Tolley®CPD

April 2017

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Spring Budget 2017 (Lectures P1006/ B1006 – 17.03/ 12.05 minutes)

The Chancellor, Philip Hammond, delivered his Spring Budget on 8 March 2017. This is intended to be the last budget delivered in the Spring. The Overview of Tax Legislation and Rates (OOTLAR) published by HM Treasury and HMRC gives a comprehensive summary of all the tax-related changes. Further information on some of the announcements will be available when the Finance Bill 2017 is published on 20 March 2017.

The next budget is time-tabled for Autumn this year, after which the event will occur annually in the Autumn.

Personal tax

Rates allowances

The Budget makes no changes to the main tax rates and allowances for the 2017/18 tax year previously announced:

- main personal allowance will be £11,500;
- basic rate band limit is set at £33,500 (higher rate tax kicks in is £45,000);
- additional rate band threshold remains unchanged at £150,000.

Note that the basic rate band limit will be different for Scottish taxpayers. This was set in the Scottish Budget to be £31,500 so that higher rate tax starts to be paid at £43,000.

The main rates of tax will remain at 20% basic rate, 40% higher rate and 45% additional rate.

National Insurance contributions (NIC)

The 2017/18 National Insurance thresholds are:

	Weekly	**Monthly**
Lower earnings limit, primary Class 1	£113	£490
Upper earnings limit (UEL), primary Class 1	£866	£3,750
Primary threshold (PT)	£157	£680
Secondary threshold (ST)	£157	£680
Upper secondary threshold (secondary NICs due for U21s and apprentices under 25)	£866	£3,750

Employees' primary Class 1 between PT and UEL	12%
Employees' primary Class 1 rate above UEL	2%
Class 1A rate on employer-provided benefits	13.8%
Class 1B rate on amounts included in a PAYE settlement agreement	13.8%

National Living Wage / National Minimum Wage

The National Living Wage will be increased to £7.50 per hour from April 2017. The following table shows all minimum wage rates for all age groups:

Category	**Current rate**	**New rate from 1 April 2017**
Workers 25 and over	£7.20 per hour	£7.50 per hour
21-24 year olds	£6.95 per hour	£7.05 per hour
18-20 year olds	£5.55 per hour	£5.60 per hour
16-17 year olds	£4.00 per hour	£4.05 per hour
Apprentices	£3.40 per hour	£3.50 per hour
Accommodation offset	£6.00 per day	£6.40 per day

Salary sacrifice

With effect from 6 April 2017, salary sacrifice arrangements, described as 'optional remuneration arrangements', may be used to achieve tax and NIC savings only in the case of:

- employer pension contributions and advice
- employer-provided childcare
- cycle-to-work schemes
- ultra-low emission company cars

Transitional provisions apply if salary sacrifice arrangement in place before 6 April 2017.

Termination payments

The Autumn Statement included details of changes to the treatment of termination payments. In para 1.8 of today's OOTLAR, HMRC indicates that although the main changes to the tax and NIC treatment of termination payments will be legislated in the Finance Bill 2017, proposals to abolish foreign service relief will be deferred to the Finance Bill 2018.

Benefits in kind

During the summer last year there was a consultation on proposals to align the date for 'making good' on benefits in kind. If an employee 'makes good' (repays) an amount to the employer in respect of a benefit in kind, the cash equivalent is reduced by the amount made good. The date by which the employee must 'make good' in order to reduce a benefit varies according to the benefit provided.

Finance Bill 2017 will include legislation to set the aligned date to be 6 July following the end of the tax year. This change will apply for benefits provided in 2017/18 onwards.

Company cars

There were no changes announced to the company car tax rates that will apply from 2017/18 to 2020/21 as already either enacted or announced in the Autumn Statement.

Enterprise Management Incentives (EMI)

In August 2009 the European Commission agreed to grant state aid approval to the EMI scheme until April 2018. The Government will now seek approval to extend the provision beyond 2018. See OOTLAR, para 2.15.

Personal service companies ('IR35')

As announced in last year's Budget, as from 6 April 2017, where a worker provides his services through a personal service company (PSC) to a public sector body, it will be up to the public sector body (or the agency responsible for paying the PSC) to decide whether or not the special rules for PSCs (known as the IR35 rules) should apply. If the IR35 rules do apply, then the public sector body or agency will deduct the tax due on the resulting deemed employment income payment from the amount due to the PSC under the contract.

In a recent change to proposals for how the public sector body (or agency) should calculate the deemed employment payment, it will be up to them whether they take account of the worker's expenses in calculating that amount. If the expenses are left out of account the worker could still claim a deduction for qualifying expenses in the normal way.

The outline of this measure is covered in HMRC's tax information and impact note.

The list of public bodies who will assume this new responsibility as from 6 April was included as Annex B to the consultation document on this change in approach.

HMRC has also recently published a revised Employment Status Tool to help anyone considering the position of a worker providing services through a PSC to decide whether or not the IR35 rules apply.

www.gov.uk/government/publications/off-payroll-working-in-the-public-sector-changes-to-the-intermediaries-legislation

Proposal dropped - sanction for hiring illegal workers

In last year's Budget the Chancellor announced an intention to temporarily deny the NIC employment allowance to employers taking on workers who do not have a legal right to work in the UK. Following consultation, this proposal has been dropped. Any employer taking on such workers already faces significant civil penalties of up to £20,000 per illegal worker (see the Checking the employee's right to work guidance note).

Upcoming consultations

The OOTLAR document gives details of a number of consultations on possible future changes to employment taxes, all to be published on 20 March 2017:

- a call for evidence on **employees' expenses**
- consultation on proposal to modernise the tax treatment of employer-provided **living accommodation and board and lodgings**
- a call for evidence on exemptions and valuation methodology for **employer-provided benefits in kind**

Pensions

The Budget did not include any new proposals in respect of the lifetime allowance or annual allowance for pension contributions.

Money Purchase Pensions annual allowance

Legislation in Finance Bill 2017 will reduce the level of the money-purchase pensions annual allowance from £10,000 to £4,000 with effect from 6 April 2017.

www.gov.uk/government/publications/reducing-the-money-purchase-annual-allowance

Foreign pensions

The Finance Bill 2017 will legislate to align the treatment of foreign pensions with UK domestic pensions.

In particular, new provisions for UK residents to be taxed on 100% of foreign pension income, instead of the current 90% were included in the Draft provisions for Finance Bill 2017, Sch 3.

Qualified recognised overseas pension schemes transfer charge

Qualified recognised overseas pension schemes (QROPS) are foreign pension schemes which meet the conditions for a tax-free transfer from a UK pension scheme. The conditions require that the foreign pension scheme is broadly similar to a UK scheme. Normally withdrawals from a UK pension scheme would be subject to tax so the QROPS concession allows someone who is permanently leaving the UK to transfer their pension pot without a tax penalty. FA 2004, s 169(1)

The government announced in the Overview of tax legislation and rates (OOTLAR), para 1.14 that it will legislate in the Finance Bill 2017 to apply a 25% tax charge to pension transfers made to QROPS on or after 9 March 2017.

Although the legitimate use of QROPS is acknowledged, it was noted that the transfer of funds which have benefited from UK tax relief provided an opportunity for a tax advantage. QROPS can be located in a lower tax jurisdiction or one which offers less restrictive withdrawal rules. As a result, QROPS schemes have been marketed as tax saving vehicles. The new law aims to preserve the legitimate purpose of transferring pension schemes, whilst penalising the tax avoidance motive.

Thus 'genuine' transfers will be identified if they meet one of the following conditions:

1. the QROPS and the person who makes the transfer are resident in the same country,

2. the QROPS and the person who makes the transfer are both resident in a country within the European Economic Area (EEA);

3. the transfer is made to a QROPS that is established or sponsored by the employer of the person who makes the transfer.

Transfers not meeting these conditions will incur a charge of 25% of the value of the fund.

There will be a five-year window following the transfer during which:

- a transfer which was not chargeable will become so if it ceases to meet the qualifying conditions regarding residence, and

- a charge which was made can be refunded if one of the qualifying conditions starts to apply

- payments out of the QROPS will be subject to UK tax rules regardless of where the individual then resides

The administrators of both the UK scheme and the QROPS will be jointly and severally liable to the tax charge. It is expected that it will be deducted from the pension fund on transfer.

Tax planning with QROPS is a niche area popular with wealthy and internationally mobile individuals. The new measures appear to fit with the Government's current anti-avoidance agenda and are expected to raise around £60 million per year, a fairly substantial sum.

However, also in line with recent anti-avoidance measures, the detail appears to be complex requiring some 29 pages of Draft legislation and 43 pages of Guidance. Practitioners whose clients may be affected by these changes are advised to study the guidance at an early stage in view of the immediate changes in the law. Existing QROPS have an early deadline of 13 April 2017 to decide whether they wish to maintain their status.

www.gov.uk/government/publications/qualifying-recognised-overseas-pension-schemes-charge-on-transfers

Dividend nil rate band reduction

In a step ostensibly aimed at addressing the unfairness in the differences in tax treatment between employees and those who provide their services through a limited company, the Chancellor announced that the dividend nil rate band will reduce from £5,000 to £2,000 from 6 April 2018. Although this will indeed impact on the users of personal service companies, it will have a wider impact, affecting anyone receiving dividends of over £2,000 a year, including shareholder directors / employees of many smaller companies.

www.gov.uk/government/publications/income-tax-dividend-allowance-reduction

Tax-advantaged investments

The annual subscription limit for Individual Savings Accounts (ISAs) will be increased to £20,000 for 2017/18. The new Lifetime ISA should be available from April 2017. The interest rate for the new NS&I Investment Bond has been confirmed at 2.2%; it will be available for 12 months from April 2017. It is thought that interest will be taxable, but the investor will be able to set his personal savings allowance against it.

Several changes are to be made to the Social Investment Tax Relief scheme with effect for investments made on or after 6 April 2017. In particular, the amount of qualifying investment a qualifying social enterprise can raise will increase in most cases, from the current three-year rolling limit of approximately €344,000 to a maximum of £1.5 million over its lifetime. This increased limit will be available to qualifying social enterprises that receive their initial risk finance investment no later than seven years after their first commercial sale.

Certain technical amendments are also to be made to the Enterprise Investment Scheme, the Seed Enterprise Investment Scheme and Venture Capital Trusts (VCTs).

Capital Taxes

The Spring Budget was light on new tax proposals overall, and inheritance tax did not feature at all.

However, it is worth being reminded of some new measures due to be introduced with effect from April 2017 which have been previously announced and the budget included some new points relating to trusts which will be of interest to private client practitioners.

Trusts default rate of income tax

The OOTLAR, para 1.1 makes a somewhat cryptic reference to a 'default rate' of income tax which will apply to trustees. This is not a new rate of tax for trusts but requires some explanation.

With effect from 6 April 2017, the Scottish parliament will be able to set a Scottish rate of income tax to apply to non-savings, and non-dividend income in Scotland. This 'main rate' of tax will apply to individuals' employment, trade, pensions and property income. It does not apply to trusts.

To correspond with the creation of a main rate for Scottish taxpayers, the same term will apply to the non-savings, non-dividend income of individuals in the rest of the UK. The inference is, of course, that the main rates for each part of the UK could diverge in due course.

The regional authority over tax rates does not extend to the standard rates applied to trusts or non-residents. Hence the introduction of a new term, 'default rate' which describes the standard rate applied to non-savings, non-dividend income of those entities. For trusts, this category is primarily property income.

Although no additional measures are proposed at present, the separation of the rates does pave the way for different rates for trusts in the future.

Inheritance tax and the non-domicile rules

Practitioners are reminded that the Finance Bill 2017 will legislate for the reform of the domicile rules which was initially outlined in the Summer Budget 2015.

The new rules will take effect from 6 April 2017. Draft legislation was published in January 2017 and the OOTLAR, para 1.26 confirmed that the measures will go ahead with only minor amendment.

For inheritance tax purposes, the key changes are:

- a non-UK domiciled person (non-dom) will become deemed domiciled after being UK resident for 15 of the past 20 years (instead of 17 years out of 20 currently)
- a person with a UK domicile of origin who has acquired a different domicile of choice will be deemed domiciled while they are UK resident
- inheritance tax will be charged on all UK residential property even when held by a non-dom through an offshore structure

The standard non-dom tax planning strategy of placing foreign property in a non-UK resident trust before the individual becomes deemed domiciled continues to be an effective way of minimising UK tax, and is, in fact specifically confirmed in the OOTLAR and draft legislation. However, this strategy will no longer work for a non-dom who had a UK domicile of origin but becomes deemed domiciled when UK resident.

Inheritance tax and residence nil rate band

The residence nil rate band has featured in press commentary in recent weeks as the date approaches on which this controversial piece of legislation becomes effective. For deaths after 6 April 2017 an increase in the nil rate band will be available where the value of a residence is bequeathed to direct descendants. Full details are given in the Residence nil rate band guidance note. No changes were announced in today's budget. IHTA 1984, s 8D

Administration

Digital tax administration (Making Tax Digital)

The government announced that it would delay the mandatory introduction of Making Tax Digital until April 2019 for unincorporated businesses and landlords that have a turnover below the VAT registration threshold. This delay is intended to give these businesses sufficient time to prepare for keeping their records digitally and providing quarterly updates.

The legislation includes powers to make regulations, including on the form and content of periodic updates and 'end of period statements'. There are also powers to set out the scope and operation of certain exemptions by regulations. Following consultation, the legislation published in draft on 31 January 2017 has been revised and expanded to cover, amongst other things, the introduction of a clause amending Value Added Tax Act 1994, Sch 11 to enable equivalent regulations (and exemptions) for VAT purposes to those proposed for income tax.

Businesses that are registered for, and pay VAT, will be required to operate Making Tax Digital from April 2019 and the quarterly updates will effectively replace the VAT return.

www.gov.uk/government/publications/making-tax-digital-for-business

Digital tax administration

The government announced that it will consult on proposals for late submission penalties and charging of penalty interest on late payments. The government previously consulted on a model for late submission penalties. The consultation will also include certain other design aspects of the tax administration system with the aim of adopting a consistent approach across taxes. This will simplify the system for taxpayers.

HMRC large business risk review

HMRC will be consulting over the summer with businesses and interested parties with regard to its process for risk profiling large businesses and promoting stronger compliance. The consultation will be released ahead of the summer recess and will run for 12 weeks.

