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Personal tax

IR35 - Christa Ackroyd revisited (Lecture P1166 – 17.11 minutes)

Summary - Christa Ackroyd, the Look North presenter, has failed in her appeal to have her deemed employment status under the IR35 legislation overturned.

In March 2018 we reported on the Christa Ackroyd case. You may remember that she was a presenter for the BBC who supplied her services through Christa Ackroyd Media Ltd, her personal service company under two successive fixed-term contracts. The first contract was dated 29 May 2001 and was followed by a later contract dated 4 May 2006 that was terminated by the BBC in 2013. It was the latter contract that was the subject of the appeal.

The First Tier Tribunal decided that the most significant factor to be taken into account when reaching their decision was the fact that the BBC could control what work Christa Ackroyd did under the hypothetical seven year contract. Other indicative factors of her employment status were that:

- The BBC had the right to specify what services her company would provide with the BBC's editor having ultimate control over programme content;
- Christa Ackroyd Media Ltd was not allowed to send a substitute for Christa Ackroyd;
- Christa Ackroyd was restricted from providing services to other UK organisations without their consent.

The case has now been heard at the Upper Tribunal. Christa Ackroyd Media Ltd appealed against the decision on the sole ground that the First Tier Tribunal had erred in law in its conclusion that the BBC had sufficient control over Christa Ackroyd to mean that an employment relationship would have arisen if the services had been directly supplied.

Decision

In deciding this case, the Upper Tribunal stated that the key question they needed to answer was:

> 'In so far as the contract does not deal explicitly with all aspects of control, is it appropriate in view of the contract, and the wider context, to conclude that ultimate control in relation to Ms Ackroyd's services lay with the BBC?'

This meant that the First Tier Tribunal had used the wrong test and made an error of law when they considered whether 'a right of ultimate control' was an implied term of the contract.

A broader approach was needed. The Tribunal needed to consider where the ultimate right of control lay by looking at all of the circumstances of the engagement. That included the BBC's obligations under its Editorial Guidelines. Through the programme's editor, the BBC had control over programme content. The Upper Tribunal agreed with the First Tier Tribunal that it did not matter that Christa Ackroyd was not contractually bound by the Editorial Guidelines because both parties understood that where needed, the BBC could enforce those Guidelines.

Although the Tribunal had taken the wrong approach, they had reached the right conclusion, as their conclusions had been relevant to a 'broader process of construing the contract and the context in order to determine the extent of the BBC's control over the "what, how, where and when" in relation to Ms Ackroyd's services'.

The Upper Tribunal concluded that the BBC had a sufficient degree of control over the provision of services by Christa Ackroyd to satisfy the control requirement necessary for an employment relationship to exist under an IR35 hypothetical contract.

Christa Ackroyd Media Limited v HMRC [2019] UKUT 0326 (TCC)

IR35 - Helen Fospero win **(Lecture P1166 – 17.11 minutes)**

Summary – Even if the presenter had been engaged directly by ITV, rather than through her personal service company, she would have been self-employed as she worked under a series of short-term contracts with no guarantee of further work and with ITV having no obligation to provide any work.

Having worked previously for Sky News and ITV over a 14-year period, in 2002 Helen Fospero was approached by the BBC. When she took up this role, she was told that she could not be an employee of the BBC, but must be engaged as an independent contractor through a personal service company and so she established Canal Street Productions Limited.

Roll forward to 2011 and she was back working for ITV. This case related to a two-year period covering tax years 2012/13 and 2013/14 where HMRC argued that she fell foul of the IR35 legislation, that she was not a contractor but employed, and so liable to pay just over £80,000 in unpaid taxes and national insurance contributions.

During this period, Helen Fospero worked for ITV as a guest presenter. Initially as a news presenter on GMTV to cover sick leave and then later in 2011 and early 2012, under casual arrangements to host several editions of "Lorraine" and the early morning programme "Daybreak". She worked as a substitute for Lorraine Kelly, with the circumstances of the two presenters being very similar.

From 2012, things became a little more formal with Canal Street Productions Limited entering into three separate agreements setting out the working arrangements between Canal Street Production Limited and ITV going forward.

Under these agreements the company agreed that Helen Fospero would:

- Would be offered around 20 days of anticipated work per annum but that this was not guaranteed;
- Would work on an assignment by assignment basis with no guarantee of future work;
- Was free to work elsewhere provided ITV had approved such work and that ITV had first-call on her time;
- Was treated very differently to employed ITV presenters who were provided with laptops, an ITV email address and rooms at ITV's studios.

Decision

As expected, in reaching their decision, the First Tier Tribunal considered what the hypothetical contract between Helen Fospero and ITV would look like.

The Tribunal concluded that there was no obligation between each engagement on ITV's part to offer work. Although the minimum number of days was set at 20, there would be no guarantee of work nor obligation for Helen Fospero to accept it. She was engaged on an assignment-by-assignment basis with no guarantee of future work at the end of each piece of work. There was no mutuality between the specific engagements

Helen Fospero undertook several hours of preparation for each engagement in her own time, which was not dictated by ITV. However, there was no right of substitution and ITV had full control over the time and location of her work as well as ultimate editorial control. However, unlike ITV's other employees, Helen Fospero had no contractual rights to holiday or sick pay or entitlement to other benefits.

