested in has no trade (or no relevant trade) of its own.

These changes have effect for disposals on or after 18 March 2015, and those who hold shares directly in UK corporate members of, for example, limited liability partnerships are advised to consider their impact carefully.

**Capital gains tax — ER and associated disposals**

It was also announced today that Finance Bill 2015 will include legislation to prevent claims for ER in respect of gains on disposals of privately held assets used in a business, unless they are associated with a significant material disposal, that is to say a disposal of at least a:

- 5 per cent shareholding in the company or
- 5 per cent share in the assets of the partnership carrying on the business.

Legislation will be introduced in Finance Bill 2015 to amend the relevant UK rules to ensure that, in order for a disposal of a privately owned asset to qualify for ER, the claimant must reduce their participation in the business by also disposing of:

- a minimum 5 per cent of the shares of the company carrying on the business or
- (where the business is carried on in partnership) a minimum 5 per cent share in the assets of the partnership carrying on the business.

These changes also have effect for disposals on or after 18 March 2015.

**Implementation of the UK’s automatic exchange or information agreement**

In compliance with the UK’s European Union obligations to improve international tax compliance and the UK’s obligations under Competent Authority Agreements with non-EU jurisdictions for the Common Reporting Standard (“CRS”), regulations will be introduced to create due diligence and reporting obligations for UK financial institutions.

The obligations require “financial institutions” to:

- identify accounts maintained for specified persons, that is, account holders who are tax-resident in jurisdictions with which the UK has entered into an agreement to exchange information about a wide range of financial accounts and investments to help tackle tax evasion
- collect and report information in a specified manner on specified persons to HMRC.
In order to correct minor errors and consolidate the rules, the regulations will also revoke and replace the current implementing regulations for the UK’s exchange of information agreement with the United States concerning the US Foreign Account Tax Compliance Act (“FATCA”).

The regulations will have effect on and after:

- 1 January 2016 in relation to the UK’s European Union and CRS obligations
- 21 days from the date these regulations are laid in relation to the FATCA agreement.

**Diverted Profits Tax**

As announced in Autumn Statement 2014, legislation will be introduced in Finance Bill 2015 for a new tax on diverted profits from 1 April 2015.

Following consultation, the legislation has been revised to narrow the notification requirement. There have also been changes to clarify rules for:

- giving credit for tax paid
- the operation of the conditions under which a charge can arise
- specific exclusions.

Notwithstanding the changes proposed, alternative asset managers with UK operations would be well advised to review the updated draft closely when published on 24 March. The scope for unintended consequences in these rules is significant.

**Pensions — lifetime allowance**

Legislation will be introduced in the new Parliament to reduce the pensions’ lifetime allowance to £1 million (down from £1.25m).

Fixed and individual protection regimes will be introduced alongside the reduction in the lifetime allowance to protect savers who think they may be affected by this change.

This change will have effect from 6 April 2016.

**Personal Savings Allowance**

In (potentially) better news, Budget 2015 announced that legislation will be introduced in a future Finance Bill to apply a “Personal Savings Allowance”. This will apply in respect of, for example, bank and building society interest.

The Personal Savings Allowance will apply for up to £1,000 of a basic-rate taxpayer’s savings income and up to £500 of a higher-rate taxpayer’s savings income each year. The Personal Savings Allowance will not be available for additional rate taxpayers (i.e., those with taxable income in excess of £150,000).
These changes will have effect from 6 April 2016, and the Personal Savings Allowance will be in addition to the tax advantages currently available to savers from Individual Savings Accounts. In the meantime, the UK government will discuss implementation issues with the savings and investment industry and other interested groups.

**Abolition of Class 2 National Insurance contributions (“NICs”)**

At Budget 2015, the government announced its intention to abolish Class 2 NICs in the next Parliament and reform Class 4 NICs to introduce a new benefit test.

The government will consult on the detail and timing of these reforms later in 2015, and members of UK LLPs (that have successfully navigated the “salaried member” rules) should monitor developments in this area.
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