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Personal tax

Termination, not discrimination (Lecture P1426 – 13.10 minutes)

Summary – The £6 million received by the taxpayer from her former employer in settlement of Employment Tribunal proceedings was received indirectly in consequence of or otherwise in connection with the termination of employment, meaning it was taxable employment income. It was not a settlement payment relating to her discrimination claims.

In April 2015, following investigations into the manipulation of interbank offered rates, Deutsche Bank AG agreed a settlement with the New York State Department of Financial Services. Under that settlement, the bank was required to pay a $600 million penalty and terminate the employment of seven key, senior employees.

Shivani Mathur was one of the employees whose employment contract was terminated. She rejected the £82,135 termination payment offered, choosing to take her case to the Employment Tribunal, where she alleged harassment, discrimination and victimisation while employed by the bank.

Prior to the full hearing, Shivani Mathur accepted a settlement of £6 million. The bank treated this as a termination payment, with all but £30,000 treated as taxable under PAYE, resulting in tax deducted of £2,677,460.

Shivani Mathur argued that the sum was not taxable as the payment was not connected to the termination of her employment. Instead, it arose as a result of her alleged complaints regarding the harassment, discrimination and victimisation she had experienced while employed, as well as the bank's desire to prevent her claims becoming public.

The First Tier Tribunal had dismissed her appeal, finding that the £6million payment was received indirectly in consequence of, or otherwise in connection with, the termination of her employment.

Shivani Mathur appealed to the Upper Tribunal.

Decision

S.401(1)(a) ITEPA 2003 states:

> "This Chapter applies to payments and other benefits which are received directly or indirectly in consideration or in consequence of, or otherwise in connection with—the termination of a person's employment."

Such termination payments are treated as employment income, and the first £30,000 of such income can be received tax-free.

The Upper Tribunal found that the words 'otherwise in connection with' permitted a wide interpretation of whether there was a link between the payment and termination.

The Upper Tribunal found that there was a 'clear and obvious' connection between the termination and the payment, meaning that the First Tier Tribunal was entitled to conclude that the £6 million paid was in connection with the termination of her employment and so taxable under s.401 ITEPA 2003. The termination was the trigger for the claim, and also the reason that she was able to negotiate such a large sum. Indeed, the settlement agreement referred to termination payments, and made reference to the £30,000 tax-free sum.

The First Tier Tribunal had not erred in law, as the termination was key to the claim.

> "Consequently, the Upper Tribunal stated that the First Tier Tribunal "was entitled to conclude that the Settlement Sum was paid, at least, "in connection" with the termination of the Appellant's employment".

The employer had correctly deducted tax from the full sum, with the exception of the:

- £30,000 termination exemption;
- £40,000 agreed between the parties for injury to feelings; and
- £400,000 legal costs paid on her behalf.

Finally, the Upper Tribunal found that "the appellant produced no persuasive evidence or arguments to support any other" apportionment of the sum received.

The appeal was dismissed.

Shivani Mathur v HMRC [2024] UKUT 00038 (TCC)

Footballer's agent fees (Lecture P1426 – 13.10 minutes)

Summary – Agent fees incurred while negotiating a transfer between football clubs were not deductible against employment income.

Baye Niasse is a professional footballer who has played for several clubs both in the UK and elsewhere.

On 1 February 2016, he joined Everton, with his agent having negotiated his transfer from FC Lokomotiv Moscow.

Under a tripartite agreement between Baye Niasse, his agent and his new club, Everton agreed to pay certain sums to his agent to discharge Baye Niasse's liability to pay fees to his agent under a Representation Contract that existed between the footballer and his agent.

The first of the payments to his agent by Everton, on behalf of Baye Niasse, was made on 1 February 2016. Further payments were made in accordance with the terms of the Tripartite Contract.

HMRC enquired into the tax returns for 2015/16 and 2016/17, later issuing closure notices, amending the returns and raising assessments on Baye Niasse for £76,410 (2015/16) and £76,463 (2016/17). A closure notice was also issued in respect of the tax year 2017/18, but it is not in issue in this case.

Baye Niasse accepted that the payments made by Everton to his agent on his behalf were either taxable as employment income (s.62 ITEPA 2003) or as an employment-related benefit (s.201 ITEPA 2003).

The issue in this case was whether the payments were deductible from employment income (s.336 or s.352 ITEPA 2003).

Decision

The First Tier Tribunal found that, under the terms of his employment, there was neither an express nor implied obligation to appoint an agent. The agent's services enabled the player to take up his position at Everton; they were not required in the performance of his duties. Baye Niasse was not obliged to incur these fees and further, they were not incurred necessarily in the performance of the duties.

Moving on to s.352 ITEPA 2003 (deductibility of agent's fees as an entertainer), Baye Niasse had argued that he was a 'theatrical artist' and an 'entertainer'. Unsurprisingly, the First tier Tribunal rejected this argument, finding that professional footballers do not perform with the 'theatrical bent' required. Further, to qualify for relief in this way, the fee must be calculated as a percentage of the earnings from the employment, which it was not.

The appeal was dismissed.

Baye Oumar Niasse v HMRC (TC09093)

Reporting requirements for salary advances

The Income Tax (Pay As You Earn) (Amendment) Regulations, SI 2024/305, simplify the reporting process for employers in respect of a salary advance made to an employee.

From 6 April 2024, salary advances can be reported on or before the employee's contractual pay day, thus avoiding having to report the advance and the regular salary payment separately. In essence, the reporting of the advance will be delayed until the remainder of the salary instalment is paid.

Following consultation on a draft version of the regulations, HMRC have amended the rules to make sure that the change only applies to advances of pay already earned by the time the advance payment is made.

The Social Security (Contributions) (Amendment No. 3) Regulations, SI 2024/306, provide equivalent provisions for NICs purposes.

Adapted from the article in Tax Journal (15 March 2024)

Marketed tax avoidance scheme failed

Summary – A marketed tax avoidance scheme designed to enable the owners of a company to extract funds from the company without incurring a charge to income tax failed.

Sharon Clipperton and Steven Lloyd took part in a scheme whereby they set up Winn & Co. (Yorkshire) Ltd, which would pay them, as sole shareholders, distributions without attracting the income tax charge usually applicable to dividends.

This entailed the creation of a subsidiary, Winn & Co. Scarborough Ltd in which Winn & Co. (Yorkshire) Ltd subscribed for 199 A shares and one B share. The latter was settled on trust for the benefit of the taxpayers on the basis that Winn & Co. (Yorkshire) Ltd was entitled to receive a small amount of any income arising and the trust property was to revert to it.

Sharon Clipperton and Steven Lloyd argued the dividend should be treated as the income of Winn & Co. (Yorkshire) Ltd as settlor.

HMRC disagreed, saying the case involved a series of pre-ordained transactions designed to deliver, in effect, a distribution to the shareholders of Winn & Co. (Yorkshire) Ltd in a tax-free form.

The First Tier and the Upper Tribunal dismissed the taxpayers' appeal and the matter progressed to the Court of Appeal.

Decision

The Court of Appeal considered that both tribunals had been correct to apply the *Ramsay* approach to decide that there was a distribution by Winn & Co. (Yorkshire) Ltd to the taxpayers. Indeed, the judge said 'the present case would seem a paradigm case' for its application.

He said he could see no reason to think that Parliament intended the words 'any other distribution … in respect of shares in the company' to charge only a distribution by a company directly to its shareholders and not a distribution intended to reach its shareholders by a more circuitous route using steps that had no business purpose and whose sole aim was the avoidance of tax.

The distribution by Winn & Co. (Yorkshire) Ltd was designed to, and did, reach the taxpayers.

On the relevance of *Khan v CRC* [2021] STC 954, which also involved a distribution, the judge said this concerned a different question and so was not relevant here.

The taxpayers suggested that the settlements legislation applied to the distribution by WS with the effect that it be treated as the income of Winn & Co. (Yorkshire) Ltd alone.

Again, the court disagreed, saying the WS dividend had 'no separate existence for tax purposes'. It should not be viewed in isolation, but rather as part of the means that the Winn & Co. (Yorkshire) Ltd distribution reached the taxpayers.

The appeal was dismissed.

Sharon Clipperton and Steven Lloyd v CRC [2024] EWCA Civ 180

Adapted from the case summary in Taxation (14 March 2024)

Capital taxes

PPR Relief topical issues (Lecture P1429 – 19.45 minutes)

Recent developments concerning public figures tax affairs and, in particular, questions regarding whether CGT is due on the sale of their property come up fairly regularly. This came up during the expenses scandal in 2009 and it is making the papers once again.

Although PPR has been a feature of UK tax legislation for at least six decades, the subjective nature of the qualifications for, in particular, what constitutes a period of ownership and also what constitutes residence, comes up almost every month in tax cases. There are also issues regarding the extent of qualifying grounds (minimum half a hectare), this element is beyond the scope of this article.