In concluding, the Tribunal disagreed with HMRC. Under a hypothetical contract, Helen Fospero would not be working as an employee, but rather as a self-employed contractor.

The taxpayer's appeal was allowed.

Canal Street Productions Limited V HMRC (TC07422)

Market value of gifts to charity **(Lecture P1166 – 17.11 minutes)**

Summary –Taxpayers in these Lead Cases were found to have made excessive claims for tax relief on gifts of shares to charities as the market value of those shares was overstated.

This appeal concerned arrangements, which HMRC described as being for tax avoidance purposes. Under these schemes shares in a number of companies were gifted to charity and tax relief claimed. The decision involved detailed discussions about the appropriate way to value shares by reference to a hypothetical sale.

As there were a number of cases that raised common issues, these appeals were selected as Lead Cases and so this case was actually five cases with similar share valuation issues that were heard together. In all five cases, the taxpayers had claimed tax relief in relation to gifts of shares in companies listed on the Channel Islands Stock Exchange to various charities:

Dr Patel	Clerkenwell shares valued as at 23 March 2005
Dr Venkataraman	Signet shares valued as at 31 March 2006
Mr Foster	Modia shares valued as at 18 October 2005
Mr Freeman	Modia shares valued as at 8 September 2005
Mr Jakeway	Your Health shares valued as at 31 March 2006

The dates above were the dates that the shares were gifted.

Under s587B ICTA 1988, tax relief is available for the market value of the gift of shares listed on a recognised stock exchange. In this case, the Channel Islands Stock Exchange is a recognised exchange for this purpose and so the sole issue before the Tribunal was the determination of the correct market value of the shares in the companies on the dates that were gifted.

The legislation states that the correct value is the market value at, or immediately after, the time when the disposal is made (whichever time gives the lower value). HMRC argued that the shares in question were placed on the Channel Islands Stock Exchange at inflated prices, resulting in overstated tax relief claims in respect of the shares that were gifted. HMRC issued closure notices that significantly reduced the amount of tax relief for each taxpayer.

Decision

The First Tier Tribunal agreed with HMRC's expert witness. He noted that the share price in each of the Companies increased significantly in a matter of a couple of days after their listing on the Stock Exchange (In excess of 1000%). In the expert's opinion these extreme share prices, which were not supported by any new public information at the time, indicated that the price paid for the companies' shares, were not appropriate indicators of the true market value of a minority share at each of the gifting dates. He considered that the direct market method of valuation was an appropriate way of determining the value of a minority share in each of the companies, although by reference to private arm's-length transactions in companies. This methodology assumed that the taxpayer was able to determine the actual market value of the companies' assets and that the lower values in that range applied.

The expert testimony was unchallenged and the market value was therefore lower than that calculated by both the taxpayer and HMRC in their closure notices.

The appeals were dismissed and the First Tier Tribunal increased the assessment amounts in line with the expert evidence.

Vipin Patel and others v HMRC (TC7404)

Update on EIS and VCT schemes **(Lecture P1170 – 17.33 minutes)**

Over recent years, restrictions on the tax reliefs for pension contributions have meant that more and more high net worth individuals have started looking at venture capital investments as an alternative to the hitherto conventional forms of provision for retirement. The main reliefs are:

- the Enterprise Investment Scheme (EIS);
- the Seed Enterprise Investment Scheme (SEIS); and
- Venture Capital Trusts (VCTs).

The EIS legislation, which has been available for many years, offers significant tax incentives to investors in the unquoted trading companies that qualify. These will typically be young high-risk businesses. It should be emphasised that there are stringent conditions associated with this and the other venture capital reliefs.

In summary, the principal EIS tax benefits are:

- income tax relief of up to 30% of the amount invested;
- no CGT if EIS shares are disposed of at a profit after three years;
- a form of CGT deferral which allows investors to hold over gains on any kind of chargeable asset against subscriptions in EIS shares;
- losses on EIS shares may be eligible for income tax relief under S131 ITA 2007; and
- EIS investments should attract 100% business relief under IHT after two years of ownership.

The SEIS regime was introduced in FA 2012 as a special relief to encourage investment in new start-up companies. The rules are largely based on the EIS and contain many of the same features. As far as the SEIS is concerned, the key differences in the reliefs available are:

- an income tax reduction of 50%, regardless of the investor's marginal tax rate; and
- gains arising on the disposal of any kind of chargeable asset can be exempted from CGT (up to a maximum of one half of the SEIS investment) by virtue of a targeted reinvestment relief.

This means that an investor could receive 50% income tax relief and 10% CGT relief (i.e. ½ x 20%) on a £100,000 SEIS investment, reducing his net cost to just £40,000. However, while the SEIS reliefs may appear to be more attractive in percentage terms, the overall amount of relief available is substantially less, given that the maximum SEIS investment in any one tax year is limited to £100,000. On the other hand, with an annual limit of £1,000,000, which can rise to £2,000,000 for 2018/19 onwards if investments are made in 'knowledge-intensive' companies, £600,000 of relief is potentially available through the EIS.