Avoidance, evasion and compliance

Promoters of Tax Avoidance Schemes (POTAS)

The government announced that it intends to introduce new legislation that is intended to ensure that promoters of tax avoidance schemes cannot circumvent the new POTAS regime by reorganising their business to either share control of a promoting business or putting persons between the promoting business and themselves. See Promoters of Tax Avoidance Schemes: associated and successor entities rules for more information and a copy of the draft clause.

www.gov.uk/government/publications/promoters-of-tax-avoidance-schemes-associated-and-successor-entities-rules

Strengthening tax avoidance sanctions and deterrents

The government previously announced in Autumn Statement 2016 that a new penalty will be introduced in respect of a person who has enabled another person or business to use a tax avoidance arrangement that is later defeated by HMRC. The government also intends to remove the defence of having relied on non-independent advice as taking reasonable care when HMRC considers whether penalties will be levied on a person or business that has used a tax avoidance arrangement.

The changes relating to reasonable care come into effect at Royal Assent and apply to inaccuracies in documents relating to tax periods which begin on or after 6 April 2017. The penalty for enablers will apply prospectively to enabling activity after Royal Assent.

Disclosure of indirect tax avoidance schemes

The government announced in Autumn Statement 2016 that legislation will be introduced in Finance Bill 2017 that is intended to strengthen the regime for disclosing indirect tax avoidance arrangements. The provisions will make scheme promoters primarily responsible for disclosing schemes to HMRC and the scope of the legislation will be extended to include all indirect taxes including the Soft Drinks Levy. These measures will become effective from 1 September 2017.

Business Taxation

Class 4 NICs

The Budget contained an announcement that the main rate of Class 4 NICs was to increase to 10% (from 9%) from 6 April 2018 and further increased to 11% from 6 April 2019. This followed on from the announcement that Class 2 contributions are to be abolished from April 2018.

This measure has now been scrapped.

Partnership taxation

It was announced at Autumn Statement 2016 that draft legislation will be published to clarify some aspects of partnership taxation, in particular in relation to profit allocations. It has been confirmed that the legislation will be included in Finance Bill 2018.

See OOTLAR, para 2.3.

Appropriations to trading stock

Currently, if a trader transfers an asset into the business as trading stock (which had previously been used as a fixed asset in the trade) then the 'cost' of the stock for the purpose of the accounts is the market value at the time it was transferred. For capital gains purposes, the trader is also deemed to have disposed of the fixed asset at market value. In this instance the trader can elect to have the cost of the stock reduced by the chargeable gain. This will reduce the gain to nil but will result in the stock having a lower cost (and therefore a higher trading profit when the stock is eventually sold).

For appropriations on or after 8 March 2017, it is no longer possible to make such an election where an allowable loss would arise on an appropriation into trading stock at market value. This means that an allowable loss will be crystallised when the appropriation takes place, and the loss will remain within the chargeable gains rules with respect to how it may be set off in the future. The aim of this provision is to remove the ability of businesses with loss-making capital assets to obtain an unfair tax advantage by converting those losses into more flexible trading losses.

Where traders have more than one asset they wish to appropriate as trading stock, it will be sensible to consider the timing of any appropriation. Where one asset stands at a gain, and one at a loss, it may be advantageous to appropriate the asset standing at a gain before or at the same time as the asset standing at a loss and make no election. This will ensure that the loss arising can be utilised more effectively within the chargeable gains rules.

See OOTLAR 2017, para 1.24 and www.gov.uk/government/publications/corporation-tax-and-income-tax-tax-treatment-of-appropriations-to-trading-stock

Trading and property income allowances

As announced at Budget 2016, a £1,000 allowance will be introduced for both property income and trading income with effect from the 2017/18 tax year, see Budget 2016 - owner-managed businesses news item. Following the publication of the draft legislation, revisions will be made to prevent the allowances from applying to income of a participator in a connected close company or to any income of a partner from their partnership.

See OOTLAR 2017, para 1.3.

Simplified cash basis

A number of measures were announced to this regime to simplify the rules, widen the eligibility criteria and extend the existing regime to unincorporated property businesses.

With effect from 6 April 2017 the entry and exit thresholds for the simplified cash basis for small unincorporated businesses are being increased.

- The entry threshold (otherwise known as the 'relevant maximum') for non-Universal Credit claimants will be £150,000, and the exit threshold will be £300,000.
- For Universal Credit claimants both the entry and exit thresholds will be £300,000.

The Government estimates this will enable 135,000 more businesses to benefit from the simplified rules, reducing their administrative burden. They may however incur a one-off cost to familiarise themselves with the rules and change to the new basis of reporting. For guidance on the current rules, see the Simplified cash basis for small businesses guidance note.

In addition, from April 2017 the rules for deductible expenditure will be simplified. The general restriction on the deduction of capital expenditure will be replaced with a more focused and limited restriction on the deduction of certain specified expenditure, in particular that incurred on, or in connection with, the acquisition or disposal of a business or part of a business. This added certainty on expenditure which can and cannot be deducted is a welcome clarification and may result in businesses deducting expenses they previously were unsure they could deduct. For 2017/18 profits can be calculated using either the new rules or the existing rules. For guidance on the current rules see the Simplified cash basis expenditure guidance note.

See OOTLAR, paras 1.44,1.45

www.gov.uk/government/publications/increase-to-the-cash-basis-threshold-for-unincorporated-businesses.

Property owners

Simplified cash basis for unincorporated businesses

As stated in the January 2017 summary of responses, the simplified cash basis will be extended to unincorporated property businesses from 6 April 2017. (OOTLAR para 1.46)

This will be the default method of calculating the property income, unless:

- the landlord makes an election not to use the simplified cash basis (separate elections must be made for different types of property businesses)
- the gross rental income exceeds £150,000
- the business is carried on by a company, an LLP, a partnership with a corporate partner, a trust or personal representatives
- business premises renovation allowances have been claimed and there is a balancing adjustment in the tax year

For those property businesses unwilling or unable to use the simplified cash basis, the accruals basis must be used to calculate the property income.

Where property is owned jointly by spouses or civil partners, if one spouse or civil partner makes an election for the accruals basis to apply then the other spouse / civil partner is excluded from using the simplified cash basis. For all other jointly owned property, each owner can choose whether to elect to use the accruals basis or to remain on the simplified cash basis.

The simplified cash basis for unincorporated property businesses is closely modelled on the simplified cash basis for unincorporated trading businesses, however there are some important differences:

- interest is allowed as a deduction without the application of the £500 limit and the related mixed purpose interest rule (instead interest will be allowed according to the existing rules for landlords, including the restriction of relief for interest in relation to residential properties starting in 2017/18 discussed in the Allowable property expenses guidance note)
- the continued ability to deduct the cost of replacing domestic items in residential properties which applies from 2016/17, see the New statutory renewals basis for property businesses [updated] news item. The initial cost of capital items used in a dwelling house will not be an allowable expense under the simplified cash basis in the same way as this is not permitted under the accruals basis

Landlords should consider carefully whether the cash basis is beneficial to them. Whilst simplified accounting may be tempting it could create other issues, particularly in relation to the timing of receipts. For example, if a tenant pays a full year's rent in advance on 31 March then the entire amount must be included in the profits for that year, which could impact areas such as the high income child benefit charge or the abatement of the personal allowance where the adjusted net income exceeds £100,000.

Rent-a-room relief

In a surprise announcement, in summer 2017 the Government will launch a consultation on rent-a-room relief, with a view to better supporting longer-term lodgings. Overview of tax legislation and rates 2017, para 2.2; Annex B

The reference to longer-term lodging may suggest that the conditions for rent-a-room relief could be altered to ensure it applies to long-term lets only. Currently anyone letting a room in their home on a short-term basis using sharing websites such as Airbnb can receive up to £7,500 per year in rents without paying income tax. When rent-a-room relief was introduced in 1992, this type of short-term letting could not be envisaged and the Government may decide this does not meet the original policy objective. ITTOIA 2005, s 789

Corporate Taxation

The Spring Statement will largely comprise a response to the OBR's forecast and will provide the opportunity to launch consultations on future reforms.

In the spirit of moving towards a single fiscal event in the autumn, the Spring Budget 2017 does not set out major changes to the taxation of companies. Minor amendments have been made to a number of announcements made in previous years, details of which are provided below.

Appropriations to trading stock

Currently, if a fixed asset is appropriated into trading stock, then the 'cost' of the stock for the purposes of the accounts is the market value at the time it was introduced. For chargeable gains purposes, there is a deemed disposal of the fixed asset at market value. In this instance an election can be made to reduce the cost of the stock by the amount of the chargeable gain, rather than triggering a disposal. This will reduce the gain to nil but will result in the stock having a lower cost, and therefore a higher trading profit, when the stock is eventually sold.

For transfers made on or after 8 March 2017, it is no longer possible to make such an election where an allowable loss would arise on an appropriation into trading stock at market value. This means that an allowable loss will be crystallised when the appropriation takes place, and the loss will remain within the chargeable gains rules with respect to how it may be set off in the future. The aim of this provision is to remove the ability of businesses with loss making capital assets to obtain an unfair tax advantage by converting those losses into more flexible trading losses.

Where companies have more than one asset that may be appropriated to trading stock, it will be sensible to consider the timing of any appropriation. Where one asset stands at a gain, and one at a loss, it may be advantageous to appropriate the asset standing at a gain before or at the same time as the asset standing at a loss and make no election. This will ensure that the loss arising can be utilised more effectively within the chargeable gains rules.

See OOTLAR, para 1.24.

Review of R&D regime

The UK has a comprehensive regime to encourage companies to invest in research and development. For an overview of the main reliefs, see the R&D expenditure credit - an introduction and the Research and development SME tax reliefs guidance notes.

Following a review of the existing regimes, the Government has announced today that administrative changes will be made to the research and development expenditure credit (RDEC) to increase certainty and to simplify claims. Action will also be taken to increase awareness of R&D tax credits among SMEs. Further details on the changes, or indeed when they are likely to have effect, have not been provided.

See OOTLAR, para 2.13.

Offshore property developers

Legislation was introduced by Finance Act 2016, ss 76-77 to ensure non-resident developers of UK land are subject to UK corporation tax on the profits generated by this activity. This was intended to create a level playing field between UK and foreign based developers. For a full examination of the new rules, see the Transactions in UK land guidance note.

The original legislation excluded profits arising from contracts entered into before 5 July 2016. The Government did not anticipate that profits arising many months or years later as a result of these contracts would not be subject to UK corporation tax. Amendments have been made to ensure that all profits recognised in a period of account beginning on or after 8 March 2017 are taxed irrespective of when the contract was entered into. Where the period of account straddles 8 March 2017, then the amounts arising between 8 March 2017 and the end of the straddling period are also taxed.

See the policy paper, draft legislation and explanatory notes published today. See also Spring Budget 2017, para 3.21.

Plant and machinery leasing

Current rules under GAAP treat leased assets as either finance leases or operating leases. Finance leases are capitalised on the balance sheet as fixed assets, with a matching lease obligation in creditors. Assets subject to operating leases are off balance sheet assets.

IFRS 16, which is the new leasing standard issued by the International Accounting Standards Board, comes into effect on 1 January 2019. This standard will radically alter the GAAP treatment of lessees of most assets, although lessors will still maintain a distinction between finance and operating leases. There are exceptions within the standard for leases of 12 months or less and low value items.

The impact for lessees will be to increase the level of debt and the value of the asset base on the balance sheet, as all leases must be capitalised. The timing of debits recognised in the accounts on operating leases will be accelerated, even though the payments for hire of the asset are likely to be uniform over the lease. Rental expenses on leases which are currently classified as operating leases will be replaced by depreciation and front loaded interest charges. Companies using IFRS may need to model the effect on their gearing, earnings per share and debt covenants as well as many other financial metrics and ratios.

The Government will launch a consultation in Summer 2017, building on the discussion document published in Summer 2016. The Government intends to maintain the current system of lease taxation, rather than changing the tax system to match the accounting. This would seem to be the most sensible approach as it should avoid awkward and complex transitional adjustments. However, one downside of this approach will be to create differences between the P&L debits and the amounts deductible for tax, requiring greater measurement and tracking of temporary differences within deferred tax.

It should be noted that some changes to the rules on long funding leases and certain anti-avoidance rules on leasing will be required as they are linked to current accounting definitions.

See OOTLAR, para 2.12.

Withholding tax exemption for debt traded on multilateral trading facility

UK tax at 20% must be withheld from certain payments of annual interest. Details of the current regime can be found in the Withholding tax on payments of interest guidance note. It has been announced today that an exemption will be introduced for interest on debt traded on a multilateral trading facility. The purpose of the exemption, which is subject to consultation in Spring 2017, is to further the development of UK debt markets.

See OOTLAR, para 2.14.

Double taxation treaty passport scheme

HMRC launched a Double Taxation Treaty Passport (DTTP) scheme for overseas corporate lenders applicable to loans taken out on or after 1 September 2010. The lender must be resident in a country with which the UK has a double taxation treaty that includes an interest or income from a debt claim article. The existence of a 'Treaty Passport' simplifies the process whereby a UK borrower is able to access reduced rates of withholding tax. See the Withholding tax guidance note for details on the scheme including links to HMRC guidance.

In order to assist businesses with raising finance, the Government announced today an intention to renew and extend the administrative simplifications of the DTTP scheme. Guidance and the revised terms and conditions applying to the scheme will be published on GOV.UK on 6 April 2017.

See OOTLAR, para 2.37.

Large business risk review

A consultation document is due to be published in Summer 2017 which aims to review HMRC's processes for assessing the risk profile of large businesses. The Government also wants to consider ways of promoting stronger compliance. Unfortunately, further details have not been provided alongside today's announcement.

See Spring Budget 2017, para 3.41.

Patient capital

'Patient capital' is a term used to describe a long-term capital investment in a growing innovative business. The investor is willing to make a financial investment in a business with no expectation of generating a quick profit, however it is possible that more substantial returns will be generated at some point in the future.

The Patient Capital Review was launched by HM Treasury and the Department for Business, Energy & Industrial Strategy (BEIS) in January 2017 as part of the Government's aim to build a modern industrial strategy. The review did not previously include consideration of the tax measures linked with patient capital for growing businesses.