The main provisions of PPR are found in section 222 TCGA 1992 and have changed relatively little since the inception of the relief in the 1960s. What has changed is the volatility of the property market which has meant that relatively short periods of ownership can result in substantial gains. The other element of change is the relative fluidity of relationships which create additional challenges in this area.

The main rule is that one can only have one PPR. This is the place that one occupies as an only or main residence, if one occupies two properties as a residence, say one at the weekend and one during the week, one has the ability to chose which one counts as the PPR.

It is not necessarily the property which has shown the greatest gain which one would elect for. The first and most important question is which property one is more likely to sell. To take this principle further; PPR is wasted if one dies in one's main residence as the uplift to probate value would extinguish the capital gain (although their may be some IHT consequences).

The other element to note is that a married couple can only have one PPR between them. This also applied to couples in civil partnerships but not to unmarried couples. So, before the wedding/civil partnership ceremony, couples should discuss that if they are going to retain two properties and use both as their residences, which one it would be beneficial to designate as their PPR. An election should therefore be made to HMRC. If an election is not made, then one looks at which residence one preponderately live at. This includes factors such as both the quantity and quality of residence.

When a couple separate, then they are once again able to have two principal residences on that basis. Although in the Oliver case, the courts looked very suspiciously at a couple who separated and reunited within days of the second property being resold.

It is possible to have periods of absence, and claim it as deemed occupation. This includes potentially the first two years after the property is bought to cover difficulties with selling old property and extended building works.

It is also possible a three-year period of absence for any reason if there is real occupation before and after the deemed occupation. It is also possible to have employment related absences of up to 4 years if transferred elsewhere in the UK and indefinite when transferred abroad. In these cases, if it is impractical to reoccupy the property then that clause can be relaxed. In addition, the self-employed are able to claim up to 4 years deemed occupation if their self-employment takes them elsewhere.

There have been a number of changes to PPR, notably the final period of deemed occupation which is allowed if the property has at any time been your only or main residence has been reduced from 36 months to 9 months. 36 months is still allowed when the taxpayer is entering a care home.

PPR remains the second most expensive tax relief that HMRC gives after pensions. So, there have always been significant issues surrounding PPR. There issues may get greater as the CGT annual exemption has reduced from £12,300 in 2022/23 to £3,000 in 2024/25. The courts have provided substantial guidance in this area so has HMRC and it is worth both taxpayers and their advisers refreshing their knowledge before disposing of properties.

Contributed by Jeremy Mindell

Reversed property transfer **(Lecture P1426 – 13.10 minutes)**

Summary - There was a disposal of properties deemed to take place at market value, resulting in CGT becoming payable. The transfers could not be treated as if they had never taken place, simply because the transfer was reversed.

On 15 November 2016, Arshad Mahmood transferred ten commercial properties to Rajay Khan Properties Limited, a company owned by his wife, with him as sole director.

Despite there being no written agreement, it was understood that the properties would be transferred at cost for £300,000. This sum would be left outstanding as a debt due from the company to Arshad Mahmood.

On the basis that the properties were transferred at cost and that the spouse exemption was available, Arhsad Mahmood did not report this on his tax return.

Following an enquiry, HMRC concluded that with the property transferred to a connected person, the disposals were deemed to take place at market value. Consequently, HMRC sought to collect £303,476 of Capital Gains Tax and charged a penalty of £81,938.52 for providing an inaccurate tax return.

In early 2019, before the assessment had been raised, Arhsad Mahmood and the company agreed to “rescind" the property deals by transferring them back into Arhsad Mahmood’s name.

Arhsad Mahmood appealed, claiming that by rescinding the transfer of the properties, no taxable disposal has taken place.

Decision

Under contract law, parties can opt to reverse a transaction as long as both parties are in agreement, which is what happened here.

However, it does not follow that the original transfer of properties can then be treated as if it had never taken place.

The First Tier Tribunal believed that Arshad Mahmood was confusing two separate principles:

1. A transaction may be void "if it is entered into on the basis of a mistaken legal assumption, but only where the mistake affects the subject matter or the performance of the transaction and is sufficiently fundamental".

   However, the Tribunal concluded that the transaction was not void as the liability to CGT had no effect on:

   - the terms or the subject matter of the transfer, which was the transfer of the properties in return for a consideration of £300,000 to be left outstanding as a debt due from the company to Mr Mahmood;

   - the way in which the transaction was to be performed, which was the transfer of legal title from Arshad Mahmood to the company using standard land registry transfer forms.

2. The parties to a transaction may agree to rescind a transaction for any reason but only if it has only been partially executed so that one or both parties still have outstanding obligations to perform. Rescission effectively cancels any further obligations which have yet to be performed.

   Here, the transaction was fully executed as the properties had been transferred to the company, registered in its name at the Land Registry and the debt of £300,000 representing the consideration for the transfer of the properties had been recorded in the company's books. Rescission was not possible. Even if rescission was possible, it would not have meant that the transfer of the properties could be ignored.

There was therefore a disposal of the properties by Arshad Mahmood that gave rise to a liability to capital gains tax.

Arshad Mahmood v HMRC (TC09056)

Investing or dealing in land **(Lecture P1426 – 13.10 minutes)**

Summary – Distributions received by shareholders during a company's liquidation did not qualify for entrepreneurs' relief as the company had never traded.

Mark Stolkin, Margeaux Stolkin and Faye Clements were shareholders in Stolkin Greenford Limited.

The company acquired the former head-quarters site of GlaxoSmithKline in Greenford, referred to as the "GSK Land". For planning purposes, the GSK Land had an allocation as Strategic Industrial Land protecting it for employment uses.

Stolkin Greenford Limited originally held the GSK Land as an investment but later, with the protection order lifted, the site became a mixed-use development and on 3 December 2013, the company appropriated it to trading stock.

On 24 November 2014, The London Borough of Ealing granted planning permission for the redevelopment of the Site which included the "provision of up to 593 homes, an extension and conversion of the Glaxo House from office to residential use, the provision of retail, restaurant and community space and a cinema".

In September 2015, having received a third-party offer, the property was sold in January 2016.

Two months later, Stolkin Greenford Limited went into members' voluntary liquidation. At this time, Mark Stolkin, Margeaux Stolkin and Faye Clements were shareholders and directors. There were no other employees.

The individuals received distributions and, believing that the company had started trading from December 2013 when the property had been transferred into trading stock, claimed entrepreneurs' relief.

HMRC disagreed and denied the claim.

The taxpayers appealed.

Decision

The First Tier Tribunal stated that dealing in land can be a trade, but equally land may be acquired, held and disposed of as an investment. Whether the activity amounted to trading involved a multi factorial evaluation. The Tribunal looked at the Badges of Trade but then also stood back to "look at the whole picture".

The Tribunal found that the company:

- owned just one valuable asset, initially as an investment. Merely deciding to sell an asset after five years did not convert a fixed asset into trading stock;
- sought planning applications for a large residential development so that the land could be sold with that development potential;
- had neither the funds nor expertise to perform the development work needed, which was to be undertaken by a third-party purchaser.

The First Tier Tribunal found that Stolkin Greenford Limited was not a trading company. Having agreed a development plan to enhance the land's value, the company had simply decided to sell the property.

The appeals were dismissed.

Mark Stolkin, Margeaux Stolkin and Faye Clements v HMRC (TC09086)

IHT and the 14-year rule **(Lecture P1430 – 19.21 minutes)**

With all the talk in recent months about the possible abolition of IHT (mainly orchestrated by the press), there is one principle of the tax which flies largely under the radar and which is, in consequence, not widely appreciated.

Most of us are familiar with the seven-year rule in relation to lifetime gifts and IHT planning, but that part of the legislation does not tell the whole story.

It is crucially important for tax advisers and financial planners to understand the significance of what is sometimes termed ‘the 14-year rule’.

Gifts made more than seven years before the donor’s death have always been exempt from IHT (S3A(4) IHTA 1984).

However, the impact of the 14-year rule is that gifts which were made more than seven years before the donor’s death and therefore fall outside the deceased’s IHT computation can affect the amount of tax payable on later gifts which are still within the seven-year window.

The importance of this facet of the IHT code was neatly summarised by these words from a financial planning commentator:

> ‘For advisers, understanding how the 14-year rule works will help clients with the timing and value of gifts to achieve better IHT outcomes. In some cases, it could mean that clients may . . . wish to cap the amount they gift or defer gifting until a later date. But, in others, there may be scope safely to make larger gifts.’

Efficient lifetime giving is a core element of IHT planning. Unfortunately, when tax advisers recommend making lifetime gifts, they are often not faced with a clean slate when it comes to the gifting record.

When giving consists of only making chargeable lifetime transfers into discretionary or life interest trusts, most taxpayers will want to keep the seven-year cumulative total of their chargeable lifetime transfers below the nil rate band (currently £325,000). If they exceed this figure, there will be an immediate IHT charge of 20% on the excess.