The background rationale for the introduction of VCTs has been explained as follows:

> 'To overcome the expected difficulty of some investors meeting the conditions for relief under the EIS, an investment vehicle similar to an investment trust (known as a VCT) was devised in 1994. An individual investor can acquire shares in a VCT whose professional managers will use the funds to make and manage investments in a range of unquoted companies.'

A VCT is a quoted company that has been approved as such by HMRC. There are currently three forms of tax relief available to an investor in a VCT:

- an investment relief, given as a 30% income tax reduction, can be claimed on the amount subscribed for new shares in a VCT, up to £200,000 per tax year;
- a dividend relief provides an exemption from income tax on dividends received from shares in a VCT (it should be noted that this relief applies to shares acquired by purchase as well as by subscription, provided that the annual value limit of £200,000 was not exceeded); and
- disposals of shares in a VCT which qualified for investment relief are CGT exempt.

As a final point, it should be borne in mind that investment relief can be clawed back in whole or part if VCT shares are disposed of within five years.

The detailed conditions for EIS

The legislation lays down various conditions which must be met and over which periods. There are three periods which are relevant, all of which terminate at the third anniversary of the date the shares were issued (or if later, three years from when trade commenced). Period A starts with the incorporation of the company or two years before the share issue if later; Period B starts with the share issue and Period C starts 12 months before the share issue.

There is a recent concept for EIS which is that of knowledge-intensive companies. Such companies qualify for higher total investment limits; a longer initial investing period for the purposes of the permitted maximum age condition and a higher number of employees. This is discussed further below.

The definition was amended for shares issued on or after 6 April 2018 in cases where the issuing company began to carry on a trade less than three years before the date that the relevant shares are issues. In that case, the operating costs conditions have to be met in the three years after the date of the share issue so it will not be possible to tell if the conditions are met at the time of the issue.

Relief is available in respect of an amount subscribed for shares in the issuing company where:

- 'relevant shares' are issued to the individual
    - Shares forming the OSC which throughout Period B do not carry any present or future preferential rights to dividends or assets on a winding up, nor any present or future rights to be redeemed
    - They are subscribed for wholly in cash and fully paid up at the time of issue
    - They are issued to raise money for the purposes of the qualifying business activity to be carried on by the company or a qualifying 90% subsidiary
    - They are issued for bona fide commercial reasons and not as part of any tax avoidance scheme
- the shares are issued before 6 April 2025
- the individual is a 'qualifying investor'
    - he is not connected with the issuing company
    - there are no linked loans in Period A
    - the existing shareholding requirement must be satisfied
- he must have subscribed for genuine commercial reasons and not as part of a scheme to avoid tax

- the issuing company is a 'qualifying company'
    - the company has a UK PE
    - it meets the trading company conditions in that it must exist only for a qualifying trade and the following are non-qualifying:
        - dealing in land, shares, securities or other financial instruments
        - dealing in goods otherwise than via a normal retail or wholesale trade
        - banking, insurance, money-lending, debt-factoring, HP or other financial activities
        - leasing
        - receiving royalties or licence fees
        - legal or accountancy services
        - property development
        - farming or market gardening
        - forestry or timber production
        - shipbuilding, coal or steel production
        - operating or managing hotels or comparable establishments
        - operating or managing nursing or residential care homes
        - generating or exporting electricity or making electricity generating capacity available
        - generating heat
        - generating any other form of energy
        - producing gas or fuel
    - it meets the financial health condition
    - the qualifying business activity is being carried on by the company or a qualifying 90% subsidiary
    - it is unquoted
    - it meets the control and independence condition
    - it meets the gross asset test
    - it meets the company employee test
    - the company's subsidiaries are all qualifying

- the general requirements are met in respect of the relevant shares:
    - the total amount of relevant investments must not exceed £12m or £20m if it is a knowledge intensive company with the annual amount being £5m
    - the money must be used for the purposes of the qualifying activity with the added proviso since 18 November 2015 that they are being issued to promote business growth and development, within 2 years of the issues
    - the shares are issued in the initial investing period (being 7 years or 10 years for a knowledge intensive company from the first commercial sale) unless special conditions are met
    - the relief must be claimed
    - there must be no pre-arranged exits
    - there must be no tax avoidance or disqualifying arrangements
- the 'risk-to-capital' condition is met which is that both of the following apply
    - it is reasonable to conclude that the issuing company has objectives to grow and develop its trade in the long-term and
    - it would be reasonable to conclude that there is a significant risk that there will be a loss of capital of an amount greater than the net investment return

Advance assurance

Companies that are seeking subscriptions under the SEIS or EIS may seek an assurance from HMRC that a prospective investment is likely to be eligible before issuing the shares. The service is discretionary and non-statutory. There is no requirement to obtain advance assurance and HMRC will not engage in protracted correspondence if there is a difference of opinion. There is no appeal process if HMRC will not give the assurance requested.

Assurance is given in respect of a particular issue of shares, in the circumstances set out in the application and will not apply if the circumstances change or there is a change in the legislation. It is not assurance as to the availability of relief to any particular investor. HMRC will not give assurance on speculative applications.

Knowledge intensive companies

1. Knowledge intensive companies are allowed to have more generous provision under EIS. They are companies which are carrying out significant levels of research and development. They can raise more finance (£10m in a 12 month period and £20m in a lifetime compared to £5m and £12m respectively for other companies), be up to 10 years old (rather than 7) and have up to 499 full time equivalent employees (rather than 249).