The Chancellor announced today that a consultation will be launched in Spring 2017, which will review the tax reliefs aimed at encouraging investment and entrepreneurship. Specific reliefs have not been mentioned, but it is assumed that it could include EIS reliefs, SEIS reliefs, VCT reliefs, entrepreneurs' relief and investors' relief.

The final recommendations from the review will be presented to the Chancellor ahead of Autumn Budget 2017.

See Spring Budget 2017, para 3.13 and OOTLAR, para 2.5.

Creative sector tax reliefs

It was confirmed today that the Government will seek State Aid approval for the continued provision of high-end television, animation and video games tax reliefs beyond 2018.

See OOTLAR, para 2.16.

Amendments to measures previously announced

A number of measures that have been announced in the past are subject to minor amendments. Details are provided below.

Deductibility of interest

Following announcements at Budget 2016, plus a period of consultation, draft legislation was published on 5 December 2016 and 26 January 2017 to restrict the tax deduction available to companies in respect of interest and similar items.

From 1 April 2017, a group will have its interest expense restricted to a maximum deduction of 30% of earnings before interest, tax, depreciation and amortisation (EBITDA) that is taxable in the UK.

The legislation also includes a modified debt cap replacing the existing worldwide debt cap to ensure that the UK net interest deduction cannot exceed the total net interest expense of the worldwide group.

An optional group ratio rule based on the net interest to EBITDA ratio of the worldwide group may result in a greater deduction in some circumstances.

Alternative rules apply to infrastructure companies which may have the effect of largely taking them outside the rules with no interest restriction even though they may be highly geared.

Groups with net interest expense of £2m or less will be unaffected by these rules.

The Government has announced a series of detailed amendments to eliminate 'unintended consequences' and reduce 'unnecessary compliance burdens' as follows:

- changes to the modified debt cap to prevent certain restrictions for carried forward interest expenses
- the alternative rules for public infrastructure groups will be simplified to eliminate the need to compare levels of indebtedness of non-qualifying group companies. Transitional rules will apply in the first year to allow any necessary restructuring to obtain the more favourable alternative treatment.
- the rules on guaranteed debt have been amended including those in relation to intra-group guarantees. See the detailed discussion on this point in 'New interest

barrier: a bar too high?' by Helen Lethaby and Helen Gunson in Tax Journal, 24 February 2017 (subscription sensitive).

- income and expenses from dealing in financial instruments will be included in the definition of interest for banking trades
- special rules will allow insurers to compute interest on an amortised cost basis as an alternative to fair value accounting

These changes will be reflected in Finance Bill 2017 and will have effect from 1 April 2017.

See OOTLAR, para 1.23.

Reform of the substantial shareholdings exemption (SSE)

Following a period of consultation, amendments will be made to the SSE reforms included in the draft Finance Bill 2017, which were originally announced at Autumn Statement 2016. Whilst we do not yet have details, the latest changes are expected to provide further clarity and certainty and take effect from 1 April 2017.

See OOTLAR, para 1.16.

Reform of loss relief

Reforms to the loss relief regime were originally announced at Budget 2016.

Legislation was included in the draft Finance Bill 2017, with further draft legislation published on 26 January 2017. The latest changes include provisions for oil and gas companies and oil contractors. All reforms take effect from 1 April 2017.

See OOTLAR, para 1.17.

Patent box

It was announced at Autumn Statement 2016 that the patent box rules would be revised by Finance Bill 2017 where two or more companies work in collaboration on R&D projects under a cost sharing arrangement.

The definition of a cost-sharing arrangement will be narrowed and the way in which payments are structured under the cost-sharing arrangement will be altered. The changes will take effect from 1 April 2017.

See OOTLAR, para 1.22.

Hybrid mismatches

FA 2016 introduced legislation to tackle aggressive tax planning involving the use of hybrid and other mismatch arrangements. It was announced in a technical note at Autumn Statement 2016 that two minor amendments would be made to the hybrid mismatch rules, and a TIIN was published today providing further details.

The first change helps to relieve the administrative compliance burden in respect of financial instruments and the second change ensures that amortisation deductions are not treated as giving rise to a mismatch. The changes take effect from 1 January 2017.

See OOTLAR, para 1.19.

Grassroots sports

It was originally announced at Autumn Statement 2015 that companies will be able to claim a deduction for contributions to grassroots sports in certain circumstances. It was announced today that the treatment of a sport governing body will be extended by Finance Bill 2017 to include its 100% subsidiaries. These provisions will have effect from 1 April 2017.

See OOTLAR, para 1.21.

Tax relief for museums and galleries

As announced at Budget 2016, Finance Bill 2017 will introduce a new tax relief for museums and galleries. Further details on the operation of the relief were announced at Autumn Statement 2016. Following consultation on the legislation contained in draft Finance Bill 2017, it was announced today that the relief will be extended to allow for exhibitions which have a live performance as part of the exhibition, provided the live performance is not the main focus.

See OOTLAR, para 1.20.

Corporation tax in Northern Ireland

For a number of years, the Government has been working with the Northern Ireland Executive to pursue the introduction of an Northern Ireland corporation tax rate of 12.5% from April 2018. It was confirmed today that all small and medium sized enterprises trading in Northern Ireland will be given the potential to benefit. Anti-abuse provisions together with other minor drafting improvements will feature in the revised legislation contained in Finance Bill 2017.

See OOTLAR, para 1.18.

VAT

Registration and deregistration thresholds

With effect from the 1 April 2017 the following thresholds will apply:

- VAT registration threshold will increase from £83,000 to £85,000.
- The VAT registration threshold for relevant acquisitions from other EU member states will also increase from £83,000 to £85,000.
- The VAT deregistration threshold will increase from £81,000 to £83,000.

Use and enjoyment provisions for business to consumer mobile phone services

The government stated that it intends to remove the use and enjoyment provisions that alleviate the need for UK VAT to be charged on business to consumer (B2C) mobile phone services provided to a UK resident person travelling outside of the EU. The change is intended to resolve the inconsistency where UK VAT is applied to mobile phones used by UK residents when in the EU, but not when the mobile phone is used outside the EU. The changes are intended to prevent telecommunication providers from using the inconsistency to avoid accounting for UK VAT and it will bring the UK into line with the internationally agreed approach. Secondary legislation and a TIIN will be published before the summer recess.

Fraud in the provision of labour in the construction sector

The government announced that it intends to have a consultation on possible options to combat missing trader fraud in the provision of labour in the construction sector. One option would be to extend the scope of the domestic reverse charge mechanism to include labour provided in the construction industry so that the recipient accounts for any VAT due. A consultation document will be published on 20 March 2017.

Split payment model

Certain overseas businesses avoid paying UK VAT on goods supplied online which undercuts UK retailers and abuses the trust of UK customers purchasing goods via an online marketplace. The government had previously announced the introduction of measures that are intended to combat VAT avoidance by online businesses in Autumn Statement 2016.

The government has now announced that it would like to collect evidence on whether it would be appropriate to introduce a new VAT collection mechanism in respect of online sales using technology that enables VAT to be collected and remitted directly to HMRC at the time the sale takes place. This is commonly referred to as the split payment method, where the supplier will receive the net amount and the VAT will be remitted directly to HMRC. The government believes that this will be another step that could be used to tackle VAT avoidance by overseas online suppliers selling goods to UK consumers. A 'call for evidence' will be published on 20 March 2017.

Penalty changes in fraud cases

The government announced in Autumn Statement 2016 that legislation will be included in Finance Bill 2017 introducing a penalty for participating in VAT fraud. The government consulted on the draft legislation and as a result they have made some minor amendments to improve clarity of the measure and to limit the naming of a company officer to instances where the amount of tax due exceeds £25,000. The new penalty will come into effect from the date of Royal Assent to the Finance Bill.

Other indirect taxes

Energy and transport taxes

Vehicle Excise Duty (VED)

The VED for cars, motorcycles and vans registered before 1 April 2017 will be increased by the Retail Price Index (RPI) with effect from 1 April 2017: Vehicle Excise Duty: increase in rates for cars, vans, motorcycles and motorcycle trade licences.

HGV VED and Road User Levy

These rates will be frozen with effect from 1 April 2017. The government has requested evidence be provided in respect of updating the existing HGV Road User Levy and they will formally issue this request in Spring 2017. The government also stated that it intends to work with the industry in order to update the levy so that it will reward hauliers that plan their routes efficiently and incentivise hauliers to make efficient use of the roads and improve air quality.

Red diesel

The government announced that it intends to request evidence on the use of red diesel in order to improve its understanding of eligible industries and their use of red diesel. The government would specifically like to receive evidence from urban red diesel users.

The call for evidence will be published on 20 March 2017.

Air Passenger Duty (APD)

The rate of APD for the year 2018/19 will increase in line with the RPI. The rates for 2019/20 will be provided in Autumn Budget 2017 in order to give airlines sufficient notice of the increase. See Air passenger duty: changes to rates for more information.

Carbon pricing

The government announced that it remains committed to carbon pricing in order to assist with decarbonising the power sector. UK prices are currently determined by the EU Emissions Trading System and Carbon Price Support. With effect from 2021/22, the government intends to target a total carbon price and will set the specific tax rate at a later date in order to give businesses greater clarity on the total price that they will be required to pay. Further details on carbon prices for the 2020s will be set out at Autumn Budget 2017.

Levy control framework

The government is aware that it will need to limit the cost for businesses and households as the UK decarbonises its energy supplies. The Levy Control Framework has already been assisting with controlling the costs of low carbon subsidies in recent years and it will be replaced by a revised set of controls. Details of these new controls will be provided later in 2017

Insurance Premium Tax

The government has reconfirmed its announcement in Autumn Statement 2016 that it will be introducing anti-forestalling measures when the standard rate increases to 12% with effect from June 2017.

The current anti-forestalling legislation is no longer relevant so new legislation will be introduced with effect from 8 March 2017.

Under the anti-forestalling measure:

(a) businesses will be required to charge the new rate of IPT on a premium received between the announcement and the rate change if the cover under the insurance contract starts on or after the date of the change. This is done by deeming the premium to be received on the date of the rate change. However, this does not apply where it is the insurer's normal commercial practice to receive pre-payments of premiums, and

(b) businesses will be required to charge the new rate of IPT on a proportion of a premium received between the announcement and the rate change if the cover under the insurance contract starts before the rate change and extends until after the first anniversary of the rate change. This is done by deeming a proportion of the premium to be received on the rate change date. That proportion is the amount which relates to the period of cover which runs from the first anniversary. However, this does not apply where it is the insurer's normal commercial practice to issue contracts for periods longer than one year.

Environmental taxes

Aggregates levy

The current rate of £2 per tonne will remain in effect.

Landfill tax

The value of the Landfill Communities Fund (LCF) for 2017/18 will remain unchanged at £39.3m and the cap on contributions made by landfill operators will increase to 5.3%.

The current cap will be maintained, subject to consideration of Landfill Tax receipts, continuing progress in reducing the level of unspent funds that are held by environmental bodies and the proportion of the LCF that are spent on administration costs.

The government announced that it intends to consult on extending the scope of landfill tax to cover illegal waste disposals that are made without the required permit or licence.

Landfill tax - definition of taxable disposal

The government previously announced at Budget 2016 that legislation will be introduced in Finance Bill 2017, and in secondary legislation, to amend the definition of a taxable disposal for landfill tax. The government has consulted in the draft legislation and changes have been introduced in order to clarify the tax treatment of material disposed of at landfill sites and give greater certainty to landfill site operators. The draft legislation has been restructured to simplify and improve ease of comprehension. The measure will come into effect after Royal Assent of Finance Bill 2017 and the changes will apply to disposals to landfill in England, Wales and Northern Ireland.

Alcohol and tobacco

The duty rates on beer, cider, wine and spirits will increase by the RPI with effect from 13 March 2017.

The government announced that it intends to have a consultation on:

(a) introducing a new duty band for still cider that has a just below 7.5% abv in order to target white ciders, and

(b) the impact of introducing a new duty band for still wine and made-wine between 5.5-8.5% abv.

Tobacco duty rates

The government has previously announced in Budget 2014 that tobacco duty rates will increase by 2% above RPI inflation and this change will come into effect from 6pm on 8 March 2017.

Minimum Excise Tax

The government announced that it will be introducing a Minimum Excise Tax for cigarettes that is intended to target the cheapest tobacco and promote fiscal sustainability. The rate will be set at £268.63 per 1,000 cigarettes. The new tax will come into effect from 20 May 2017. Please see Minimum Excise Tax for cigarettes for more information.

Tobacco: Illicit Trade Protocol - licensing of equipment and the supply chain

Following the announcement made in Autumn Statement 2015 and following technical consultation on the draft legislation produced in December 2016, legislation will be introduced in Finance Bill 2017 that will be intended to control the use and ownership of tobacco manufacturing machinery in the UK. The changes are intended to prevent the illicit manufacture of tobacco products in the UK by introducing powers to establish a licensing regime for this type of machinery.

Powers will also be introduced to provide for forfeiture of unlicensed tobacco manufacturing machinery and penalties for failure to comply with the conditions of a licence. The legislation will take effect from the date of Royal Assent.

Heated tobacco products

As announced in Budget 2016 the government will be consulting on the duty treatment of heated tobacco products. The consultation will be launched on 20 March 2017 and the consultation document should be available on this date.

Soft drinks levy

The levy for sugar that is added to drinks with a total sugar content of at least five grams per 100 millilitres will be set at 18 pence per litre and drinks with a sugar content of at least eight grams will be set at 24 pence per litre. Manufacturers and importers who take reasonable steps to reduce the sugar content will pay less or alleviate the need to pay the levy at all.

Following consultation the legislation has been revised to include a criminal offence for evasion of the levy. Minor amendments have also been made to improve clarity. The levy will take effect from April 2018.

Gaming duty

Gross gaming yield (GGY)

The government previously announced in Budget 2016 that they will include legislation in Finance Bill 2017 that will raise the GGY bandings for Gaming Duty in line with inflation based on the RPI. The revised GGY will be used to calculate the amount of Gaming Duty due for accounting periods starting on or after 1 April 2017.