Where clients wish to be more generous than this, they may consider making outright gifts which qualify as potentially exempt transfers (PETs). As mentioned above, PETs never attract an IHT charge during the donor’s lifetime and will be exempt once he has survived the requisite seven years. Of course, if the donor dies within seven years of making the gift, the PET becomes a chargeable transfer and this will usually impact on the amount of IHT which may then be payable. But how is this to be calculated?

In order to answer this question, it is necessary to determine how IHT is computed following a death. There are in fact two computations, one for the tax on the estate itself and the other for the tax on gifts which fall within the last seven years of the donor’s life.

Broadly speaking, the tax on the deceased’s estate is based on the IHT value of the estate less any available nil rate band. This latter figure will include:

(i) the deceased’s residence nil rate band (if available);

(ii) any transferable nil rate band from a pre-deceased spouse or civil partner; and

(iii) any transferable residence nil rate band from a pre-deceased spouse or civil partner.

The available nil rate band is reduced by all the chargeable transfers (including failed PETs) which were made in the seven years before death. Any gifts which pre-date this seven-year period are ignored for this purpose – the 14-year rule has no relevance here.

In this context, it is important to remember that the chargeable lifetime transfers and failed PETs from the last seven years **never** reduce the residence nil rate band (including any transferable residence nil rate band).

It is also necessary to look at each lifetime transfer in strict chronological sequence, going back over the seven years before death. This includes PETs which have now become chargeable. HMRC are seeking to assess the tax which would have been due at the time when they were made (but using current rates). This will in turn pick up chargeable transfers in the seven years prior to the gift in question which of course means that chargeable transfers made up to 14 years before the taxpayer's death can determine the IHT payable.

That, in a nutshell, is the 14-year rule. The IHT position is illustrated in the mini-case study below.

Illustration

Edward, a widower, is the father of Poppy and Hector. He is also the grandfather of five grandchildren. Edward's wife utilised her nil rate band and her residence nil rate band in full when she died.

Edward's gifting history is as follows:

Year 1	£300,000 to a discretionary trust for the grandchildren
Year 4	£100,000 gift to Poppy
Year 7	£50,000 gift to Hector
Year 9	£75,000 to a discretionary trust for the grandchildren

Year 13 Edward dies, leaving an estate of £800,000 (including a family home value at £420,000) – his whole estate is split between his two children, Poppy and Hector.

Let it be assumed that the lifetime gifts and Edward's death occur on the same date in the relevant calendar year and that Edward's annual IHT allowance of £3,000 has been fully utilised.

Start with the calculation of the IHT on Edward's death estate.

The transfers in Year 7 (failed PET of £50,000 to Hector) and Year 9 (chargeable lifetime transfer of £75,000 to the grandchildren's discretionary trust)) have to be included as part of the IHT computation on Edward's death.

This uses up £50,000 + £75,000 = £125,000 of Edward's nil rate band, leaving an available amount of £325,000 – £125,000 = £200,000.

Edward's lifetime transfers do **not** reduce his residence nil rate band.

His available nil rate band is £200,000 and his residence nil rate band (given that his residence passes to his two children) is £175,000.

As a result, the IHT on Edward's death estate is based on £800,000 – £200,000 – £175,000 = £425,000, i.e. 40% x £425,000 = £170,000.

We then have to calculate the IHT on the lifetime transfers made in the seven years before Edward's death.

The PET of £50,000 to Hector in Year 7 has become chargeable. It is necessary to include any chargeable transfers occurring in the seven years prior to this gift in order to calculate the IHT due. This will include the chargeable lifetime transfer of £300,000 made to the grandchildren's discretionary trust in Year 1, but not the gift of £100,000 to Poppy in Year 4 (given that this has become exempt because it was made more than seven years before Edward's death).

Because the £300,000 + £50,000 = £350,000 exceeds the current nil rate band by £25,000, this means that there will be an IHT liability of 40% x £25,000 = £10,000. However, this sum will be further reduced by IHT taper relief of 60% since Edward died exactly six years after the date of the gift to Hector, leaving a tax bill of £4,000 for Hector to pay.

Next it is necessary to assess the chargeable lifetime transfer of £75,000 in Year 9. Looking back over the previous seven years, we only need to include the failed Year 7 PET to Hector. The PET to Poppy in Year 4 is exempt and the Year 1 chargeable lifetime transfer to the grandchildren's discretionary trust was made more than seven years previously. The total of the two chargeable transfers is £50,000 + £75,000 = £125,000, i.e. well under the nil rate band of £325,000. Therefore, the trustees of the Year 9 discretionary trust transfer have no tax to pay.

As mentioned in above, the transfers made in Year 4 and Year 1 do not need to be revisited in view of the fact that they were made more than seven years before Edward's death.

The IHT payable on Edward's lifetime gifts – following his death – is £4,000.

If the gift to Hector in Year 7 had been limited to £25,000, there would have been no tax on this transfer, but there would then have been an extra £25,000 in Edward's estate. Ignoring any capital growth, this would have resulted in an additional tax liability of £10,000.

However, if the gift to Hector had been delayed by one year, this transaction would have avoided tax altogether by ensuring that there was a gap of seven years between the date of the gift to Hector and the original gift of £300,000 into the discretionary trust. Of course, this must be balanced against the likelihood of the client surviving his gifts by seven years, i.e. the earlier that a gift is made, the sooner it will fall outside the estate altogether.

Contributed by Robert Jamieson

MDR and the 12-month return amendment period

Summary – If a property is reclassified as residential rather than non-residential and the 12m return amendment period, has expired, MDR cannot be claimed.

In August 2017, Daniel Ridgway bought a property for £6.5m. The property consisted of two separate registered titles:

1. A semi-detached house and gardens;

2. The Old Summer House (on adjoining land) that had originally been used as a garage and later as an artist's studio.

Daniel Ridgway was advised that if:

- the Old Summer House was in commercial use on completion, then the purchase could be treated as mixed use, with lower rates of SDLT applying.

- there was no commercial use, then multiple dwellings relief could be claimed.

Just prior to completion, at Daniel's Ridgeway's request, the vendors granted a 6-month commercial lease of the Old Summer House to be used as a photographic studio, with the lease containing a covenant that the Old Summer House should not be used for residential purposes.

On completion, Daniel Ridgway submitted a land transaction return on the basis of mixed use, and SDLT of £314,500 was paid at the lower non-residential rate.

If SDLT had been paid at the residential rate it would have amounted to £888,750. With the benefit of multiple dwellings relief, the SDLT would have amounted to £577,500.

HMRC opened an enquiry into the land transaction return and in February 2021, issued a closure notice on the basis that the Old Summer House was residential property because it was "suitable for use as a dwelling". The land transaction return was amended to charge SDLT at the residential rate, without the benefit of multiple dwellings relief.

Daniel Ridgway appealed to the First Tier Tribunal on the basis that:

- the Old Summer House was not residential property; or

- if the Old Summer House was residential property, then he was entitled to claim multiple dwellings relief.

The First Tier Tribunal had found that:

- the Old Summer House was residential property as asking the seller to grant the commercial lease as they did, invoked the SDLT anti-avoidance rule (s.75A FA 2003);

- multiple dwellings relief was available, as there was no requirement for Daniel Ridgway to claim that relief.

Interestingly, neither party had raised the anti-avoidance rule. They only became aware that the First Tier Tribunal had considered it when their decision was released.

Both parties appealed to the Upper Tribunal:

- Daniel Ridgeway argued that the property was not residential;
- HMRC disputed the availability of multiple dwellings relief as no claim had been made, and it was now too late to amend the SDLT return to include such a claim.

Decision

Before the Upper Tribunal, both sides accepted that s.75A did not apply, and the Upper Tribunal agreed.

The Upper Tribunal found that, despite the covenant, use of the Old Summer House as a photographic studio was a breach of planning control laws, as the property came with planning permission for use as a residential property. With conflicting legal restrictions, the physical attributes of the property were more relevant. Having reviewed plans and photographs of the building, the Upper Tribunal found that the property was suitable for use as a dwelling. and so mixed-use rates did not apply.

But was Multiple Dwellings Relief available? The Upper Tribunal found that there was no mistake in submitting the original return but rather Daniel Ridgeway had made an error by concluding that the property was non-residential property. S.58D(2) FA 2003 states that Multiple Dwellings Relief must be claimed in a return or an amended return and this had not been made.

The Upper Tribunal stated:

> 'Where a relief requires a claim, and a claim is not made in accordance with any procedural requirements, the taxpayer will not be entitled to relief.'

Daniel Ridgeway v HMRC [2024] UKUT 00036 (TCC)

Administration

‘Innocent abroad' relying on agent’s expertise

Summary – An IT consultant’s actions were not deliberate but rather he had failed to take reasonable care when submitting his tax return.