It is necessary that the company has prior accounting periods for which it is required to have filed statutory accounts with Companies House where it has sufficient levels of R&D expenditure.

The R&D expenditure must be:

- At least 15% of operating costs in one of the last three years or
- At least 10% of operating costs in each of the last three years.

The company must also then be able to show that either:

- The majority of its business will be derived from the IP being created or
- That its workforce has sufficient qualifications which are relevant to the R&D.

Growth and development and the risk-to-capital condition

These are new requirements designed to focus away from lower risk investments. These are gateway tests and are arguably highly subjective. Money must be being raised for growth and development and the investment must carry a significant risk that the investor will lose more capital than they gain as a return.

Growth and development is not defined in the legislation and HMRC take the following as generic indicators of growth:

- Increasing revenues over time
- Increasing a company's customer base
- Increasing the number of employees

The money may not be used primarily to cover pre-existing day to day expenditure.

The risk-to-capital condition is a principles-based condition that depends on taking a reasonable view as to whether an investment has been structured to provide a low-risk return for investors. The condition is designed to deter tax planning. The problem lies in the fact that HMRC are challenging a number of cases, often picking on phrases in business plans and shareholders agreements.

Pitfalls

There are many reasons why SEIS or EIS relief may not be available. They include:

- Shares must be paid up in cash at the time of issue (since the purpose is to raise funds for the business). Shares issued on the conversion of loans will not qualify.
- Companies can raise funds from both SEIS and EIS but SEIS shares must be issued at least one day before any EIS shares
- In order that the investors bear risk, there are a number of anti-avoidance measures one of which is the pre-arranged exit rules. These are not only about exits but care needs to be taken that at the time of the share issue there are no arrangements:
    - For the disposal of any shares in the company;
    - For the disposal of a substantial part of the assets of the company; and

- For the protection against the risks of making the investment.

  HMRC have for the last six years or so considered that the anti-dilution rights are a protection

- The age requirement (7 or 10 years) is linked to the earliest first commercial sale of the company or a subsidiary or any person who has carried on the business although there are two other possibilities
  - It has previously raised State aid risk capital and is raising further funds for the same business activities (although HMRC have been known to challenge this)
  - The company is raising funds of at least half the average turnover of the last five years and will employ those funds solely to enter a new product or geographic market
- Ceasing to trade causes loss of EIS status unless the reason for cessation is as a result of administration or liquidation for bona fide commercial reasons
- Shares issued must remain eligible shares
- The company cannot repurchase any of its share capital

Abingdon Health Ltd [2016] TC05525

In this case, the question being considered was whether the EIS shares had preferential rights as there was a type of growth shares issued to management which meant they could only receive capital above a hurdle. It was found that the fact that a winding up which would trigger the preferential rights associated with the EIS shares was highly unlikely but that this was irrelevant since a preferential right is either present or absent. The legislation simply requires the shares to carry preferential rights, not that they are likely to be exercised.

Flix Innovations Ltd v Revenue and Customs [2016] BTC512

This was a similar case to the Abingdon case but in this case there were deferred shares. The EIS shares ranked about the deferred shares for repayment capital on a winding up so they had a preferential rate. In this case, the irrelevant point is that the deferred shares were issued for commercial reasons.

GDR Food Technology Ltd [2016] TC05219

This case involves a more esoteric point which is not covered above. A company must claim SEIS before EIS (i.e. once an EIS claim has been made, you cannot claim for SEIS). Shares were issued in this company but the agents erroneously issued an EIS1 compliance certificate and not an SEIS1 form. This was found to be determinative in identifying the type of shares issued.

Bell [2016] TC04969

This case highlights the need to be careful about meeting of the relevant conditions. You cannot get EIS relief if you are a director, unless it is within three years within a previous issue of shares which qualified. They got the dates wrong and it was outside the relevant period so EIS relief was not available.

Robert Ames v HMRC [2018] UKUT 0190

Robert Ames did not claim income tax relief on his EIS shares as he had no taxable income so there was no benefit to be derived from doing this. However, he wanted to claim the corresponding CGT disposal relief when the shares were sold for a considerable profit. HMRC refused to allow the disposal relief due to the failure to make the IT claim. An important point to note!

Oxbotica Ltd [2018] TC06538

This company only issued £316 of share capital – it was a spin out tech company from Oxford University. HMRC argued that this was not meaningful enough to be of any use in the business. But the FTT found no minimum investment is required.

Contributed by Ros Martin

Capital Taxes

Business disposal with attached goodwill? (Lecture P1167 – 13.31 minutes)

Having regard to the remarkable events of the recent cricketing summer, the speaker's eyes were instinctively drawn to the First-Tier Tribunal's decision in The Leeds Cricket Football & Athletic Company Ltd v HMRC (2019) which concerned the sale of Headingley Cricket Stadium towards the end of 2005.

For many years, the company in question had owned the freehold of Headingley that it leased to Yorkshire County Cricket Club (YCCC). On 30 December 2005, the freehold was sold to YCCC, together with various commercial enterprises. In addition to its ownership of the property, the company had been carrying on three distinct business activities:

1. hospitality;

2. advertising; and

3. catering.