Remote gaming duty – freeplays

The government announced in Budget 2016 that it will include legislation in Finance Bill 2017 to amend the definition of gaming payment and prizes and change the tax treatment of freeplays for remote gaming duty. The government consulted on the changes and the draft legislation has been amended to ensure that the change is proportionate. The legislation is intended to ensure that freeplays used to participate in remote gaming will have a value as stakes when calculating the dutiable profit of the operator and freeplays given as prizes will not be deductible.

Personal tax

Professional bodies approved for tax relief - HMRC List 3

HMRC updated its 'List 3' (deduction for fees and subscriptions paid to approved professional organisations and learned societies under ITEPA 2003, s343) in February 2017.

Latest additions include:

- BASE UK, from 2016-17
- European Society of Intensive Care Medicine (ESICM), from 2016-17
- Institute of Chartered Accountants of Pakistan (ICAP), from 2016-17
- International Association of Teachers of English as a Foreign Language from 2016-17
- Social Work England, from 2018-19

http://www.gov.uk/government/publications/professional-bodies-approved-for-tax-relief-list-3

Business investment relief **(Lectures P1007/ P1008 - 20.02/ 8.56 minutes)**

Business Investment Relief is a relief which allows remittance basis taxpayers to remit their overseas income and gains to the UK tax-free as long as they use the money for the purpose of making a commercial investment in a company – The legislation relating to Business Investment Relief was brought in by FA 2012 and can be found in Ss809VA – 809VO ITA 2007.

With effect from 6 April 2012, there is deemed to be no remittance of foreign income or gains by a non-UK domiciled individual, provided that:

- a relevant event occurs; and
- the individual makes a claim on or before the first anniversary of 31 January following the end of the tax year in which the income or gains would otherwise have been regarded as remitted to the UK (S809VA ITA 2007).

A relevant event occurs if the money in question is:

- used by a person to make a qualifying investment (ie. directly); or
- received in the UK in order to be used by someone else to make a qualifying investment (ie. indirectly).

The qualifying investment must be made by what is known as 'the relevant person' within 45 days of the money being received in the UK. By virtue of S809M ITA 2007, the investor can either be the non-UK domiciliary himself or else some other person mentioned in that section such as a trust of which he is a beneficiary or a close company in which he is a shareholder.

It was originally provided that a qualifying investment covered the subscription of new shares or securities in and making of loans to a company (referred to in the legislation as 'the target company') (S809VC ITA 2007). In addition, at the time of the investment, the target company must meet Condition A and the investor must meet Condition B.

Condition A

This is set out in S809VD ITA 2007 and currently specifies that the target company must be either an eligible:

- trading company; or
- stakeholder company; or
- holding company.

There is no requirement that the company has to be incorporated in the UK.

The company invested in must always be a private company, none of whose shares are listed on a recognised stock exchange. Investments in LLPs and other non-corporate structures are excluded.

Eligible trading company

An eligible trading company is a company which is carrying on at least one commercial trade (see S809VE ITA 2007) or is preparing to do so within the next two years – this is the present position, but changes are in the offing.

A couple of points should be noted:

1. property businesses count as commercial trades – this includes property letting (both residential and commercial) as well as property development; and
2. the company's trading must represent at least 80% of its overall activities – this is similar to the test used for entrepreneurs' relief (it is understood that HMRC measure the percentage by reference to turnover alone).

Eligible stakeholder company

This is a company that exists wholly for the purpose of making investments in eligible trading companies, ie. it is effectively an investment company. There is no need to have a controlling interest. HMRC state that 'minor or incidental' non-qualifying activities can be ignored. A stakeholder company must hold all its investments directly – no intermediate holding company structures are allowed.

Eligible holding company

The third permitted category is an eligible holding company. This is a 51% test and all the holding company's subsidiaries must be trading companies. In this context, the 80% test is applied to the group as a whole rather than on a company-by-company basis. Intermediate holding companies *are* permitted.

Condition B

Condition B is explained in S809VF ITA 2007. This section states that, at the time of the investment, the investor must not:

- have obtained a 'related benefit';
- have become entitled to obtain a 'related benefit'; or
- be expecting to obtain a 'related benefit'.

For this purpose, a benefit represents anything in money or money's worth that would not be provided in the ordinary course of business. This restriction will not be a problem for items such as director's fees or normal benefits in kind. Benefits are related if, broadly, they are directly or indirectly attributable to the making of the investment and would not have been available had the investment not been made.

In summary, therefore, the following points about the form of the investment should be emphasised:

1. There are no upper or lower limits on the amount of remittance basis income or gains that can be invested. Nor are there any restrictions on the size of the investment.
2. Relief is not restricted to UK-resident companies nor is there a stipulation that the business must be carried on wholly or mainly in the UK.
3. All types of trade are sanctioned – this regime is much more flexible than the SEIS, EIS and VCT legislation.
4. There is no embargo on the investor working for the company. It is quite in order for a non-UK domiciliary to invest money in his own company (or in a company owned by other members of his family).
5. Any form of investment can qualify: ordinary shares, preference shares, loans etc.
6. As an alternative to investing directly, the individual can, if he wishes, make his investment via an offshore trust of which he is a beneficiary or a personal investment company in which he is a shareholder.

Business Investment Relief is clawed back (ie. there is deemed to be a remittance to the UK) where there is:

- a 'potentially chargeable event'; and
- 'appropriate mitigation steps' are not taken within the 'relevant grace period' (S809VG ITA 2007).

Potentially chargeable event

A potentially chargeable event occurs if:

- the target company ceases to be an eligible company (eg. because it obtains a stock exchange listing);
- the investor disposes of all or part of the qualifying investment;
- value is extracted from the company other than on a sale or in the ordinary course of business; or
- the start-up requirement of two years is not met (S809VH ITA 2007).

S809VI ITA 2007 explains the appropriate mitigation steps that must be taken, following a potentially chargeable event, in order to prevent the affected income or gains being treated as remitted to the UK. Where the potentially chargeable event is a disposal of all or part of the holding, the proceeds from the disposal must either be taken offshore or alternatively reinvested in another qualifying company. In any other case, the individual must dispose of the *entire* holding (or whatever part still belongs to him) and either take the proceeds offshore or else reinvest them. The relevant grace period is normally 45 days, although it can sometimes be longer.

In 2015, the Government announced that they would be consulting on ways in which the BIR rules could be amended in order to increase the take-up. They made it clear that they wanted to expand the scope of the Business Investment Relief by making it easier and more attractive for potential investors to bring their money from overseas in order to put it into UK businesses. The changes set out in S18 FB 2017 are the result. They widen the types of business in which an investment can be made and they modify the anti-avoidance legislation so that ITA 2007 does not discourage genuine investment. They also clarify parts of the rules which were previously unclear.

The various amendments, which all come into force on 6 April 2017, are as follows:

1. The wording of S809VC ITA 2007 has been altered so as to allow an investor to claim Business Investment Relief on the acquisition of existing shares in a company, ie. shares no longer have to be subscribed for.

2. In S809VD ITA 2007, the start-up period for a company has been extended from two to five years. In addition, the revamped section provides for the introduction of a new eligible hybrid company. Such a company will be a combination of both a trading company and a stakeholder company – previously, an investment could only be made in a company that carried out one of these roles rather than a combination of both of them.

3. S809VE ITA 2007 clarifies the position in relation to corporate partners. Investment in LLPs and other forms of partnership was excluded from Business Investment Relief *ab initio* – see above. It has always been the Government's position that this exclusion encompassed corporate members of LLPs and other partnerships – indeed, HMRC are known to have refused claims, on a consistent basis, for Business Investment Relief on investment in such corporate members.

> Feedback to the Government has suggested that the legislation is not completely clear in this respect. The amendment here addresses this concern by stating explicitly that a company that is a member of an LLP or a partner in a partnership is not to be regarded as carrying on the trade of the LLP/partnership. This means that, unless the target company is carrying on a commercial trade in its own right, it will not qualify for Business Investment Relief.

As mentioned in above, a potentially chargeable event occurs if value is extracted other than on a sale or in the ordinary course of business. This can be described as the 'extraction of value' rule. Hitherto, it has been breached if an investor receives any abnormal benefit, directly or indirectly, from the company in which they have invested or from any company associated with this company (these are called 'involved' companies), whether or not the benefit was connected with the investment. The revised wording removes the reference to an 'involved' company. In other words, the extraction of value rule will only be treated as having been breached if an abnormal benefit is received in circumstances directly or indirectly attributable to the investment – the fact that it comes from what was formerly described as an 'involved' company will no longer be automatically fatal.

Where a company fails to satisfy the new five-year start-up time limit, the grace period allowed will be extended to two years from the date when the investor first became aware, or ought reasonably to have become aware, that the company was what ITA 2007 calls 'non-operational'.

Contributed by Robert Jamieson

Beneficial loan rate fall

The Taxes (Interest Rate) (Amendment) Regulations, SI 2017/305, reduce the official rate of interest applicable to employment-related 'beneficial' loans from 3% to 2.5% per annum with effect from 6 April 2017. The rate has stood at 3% since April 2015.

Tax Journal (15 March 2017)

PAYE Notice of coding

Summary – As neither the employer nor agent had agreed to accept electronic communications, the employer had done all that was required and their appeal was allowed.

HMRC claimed that they had electronically issued a notice of coding, taking into account an employee's company car, to the taxpayer's agent whom it believed was authorised to receive such communications.

The taxpayer said neither it nor the agent had received the coding notice and that they were not set up to receive electronic communications. Consequently, the taxpayer underpaid PAYE tax and National Insurance.

HMRC issued a reg 80 determination on the employer to collect the underpayment.

The taxpayer claimed that on the basis that the employer had taken reasonable care to comply with the PAYE regulations and the underpayment was not its fault, HMRC should reduce the reg 80 determination to zero and raise a reg 72(5) determination on the employee to pay the tax.

Decision

The First-tier Tribunal said, under reg 196(1), if HMRC used an approved method of electronic communication it was presumed it was received unless the contrary was proved. However, HMRC could only communicate electronically if the employer or its agent had consented.

Although the agent was authorised using form 64-8, nothing alluded to acceptance of electronic communications. The only email address held by HMRC was the previous agent's.

The judge agreed that the employer had done all that was required to effect a change of agent and to alert HMRC to the employee's company car.

The taxpayer's appeal was allowed. The department should not have issued a reg 80 determination. It should vacate it and make a direction under reg 72.

COS Systems Ltd v Revenue and Customs Commissioners (TC5660)

Latest PAYE and NIC guides

CWG5 (2017): Class 1A NICs on benefits in kind

The latest version of its employers' guide to Class 1A NICs on BIKs

www.gov.uk/government/publications/cwg5-class-1a-national-insurance-contributions-on-benefits-in-kind

CWG2 (2017): Employer further guide to PAYE and NICs

This is the latest version of its guide that should be used from 6 April 2017.

www.gov.uk/government/publications/cwg2-further-guide-to-paye-and-national-insurance-contributions

Booklet 480 (2017): Expenses and benefits - a tax guide

HMRC’s recently updated guide is available to download from the government’s website *www.gov.uk/government/publications/480-expenses-and-benefits-a-tax-guide.*

Spotlight 37 – targeted list of tax avoidance schemes

HMRC has added Spotlight 37 to its targeted list that concerns a disguised remuneration scheme using an umbrella company

The contractor becomes an employee of the company and is paid a small basic wage with little or no tax and NICs deducted. The second part of the payment is used to advertise the contractor’s services on a job board.

They immediately receive loyalty points in return for keeping their details on the job board. The loyalty points can be cashed in by the employees shortly after, with no deductions made for tax or NICs. The contractor usually has to pay a large fee to the third party running the job board.

HMRC says it will challenge all users of this scheme and any umbrella companies involved. Receiving and redeeming the loyalty points is taxable income, which forms part of the contractor's employment income from the umbrella company.

www.gov.uk/government/publications/tax-avoidance-schemes-currently-in-the-spotlight

Capital Taxes

CGT Annual exemption

The Capital Gains Tax (Annual Exempt Amount) Order, SI 2017/377, sets the annual exempt amount for the tax year 2017/18 at £11,300 (subject to Parliamentary approval).

Tax Journal 15 March 2017

Taxing disposals of land in the UK

'Profits from Trading in and Developing Land in the UK' legislation introduced in Finance Act (FA) 2016 looked to ensure that for disposals made on or after 5 July 2016, all profits from dealing in or developing land in the UK were brought into charge to UK tax. Where the contract was entered into before 5 July 2016 but the transfer takes place a short time later, such transactions were excluded. However, some developments involved extended contracts with transfers being made over months or years. It was not intended that such transactions were excluded.

To remedy this, legislation will be introduced in Finance Bill 2017 to the effect that all profits from dealing in or developing land in the UK that are recognised in the accounts on or after 8 March 2017 will be taxed. This will be the case even if the contract for disposal was entered into prior to 5 July 2016.

www.gov.uk/government/publications/income-tax-and-corporation-tax-disposals-of-land-in-the-uk

Valuation – Hereditament

Summary – The Supreme Court reversed the Court of Appeal's decision and held that, based on the facts, the Upper Tribunal had been correct that ***a hereditament was to be valued as it existed at the time and not based on the property's state after restoration was complete.***

The taxpayer owned the freehold of the first floor of an office building which, on the 2010 rating list, was listed as a hereditament 'offices and premises'. However, on 6 January 2012, the taxpayer proposed that the description should be 'building undergoing reconstruction' and that the rateable value should be reduced to £1.

The Valuation Tribunal concluded that on 6 January 2012, the building was in reasonable repair but on appeal to the Upper Tribunal, the decision was reversed. The premises had been stripped to such an extent that to replace its major building elements would go beyond the meaning of repair.

The Court of Appeal reversed this decision stating that Schedule 6 of the Local Government Finance Act 1988 meant that, based on the facts found by the Upper Tribunal, the repairs would return the premises to their former state and so the premises should be valued as if they were in a state of reasonable repair. The case was referred to the Supreme Court.

The central issue in the appeal was whether the premises should be rated based on the physical condition on 6 January 2012 or whether Schedule 6 para 2(1)(b) of the 1988 Act (para 2(1)(b)), as amended by the Rating (Valuation) Act 1999 (the 1999 Act), required a valuation officer to assume that they had been in reasonable repair as 'offices and premises' on that date.