Scott Thompson was an IT consultant who had been employed by Ciber Ltd but from 2013, he made the decision to become self-employed. He appeared to work through an organisation called Catch Resourcing and be paid through two organisations, Big Fat Buddha and Atlas Trustees Ltd. He believed that the money he received from these organisations was net, after having deducted PAYE and NICs. In fact, neither deducted or accounted for tax and NICs on the payments made to him.

Scott Thompson claimed that he notified his accountants, B2B, of these arrangements and engaged the firm to compile and submit his 2013/14 tax return. The return was submitted and included his employment income from Ciber Ltd but nothing from his new self-employed activity.

Although he received the return for checking and signing, this was the first tax return he had submitted and he claimed that he was not sure what to look for. He simply signed the return, relying on B2B to have ensured that it was correct.

Following an enquiry, HMRC sought to collect additional tax and a penalty for an inaccurate return based on deliberate behaviour. HMRC claimed that he had failed to tell his accountant about the sources of income that he knew were taxable.

Scott Thompson accepted the additional tax was payable but replied in a letter dated 26 November 2016 "I do however contest the penalty......". As far as he was concerned, his letter was an appeal against the penalty which had been accepted by HMRC.

In 2022, he was surprised when a bailiff arrived at his door, informing him that “she had been sent by HMRC in respect of the penalty and advised him that he had a right to appeal against the penalty.”

Scott Thompson submitted a formal appeal against the penalty on 23 January 2023, which was clearly late.

Decision

The First Tier Tribunal admitted the late appeal, finding that the earlier letter sent comprised a valid appeal against the penalty. The Tribunal stated:

> 'We are dealing here with an unrepresented litigant in person who having been sent a letter telling him that he was going to be liable to penalties, responds that “I do however contest the penalty”.

The First Tier Tribunal found that Scott Thompson had clearly stated that he wanted to appeal the penalty, just not in the formal way. HMRC should have treated it as an appeal.

The Tribunal stated that it was clear that whilst Scott Thompson was a highly competent IT consultant, “he was an innocent abroad when it came to business structures and taxation.” Understandably, he relied on his umbrella company and accountant to provide the services they had held themselves out as being competent to do, believing:

- the umbrella company would pay him under deduction of tax;
- his accountants would deal correctly with his new self-employed income.

His behaviour had not been deliberate but was found to have been careless. Simply signing the return and sending it to HMRC was not acceptable. He had a duty to check the work undertaken and if he had done so, he would have realised that his self-employed income was not included. He had not taken reasonable care. The First Tier Tribunal ordered that the penalty be reassessed on that basis.

The appeal was allowed in part.

Scott Thompson v HMRC (TC09073)

Late DOTAS disclosure

Summary – An umbrella company was found to be a promoter. Having failed to notify certain arrangements, a £900,000 penalty was payable.

IPS progression Limited was an umbrella company providing PAYE payroll services in respect of individuals whose personal services were made available by recruitment agencies to end users.

The First Tier Tribunal found that the company:

- was a promoter in relation to arrangements which involved trying to avoid income tax and NICs by treating a portion of the payments made to the employees as a loan (referred to as the 'ILO bonus') rather than as income and that such arrangements were notifiable because they constituted a standardised tax product;
- did not have a reasonable excuse for failing to notify the arrangements within the required deadline and set a penalty of £900,000 for that failure.

The arrangements were notifiable arrangements for DOTAS because they constituted a standardised product. The arrangements involved standardised documentation determined by the company, which did not need to be tailored to any material extent in order to be implemented in relation to each of more than 1,500 employees and the main purpose of which was to obtain a tax advantage for them.

In accordance with Root2tax and Root3tax [2017] UKFTT 696 (TC), a tax advantage can include an arrangement under which a person pays less tax than they are required to pay, i.e. even if in law the tax advantage does not exist. In this case, therefore, there was a tax advantage even if the ILO bonus payments were in fact payments of salary or bonus that were taxable.

The First Tier Tribunal also decided that the company was a promoter because the effect and purpose of its service was that the employees would receive part of their earnings tax free and the method IPS employed to do so 'served no purpose other than to provide a justification for not paying tax on the amounts identified as “ILO bonus”'.

The evidence pointed to 11 April 2016 as being the date when the first employee started work under the arrangements.

The company was therefore required to make a DOTAS disclosure by 18 April 2016.

More than six years later, on 25 April 2022, the company made a protective disclosure.

Because the protective disclosure included all the prescribed information required to be included in a disclosure, the additional language disputing that the disclosure was not required to be made and was therefore made only on a protective basis did not preclude it from being a notification that satisfied the disclosure obligation (although, in this case, very late).

The Tribunal also noted that even if a person's DOTAS disclosure is made without adding the protective wording, this does not preclude them from arguing that disclosure was not required.

Finally, the Tribunal decided that IPS did not have a reasonable excuse for failing to disclose on time. Although IPS claimed that it had obtained specialist advice from consultants that a DOTAS disclosure was not required in relation to the arrangements, IPS could no longer locate this advice so it was not in evidence before the First Tier Tribunal.

In deciding to set the penalty at £900,000, the First Tier Tribunal took account of all relevant considerations, including (among other points):

- the desirability of setting the penalty at a level that appears appropriate for deterring IPS and others from similar compliance failures in the future;

- the amount of fees received by the company as the promoter, which, in this case was around £3.6m;

- the fact that the failure in this case was not deliberate but was still more than 'simple carelessness' since the company had been made aware of the issue of DOTAS notifiability as far back as 1 November 2017 when it should either have submitted a disclosure (even if on a protective basis) or have taken all appropriate steps to satisfy itself that no disclosure was required; and

- the fact that the company ceased to use the undisclosed arrangements after 5 April 2018 – the Tribunal gave only 'little mitigating weight' to this.

HMRC v IPS Progression Ltd (TC09071)

Adapted from the case summary in Tax Journal (1 March 2024)

HMRC jeopardy amendments (Lecture B1430 – 8.44 minutes)

This article will consider HMRC's jeopardy amendments, the circumstances in which they can be issued, and practical points for advisers.

What is a jeopardy amendment?

Jeopardy amendment is the term used to describe an amendment made by an HMRC officer to a taxpayer's Self Assessment when an enquiry cannot be closed. HMRC's guidance notes that this is not a routine process (see COM71040) and should only be used in certain circumstances.

A jeopardy amendment can be issued to an individual, a trust, or a company, where there is an open Self Assessment enquiry, and there is evidence that the Self Assessment is inadequate. A jeopardy amendment cannot be issued to a partnership, but one can be issued to a partner in the partnership (providing there is an open s9A enquiry for the same year).

The relevant statutory provisions are at TMA 1970, s9C (ITSA) and FA 1998, Schedule 18, paragraph 30 (CTSA).

When will a jeopardy amendment be issued?

The legislation (see TMA 1970, s9C(2), for ITSA, with similar provisions under the CTSA regime) provides that a jeopardy amendment may be made where an officer forms the opinion:

a) "That the amount stated in the self-assessment contained in the return as the amount of tax payable is insufficient, and

b) That unless the assessment is immediately amended there is likely to be a loss of tax to the Crown".

The circumstances in which an HMRC officer will, in practice, issue a jeopardy amendment, include situations where the officer discovers, or has evidence to suspect, that (see EM1953):

- An individual taxpayer, a partner, or a company intends to dispose of significant assets;
- An individual taxpayer, a partner, or a company intends to become non-resident;
- An individual taxpayer or a partner intends to apply for bankruptcy, or a company intends to go into liquidation;
- An individual taxpayer or a partner may be about to go to prison.

A jeopardy amendment will not be issued once a company has gone into liquidation, or an individual has been made bankrupt. HMRC may issue a jeopardy amendment to a company where the officer establishes that the company's director may be about to go to prison.

Officers are instructed to consider making a jeopardy amendment where a taxpayer will not agree to make a payment on account, and the officer is of the opinion that tax is at risk.

An HMRC officer will also consider making a jeopardy amendment where the taxpayer refuses to co-operate. However, the officer must have already established, with some degree of certainty, that the self-assessment is deficient. Advisers need to consider whether a deficiency has been established, if the officer raises a jeopardy amendment in such circumstances.

Appeals

The client has the right of appeal against a jeopardy amendment. The appeal must be made in writing, setting out the grounds for appeal, and submitted within 30 days of the issue of the amendment. The appeal will not be settled until after the enquiry is concluded.

The client does not have the ability to request a statutory review, or appeal to the tribunal, during an enquiry in respect of the jeopardy amendment until the matters to which the amendment relates are settled by a partial or final closure notice. However, there can be an appeal to the tribunal in relation to the officer's decision about a postponement application, see below.