The hospitality operation consisted of selling corporate hospitality packages to business customers and looking after the guests throughout the day. The advertising operation involved selling advertising packages for boards and hoardings at the ground – there was a significant overlap here with the hospitality business. The catering operation employed 19 full-time staff to provide meals and refreshments to visitors to the stadium on match days. After the sale, the company gave significant assistance to YCCC to ensure a smooth handover of the businesses – this included the transfer of relevant client details. The catering business was licensed back by YCCC to the company in return for an annual fee.

The principal question before the First-Tier Tribunal was whether these operations constituted a trading business carried on by the company prior to the sale. If so, the disposal of the land and the related goodwill gave rise to a capital gain which would be eligible for rollover relief.

The parties involved certainly thought that this was the case, given that the sale contract:

- included a specific provision that the property and the goodwill of the businesses were to be sold; and

- defined the applicable goodwill in great detail.

There was also a deed of assignment of the goodwill pursuant to the contract.

HMRC argued that the sale was not a disposal of a business (plus any associated goodwill) but instead was merely a transfer of land with attached income streams. This gave rise to different tax consequences – for example, rollover relief would not be available. HMRC said that the income streams were not capable of existence without the land and that no business was being carried on. So there was no goodwill (the Special Commissioner in Balloon Promotions Ltd v Wilson (2006) emphasised that 'goodwill cannot subsist by itself but must be attached to a business').

The judges rejected these arguments. They held that the company had clearly been carrying on a business. The activities satisfied the tests devised by Berner J in Ramsay v HMRC (2013) since they represented a serious undertaking which was earnestly pursued and which was conducted in accordance with recognised business principles. The company did transfer the property and the business (including the goodwill associated with the business). The transaction was not simply a transfer of land with attached income streams. The goodwill was not subsumed into the value of the property. It had been generated over time by hard work and effort. The business had an established client base and reputation that distinguished it from similar newly set up enterprises. Furthermore, the business operations did not have a connection with Headingley per se, given that YCCC also played cricket at other grounds in the county.

HMRC's contention that there was no business capable of transfer and that there was no goodwill in any event is reminiscent of their arguments advanced in Villar v HMRC (2018) relating to the goodwill of a professional practice – another case which they lost. As one commentator astutely observed:

'I think it would be interesting for HMRC to attend a meeting where somebody (I mean a real person) is trying to buy a business and let them see the reaction when the purchaser refuses to pay anything for the goodwill on the grounds that no goodwill exists. They might be in for a surprise.'

Contributed by Robert Jamieson

Entrepreneurs' relief and non-trading (Lecture P1168 -17.22 minutes)

Given the value of entrepreneurs' relief, there are constant fears that this CGT benefit may be withdrawn on the ground that its expense is becoming too costly for Government. Hopefully, this will not transpire (especially in the light of the changes made by FA 2019), but, while the relief continues, the relevant conditions are being, in the words of one commentator, 'regularly stress-checked by HMRC'.

The recent case of Potter v HMRC (2019), which was heard by the First-Tier Tribunal, raises two questions of practical interest in connection with this important relief:

1. When does a diminution or temporary suspension of trading activities fall to be treated as a cessation of those activities?

2. In what circumstances can investment activities lead to a loss of entrepreneurs' relief?

The taxpayer (P) was a shareholder director in a company called Gatebright Ltd (G Ltd) which traded as a broker on the London Metal Exchange. The deals with which G Ltd was involved were complex and could take months to complete. They depended heavily on finance being available. Following the financial crash in 2008, banks withdrew credit lines, there was little credit available elsewhere and no real appetite for risk-taking among P's prospective clients. The volume of trades declined dramatically.

G Ltd was a successful business which had built up retained profits in excess of £1,000,000. In order to safeguard these reserves, P used £800,000 to purchase two six-year investment bonds which matured in November 2015. The capital was locked up over this period, but the bonds paid annual interest of £35,000 which appears to have been distributed to P and his wife (who was also a shareholder) by way of dividend. The remaining £200,000 was kept as working capital for the company. P told the First-Tier Tribunal that he was not doing this in order to 'sit back and live off the income' and he emphasised that what he wanted was to preserve the current position until another trading opportunity arose.

G Ltd's last invoice was issued in March 2009. After that, P kept working his network of contacts to find new business without success, but, after suffering some ill-health and various other misfortunes (including losing his regulatory licences and having his house ransacked by a gang of local youths), he decided to call it a day when he again had to be admitted to hospital in June 2014. G Ltd went into voluntary liquidation in June 2015 and this was completed on 11 November 2015.

HMRC refused to accept that P and his wife were entitled to entrepreneurs' relief for 2015/16 in relation to the CGT liability occasioned by the voluntary liquidation, using the argument that G Ltd was not a trading company during the requisite period.

By virtue of S169I(2)(c) TCGA 1992, a capital distribution made during a winding up can benefit from an entrepreneurs' relief claim, given that this is treated as a disposal of an interest in shares under S122(1) TCGA 1992. The relief is subject to the various conditions in S169I(7) TCGA 1992 being met. Prior to FA 2019, these were:

(i) The company must have been a trading company throughout the 12 months prior to the cessation of its trade;

(ii) Throughout the 12-month period before the company ceased to trade, the shareholder receiving the capital distribution must have:

- held 5% or more of the company's ordinary share capital and voting rights; and

- served as an officer or employee of the company.