Decision

The Court of Appeal had erred in having interpreted Sch 6 to the 1988 Act as having entailed a major departure from the reality principle by having required that the hereditament be assumed to be in a reasonable state of repair for the mode of occupation listed in the rating list, namely as offices and premises.

The repairing assumption within Schedule 6 of the 1988 Act had not removed the reality principle to that extent. The premises had been undergoing reconstruction on the key day and the Upper Tribunal had been entitled to alter the rating list as it had to reflect that reality.

The appeal was allowed and the Upper Tribunal's determination restored.

Court of Appeal, Civil Division, [2015] 4 All ER 1014 Reversed.

**Newbigin (Valuation Officer) v S J & J Monk (a firm)(2017) UKSC 14*

Claim for capital losses was careless

Summary – A claim for loss relief on a waived loan was careless. The taxpayer should have known that his loan had been converted into shares a few yeasr earlier.

Mr Fry was the sole shareholder and director of KXDNA and in 1999 he loaned close to £1 million to the company to finance the administrative and management costs in opening a related company, KX Gym UK Limited.

In 2004, additional investment was sought, a second director appointed and Mr Fry's loan was converted into shares.

KX Gym, an associated company, had borrowed £7.7m from KXDNA and in 2009, KXDNA agreed to waive this loan.

Mr Fry's was advised that the loan waiver gave rise to a capital loss for him as it was his loan money that had effectively funded the associated company loan and so he claimed CGT relief under S253 TCGA 1992.

HMRC:

- disallowed the claim, issuing an assessment to recover the tax;
- issued a penalty for £163,000 for careless behaviour for an inaccuracy in his return.

Mr Fry later withdrew his s 253 claim but appealed against the penalty.

Decision

By checking the company's accounts Mr Fry would have known that his loan had been converted into shares and so relief for his loss was not available. The judge concluded he had been careless and the conditions for a penalty were met.

However, the penalty had been calculated based on the full loss. In reality only a small amount had been claimed against gains in 2009/10 with the bulk being carried forward for relief in future years.

The Tribunal noted that Mr Fry was working in Switzerland and trying to obtain employment in the USA, where his wife and son resided and had no intention to return to the UK. It was unlikely that the remainder of the loss that was being carried forward would be used.

The penalty of £163,000 was disproportionate to the carelessness which had occurred and should be recalculated by reference to the used portion of the loss. The penalty was reduced to just over £5,000.

Simon Fry v Revenue and Customs Commissioners (TC05651)

Failed double trust arrangement rectified by High Court (Lecture P1009 - 14.43 minutes)

A failed double trust scheme was the subject of an interesting High Court case in *Bullard v Bullard (2017)*.

The arrangement was created in 2002 on the advice of a well-known firm of solicitors after the taxpayer (Mrs B) realised that the value of her home had increased by an amount likely to be caught in the IHT net. The lawyers advised Mrs B to adopt a double trust structure that was a planning device widely used at the time. This required her to set up a life interest trust to which she would then sell her house in return for a market value IOU (the first trust). Mrs B subsequently gifted this IOU to an interest in possession settlement in favour of her two adult children and five grandchildren (the second trust).

The purpose of the arrangement was that there would be no initial IHT charge. The sale of Mrs B's house to the first trust was for full market value and so fell outside the scope of IHT and, because it was a *sale*, it could not be caught by the gift with reservation rules even though Mrs B continued to occupy the property. The pre-owned asset legislation had not yet been invented. The intention was that the gift of the IOU to the second trust was a potentially exempt transfer (PET) which would become IHT-exempt once Mrs B had survived a further seven years.

The tax planning idea would have worked if all Mrs B's grandchildren had been adults at the time when the trusts were established. Unfortunately, none of them were. The interest in possession settlement (the second trust) was thus caught by S31 Trustee Act 1925 whose default effect is to divest any interest of a minor in trust property and replace it with a contingent interest in accumulations of income held until the beneficiary attains his or her majority (unless, of course, the trust deed provides otherwise).

The result of this provision was that the second trust was not considered to be an interest in possession settlement for the purpose of avoiding an immediate IHT charge, at least as far as the grandchildren were concerned. Moreover, the person who drafted the trust deed for Mrs B had included a provision expressly applying S31 Trustee Act 1925!

This clearly showed an intention that the section should apply, despite the fact that the trust was described as an interest in possession settlement for the minors (which it certainly was for the two adult beneficiaries).

When this was drawn to Mrs B's attention, she brought the case to the High Court asking for the deed to be rectified.

In the High Court, the judge took as his precedent *Re Butlin's Settlement Trusts (1976)* where it was stated that rectification is available 'where the words of the document were purposely used but it was mistakenly considered that they bore a different meaning from their correct meaning as a matter of true construction'.

The judge decided that there was convincing proof that Mrs B had intended to create an interest in possession settlement because she understood that that would imply no immediate charge to IHT. He went on:

> 'In the present case, the evidence satisfies me that the claimant wanted and intended to create an interest in possession trust, whereby all the primary beneficiaries obtained interests in possession. By using language, the legal effect of which the claimant mistook, she has failed to do so. The Court therefore has power to rectify the trust deed to create the interests in possession intended.'

The judge granted the request for the deed to be rectified. It is understood that this was effected by *excluding* the operation of S31 Trustee Act 1925.

It should be noted that HMRC declined to be joined into these proceedings.

Contributed by Robert Jamieson

Non-domicile taxation and overseas trusts

New rules were to be introduced give protection to trusts created by non-domiciled individuals before they become deemed domiciled under the new rules.

HMRC has published a note advising that it has not been able to incorporate all of the changes arising from consultation on the legislation for overseas trusts in the current Finance Bill,.

The following provisions have been omitted from the Finance Bill 2017 but will be included in a future Bill:

Capital Gains Tax TCGA Schedule 5:

- disregard of section 87 capital payments to non-residents
- disregard of section 87 capital payments to migrating beneficiaries

- transfer of s 87 benefits charge to the settlor where the beneficiary is a close family member of the settlor and is not liable to CGT on the payment
- attribution of gains to recipients of onward gifts (recycling rule)

Chapter 5 of Part 5 of ITTOIA (Settlements):

- benefits charge for settlor and close family members of settlor
- benefits charge on settlor when beneficiary is close family member and is not taxable on the benefit
- attribution of deemed income to recipients of onward gifts (recycling rule)

Chapter 2 of part 13 of ITA 2007 (Transfer of Assets Abroad)

- attribution of deemed income to recipient of onward gift (recycling rule)

www.gov.uk/government/publications/non-domicile-taxation-technical-briefing-on-overseas-trusts

Administration

Making Tax Digital: What do we know now? (Lecture P1010 – 22.45 minutes)

On 15 August 2016 HMRC released six consultation documents on Making Tax Digital (MTD) and from 2018 the tax system will become increasingly digital with most businesses, the self-employed and landlords needing to use software or apps to keep their business records and to update HMRC on a quarterly basis within one month of the quarter end.

On 31 January 2017 HMRC published their consultation responses which made minor concessions but HMRC are still aiming to introduce MTD in the following phases:

- Business income tax with effect from the first accounting period beginning after 5 April 2018
- VAT in 2019; and
- Corporation tax and in 2020.
- Partnerships with turnover over £10m will be able to defer their income tax MTD obligations until 2020.

At Spring Budget 2017 it was confirmed that a one-year deferral until April 2019 will apply to sole traders with a turnover below the VAT threshold (£85,000 from 1 April 2017). This means that only those unincorporated businesses with a turnover in excess of the VAT threshold will be required to start using the new reporting regime from April 2018. Those with a turnover under £10,000 are exempt from the requirements altogether.

A taxpayer with a year end of 31 August 2018 and turnover in excess of £85,000 would be within MTD from 1 September 2018. Their first update would be for quarter to 30 November 2018 that must be submitted by 31 December 2018.

If their turnover was under £85,000 then the first quarterly upload would be to 30 November 2019.

Taxpayers that align their year end with the tax year would have their first quarterly upload to 5 July 2018 with no SAR needed for 2018/19 – assuming their turnover exceeded £85,000. It would be a year later for those under £85,000.

Unless HMRC introduce anything to the contrary, traders with year ends of 31 March would not fall within MTD until the year to 31 March 2020 with their first quarterly upload being the three months to 30 June 2019. The year to 31 March 2020 is the first accounting period starting after 5 April 2018.

Presumably those 31 March clients with turnover under the VAT limits will come within MTD a year later i.e. year to 31 March 2021 with their first quarterly upload being for the quarter to 30 June 2020. This seems too good to be true!!

HMRC confirm that extensive piloting will be undertaken in 2017 to ensure a smooth transition to MTD.

The underlying tax rules will be simplified to support these changes.

1. Bringing business tax into a digital age

Digital record keeping and regular updates to HMRC are central to Making Tax Digital. Businesses will be required to update HMRC quarterly with summary data that is uploaded direct from their software or app and then at the end of the year, businesses will have ten months to complete any annual tax adjustments that are needed. Taxpayers will be supported in a number of ways through product guidance, free software, financial support, extra tax relief and training sessions.

In their consultation response HMRC did confirm that spreadsheets were an option BUT the spreadsheets will have to go through some form of MTD compatible software in order to upload into the HMRC system. Software developers will be left to develop this conversion software!

2. Simplifying tax for unincorporated businesses

There is a general desire to simplify the tax system. There was a proposal to extend the current cash basis threshold from £83,000 to £150,000 for unincorporated businesses.

Budget 2017 has now confirmed that the cash basis threshold will increase to £150,000 from April 2017.

Additionally they are looking at reforming the capital v revenue distinction and giving upfront relief for all types of expenditure within the cash basis. Property will be excluded.

3. Simplified cash basis for unincorporated property businesses

Under the proposals, unincorporated landlords would have a default cash basis rather than the accruals basis. If they wish to remain in accruals accounting a specific election must be made.

Budget 2017 confirmed that cash accounting for unincorporated landlords will have a turnover restriction of £150,000 and will be introduced from April 2017.

However, this will not be available to partnerships where they have a corporate partner.

4. Voluntary pay as you go

The current payment dates of 31 January and 31 July will not be altered but quarterly updating will offer the opportunity to pay tax more regularly if preferred.

The consultation considers how taxpayers might make and manage more regular payments and how the payments will be allocated across the taxes.

5. Tax administration

Making tax digital is intended to be easy for taxpayers to understand and give them time to correct matters if need be.

A new penalty regime will be introduced for late filing and late payment and aimed at repeat offended.

Following a one year period of grace at the start, late submission penalties will follow a graduated model with each non-deliberate failure attracting penalty points and a penalty being charged once accumulated points reach a level to be decided.

Late payment penalties will be fair and proportionate with the opportunity to rectify the position before penalties apply

Penalty interest is being considered.

6. Transforming the tax system

HMRC plan to use third party information more effectively by pre-populating the taxpayers Digital Tax Account with payroll information, bank and building society interest as well as other income streams in due course.

Taxpayers will see a complete and up-to date picture of all their tax liabilities in their Digital Tax Account, will be able to update it with any additional income and use their accounts to answer questions about their tax code.

Making Tax Digital is not going to disappear. The scheduled start date is 2018 for some clients so it is important that our staff and clients are ready for this significant change.

HMRC case study – Eve

Eve has a MTD accounting app on her Smartphone and is able to capture her receipts at point of purchase by taking photos of her receipts that are then captured by her software and invoices are stored electronically on the cloud. Some stores send her electronic invoices that her software is able to capture immediately.

When the invoice is captured in her software, her app populates the amounts recognised from each receipt. She is prompted to confirm that the receipt is for a business purpose and to identify which category of spend this should be allocated to whether that is motor expenses, materials etc. Going forward, future receipts from the same supplier will automatically follow the same categorisation but Eve can select an alternative categorisation if appropriate. Capturing invoices in this way is already possible but will have become a lot more sophisticated by 2018.

Contributed by Dean Wootten

Making Tax Digital: Which software should we be using? (Lectures B1007/ B1008 – 19.40/ 14.28 minutes)

Introduction

All the main software providers offer fundamentally the same service – cloud based accounting software. The focus of cloud based technology is that your accounting software is not actually on your PC, laptop or phone – it is on a server which you would access via a WIFI connection. The advantage of this is that any authorised person can access the software immediately. So bookkeepers, owners and accountants have immediate access to the accounting software of the business.

The data is automatically backed up and anyone accessing the software can see the very latest position. It is this cloud based technology that practices need to utilise to benefit from the opportunities that MTD brings.

As practitioners we may have a software preference but ultimately we will need to be seen to support various software packages. We cannot ask a client to switch from Quickbooks to Xero or from Sage to KashFlow if they are very comfortable with their current program. Our objective must be to ensure clients keep their data entry up to date – if they have something that works from that perspective it is best that we work with their existing software. We may have to persuade them to utilise the cloud based functionality of their software but if they are comfortable with the software this should not be too much of an issue.

When it comes to clients currently without software we will undoubtedly have a preferred offering in mind for that particular client. Whether we recommend FreeAgent, KashFlow, Quickbooks, SageOne, Xero etc will very much depend on the nature and size of the client.

Our focus should always be "what affordable software do we think this client will use best". As a firm we should be able to deal with any of the main software packages. It may be that certain groups of clients are drawn to a particular provider in terms of price and we then become significant users of that software but there will always be clients who prefer something else so our skill set must be wide.

If the client keeps their records up to date then MTD will be fairly straightforward – as HMRC keep telling us! If the client is a little haphazard with data entry and we are trying to input the missing data then MTD becomes a problem. The matching of software to client will be key to the MTD process.

Some software providers offer a trial balance feed into your accounts producing software. It is however open to debate whether you still need accounts producing software given the capability of the software on offer. You will certainly need accounts producing software for your corporate clients for the disclosure requirements but unincorporated clients do not need that level of detail or disclosure. If the accounting software can produce an acceptable profit and loss account and balance sheet for a sole trader why do we need to put the data through our own internal software to produce the same? Some firms may use this process for an audit trail but surely we can have the same through the client's software?

Software generally

All providers tend to offer a complete cloud based product with a monthly licence fee. There is no fixed period for the licence with taxpayers free to cancel their licence at anytime. The licence fees vary depending on the size of the business and what your client needs from the software. All the main software providers will be MTD compliant with the ability to upload summary data direct into the taxpayers Digital Tax Account.