Postponement applications

The client can also submit a postponement application. However, there needs to be a valid appeal before the postponement application can be made. The normal rules apply, in that the postponement application:

- Must be made in writing;
- Must be made within 30 days of the issue of the amendment;
- Must set out the amount of tax believed to be overcharged;
- Must set out the reason why the taxpayer believes it is overcharged;
- Does not need to be made at the same time as the appeal.

HMRC will seek to agree the amount of tax, if any, to be postponed. If agreement cannot be reached, the client can write to the tribunal to ask it to decide the amount to be postponed. The request must be made within 30 days of HMRC's letter notifying the client of the amount, if any, that it agrees can be postponed. Given the circumstances in which jeopardy amendments are issued, HMRC's internal guidance is that any postponement application should be "considered carefully". It is unlikely that HMRC will agree that the full amount of tax charged should be postponed, but each case must be considered on its merits.

HMRC's Alternative Dispute Resolution ("ADR") process can be used to determine the amount of tax to be postponed. HMRC do not consider that ADR is suitable for cases where the taxpayer has refused to co-operate or has withdrawn co-operation.

HMRC officers are instructed that, if they receive more information, such that the tax postponed is excessive, they should agree a revised figure of tax with the taxpayer or refer the application back to the tribunal.

Practical considerations

It is important to remember that the issue of a jeopardy amendment is not a routine process. The relevant provisions should only be used where there is a risk of the loss of, typically, substantial amounts of tax. This will be most likely in cases where it has been determined that there has, for example, been an omission of taxable profits, but the taxpayer has not made a payment on account or the officer has information suggesting that the taxpayer is about to remove assets abroad, or become bankrupt, in the case of an individual, or bankrupt, in the case of a company. Where the adviser has carefully managed the tax enquiry, and the client has co-operated, and made appropriate payments on account, the possibility of a jeopardy amendment should not become an issue.

Contributed by Phil Berwick, director at Berwick Tax

Deadlines

1 April 2024

- Corporation tax for periods to 30 June 2023 (SMEs not liable to pay by instalments)

5 April 2024

- 2023/24 tax year end
- Pay previously unpaid class 3 NICs for 2016/17

6 April 2024

- Start of 2024-25 tax year. Ensure payroll and other systems are updated.

7 April 2024

- VAT returns and payment deadline for 29 February 2024 electronic quarter payments

14 April 2024

- Forms CT61 and tax paid for the quarter ended 31 March 2024

19 April 2024

- PAYE, NIC, CIS and student loan liabilities for month to 5 April 2024 (non-electronic)
- PAYE liability for quarter to 5 April 2024 if average monthly liability is less than £1,500

21 April 2024

- File online monthly EC sales list for businesses based in Northern Ireland selling goods
- Supplementary intrastat declarations for March 2024
  - arrivals only for a GB business
  - arrivals and despatch for a business in Northern Ireland.

22 April 2024

- PAYE, NICs and student loan liabilities

30 April 2024

- Accounts to Companies House:
  - private companies with 31 July 2023 year end
  - public limited companies with 31 October 2023 year end
- CTSA returns for companies with accounting periods ended 30 April 2023

News

Raising standards in the tax advice market

The government is consulting on options to raise standards in the tax advice market. The document presents three options:

1. Mandatory professional body membership: this would require advisers to hold membership of a recognised professional body;

2. A hybrid, joint HMRC-industry enforcement model: members of the professional bodies would continue to be supervised by those organisations, while unaffiliated practitioners would be under HMRC supervision;

3. Regulation of the industry by a government body: this would in effect be independent regulation of the tax advice market.

As well as generating greater trust in the tax advice market, regulation would, the government believes, result in 'improved quality of service to clients and therefore tax compliance, from higher quality tax advice and tax services'. It could also lead to a reduction in the tax gap and improve HMRC efficiency by reducing work needed to correct errors.

The documents states that improving quality should support a level playing field, where all tax practitioners must meet high standards to practise.

Comments should be emailed to raisingstandardsconsultation@hmrc.gov.uk by 29 May 2024.

https://www.gov.uk/government/consultations/raising-standards-in-the-tax-advice-market-strengthening-the-regulatory-framework-and-improving-registration

Taxation (14 March 2024)

Business taxes

SEISS Claim Rejected (Lecture B1426 – 22.00 minutes)

Summary – Despite being invited to join the Self Employment Income Support Scheme, the taxpayer was denied relief as they were not trading on a self–employed basis at the appropriate time.

Shane Ellis had traded for a number of years as a self-employed franchisee but in February 2018, he incorporated and began trading through Ellis SAJ Limited.

Having received what he considered to be invitations to make claims, in May and August 2020, Shane Ellis claimed and received payment under the SEISS scheme.

His 2018/19 tax return included self-employed income but he declared that his self-employment had ceased on 27 September 2018. His return for the following year included employment income but no self-employment income.

In August 2021, with the taxpayer having ceased trading prior to 2019/20, HMRC issued an assessment to recover £14,070 in respect of the incorrectly claimed SEISS payments.

Following an unsuccessful review, Shane Ellis appealed to the First Tier Tribunal. He argued that HMRC should never have sent him the invitations as he had already notified them of his change of status. Having received the invitation, he claimed that the wording was confusing. He understood the words 'continue to trade' to include trading through a limited company.

HMRC sought to have the appeal struck out.

Decision

Unsurprisingly, the assessment was found to be valid. Based on the facts of the case, he was not eligible to claim relief under the SEISS.

The appeal was dismissed.

Shane Ellis v HMRC (TC 09087)

Eat Out to Help Out (Lecture B1426 – 22.00 minutes)

Summary – An LLP's claims under the Eat Out to Help Out scheme were valid and accurate and HMRC's assessment was not objectively reasonable.

This case concerned the Eat Out to Help Out Scheme that operated for three days per week (Monday, Tuesday and Wednesday) throughout August 2020, designed to encourage customers back into restaurants following the COVID lockdown in 2020.

Restaurants operating under the scheme applied a discount to qualifying sales (not alcohol) made at the restaurant equal to the lesser of £10 per diner or 50% of the value of the customers meal.

The restaurant was then able to claim the amount of discount by way of a support payment from HMRC.

Café Jinnah LLP registered for the scheme and made five claims totalling £103,351 for the five weekly periods in August 2020.

Initially HMRC paid the amount claimed but later sought to clawback £63,766, on the basis that the café had overstated payments made for meals supplied under the scheme. Following an investigation HMRC argued that cash which the cafe claimed was paid for those meals, was not so paid.

The café disagreed and appealed.

Decision

The First Tier Tribunal commented that this is the first case concerning this scheme and as a "reverse suppression" case, it is somewhat unusual as normally HMRC are arguing that cash sales are understated, rather than overstated.

The Tribunal also noted that Café Jinnah LLP had paid VAT and the LLP members had paid income tax on the full amounts, including the cash receipts received for the supply of the meals under the scheme.

The First Tier Tribunal accepted that the HMRC officer genuinely believed that the LLP's claim was overstated as bank statements did not show additional takings during scheme days.

However, the First Tier Tribunal found that the officer had not been objectively reasonable in the conclusions that he reached.

Having been told that a large number of new customers came to the restaurant on scheme days and that most paid in cash, the officer believed that this should have been reflected in significant bank deposits but this was not the case. He believed that the meals were being paid solely by credit card.

The First Tier Tribunal found that it was unreasonable for HMRC to assume that meals were paid solely by credit card on scheme days.

The LLP stated that figures appearing on bank statements at this time would not match takings. With banking hours restricted during COVID and with long queues, the LLP chose to pay out more as cash expenses, including staff wages and drawings, with the balance of cash kept on site in a secure safe.

The First Tier Tribunal stated:

> "there was significant corroborating evidence to support these additional takings. The officer had been told of the change of pattern of eating habits, the way in which the restaurant could be reconfigured, the difficulties with taking cash to the bank. It seems to us that the scheme was having precisely the desired effect."

The HMRC officer had overlooked a number of relevant factors:

- RTI records showing wages were paid but not from the bank account;
- VAT and income tax had been accounted for paid on the additional takings;
- both the partnership accounts and the LLP balance sheet showed an increase in cash in hand;
- an analysis of purchases suggesting an increased supply of meals, not supported by credit card payments.

The First Tier Tribunal concluded by saying the HMRC officer did not seriously consider any other matters which could have supported the claim. Consequently, the First Tier Tribunal found that HMRC's assessment was not objectively reasonable.

The appeal was allowed.

Café Jinnah LLP v HMRC (TC09085)

A company law problem for one-man companies (Lecture B1428 – 6.14 minutes)

When the only shareholder director of a company dies, this can cause severe difficulties for the personal representatives who are looking after the deceased's estate, unless the company's Articles of Association make suitable provision.