(iii) The capital distribution must be made within a period of three years following the cessation of trade (note that HMRC have no discretion to extend this time limit).

In other words, in order to satisfy these conditions, G Ltd's trade must not have ceased before 12 November 2012 and the company must have been a trading company for at least 12 months ended on 12 November 2012 (or any later date up to 11 November 2015).

HMRC's contention was that, because G Ltd issued no further invoices after March 2009, it had ceased to be a trading company outside the three-year period referred to above. Accordingly, entrepreneurs' relief was not due.

In this context, a trading company is a company 'carrying on trading activities whose activities do not include to a substantial extent activities other than trading activities' (S165A(3) TCGA 1992). As is well known, 'substantial' has been unilaterally understood by HMRC to mean 'more than 20%'.

One argument is that G Ltd was carrying on trading activities throughout the required 12-month period. The term 'trading activities' is defined in S165A(4) TCGA 1992 as follows:

'"Trading activities" means activities carried on by the company:

- in the course of, or for the purposes of, a trade being carried on by it;
- for the purposes of a trade that it is preparing to carry on;
- with a view to its acquiring or starting to carry on a trade; or
- with a view to its acquiring a significant interest in the share capital of another company that:

  - is a trading company or the holding company of a trading group; and

  - if the acquiring company is a member of a group of companies, is not a member of that group.'

The First-Tier Tribunal concluded that, although G Ltd may not actually have been carrying on any trade after it issued that final invoice in March 2009, the company could be considered to be 'preparing to carry on its old trade once the economic environment permitted it'. G Ltd had therefore continued to be a trading company.

Interestingly, the taxpayer's skeleton argument expressed the position slightly differently:

> *'If the shop is open but nobody buys anything, it does not change its business classification.'*

The judge went on to comment on this line of argument:

> 'That is true up to a point. If there comes a time when it is clear that there is no realistic possibility of the efforts to drum up new business leading to future trading transactions, it can no longer be said that the trading activities are being carried out for the purposes of a trade or for the purposes of a trade that the company is preparing to carry on. At that point, the company must cease to be a trading company.
>
> Applying these principles to the present case, I am of the view that, in November 2012, matters had not reached that point. It would still be reasonable for (P and his wife) to believe that their continued efforts would ultimately result in new business. They could not have known of the future health problems which would further disrupt the continuity of the negotiations for deals and ultimately cause them to cease their efforts and dissolve the company.'

Given that the First-Tier Tribunal had accepted that G Ltd was still a trading company in November 2012, we must now examine whether it was disqualified from being a trading company because its activities represented – to a greater extent than 20% – activities which were not trading activities. In other words, was G Ltd carrying out substantial investment activities?

HMRC's argument was that, even if G Ltd was carrying out trading activities from the time when the company made the two bond investments (which they denied), most of the assets of the company and virtually all of its income were derived from the bonds. How could this be anything other than substantial?

This line of attack was defused by the First-Tier Tribunal's observation that the CGT legislation focuses on 'activities', i.e.. what the company actually did. The judge said:

> 'Once the company had put its money into the bonds, it did not, indeed could not, do anything else in relation to them for six years until they matured. There were no investment activities. The company was locked into the bonds during their term and the directors did not do anything in relation to them.'

The conclusion, therefore, was that, when one stands back and looks at the activities of the company as a whole, its activities were entirely trading activities directed at reviving the company's trade and putting it into a position to enable it to take advantage of the gradual improvement in global financial circumstances.

The appeal was allowed: P and his wife were entitled to claim entrepreneurs' relief on the disposal of their respective holdings in G Ltd.

The question of the extent to which investments can deprive a company of its trading status is one which arises not infrequently. The First-Tier Tribunal correctly pointed out that the legislation focuses on 'activities', and not on assets or income. Thus it is the company's 'activities' which must be examined. Of course, some investments require more activity than others. For example, keeping a quoted share investment portfolio under constant review and actively managing it may well amount to a substantial part of the activities of a company which also carries on a trade. However, the decision in Potter v HMRC (2019) undoubtedly gives support to the view that a trading company may be able to make a significant long-term passive investment without endangering its trading standing for entrepreneurs' relief purposes.

Contributed by Robert Jamieson

Entrepreneurs' relief and life interest trusts **(Lecture P1169 – 12.45 minutes)**

If a business asset such as a shareholding in a family trading company is held in a discretionary or accumulation trust, a subsequent sale of those shares by the trustees can never qualify for entrepreneurs' relief. The trustees' CGT will always be at the rate of 20% (or 28% for tax years prior to 2016/17).

However, the sale of shares held in a life interest trust where there is a 'qualifying beneficiary' (as defined in S169J(3) TCGA 1992) can attract this valuable relief provided that the life tenant is prepared to surrender all or part of his personal entrepreneurs' relief entitlement, in which case the 10% rate will be in point.

In order for there to be a 'qualifying beneficiary' where a pre-FA 2019 sale of shares is concerned, three separate conditions set out in S169J(4) TCGA 1992 must be satisfied throughout a period of 12 months ended in the three years up to the date of the trustees' disposal:

- the company to which the shares relate must have been a trading company or the holding company of a trading group;

- the life tenant must have been an officer or employee of the company (or, where the company is a member of a group, of any other member of its group); and

- the life tenant must have personally held at least 5% of the company's ordinary share capital and voting rights.