Sales invoices can be generated from the accounting software and e-mailed directly to the customer. There is normally a facility for setting up recurring sales invoices and an automated service for reminders for late paying customers. Quotes and estimates can also be generated from the software.

Supplier invoices can be entered into the software in various ways including scanning into a mobile phone app.

Most software providers offer automatic bank feeds where transactions are imported into the software from the client's online bank account. The client need only allocate the receipts and payments to the correct accounts – most of the providers offer prompts in this regard.

All offer integrated VAT returns and payroll although the payroll option tends to be for an additional monthly fee. The VAT and payroll services feed directly into the HMRC system.

All the software packages look very similar. The home page is generally a "Dashboard" from which you can easily navigate to the various sections of the software.

Full support is offered on all software packages. This is generally a combination of webinars, FAQs, Chat facilities and telephone support.

There are online services available which seamlessly move accounting data from one software package to another. Such a service can be found at www.movemybooks.co.uk and it tends to be free when converting to Xero or Quickbooks.

Software such as FreeAgent and KashFlow do not have the same converting services and it may be prudent to change providers at a year end if these are your chosen providers.

If the taxpayer is moving from manual records to software then data conversion is not so much of an issue. It would seem sensible to make the move at the start of an accounting year though.

The specific software offerings are as follows:

FreeAgent

This software is not as well known as some of the other software providers but it is extremely popular with over 50,000 users.

It offers the standard cloud based offering that you would expect and is aimed at freelancers, small business owners and accountants. The software is visually appealing and is relatively easy to use.

		Sole Trader	**Partnership/LLP**	**Limited Company**
Monthly licence fee: - Introductory 6 months - Ongoing		 £9.50 + VAT £19 + VAT	 £12 + VAT £24 + VAT	 £14.50 + VAT £29 + VAT
USP:		Fills 90% of the self-employment SAR	Profit share calculation	Corporation tax estimates (and Directors SAR)
Other useful features		Tax timelines Time tracking	Tax timelines Time tracking	Tax timelines Time tracking

FreeAgent also offers an Accountants Partner Programme which interacts with the client's software. This Programme allows the practice to access client software from a Practice Dashboard and use facilities that are more akin to the accountant rather than the client.

These facilities would include profit and loss accounts, balance sheets, aged debtors and creditors, trial balances which feed into accounts production software, IR35 deemed salary calculations and automated dividend vouchers.

When your practice goes onto the Accountants Partner Programme clients can enjoy discounts of between 30% and 50% off the monthly licence fees.

KashFlow

This software is owned by IRIS and is aimed at the smaller business. The software has good user functionality and will certainly be of interest to accountants that use IRIS within their practice.

		Starter	**Business**	**Business + Payroll**
Monthly licence fee: - Introductory period - Ongoing		 Free 14 day trial £7 + VAT	 Free 14 day trial £13 + VAT	 Free 14 day trial £18 + VAT
USP:		Up to 10 sales invoices and 25 bank transactions per month. No recurring functionality	Comprehensive services	Comprehensive services plus fully functional payroll
Other useful features		CIS functions Asset registers	CIS functions Asset registers	CIS functions Asset registers

KashFlow also offers an Accountants Programme which interacts with the client's software.

Uniquely KashFlow also offers a unique branding function whereby the client's software can be configured to match the look and feel of their accountant's website and brand.

KashFlow integrates into the IRIS accountancy platform, giving you a complete picture of the client's business, including all work carried out to prepare tax and accounts. For practices that currently use IRIS the compatability with your existing systems will be of interest.

QuickBooks

This software is probably the best known and the most prominently advertised UK software

		Self-employed	**Small business - Essentials**	**Small business - Plus**
Monthly licence fee: - Introductory 6 months - Ongoing		 £2.99 + VAT £6 + VAT	 £10.50 + VAT £15 + VAT	 £15 + VAT £25 + VAT
Payroll cost:			Included	Included
USP:		1 user restriction and restricted sales invoice functionality. Not for VAT registered.	3 user restriction. Inventory tracking	5 user restriction. Manage stock, track employee time
Other useful features		Separate business and personal transactions/snap and sort receipts	Manage CIS deductions	Create budgets and purchase orders

QuickBooks is certainly the most widely used software but they are facing increased competition from comparable products. Their pricing structure is very competitive but we should not lose sight of the fact that we want clients to use something that is very simple. Other providers may have the edge in that regard.

SageOne

This software has a well known brand name and does offer the full suite of accounting software to accountants. It also has the advantage of being very familiar to staff. Sage are also putting a lot into their cloud based offering so I believe this improved offering is worthy of serious interest – especially if SAGE products are widely used in the office.

		Start	**Accounting**
Monthly licence fee: - Introductory 3 months - Ongoing		 £3 + VAT £6 + VAT	 £10 + VAT £20 + VAT
USP:		Enough basic functions for the smaller business – including VAT	Multi-user, Unlimited invoices
Other useful features		Tracking invoices	Cash flow forecasts

Sage Payroll is also available from £5 per month for up to 5 employees with a further 50% discount off that sum for the first 3 months. The monthly fee increases in bands depending on the number of employees on the payroll.

They also offer a Partner Edition for accountants – essentially a dashboard where you can see all your Sage One clients. The practice tools this offers look very useful and are aimed at increasing efficiency.

Xero

This software is becoming very popular and is often favoured by firms looking for a cloud based solution for their clients.

		Starter	**Standard**	**Premium**
Monthly licence fee: - Introductory 3 months - Ongoing		 £7.50 + VAT £10 + VAT	 £16.50 + VAT £22 + VAT	 £20.62 + VAT £27.50 + VAT
Payroll cost:		Free for 6 months then £5/mth for under 5 employees, £1 per each additional employee	Free for 6 months then £5/mth for < 5 employees, £1 per each additional employee	Free for 6 months then £5/mth for < 5 employees, £1 per each additional employee
USP:		Monthly restrictions of 5 invoices, 5 bills and 20 bank transactions	Inventory tracking	Inventory tracking
Other useful features				Multi-currency

This is a very user friendly package and is likely to prove popular with clients. Accountants are also finding this software more user friendly than its better known rivals.

Contributed by Dean Wootten

Making Tax Digital: How do we become a Digital Practice? (Lecture B1009 – 10.31 minutes)

MTD should be regarded as a huge opportunity for accountancy practices – albeit with a steep learning curve for clients!

We will undoubtedly experience problems along the way but over time the problems will become less and less.

Initially practitioner's workloads might be an area of concern. The calendar quarters are likely to be very popular. In the short term we will have to plan for this but as clients become more comfortable with the software our constant online access should even out the practitioner's workload.

Client data is constantly available to accountants and it should be feasible to create data exception reports within the accountant's dashboard which would identify any problems at an early stage. Indeed the software is expected to have "prompts and nudges" to highlight likely errors. Accountants using the software to its full capability will thrive within the MTD system.

Accountants will need staff with different skill sets to compliment their current staffing levels. Apprentices with an interest in IT are likely to be in high demand.

In my opinion it would be advisable to migrate selected businesses to cloud based accounting software a year before MTD commences. This would be for the year ended 31 March 2018 for your selected clients. Use this period to ensure that clients are comfortable with the software and that, as their agent, you get into habit of reviewing client data monthly and/or on an exception basis. Teething problems can be ironed out on your firm's pilot scheme and you can form a clear idea of how MTD should be rolled out to clients generally. You will not only be learning what you need to do but also how the clients react to their new found responsibilities.

It might be that we can offer a complete bookkeeping solution to some clients that would rather not deal with this themselves. Costs will be a factor but using the software to its full extent will reduce that pressure. Direct bank feeds will be an essential tool when offering the complete package.

Making Tax Digital will happen and practitioners need to start addressing the changes as soon as possible by communicating with clients to outline the changes and ensuring that that they are considering the optimum way forward in terms of software to use and when to comply.

Software providers such as FreeAgent, KashFlow, QuickBooks, Sage and Xero all have suitable offerings. Spreadsheets will be accommodated under MTD but it might be advisable to move clients across to a fully integrated cloud based software package.

It is worth spending the next few months researching software and decide:

- what cloud based software suits your client base
- how best to train your staff to use the software effectively

Remember to review your clients' information regularly and utilise the software to add value to your service. Interpreting information and providing that value added advice to clients will be of major importance to firms wanting to increase their profitability.

Becoming a "digital practice" is definitely the way forward and indeed the only way forward.

Contributed by Dean Wootten

CC/FS17: Higher penalties for offshore matters

This factsheet provides details of the higher penalties that may be charged for Income Tax, Capital Gains Tax and Inheritance Tax when an offshore matter is involved.

HMRC may charge a penalty of more than 100% in certain categories of 'territory' for:

- an inaccuracy in a return or document
- a failure to notify chargeability to tax
- the deliberate withholding of information where a tax return is > 12 months late

Offshore matter

An offshore matter is an inaccuracy, failure to notify or deliberate withholding of information that results in a potential loss of revenue or a liability that relates to:

- income arising from a source in a territory outside the United Kingdom (UK)
- assets situated or held in a territory outside the UK
- activities carried on wholly or mainly in a territory outside the UK

The penalty depends on territory

The penalty percentage range is determined by the place where the income or gains arose. For Inheritance Tax it is the place where the asset was located.

The places or territories are divided into 3 categories and can be viewed at www.gov.uk/guidance/penalties-an-overview-for-agents-and-advisers

Category 1:

- Have agreed to exchange information automatically with HMRC
- Maximum penalty is 100% of the tax

Category 2

- Territories that will exchange information with HMRC but only if prompted
- Maximum penalty is 150% of the tax

Category 3

- These territories have not agreed to share information with HMRC
- Maximum penalty is 200% of the tax

Offshore asset move penalties

Taxpayers may be liable to an offshore asset move penalty where:

1. an earlier penalty has been charged for a failure to comply with certain Income Tax, Capital Gains Tax or Inheritance Tax obligations; and

2. there is a related transfer of, or change in the ownership arrangements for, an asset situated or held in the UK

The offshore asset move penalty is 50% of the amount of the underlying penalty and is in addition to that penalty.

www.gov.uk/government/publications/compliance-checks-penalties-for-income-tax-and-capital-gains-tax-for-offshore-matters-ccfs17

Legitimate expectation and the jurisdiction of the First Tier Tribunal

Summary – The Upper tribunal found that the First Tier Tribunal did not have jurisdiction to consider the taxpayers' legitimate expectation that no penalty would be imposed.

Mr and Mrs Birkett are partners in a number of partnerships operating residential care homes. The partnerships made contributions to a trust as part of a scheme designed to reduce the taxable profits of the partnerships.

HMRC opened enquiries into the partnerships' returns and issued information notices under Schedule 36 FA 2008.

The taxpayers appealed but initially the First Tier Tribunal misplaced the appeal papers and HMRC were not notified of the appeal. HMRC issued daily penalties on the basis that no appeal had been lodged but refused to withdraw the penalties once informed of the appeal.

The partnerships appealed to the Upper Tribunal. Had the First Tier Tribunal erred in law when finding that it did not have jurisdiction to consider Mr and Mrs Birkett's legitimate expectation that no penalties would be imposed once they appealed?

Decision

The Upper Tribunal noted that the jurisdiction of the tribunal on an appeal under para 47(a) Schedule 36 FA 2008 is confined to deciding whether the statutory requirements under para 40 are met. This means that the First Tier Tribunal cannot review the decision of the HMRC officer on any other grounds. The First Tier Tribnal does not therefore have jurisdiction to review the decision on the grounds that it was unfair to issue the penalties because the appellants had a legitimate expectation.

The Upper Tribunal pointed out that, although the First Tier Tribunal does not have judicial review jurisdiction, it may consider questions of public law in the course of exercising the jurisdiction which it does have. Here, this meant that although the First tier Tribunal did not have a discretion when deciding whether a penalty should be imposed, it could substitute its own decision as to the correct amount

Finally, the Upper Tribunal found that there had been no infringement of the European Convention on Human Rights A1P1. There is no UK law provision for the suspension of daily penalties while the initial penalty is challenged by way of appeal. Furthermore, the failure to include such a provision is not 'burdensome, arbitrary, unfair or excessive'.

R & J Birkett trading as The Orchards Residential Home et al v HMRC [2017] UKUT 89

Adapted from Tax Journal (10 March 2017)

German sub-contractors a reasonable excuse?

Summary – The company had a reasonable excuse for their non filing of CIS returns for German sub-contractors.

Schotten & Hansen (UK) Limited (SH) supplies and fits wooden flooring bought from a German company that is owned and run by Mr Hansen's brother. Fitters are supplied by Roland Langenegger GmbH (RL) who travel to the UK with SH paying for the labour and separately paying for their travel costs and subsistence. SH had not operated the Construction Industry Scheme as they believed that as the work was performed by fitters supplied by a German company the scheme did not apply to them.

HMRC disagreed with that approach arguing that they were late filing their Returns and that they had no reasonable excuse. They argued that there is no provision in the CIS legislation to apply gross status retrospectively and they calculated that over the period, a total of £395,031.67 should have been deducted.

In May 2014 it was confirmed that SH had now registered as a Contractor for CIS purposes and that RL was in the process of registering as a sub-contractor. By notice dated 14 July 2014, HMRC issued confirmation that RL's sub-contractor's payment status was gross. SH argued that there had been no loss of revenue because RL had gross status and would have had gross status

It was agreed that although SH should have made deductions at the rate of 30% on payments made to RL totalling £395,031.67, HMRC were prepared to relieve SH of that liability but still sort penalties. SH argued that the penalties were neither reasonable nor proportionate not least because there never would have been a loss of revenue.

Decision

As Danish nationals who had moved to the UK, the Tribunal held that it was not unreasonable:

- For SH to assume that their accountants would have advise on any relevant compliance issues arising from the information provided to them,
- That SH was not aware of the filing obligations of the CIS, and
- That SH did not itself investigate the CIS or seek out CIS340.

In this particular combination of circumstances, the Tribunal found that SH had a reasonable excuse for the non-filing of the CIS Returns for which the penalties have been determined.

Schotten & Hansen (UK) Limited V HMRC (TC05679)

Defective closure notice but wrong route taken

The taxpayer was in dispute over two tax avoidance schemes. In February 2016, HMRC issued two closure notices under s28A TMA 1970 but these failed to set out the tax payable.