Companies with Articles based on Schedule 1 of The Companies (Model Articles) Regulations 2008, which came into force on 1 October 2009, do not have a problem, given that Article 17 reads as follows:

> '**Methods of appointing directors**
>
> 17 (1) Any person who is willing to act as a director, and is permitted by law to do so, may be appointed to be a director:
>
> (a) by ordinary resolution; or
>
> (b) by a decision of the directors.
>
> (2) In any case where, as a result of death, the company has no shareholders and no directors, the personal representatives of the last shareholder to have died have the right, by notice in writing, to appoint a person to be a director.
>
> (3) For the purposes of paragraph (2), where two or more shareholders die in circumstances rendering it uncertain who was the last to die, a younger shareholder is deemed to have survived an older shareholder.'

As can be seen, Article 17(2) makes the necessary provision for a person to be appointed by the personal representatives.

However, companies having earlier Articles may well be in trouble, unless there is an express Article included which authorises the appointment of a director.

Without a director (or secretary) having the authority to register the personal representative's or beneficiary's name in the register of members, the company is effectively trapped in a vacuum. A personal representative or beneficiary cannot exercise any right as a shareholder unless they are registered in the register of members. As a result, they are unable to pass a shareholder resolution to appoint a director or to amend the Articles.

In such circumstances, it is necessary to apply to the court for an order to appoint a new director so as to bring the company out of its vacuum. This is an expensive and time-consuming mechanism.

It may sometimes be the case that the Articles provide for there to be an appointment in the will of a permanent director (i.e. one who does not have to retire by rotation) to succeed the testator.

Everyone should of course have a will, but it is particularly important in this situation that a sole shareholder director should have a valid will which is kept up to date. That person should ensure that their will is, at all times, consistent with the company's Articles in order to reduce the likelihood of any conflict or confusion between the two documents, with particular reference to the ability to transfer the shares on the sole shareholder director's death.

If you have a client who is a sole shareholder director, it is imperative that their company's Articles are reviewed as soon as possible as part of any succession planning.

Contributed by Robert Jamieson

Pillar 2 part 3 – Effective tax rate and top-up amounts (Lecture B1429 – 29 16 minutes)

Introduction

The effective rate of tax is calculated for each jurisdiction in the which the group operates. Broadly this is the tax expense divided by the accounting profit before tax.

Tax expense in Pillar 2 terms is called the 'covered tax balance'. Profit before tax in Pillar 2 terms is called the 'adjusted profits'.

This session introduces the fundamental principles of how the effective tax rate is calculated and how the top-up amount for a territory is calculated and allocated between members in the territory. It also looks at the substance based income exclusion amount in more detail.

All legislative references are to Finance (No. 2) Act 2023.

Effective tax rate (s.132)

1. Calculate the 'adjusted profits' for the period of each 'standard member' (i.e. not an investment entity or minority-owned member) in that territory;

2. Subtract the sum of the losses of members that made a loss in the period from the sum of the profits of members made a profit in the period;

3. If 2 is nil or a net loss, the effective rate is deemed to be 15% (so that no top-up amount arises) and the calculation finishes;

4. If 2 is a net profit, calculate the combined ‘covered tax’ balance (sum of the positive and negative covered tax balances) for the ‘standard members’ of the group in that territory (which can be negative);

5. If the balance in 4 is nil, the effective tax rate is nil (which means 15% top-up tax may be payable);

6. If the balance in 4 is not nil, divide the balance in 4 by the result of step 2;

7. Except where step 3 or 5 applies, step 6 is the effective tax rate (when converted to a percentage).

Stateless member (s.132)

In the event that a member of the group is treated as not located in any territory, it is deemed to be the sole member of a group located in a nominal territory.

As it is a nominal territory, it will not have to calculate any multinational top-up tax and its revenue and profits will not be included in any MNG when calculating whether that MNG is liable to the top-up tax or how much top-up tax is payable.

This can arise with US subsidiaries of a US parent where the subsidiaries have ‘checked the box’ for US tax filing purposes, making them transparent entities and not subject to corporate income tax.

Total top-up amount for a territory (s.194)

1. Calculate 15% minus the effective tax rate of standard members of the MNG located in the territory;

2. If 1. is nil or negative, the top-up amount is nil, otherwise continue;

3. Calculate the aggregate adjusted profits minus aggregate adjusted losses of members located in the territory;

4. Deduct the substance-based income exclusion amount (s.195) for the period for the territory from the amount in 3;

5. If the result in 4. is nil or negative, the top-up amount is nil, otherwise continue;

6. Multiply the percentage in 1. by the result in 4.

Example

A MNG has 5 members (A Inc., B. Inc, C Inc., D. Inc and E Inc.) in the territory of Erehwon, a low-tax jurisdiction.

The members' adjusted profits for the year ended 31 December 2024 are:

	£
A Inc.	15,340,210
B Inc.	(14,570,855)
C Inc.	7,450,998
D Inc.	20,190,453
E Inc.	6,701,345
Net profit	£35,112,151

Assume that the effective rate of the members in Erehwon is 2.32377%. and that there is no 'substance based income exclusion' amount (see below).

What is each company's top-up amount for the accounting period?

Analysis

1. Calculate 15% minus the effective tax rate of standard members of the MNG located in the territory (15% - 2.32377% =) 12.67623%

2. If 1. is nil or negative, the top-up amount is nil, otherwise continue - N/A

3. Calculate the aggregate adjusted profits minus aggregate adjusted losses of members located in the territory

   Aggregate adjusted profits minus aggregate adjusted losses of A, B, C, D and E is £35,112,151

4. Deduct the substance-based income exclusion for the period for the territory from the amount in 3 - N/A

5. If the result in 4. is nil or negative, the top-up amount is nil, otherwise continue - N/A

6. Multiply the percentage in 1. by the result in 4.

   12.67623% x £35,112,151 = £4,450,897

Allocation of top-up amounts - 9-step approach (s.193)

1. Determine the total top-up amount for the member's territory for the accounting period (as above);

2. If 1. is nil, there is no top-up amount, otherwise continue;

3. Determine the adjusted profits of the member for the period;

4. If there is no adjusted profit, there is no top-up amount, otherwise continue;

5. If this is the only standard member located in the territory, the member's top-up amount equals the total top-up amount for the territory, otherwise continue;

6. Determine the adjusted profits of all other standard members in the same territory;

7. Aggregate the adjusted profits of all standard member in 6. that have profits;

8. Divide the member in question's adjusted profit by the result of 7;

9. The member's top-up amount is total top-up amount for the territory (step 1) multiplied the result of step 8.

This is required where the responsible member has different ownership percentages in different entities in the territory.

Analysis of previous example

B Inc. does not have an adjusted profit, so its top up amount is nil.

A, C, D and E have top-up amounts pro-rata to their relative adjusted profits. Their aggregate adjusted profits are £49,683,006, so their top up amounts are:

	£
A Inc. (4,450,897 x 15,340,210 ÷ 49,683,006)	1,374,266
C Inc. (4,450,897 x 7,450,998 ÷ 49,683,006)	667,504
D Inc. (4,450,897 x 20,190,453 ÷ 49,683,006)	1,808,780
E Inc. (4,450,897 x 6,701,345 ÷ 49,683,006)	600,347
	£4,450,897

If, for example, the responsible member owned 100% of A and C, and 80% of D and E, the top up tax payable would be 100% x (1,374,266 + 667,504) plus 80% x (1,808,780 + 600,347), i.e. £3,969,072.

Substance based exclusion amount (s.195)

This is the sum of:

1. the 'payroll carve-out' amount plus

2. the 'tangible asset carve-out' amount for the period for each member in the territory

It plays no part in the calculation of the effective tax rate in a territory, but is deducted in Step 4 of the calculation of the total top-up amount for a territory, although the filing member can elect not to calculate the amount for the period.

The payroll carve-out amount is 5% of the eligible payroll costs for the period and the tangible asset carve out amount is 5% of the eligible tangible asset amount for the period, however transitional rules (Schedule 16) mean that the 5% figure only applies for accounting periods beginning from 2033.

For accounting periods beginning in the following years, the following percentages apply:

2023	10.0%	2028	9.0%
2024	9.8%	2029	8.2%
2025	9.6%	2030	7.4%
2026	9.4%	2031	6.6%
2027	9.2%	2032	5.8%

Eligible payroll costs (s.196)

All employment costs (e.g. salaries, wages, bonuses, costs of benefits provided, payroll and other employment taxes and social security payable) incurred by a member on individuals, where the costs are primarily incurred in respect of work done in the course of the ordinary operating activities of the member or wider group.

At least some of the work must be carried out in the member's territory and the costs must not be specifically excluded. Where an employee carries out the work in the period both in the territory in which the member is located and outside that territory, and the proportion of the time spent carrying out the work in that territory in the period is 50% or less, the payroll costs in respect of the employee are pro-rated to determine how much of those costs are eligible payroll costs.