It should be noted that there is no requirement for the trustees themselves to pass the 5% test.

Where the requirements above are satisfied and where the life tenant is willing to assign the benefit of all or part of his lifetime entrepreneurs' relief limit to the trustees, they can claim entrepreneurs' relief of up to £10,000,000 and the trust gain will only be chargeable at 10%.

As a result of what has always been assumed to be an oversight, there is no rule in TCGA 1992 which states that the life tenant must have been a 'qualifying beneficiary' for at least a 12-month period. Thus it has been possible for, say, a discretionary trust to 'parachute in' a suitable beneficiary as a life tenant for a short period, during which time the shares are sold. Because the trust (or the relevant part of it) has been converted to a life interest one, it now meets the conditions set out in S169J TCGA 1992 and so an appropriate claim can be made. If the life interest is subsequently revoked, this does not cause the claim to fail.

At a meeting of the Capital Taxes Liaison Group in 2017, the minutes of which were published by the CIOT on 19 September 2018, HMRC indicated that, in their opinion, such a planning ploy did not work. This followed, they said, from the words of the statute which is written in terms of a 'qualifying beneficiary', and not simply of an individual. Interestingly, HMRC have previously given advice with contradicted this standpoint. However, they were saying in 2017 that the technical adviser who had provided that guidance was wrong. A senior HMRC official confirmed that he had asked his technical colleagues to withdraw the advice and clarify the situation, but there was no mention of the fact that, if and when they did that, it would surely be necessary for HMRC to specify an effective date from which the corrected interpretation would apply to trust disposals.

In the event, this may all prove to have been unnecessary. On 6 August 2019, the First-Tier Tribunal published Judge Guy Brannan's unequivocal decision in The Quentin Skinner 2005 Settlements v HMRC (2019), in which he categorically stated that the relevant part of TCGA 1992 did not have the meaning contended by HMRC.

The facts of this case were as follows:

- Three beneficiaries had been given life interests in three settlements on 30 July 2015 and then on 11 August 2015, shares in a trading company called DPAS Ltd were transferred to the settlements.

- DPAS Ltd had been the personal company of each of the three beneficiaries since 2011 under the pre-FA 2019 definition of this term in S169S(3) TCGA 1992.

- Each of the three beneficiaries was an officer of DPAS Ltd.

- On 1 December 2015, the trustees disposed of the shares in DPAS Ltd.

- On 31 January 2017, the trustees (together with each of the three beneficiaries) made claims for entrepreneurs' relief in accordance with the provisions set out in S169M TCGA 1992.

Although HMRC refused leave to make such claims, this rejection has been overturned by the First-Tier Tribunal. It will be interesting to see whether HMRC seek to take this case to the Upper Tribunal. Either way, a change in the wording of the statute is likely.

Contributed by Robert Jamieson

Trading loan or investment? **(Lecture P1166 – 17.11 minutes)**

Summary – Without a loan used for trading purposes, there was no qualifying loan and the loss was disallowed.

On 25 February 2010, Steven Flashman made a payment of £130,000 to Emerging Markets Investment Ltd but by September 2011, he was informed that the company had run into financial difficulties. On 23 June 2013 Mr Flashman received £30,000 as repayment of £130,000 that he had advanced three years earlier.

Steven Flashman argued that the £130,000 paid to Emerging Markets Investment Ltd was a qualifying loan and that, he had suffered a loss of £100,000 His 2014/15 tax return was filed on time, showing net capital gains of £264,314 after deducting the £100,000 loss.

HMRC argued that no loss relief was available under s253 TCGA 1992 as the monies had not been loaned for the purpose of a trade but rather, they were an investment. A closure notice was issued on 13 October 2017.

Steven Flashman appealed.

Decision

The First Tier Tribunal concluded that two companies, EMI Wealth Ltd and Emerging Markets Investment Ltd (companies whose names were used interchangeably during communications), were not engaged in any trading activity. Their primary role was that of marketing activity and to propose a scheme to potential investors and then to sign up those investors who were attracted by the potentially high returns.

The Tribunal concluded that Mr Flashman did not make a trading loan to Emerging Markets Investment Ltd (or to EMI Wealth Ltd) and so the loss of £100,000 was disallowed.

Mr Steven Flashman v HMRC (TC07419)

PPR and ESC D49 (Lecture P1166 – 17.11 minutes)

Summary – The First Tier Tribunal had no jurisdiction to consider HMRC's refusal to apply an extra statutory concession and so the appeal was struck out.

On the face of it, this case concerned the availability of Private Residence relief. However, the real issue was whether or not a Tribunal has jurisdiction to consider HMRC's refusal to apply an extra statutory concession.

Andrew and `Melanie White bought four interests in land in 2001 and 2002 which they converted into a single dwelling. They eventually took up residence in the property, some time between September 2003 and November 2003.

HMRC argued that the date of acquisition of a property acquired in stages starts from the date of the first unconditional contract and so, in this case, on 11 June 2001. As the couple did not occupy the completed property until September or November 2003, it was outside the maximum two-year time limit permitted by ESC D49 as deemed occupation and so PPR relief was denied.