The taxpayer applied for judicial review on the ground that the closure notices had not amended his returns in line with s 28A(2)(b). He claimed that he owed no further tax.

The High Court judge said that s28A did require that a closure notice amended a taxpayer's return by stating the tax due. Section 114(1) could apply, but only if there had been an assessment. In this case, HMRC's statement that the taxpayer's return had been amended could not constitute an assessment within the opening words of s 114(1).

Unfortunately, the judge also said that the taxpayer should have appealed to the First-tier Tribunal against the conclusions in the notices under s 31(1)(b). It would have used s 114(1) to correct the defects in the notice.

The taxpayer's application for judicial review was an abuse of process and was therefore dismissed.

R (on the application of Archer) v CRC, Queen's Bench Division

Taken from Taxation (16 March 2017)

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Deadlines

1 April 2017

- Corporation tax rate falls to 19%
- New rules to remember:
    - BEPS project introduces limit on interest deductions for large groups
    - New losses carried forward to set against other income including groups
    - Only 50% of group profits sheltered by carry forward losses -£5m de minimis
    - Amended Substantial Shareholding Exemption rules

6 April 2017

- Personal allowance increased to £11,500 for 2017/18; CGT AEA remains at £11,100
- Don't forget the following are effective from 6 April 2017:
    - Apprenticeship levy
    - Voluntary payrolling of of non- cash vouchers and credit tokens
    - Most benefits under salary sacrifice schemes taxed as if cash (Cars , accommodation, school fees from 6 April 2021)
    - £500 employer provided pension advice
    - £1,000 trading and property income allowance
- ISA limit increased to £20,000 and NEW lifetime ISAs
- Cash basis threshold increased from £83,000 to £150,000
- Finance cost restrictions for residential landlords transition starts
- New deemed domicile rule for IT, CGT and IHT
- New IHT residence nil rate band

7 April 2017

- Electronic due date for VAT returns and payment for 28 February 2017 quarter

14 April 2017

- Due date for the quarterly corporation tax instalment for large companies depending on accounting year end.
- Forms CT61 must be submitted and paid for quarter ended 31 March 2017

19 April 2017

- Deadline for final 2016/17 payroll report using either FPS or EPS
- Due date of payment of PAYE, NIC, construction scheme industry and student loan liabilities for month ended 5 April 2017 if not paying electronically.
- File monthly construction industry scheme return by this date.
- Due date of payment of PAYE liability for quarter ended 5 April 2017 if average monthly liability is less than £1,500.

21 April 2017

- File online monthly EC sales list by this date.
- Submit supplementary Intrastat declarations for March 2017 by this date.

22 April 2017

- PAYE, NIC and student loan liabilities should have cleared HMRC's bank account

30 April 2017

- Companies House should have received accounts of private companies with 31 July 2016 year end and public limited companies with 31 October 2016 year end.
- HMRC should have received corporation tax self-assessment returns for companies with accounting periods ended 30 April 2016.
- ATED returns should be filed and paid for 2017/18 and amended for 2016/17

1 May 2017

- Due date for the payment of corporation tax liabilities for accounting periods ended 30 June 2016 for small and medium-sized companies not liable to pay by instalments.

5 May 2017

- Last day for 2017/18 tax credit claim to be backdated to 6 April 2017

HMRC News

Child trust funds annual subscription limits and removal of 'lifestyling'

Around 6 million children hold a Child Trust Fund (CTF) with around 4.7 million being stakeholder CTFs.

In the Autumn Statement 2016, the government announced that the CTF annual subscription would increase to £4,128 from 6 April 2017.

The CTF rules require account providers to adopt a 'lifestyling' investment strategy for stakeholder CTFs that aims to minimise the variation in capital value of the account caused by market conditions. Under the current CTF rules, the lifestyling process must have commenced before the stakeholder CTF holder reaches 15 years of age and continue until the account holder reaches 18 years of age, when their account matures. This requirement will be removed and may affect the investment strategy adopted and future returns for these accounts.

Other minor updates will also be made to the CTF regulations. Provisions within the CTF regulations relating to the transfer of accounts will also be updated to reduce the information that must be passed between account providers on the transfer of an account.

www.gov.uk/government/publications/child-trust-funds-lifestyling-of-accounts-annual-subscription-limits-and-other-updates

Off-payroll working in the public sector - contracts in scope

On 1 March 2017 HMRC published additional guidance on the scope of changes as they affect managed service companies and contracted-out services.

Where the rules apply, people who work in the public sector through an intermediary will pay employment taxes in a similar way to employees.

The new provisions apply when:

- the client is a public authority;
- a worker personally performs services, or is under obligation to personally perform services for the client and provides those services via an intermediary (usually their own personal service company) which can include an intermediary that is also a managed service company;
- the services are provided under circumstances where, if the contract had been directly with the client, the worker would be regarded for Income Tax purposes as an employee of the client or the holder of an office with the client, or the worker actually is an office holder with the client

Managed service companies (MSC)

With effect from 6 April 2017, where a company is a MSC and all the conditions above apply, the new rules will apply and not the MSC legislation.

Contracted-out services

The legislation also requires that workers provide their services personally to the public sector client. This condition is not met where the public authority has contracted out the service to a third party (for example an outsourcing company) in such a way that that entity does not as part of that provide the public sector with the services of the worker or workers.

Outside the scope

The intermediaries legislation is about situations where the worker provides their services to the client through their own company. This might be a PSC they own or control, a partnership or via another individual and includes those which are MSCs. It is not relevant to situations where an agency or consultancy sends their workers who are employed directly and PAYE and NIC deducted.

www.gov.uk/guidance/off-payroll-working-in-the-public-sector-scope-of-the-reform-and-preparing-for-6-april-2017

Additional guidance was also issued and is aimed mainly at agents who provide advice to contractors carrying out public sector work through a personal service company.

www.gov.uk/government/publications/off-payroll-working-in-the-public-sector-reform-of-the-intermediaries-legislation-technical-note

Employment Status Service tool launched

HMRC has launched its new online tool that can be used to check if the intermediaries legislation applies to a particular engagement in the private or public sector. This replaces the old employment status indicator tool.

Interested parties can use the Employment Status Service tool to obtain the HMRC view of whether any current and prospective workers would fall within the off-payroll rules from 6 April 2017.

The service is anonymous and will not store any information or the result given. You'll be able to print your result for your own records.

HMRC will stand by the result given unless:

- a compliance check finds the information provided is not accurate;
- contrived arrangements were designed to get a particular outcome from the service.

www.gov.uk/guidance/check-employment-status-for-tax

Pensions advice - draft updates to EIM guidance

HMRC has published draft updates to the Employment Income Manual for the new statutory exemption of £500 in a tax year for pensions advice provided to employees from April 2017.

www.gov.uk/government/publications/pensions-advice

Tackling disguised remuneration - draft EIM guidance updates

HMRC has published draft updates to the Employment Income Manual incorporating changes to the disguised remuneration rules introduced by Finance Act 2016 and proposed in Schedule 16 to Finance Bill 2017.

Note that this update does not cover the:

- new loan charge (Schedule 17 to Finance Bill 2017);
- extension to self-employed schemes (Schedule 18 to Finance Bill 2017); or
- restrictions on employer deductions (clauses 50 and 51 of Finance Bill 2017).

Guidance for these areas will follow later in 2017.

www.gov.uk/government/publications/tackling-disguised-remuneration-draft-guidance-for-changes-to-part-7a

Business Taxation

Class 4 NIC increase abandoned

On 15th March, the Prime Minister announced that the government will not proceed with the Class 4 NIC increase announced in the Spring Budget although it will look again at further proposals once Matthew Taylor has reported on his review of self-employment.

The Chancellor confirmed this in a letter to the House of Commons Treasury committee saying that:

> 'It is very important both to me and to the Prime Minister that we are compliant not just with the letter, but also the spirit of the commitments that were made'.

Under the 'tax lock' commitment contained in the National Insurance Contributions (Rate Ceilings) Act 2015, the government said that they would not to raise income tax, Class 1 NICs, or VAT during the current Parliament.

He said he had been persuaded to make the change 'in the light of what has emerged as a clear view among colleagues and a significant section of the public'.

Offset of trading losses against income

Summary – Loss relief was denied due to ineffective declaration of trust and property not being trading stock.

Father and son, Stephen and Lawrence Schechter, appealed against closure notices issued by HMRC following an enquiry into their 2008/09 self-assessment tax returns. As the circumstances and other issues in the cases were substantially the same, the appeals were heard together.

Both taxpayers are shareholders and directors of Vinexsa International Limited (Incorporated in the Bahamas) that owns:

- Two flats in London. Shortly after Stephen Schechter and his wife moved to the UK from the US, Vinexsa acquired a London flat for their use that was partly financed with a mortgage from Coutts. The leasehold title included a main flat (Flat 10) and a separate 'butler's apartment' (Flat B) which was used to store Stephen Schechter's work files. Stephen arranged for the titles to flat 10 and flat B to have separate leases granted for each unit. Flat B continued to be used to store his old files until 2002 from which date Vinexsa let flat B to Schechter & Co,.

- 100% of Sweet Revenge Limited that in turn owns a property in France. The property was bought with the intention of developing it and then selling it. However, once developed it was decided to keep the property to allow the grounds to mature and so fetch a higher price. The property was let to holiday makers.

To ensure that tax credits were available for US taxes suffered by Stephen and Lawrence Schechter, they were advised that both companies should hold their assets as nominees for the Vinexsa shareholders. Nominee agreements and a declaration of trust were effected, with the aim of transferring beneficial interest to the shareholders.

The taxpayers looked to claim relief for their property expenditure as losses set against other taxable income. However, HMRC denied the relief and the taxpayers appealed.

Decision

The Declaration of Trust and the Nominee Agreement were executed before the abolition of stamp duty and so both were liable to fixed stamp duty. The duty had not been paid, rendering them inadmissible as evidence. The appeal failed.

However, the judge continued to set out what the findings would have been had these instruments been stamped.

The judge said that he would have found that neither the Nominee Agreement nor the Declaration of Trust were effective in transferring beneficial ownership to the Vinexsa shareholders because:

- the bare trust in respect of the London flat was a sham and was never respected by Vinexsa or its shareholders; and

- for the French property, neither the Nominee Agreement nor the Declaration of Trust could extend to assets not owned by Vinexsa itself (such as assets owned by its subsidiary Sweet Revenge).

During the case management hearing it became apparent that the UK and French properties were treated as fixed assets in the respective financial statements of Vinexsa and Sweet Revenge.

- The judge later concluded that there was nothing to indicate that the London flat had been appropriated to trading stock at any stage.

- The judge was satisfied that the French property was originally bought as a development project with a view to realising a profit after the development was completed. However, Stephen Schechter said that there was no intention that Sweet Revenge would ever sell the French property. Instead, the intention was that Sweet Revenge would continue to own the property, and Vinexsa would sell the shares in that company to a purchaser. The judge concluded that the property was not held as trading stock.

The appeals were dismissed.

Stephen Schechter Lawrence Schechter v HMRC (TC 05677)

Film partnerships trading?

Summary - A scheme implemented by two film partnerships failed as they had not been trading.

By claiming 100% first year allowances on expenditure for the production and acquisition of a film, ss 130 – 144 ITOIA 2005 allow individuals who are resident but not domiciled in the UK, to generate income tax losses to set against their taxable income. Under s134, this treatment is only available to taxpayers carrying on a trade.

As part of a single transaction, two film partnerships:

- Acquired film rights in Oliver Twist, The Queen and Irina Palm;
- Agreed a 15 year leaseback in return for fixed, increasing, secured and guaranteed rental payments.

The issue was whether the partnerships were carrying on a trade. Both the First Tier and Upper Tribunals had found that no trade was established.

Decision

Following Eclipse [2015] EWCA Civ 95, whether or not an activity constitutes a trade 'depends upon an evaluation of all the facts relating to it against the background of the applicable legal principles'.

The Court of Appeal refused to consider the purchase and leaseback of the films in isolation as 'inherently trading activities' or to take into account the borrowings made and the losses incurred by the partners in their personal capacities.

The appeal was dismissed and their application for judicial review also failed as the guidance that they relied on did not apply in cases of suspected tax avoidance and HMRC had reasonable grounds to suspect tax avoidance.

Samarkand Film Partnership and others v HMRC [2017] EWCA Civ 77

Loan relationship scheme failed

Summary –The accounting treatment of the contingent asset debt claims in exchange for shares recorded at no value was GAAP compliant but, FA 1996 s 84(1) corrected the imbalance that arose.

GDF Suez Teesside (GST) had transferred Enron debt claims in excess of $1billion to a wholly owned Jersey subsidiary, Teesside Recoveries, in return for new shares. GST's accounts attributed no value to the debt claims as they represented contingent assets with 'considerable uncertainty over the timing and amounts of further distributions by Enron'. Hence the share consideration had no value on exchange. The intention was that the profit inherent in the transferred debt claims should never be taxed as the claims were not recognized in GST's accounts prior to the transfer.

The First-tier Tribunal found that this accounting treatment was correct under GAAP but also found that under FA 1996 s 84(1) GST must recognise a taxable profit for tax purposes, representing the value of the shares allotted to it in exchange for the assignment of the claims. GST argued that with nothing in the accounts, the First Tier Tribunal had 'invented' a non-existent credit to arrive at what it considered to be a 'fair' result.

The Upper Tribunal considered whether

1. the claims had been correctly accounted for under GAAP?

2. GST needed to recognize a taxable profit equal to the fair value of the transferred assets?

3. HMRC's closure notice for the period ended 5 December 2006 had any standing given that there was no valid enquiry into the corporation tax return for that period?

Decision

The Upper Tribunal concluded that:

1. The First Tier Tribunal was entitled to conclude that the taxpayer's financial statements complied with GAAP.

2. The First Tier Tribunal was correct in saying that GST needed to recognize a taxable profit to balance out the accounting treatment in both companies for tax.

   Teesside Recoveries had a positive balance sheet reflecting the fair value of the transferred claims now valued but GST's shareholding in Teesside Recoveries had no value in its financial statements. Such an adjustment reflected economic reality.

3. The taxpayer had argued that there was no valid closure notice for the enquiry, as the original enquiry letter had contained the wrong year end. After the initial error, subsequent correspondence from both HMRC and the taxpayer's advisers had used the correct year end, and the UT concluded that there was no arguable ambiguity about what was meant.