Someone is an employee if regarded as such under the law of the member's territory or anyone acting exclusively under the direction and control of the member (including part-time workers)

The following costs are excluded:

- Those taken into account in determining the underlying profits of a PE of the member;
- Costs capitalised into the carrying value used to calculate the eligible tangible asset amount (but see s.197 below);
- Core international shipping costs (covered in Part 3);
- Ancillary international shipping costs (covered in Part 3).

Example

A UK ultimate parent company of a qualifying MNG has one member located in the low-tax territory of Ruritania. It has an adjusted profit in its year ended 31 December 2024 of £1,530,985 and an effective tax rate of 7.53509%.

Included in its adjusted profits are payroll costs of £329,700. This includes £56,940 relating to a PE of the member located in a different territory.

Calculation of top-up amount (s.194)

1. Calculate 15% minus the effective tax rate of standard members of the MNG located in the territory - 15% minus the effective rate in Ruritania (15% - 7.53509%) 7.46491%

2. If 1. is nil or negative, the top-up amount is nil, otherwise continue - N/A

3. Calculate the aggregate adjusted profits minus aggregate adjusted losses of members located in the territory: £1,530,985

4. Deduct the substance-based income exclusion amount (s.195) for the period for the territory from the amount in 3

   1,530,985 minus [9.8% x (329,700 - £56,940)] **£26,730**), i.e. £1,504,255

5. If the result in 4. is nil or negative, the top-up amount is nil, otherwise continue - N/A

6. Multiply the percentage in 1. by the result in 4: 7.46491% x £1,504,255, i.e. £112,291

The eligible payroll costs have reduced the top-up amount by (7.46491% x £26,730), i.e. £1,995.

It might cost more in professional fees to calculate the amount of eligible costs than the reduction in the top-up amount, hence why the filing member can elect not to calculate it.

Eligible tangible asset amount

This is the average of the opening and closing carrying values of eligible tangible assets recorded in the consolidated financial statements multiplied by the relevant percentage. The relevant percentage will be 5% for accounting periods beginning in 2033 onwards, but there are transitional percentages (Schedule 16) that apply before this.

For accounting periods beginning in the following years, the following percentages apply:

2023	8.0%	2028	7.0%
2024	7.8%	2029	6.6%
2025	7.6%	2030	6.2%

2026	7.4%	2031	5.8%
2027	7.2%	2032	5.4%

If there is no value recorded at the start or end of the period, the value is calculated as if it was recorded at that time. For example, the member might acquire its first item of property, plant and equipment on 1 April 2024. The eligible amount (subject to the conditions below) would be the average of the carrying amount on 1 April 2024 and on 31 December 2024.

Similarly, if the member joined the group on 1 April 2024, the eligible tangible assets amount would be based on the carrying value initially recognised in the consolidated financial statement on 1 April 2024 and the carrying value in the consolidated financial statements on 31 December 2024.

If a member leaves the group on (say) 8 May 2024, the eligible tangible assets amount would be based on the average of the carrying values on 1 January 2024 and then on 8 May 2024.

Carrying amounts include purchase accounting adjustments related to the assets on the initial consolidation of the member in the group accounts (i.e. the fair value adjustments made in accordance with generally accepted accounting principles), but must exclude the effect of any other revaluations carried out.

Eligible tangible assets

- Property, plant and equipment located in the member's territory;
- Natural resources located in that territory (e.g. oil or gas reserves recorded in the consolidated financial statements)
- Right of use asset where the underlying asset is a tangible asset located in the member's territory;
- Licences or similar rights granted by a government of the territory to use a tangible asset, where it is expected that the member will incur significant expenditure in enhancing the value of tangible assets in that territory (irrespective of whether those assets are subject to the right) – e.g. an exploration licence to search for mineral resources in the territory.

The following assets are excluded:

- Property (including land and buildings) held for sale (IFRS 5), held to lease out or held for investment purposes (irrespective of whether they were sold, leased out or held for investment in the period);
- Used in the course of a core or ancillary international shipping activity (if there is an ancillary international shipping profit cap of more than nil in the period, only the eligible proportion of the asset is excluded.

Other issues

Assets located in more than one territory

Where an asset is only located in the same territory as the member for part of the period, it is regarded as located in that territory for the whole period. Where the proportion of the period in which the asset (or in the case of a right, the asset to which the right relates) is located in the territory is 50% or less, the carrying values are multiplied by that proportion

Impairment losses and reversals

Impairment losses and reversals are included in the carrying amounts. Reversals are limited to the amount that would give the assets their carrying value as if no impairment loss had been recognised originally (automatic if IFRS or impairment accounting similar to IFRS has been used).

Example

UP Ltd is the UK ultimate parent company of a qualifying MNG has one member, MTUT Inc. located in the low-tax territory of Ruritania. It has an adjusted profit of £1,530,985 in its year ended 31 December 2024 and an effective tax rate of 7.53509%. MTUT has elected not to include eligible payroll costs, but has property, plant and equipment located in Ruritania and used in its trade of professional services.

The items had the following carrying values:

	1 January 2024	31 December 2024
	£	£
In MTUT Inc.'s local accounts	1,530,261	1,782,541
In UP Ltd's consolidated financial statements	1,930,400	2,150,308

Neither MTUT Inc. nor UP Limited has an accounting policy of revaluing property, plant and equipment.

Calculate the top-up amount for Ruritania.

1. Calculate 15% minus the effective tax rate of standard members of the MNG located in the territory: (15% - 7.53509%) 7.46491%

2. If 1. is nil or negative, the top-up amount is nil, otherwise continue - N/A

3. Calculate the aggregate adjusted profits minus aggregate adjusted losses of members located in the territory: £1,530,985

4. Deduct the substance-based income exclusion amount (s.197) for the period for the territory from the amount in 3.

   - Average carrying value in consolidated financial statements (1,930,400 + 2,150,308) ÷ 2 = £2,040,354 x 7.8% **= £159,148**

   - Adjusted profits (1,530,985 – 159,148) £1,371,837

5. If the result in 4. is nil or negative, the top-up amount is nil, otherwise continue - N/A

6. Multiply the percentage in 1. by the result in 4.

   7.46491% x £1,371,837 i.e. £102,406

The eligible tangible asset amounts have reduced the top-up amount by (7.46491% x 159,148), i.e. £11,880.

The filing member can choose to include or exclude a qualifying asset or not to calculate a tangible asset substance-based income exclusion amount.

Contributed by Malcolm Greenbaum

VAT and other indirect taxes

Sports nutrition bars (Lecture B1426 – 22.00 minutes)

Summary – Sports nutrition bars containing a flapjack and either a cake bar or brownie were standard-rated confectionery.

Tim Davies had a background in sales, marketing and business development and was a keen sportsman with an interest in maintaining an active lifestyle.

He believed that he had found a gap in the market for selling a product to those carrying out vigorous exercise which provided both:

- carbohydrates before exercise for energy; and
- protein afterwards to help rebuild muscle.

Together with Mike Naylor, a sports nutritionist, he set up Duelfuel Nutrition Limited for the purpose of developing and marketing this opportunity. Mike Naylor advised as to the necessary nutritional content (proteins, carbohydrates, fats, vitamins and minerals).

The product developed was sold through supermarkets and at gyms, and included a:

- flapjack (to provide carbohydrates before exercise for energy); and
- cake or brownie (protein afterwards to rebuild muscle).

Tim Davies concluded that zero rated VAT treatment was essential to ensure it was as commercially viable as possible and so took advice from a VAT consultant, concluding amongst other things that using oats as the only cereal in the flapjack was important and both the flapjack and cakes needed to be baked.

HMRC disputed the VAT classification, arguing that the product was standard rated. The company appealed, arguing that a flapjack and either a cake bar or brownie packaged and sold together were zero rated for VAT purposes (Item 1 of Group 1 Schedule 8 VATA 1994).

Both parties agreed that the products were 'food of a kind used for human consumption' within Item 1. However:

- Duelfuel Nutrition Limited argued that the product qualified as ‘cakes’ making them zero rated.
- HMRC argued they fell within Excepted Item 2 and were standard rated confectionery because either:
  - Note 5 deemed the products to be confectionery; or
  - If Note 5 did not apply, the products were confectionery on general principles.

Decision

The First Tier Tribunal questioned what would happen if the Tribunal found that one item was standard rated, while the other was zero rated, meaning that the issue of composite or multiple supplies would need to be considered.

Acknowledging that this was not something that had been debated to date, both counsel agreed that the Tribunal should simply decide the VAT status of the individual products and, if necessary, the parties would bring the issue to the Tribunal at a later date.

The First Tier Tribunal adopted a multifactorial test, and examined the:

- nature and description of the products including size and appearance;
- ingredients;
- the manufacturing process;
- taste and texture as well as when the products were consumed;
- packaging and where the products were sold.

The Tribunal concluded that the ordinary person would not consider these to be cakes. A typical cake would be a high-calorie food eaten by everyone as a treat. This product was not made, marketed or consumed in this way.

Although the ordinary person would find that the products were not confectionery, these were 'sweetened prepared food which is normally eaten with the fingers', meaning they qualified as standard rated confectionary.

Duelfuel Nutrition Limited v HMRC (TC09055)

Organix and Nakd bars **(Lecture B1426 – 22.00 minutes)**

Summary – Having been remitted back to the First Tier Tribunal, a new panel has found that both Organix and Nakd bars were 'confectionery' for VAT purposes.

Back in 2018, Morrisons made a number of appeals seeking to recover £1million of output tax on various types of 'Organix' and 'Nakd' bars, arguing that they were zero, rather than standard rated.

Having consolidated the appeals into one, the First Tier Tribunal found that the bars were confectionery, not cake, making them standard rated.

On appeal to the Upper Tribunal, it was found that in reaching its decision the First Tier Tribunal had wrongly treated certain factors as irrelevant. The Tribunal should have considered the:

- healthiness of the products and their marketing as healthy; and
- fact that the products do not contain ingredients associated with traditional confectionery (cane sugar, butter or flour).

The Upper Tribunal remitted the appeal back to the First Tier Tribunal to be heard by a new panel.

Decision

The First Tier Tribunal stated that it needed to consider if the 'ordinary person in the street' would see these products as confectionery.

The First Tier Tribunal concluded that the products looked, felt and tasted like confectionery, being similar in size to chocolate bars and intended to be eaten with hands.

The Tribunal noted that although the bars were made with dried fruits, nuts and oats, "the absence of traditional confectionery ingredients" did not outweigh factors such as the look, feel, and taste of the products.

The Tribunal gave little weight to the 'healthy' marketing angle employed, stating that marketing is aimed at maximising sales rather than to inform the customer of a products health benefits. Indeed, all of the bars fell within the Food Regulations 2021 as food which is 'less healthy'.

Both the Organix and Nakd bars were found to be standard rated 'confectionery'.

WM Morrison Supermarkets Plc v HMRC (TC09095)

Floor space v turnover for overhead apportionment (Lecture B1426 – 22.00 minutes)

Summary - The dual use of the hospitality and entertainment areas meant that the special method based on floor space, rather than turnover, did not guarantee a more precise calculation of recoverable input VAT than the standard method.

Hippodrome Casino Ltd operated a 'Las Vegas style experience' with its venue including live gaming, gaming machines, bars, a restaurant, lounges, conference spaces and a theatre.

Gaming activities generated high exempt income while hospitality and entertainment income were standard rated and accounted for significantly less of the total income.

Had the company adopted the standard partial exemption method, non-attributable VAT incurred on overheads would have been apportioned between taxable and exempt supplies based on turnover.

Believing that this did not produce a fair result, the company sought to use the Standard Method Override based on floor area. The company argued that this more accurately reflected the economic use of the expenditure than the standard recovery method.

On appeal, the First Tier Tribunal found in the taxpayer's favour, agreeing that the special floor area method did provide a more precise calculation for allocating overheads.

HMRC appealed to the Upper Tribunal, arguing that the First Tier Tribunal had erred in law. The First Tier Tribunal had failed to consider the fact that floorspace had a dual purpose; floorspace used for taxable supplies was also effectively used economically for exempt supplies of gaming.

Decision

The Upper Tribunal found in HMRC’s favour. The First Tier Tribunal had made an error of law by failing to give reasons for rejecting HMRC's argument that the hospitality and entertaining floor space had a dual purpose.

The Upper Tribunal remade the decision rejecting the ‘flawed’ Standard Method Override, which did not guarantee a more precise calculation of economic use than that the standard turnover method. The hospitality and entertainment areas were also used economically for the gaming activity. The bars and restaurants were not profitable on their own but rather enabled customers to stay longer, by having have a break, drink, or eat some food and so spend more money on exempt gaming activities.

HMRC v Hippodrome Casino Ltd [2024] UKUT 00027 (TCC)

Land Rovers: commercial vehicle or car? (Lecture B1426 – 22.00 minutes)

Summary – Land Rovers converted to become cars were not subject to the self-supply rules as the vehicles were not available for private use.

Three Shires Trailers Limited bought and sold trailers.

In August 2021, the company bought two Land Rover Discovery vehicles, which were to be used to transport trailers to customers, to collect trailers from suppliers and to enable staff to attend trade fairs around the country.

On the basis that the vehicles were commercial vehicles used in the trade, the input VAT was reclaimed in full.

However, a few days after purchase, three-fold-up seats with seat belts were installed behind the driver and passenger seats and the side windows and back windows, which had been blacked out, were cleared. This was to enable more people to be transported to trade shows. The company that carried out the work advised that the seats were 'not permanent' and did 'not affect the status of the vehicles for tax purposes'.

Initially, HMRC disallowed the input tax claim on the basis that the vehicles were now ‘blocked’ cars.

Following a review, the input VAT was allowed but HMRC sought output VAT on the self-supply arising from converting the vehicles from commercial vehicles to cars.

Confirming that the vehicles were kept on the business premises and not used privately or kept at employee homes, the company argued that a self-supply charge was not due. These were ‘qualifying’ cars (Article 5 VAT (Cars) Order 1992).

Decision

The First Tier Tribunal confirmed that the vehicles had been converted from commercial vehicles to cars.

As a ‘qualifying’ motor vehicle used exclusively for business purposes and not made available for private use:

- input VAT was recoverable;
- the self-supply output VAT charge was not in point.

The appeal was allowed.

Three Shires Trailers Limited v HMRC (TC09044)

NHS trust car park fees (Lecture B1426 – 22.00 minutes)

Summary – Charges for car parking operated by an NHS Trust on their sites was not standard rated, meaning that the output tax was repayable.

This is an important case that looks at charges levied for car parking at healthcare sites operated by NHS foundation trusts where:

- The trust argued that it was engaging as a public authority under a special legal regime and that there were no "significant distortions of competition", making them a non-taxable person (S.41A VATA 1994);
- HMRC argued that VAT should be levied at the standard rate of 20% as the Trust was not acting as a public authority. Alternatively, if it was VAT should still be charged as there would otherwise be significant distortions of competition.

The claim to recover VAT does not extend to income generated where the management of car parking was outsourced to a third-party operator.

The Trusts in this case was Northumbria Healthcare NHS Foundation Trust but it should be noted that there are around 50 similar appeals by other NHS bodies stayed behind the decision. The total tax at stake is in the region of £70million.

Both the First Tier and Upper Tribunals dismissed the Trust's appeal and the case moved to the Court of Appeal, with the Trust arguing that the Upper Tribunal had erred by concluding that the Trust did not supply car parking under a special legal regime.

Decision

The Court of Appeal found that Northumbria Healthcare NHS Foundation Trust was acting as a public authority under a special legal regime, rather than under the same legal conditions as private car park operators. Under the 2015 Parking Principles and the other guidance produced by the Department of Health, Northumbria Healthcare NHS Foundation Trust had a legal duty to follow these guidelines by providing parking as they did for patients, visitors, carers and certain staff. With car parking provided under a special legal regime, the Trust was acting as a public authority.

When looking at distortion of competition, the Court of Appeal found that HMRC had failed to demonstrate that a significant distortion of competition would arise if VAT was not charged.

The Court of Appeal stated:

> "*Distortion, let alone significant distortion, cannot be assumed based on participation in the car parking market, or based on a finding that competition exists".*

HMRC needed to provide 'findings of fact, based on evidence' and not merely assumptions. The facts needed to demonstrate that by not charging VAT, the Trust had created significant distortion of competition.

The Court of appeal stated that:

> "In order for HMRC to demonstrate that there would be significant distortions of competition, additional evidence would be required to particularise the distortions. This would need to include some form of economic assessment".

These findings of facts were not present in this case.

The Court of Appeal set aside the earlier decision.

Northumbria Healthcare NHS Foundation Trust's claim for the repayment of VAT was allowed.

Northumbria Healthcare NHS Foundation Trust v HMRC [2024] EWCA Civ 177

R&C Brief 1 (2024): Live web streaming of funeral services

This Revenue and Customs Brief confirms that the supply of live web streaming of funeral, burial, or cremation services should be treated as exempt under Item 2 to Group 8, Schedule 9 VATA 1994.

Any tax incurred by an undertaker, cemetery or crematorium operator on the cost and overheads of providing such a supply is not normally recoverable.

Where live web streaming of funeral, burial, or cremation services is supplied by a third party for a separate consideration, that web streaming is not within the scope of this exemption, and will be subject to the standard rate of VAT.

If VAT has been previously charged or claimed incorrectly, then an adjustment can be made on the VAT Return.

https://www.gov.uk/government/publications/revenue-and-customs-brief-1-2024-live-web-streaming-of-funeral-services