GDF Suez Teesside v HMRC [2017] UKUT 68

Loan relationship – unallowable purpose

Summary – A loan relationship scheme failed as a result of FA 1996 Schedule 9 paragraph 13 (unallowable purpose).

Travel Document Service (TDS) and Ladbroke Group International (LGI), members of the Ladbroke Group, implemented a tax avoidance scheme, notified under DOTAS, exploiting a perceived loophole in the taxation of loan relationships using a form of derivative contract known as 'total return swap'. It then depressed the value of the shares by novating a large loan liability into the subsidiary from another group company. By reducing the fair value of the shares in its subsidiary, the taxpayer intended to accrue a large loan relationship debit in the shareholding company.

The issue was whether Schedule 9 paragraph 13 FA 1996 was at that time, capable of applying to such a deemed loan relationship; and, if so, whether the taxpayer's purpose had been unallowable. S.91B FA 1996 provided for shares to be treated as rights under a creditor relationship in certain situations, with the result that the debits and credits to be brought into account in respect of them were determined on the basis of fair value accounting.

Decision

The Upper Tribunal found that there was no 'conceptual or practical difficulty' in identifying the subjective purpose of a party to a deemed loan relationship.

They also found that the fact that TDS had a valid commercial purpose in owning the shares before, during and after the swaps did not preclude a finding that, during the period of the swap, it had an additional purpose in owning them; namely, to obtain a tax advantage.

Travel Document Service and Ladbroke Group International v HMRC [2017] UKUT 45

Adapted from Tax Journal (3 March 2017)

Payments to EBTs

Summary – The First Tier Tribunal found that payments made to employee benefit trusts by three companies were not deductible for corporation tax.

The main question was whether the payments to the EBTs were made wholly and exclusively for the purposes of the companies' trades.

Referring to Scotts Atlantic Management [2015] UKUT 66 the First Tier Tribunal noted that:

- the test failed if any expenditure is incurred partly for a non trading purpose;
- to identify the purpose, the tribunal must look 'into the taxpayer's mind';
- what matters is the purpose of the payment rather than its effect or the wider arrangements.

The Tribunal found that the object of the payments was partly to provide the employee benefit trusts with funds that could be used by the directors to defer the PAYE and NIC costs that would arise on a payment of a cash bonus, while at the same time obtaining a corporation tax deduction for the payment, which would not have been available on a dividend payment.

Alway Sheet Metal and others v HMRC (TC 05686)

Adapted from Tax Journal (17 March 2017)

VAT

Updated VAT Notice 733: Flat Rate Scheme for Small Businesses

HMRC have issued the final Notice 733 in anticipation of the new Limited Cost Trader rate effective from 1 April 2017. The new category has a 16.5% rate, which means there is virtually no credit for input tax. Consequently, the VAT payable by traders will increase for those traders who buy less than £250 of relevant goods in a VAT quarter or spend less than 2% of their total VAT inclusive turnover for the quarter on relevant goods.

Relevant goods and specific exclusions

These are goods that are used exclusively for the purposes of the taxpayer's business.

One of the latest changes to the VAT Notice is that there is an addition to the exclusions for relevant goods for goods for resale where the goods do not relate to the main business activity. This effectively blocks the planning measure that has been suggested of introducing a secondary activity selling goods.

The full list of exclusions included in the Notice is:

- vehicle costs including fuel, unless you're operating in the transport sector using your own, or a leased vehicle;
- food or drink for you or your staff;
- capital expenditure goods of any value;
- goods for resale, leasing, letting or hiring out if your main business activity doesn't ordinarily consist of selling, leasing, letting or hiring out such goods;
- goods that you intend to re-sell or hire out, unless selling or hiring is your main business activity;
- any services.

Supplies that aren't relevant goods

HMRC do not consider the following to be relevant goods:

- accountancy fees (Services);
- advertising costs (Services);
- an item leased/hired to your business (Services as ownership will never transfer);
- food and drink for you or your staff (Excluded goods);
- fuel for a car this is excluded unless operating in the transport sector using your own, or a leased vehicle;
- laptop or mobile phone for use by the business (Capital expenditure);
- anything provided electronically, eg a downloaded magazine (Services);
- rent (Services);
- software you download (Services);
- software designed specifically for you (bespoke software), (Service even if it is not supplied electronically.

Were supplies of insurance separate from the main supply?

Summary – The taxpayer made a separate exempt supply of insurance and so the Upper Tribunal dismissed HMRC's appeal.

Wheels Private Hire Ltd (Wheels) operates a taxi business. Where drivers do not have their own car, they can rent vehicles and radios for £120 per week from Wheels.

In addition, there was the option for drivers to buy their car insurance through Wheels via their fleet contract with a third party insurance company. Alternatively they could arrange their own cover. Most drivers took up Wheels insurance.

Wheels charged standard rated VAT for the car hire but argued that the insurance was a separate, exempt supply (VATA 1994 Sch 9 Group 2).

Decision

Relying on the BGZ Leasing Court of Justice of the European Union case, which was not considered at the First-tier Tribunal, the Upper Tribunal dismissed HMRC's appeal. They rejected the argument that Wheels could not make exempt supplies of insurance, concluding that the optional charge for insurance was a separate supply of insurance.

HMRC v Wheels Private Hire [2017] UKUT 51

Transfer of land in lieu of payment of tax

Summary - A transfer of land in lieu of payment of tax arrears is not subject to VAT

A Polish company traded in real estate. As permitted under Polish law, the company had transferred a plot of land to the State to settle arrears of tax.

Was this land transfer subject to VAT?

Decision

The Advocate General said that the payment of tax is the discharge of a personal, legal duty with the transfer of land simply representing the form that the tax payment is made.

Transferring property to pay tax was not an economic activity carried out by a taxable person. The Advocate General considered that when paying tax debts, the plot transferred had been valued according to objective criteria and no competition arose.

The transfer of land could not be subject to VAT.

Minister Finansów v Posnania Investment SA (Case C-36/16)

VAT treatment of e-books

The EU VAT Directive provides that Member States may apply a reduced VAT rate to the 'supply of books on all physical means of support' but this does not include e-books, as electronically-supplied services are specifically excluded. E-books are therefore standard rated.

Is it right that books supplied on paper, or audiobooks supplied on CD or USB sticks may be subject to the reduced rate while e-books are standard rated?

In the Polish case of Rzecznik Praw Obywatelskich*, the* CJEU concluded that the different VAT treatment between e-books and physical books was allowed as the EU legislation must have considered it necessary to make electronic services subject to simple and uniform rules so that the VAT rate applicable to them be established with certainty.

The appeal succeeded and the penalties were set aside.

Landlord repaying rent under a deal with liquidator

Summary - Landlord repaying rent to a wholly owned company under a deal with liquidator was an agreed reduction in rent

Mr Brady owned a property that was let to Allito Color Group Ltd, a company connected to and controlled by him. Having opted to tax the property, he charged and accounted for standard rated VAT on the rent of £20,000 a month.

In February 2011 an administrator was appointed to the company and then later, in April 2012, a liquidator was appointed because the company was insolvent.

Four years later in February 2015 Mr Brady repaid £300,000 to the company through the liquidator and issued a credit note to the company. He claimed that the amount repaid was rent.

Mr Brady claimed the VAT back on the credit note from HMRC but HMRC refused the claim so Mr Brady then claimed bad debt relief for the VAT that HMRC also refused.

The taxpayer appealed saying that either:

- the credit note discharged the company's liability to pay the rent; or
- If the First-tier Tribunal disagreed on this point, his alternative argument was that he had not been paid the outstanding rent and was entitled to bad debt relief.

HMRC contended that the £300,000 payment was to the liquidator to settle a claim and was outside the scope of VAT.

Decision

The tribunal decided that the £300,000 was a repayment of the rent that had been invoiced and that it had not been made in consideration of an agreement not to litigate.

The taxpayer was therefore entitled to a repayment of VAT on the credit note.

As a result, there was no need to consider the bad debt relief claim but the judge concluded the debt would have been bad.

The taxpayer's appeal was allowed.

Terence Patrick Brady v HMRC (TC05622)

VAT saving tips for charities (Lecture B1010 – 15.13 minutes)

Background

One of the most common VAT questions asked by clients is as follows: we are doing some work or selling goods to a charity and the charity has told us not to charge VAT because charities are exempt from paying the tax (the finance officer or treasurer of the charity will often be waving a charity number around with great enthusiasm). Unfortunately, such claims of universal VAT exemption are wildly inaccurate.

The challenge for advisers is to be aware of the concessions available to charities in the VAT legislation, which means that some goods and services they pay for are not subject to VAT or subject to the lower rate of 5% in some cases. These concessions are very worthwhile and I will share some of them in this presentation.

Rental charges

On the basis that rent and wages are often the two main overheads of many charities, let us start with the issue of rent, and the potential to override an option to tax election made by a landlord.

The starting point is that a landlord who has made an option to tax election on a building must charge 20% VAT on all income earned from the building, unless it relates to residential property. So a landlord who has opted to tax a building consisting of a ground floor shop and a first floor flat will charge VAT to the tenant in the shop but not to the tenant in the flat – the latter income is still exempt from VAT. This means that despite his option to tax election, the landlord is still partly exempt as far as this building is concerned.

So what is the position as far as charities are concerned and an override of the landlord's election?

The charity must be using the building (or part of the building if there are clearly defined areas) for a 'relevant charitable purpose' other than as an office for general administration purposes.

The charity does not need to complete a certificate but the landlord should ask the charity to certify its use of the building in writing and the letter should be signed by a senior officer of the charity eg CEO, Trustee etc.

If a building is partly used for charitable purposes (ie the good causes of the charity for which it was established) and partly for business purposes (eg a charity shop) and the different areas are clearly defined, then the landlord should apportion the rent in a fair and reasonable manner .

Example 1

Manchester Homeless Charity rents a building from John for £6,000 per month excluding VAT. John has made an option to tax election on the building so wants to add £1,200 VAT to each monthly payment. The charity uses the building as follows:

- The ground floor is used as a shop to raise funds for the charity by selling donated goods.

- The first floor is used to give free meals, washing facilities and general care for homeless people.

- The second floor is used as the general office of the charity to deal with payroll, IT and staffing administration.

The rent relevant to the first floor will be exempt from VAT, despite the option to tax election. An easy calculation would be to only charge VAT on 2/3 of the rent ie based on a simple square footage split of two floors being taxable and one being exempt.

Reference: HMRC Notice 742A, para 3.5.

Advertising costs

Let us stick with Manchester Homeless Charity from the previous example. The trustees have decided to launch an advertising campaign to encourage donations from the general public and also seek more donated goods for its shop. What is the situation with the VAT charged on the cost of the advert by, say, a newspaper, radio station or website?

There is a specific HMRC notice on this subject – Notice 701/58. The relevant legislation for the zero-rating of charity advertising is VATA1994, Sch 8, Group 15, Item 8.

A supply of advertising to a charity registered with The Charity Commission (or to a charity which is not registered with the Commission but is recognised for its charitable aims by HMRC) is zero-rated. This includes the advertising charge relevant to the business activities of the charity ie the shop in my example.

Many charities carry out their business activities under a separate trading company, which is not a registered charity, even though it will be owned by the charity and usually gifts all of its profits back to the charity. These companies must pay VAT on their advertising costs because they are not a charity. Doesn't life get complicated?

One of the conditions of zero-rating is that the advert in question must 'communicate with the public' (see paras 3.1 and 3.2 of Notice 701/58).

The zero-rating extends to the costs of designing an advert.

Note – for more analysis about the question: "What is a charity?" - see para 2.2 of HMRC Notice 701/58.

Website costs and advertising agencies

I had a call from an accountant about a year ago whose client was a website designer. The client was told by a charity that work he had carried out designing its website should be zero-rated as the website was partly used by the charity for advertising purposes. This is incorrect. However, if the designer was actually designing a specific advert for use by a charity on a third party's website (the charity buying advertising space), then this supply would be zero-rated as linked to the advert (VAT Notice 701/58, para 3.7).

Another query I had concerned an advertising agent, who earned a commission from a charity for arranging adverts in various publications designed to maximise exposure to promote its good causes. The charity told the agent not to charge VAT on his commission (surprise, surprise) because it related to a supply of advertising.

This claim would have been correct if the agent was acting as a principal and buying and selling advertising space but not if he is acting as agent and earning a fee for his services.

Zero-rating construction/purchase of new building used for relevant charitable purpose

If a new building is purchased by a charity (or builders supply construction services to the charity because it is acting as the developer itself) then zero-rating will apply if the new building will be used wholly for a relevant charitable purpose (Notice 708, sections 3 and 4).

The issue about what is business and charitable use can often be a difficult challenge. For example, charity shops are obviously involved in business activities and a building that is only used by a religious organisation as a place of worship will obviously be wholly used for non-business purposes. But the waters get cloudy when eg sub-letting and coffee shops become part of the equation. And to add a further twist, the charity can still certify that a building is wholly charitable (a certificate needs to be issued by the charity in both situations above to secure zero-rating) as long as at least 95% of use is charitable ie there is scope for a small amount of non-charitable activity in the building eg from perhaps a very small coffee shop area (HMRC Notice 708, para 17.11).

Note - the 5% or less non-charitable use requirement is subject to a self-supply charge if it is exceeded in the 10 year period following the completion of the building (HMRC Notice 708, section 19)

Fuel and power

Supplies of gas and electricity to a charity for non-business purposes will be subject to 5% VAT when charged by the fuel supplier. But what happens if a building is partly used for charitable purposes and partly for business purposes, such as the building used by Manchester Homeless Charity considered above?

The charity must certify to the fuel supplier the proportion of the building that qualifies for the reduced VAT charge ie based on its non-business use.

If the qualifying part of the building exceeds 60% of the total building use, then the entire supply of fuel and power will be subject to 5% VAT - a very good result.

Reference: HMRC Notice 701/19, section 3.

Four year adjustment period for errors

You might have discovered that some of your charity clients have been overcharged VAT in some cases. The challenge in such cases is to go back to the supplier and ask for a VAT credit for supplies made to the charity in the last four years ie the error correction period we have in the world of VAT. The supplier will not be out of pocket because he will reduce the output tax on his next VAT return.

Contributed by Neil Warren