It was common ground between the parties that the facts of this case took it outside the strict provisions of the legislation but Andrew and Melanie White appealed against HMRC's decision not to apply ESC D49 to the gain made on the disposal of their property.

Decision

The First Tier Tribunal stated that the statutory provisions did not permit any delay in the commencement of occupation if full principle private residence relief was to be granted.

Before the Tribunal could consider whether or not the provisions of ESC D49 should be applied to the facts of this case, they stated that they needed to decide whether or not they had jurisdiction to consider it. The Tribunal stated that their jurisdiction is statutory and they could see nothing in the legislation that required or permitted them to consider ESC D49 and so, as a result, they struck out the appeal in accordance with Rule 8(2)(a) of The Tribunal Procedure (First-tier Tribunal)(Tax Chamber) Rules 2003 on the grounds that the Tribunal did not have the jurisdiction to consider the appeal.

Andrew White and Melanie White v HMRC (TC07434)

Off plan PPR (Lecture P1166 – 17.11 minutes)

Summary – It seems that we have come full circle with the Court of Appeal deciding that Mr Higgins was correct when arguing that ownership for private residence relief purposes starts from completion, rather than the date of exchange.

Detailed facts of the case can be found in our November 2018 notes, where Steve Sanders took a look at the Upper Tribunal's decision to overturn the First Tier Tribunal's decision in favour of HMRC. In summary, Mr Higgins entered into an 'off-plan' contract in October 2006 but had no right to access the building while the flat was under construction. After delays to the development due to funding issues, the apartment was finally finished in December 2009 and the contract legally completed on 5 January 2010 after which point Mr Higgins had a legal right of occupation. He moved in at that time and occupied it as his main residence until he sold it two years later.

The First Tier Tribunal found that the period began when legal title to the property and a right of occupation occurred. The Upper Tribunal disagreed finding that the period of ownership for CGT began from exchange of contracts and therefore started on 2 October 2006 when unconditional contracts were signed with the developer.

Mr Higgins appealed to the Court of Appeal

Decision

The Court of Appeal noted that, when buying a property, it was normal practice for there to be a period of time between exchange and completion. They considered it to be extremely unlikely that Parliament had intended the PRR rules to result in the typical homebuyer being denied PPR relief for this period of time. Adopting HMRC's argument, whereby the period of ownership for PPR relief runs from exchange of contract would mean that very few people buying a new home would qualify for 100% PPR relief.

The Court of Appeal found nothing in legislation stating that a short gap between contract and completion could be ignored for PPR relief purposes. However, they found that it was not necessary to measure the period of ownership for PPR relief by the statutory deemed times of acquisition and disposal (s28 TCGA 1992). Instead, the term 'period of ownership' for PPR purposes should be given its ordinary meaning. The period of ownership should therefore begin from the date that the purchase was completed. In this case that was from 5 January 2010.

Higgins v HMRC [2019] EWCA Civ 1860

Exempt gift to Jersey trust **(Lecture P1166 – 17.11 minutes)**

Summary - Restricting the gifts to charities IHT exemption to UK charities goes against the EU directive on the free movement of capital.

In 2007, Beryl Coulter, a Jersey resident left her residuary UK estate on trust for the purpose of building homes for elderly residents in Jersey, so for charitable purposes.

HMRC argued that the legacy was not a transfer to 'a trust established for charitable purposes' because s23 IHTA 1984 required it to be established in the UK. The trust was established under Jersey law and so was not a UK charity.

HMRC charged some £600,000 IHT on the legacy, holding that it was not a gift to a charity. The High Court and Court of Appeal agreed with HMRC that the charity exemption was limited to UK charities, though had this been a UK trust it would have been available.

The executors argued that distinguishing between Jersey and UK trusts in this way was contrary to EU law on the free movement of capital. This forbids restrictions on the free movement of capital between EU member states, and between member states and third countries.

Decision

However, Jersey is not part of the UK. The Supreme Court agreed with the Court of Appeal that Jersey should be regarded as a third country for the purpose of a transfer of capital from the UK. This meant that the EU rules on the free movement of capital applied to transfers between the UK and Jersey. S23 IHTA 1984 restricted the relief to trusts governed by UK law and that was incompatible with EU law and could not be justified on administrative grounds. Consequently, they found that the trust did qualify for relief under s 23.

The appeal was allowed.

Routier & Anor v HMRC [2019] UKSC 43

Growth shares in family investment businesses (Lecture B1168 – 7.39 minutes)

What are growth shares?

Growth shares are a type of alphabet share which may or may not have voting or dividend rights. They will however, always carry capital rights BUT only when the company's value exceeds a pre-determined amount, known as the hurdle amount.

This pre-determined amount is normally what the company is worth today – or possibly a little more so as to ensure that the shares have no "hope" value on issue.

Incentivising key employees

Historically, growth shares have been used to incentivise key employees to help grow a company and are considered to be alternatives to approved share schemes such as EMI.

When this new class of shares is created, employees buy them at their low market value at issue, normally with no dividend or voting rights. Over time, assuming that the company increases in value above the hurdle amount, the employees will share in the increased value above the hurdle.

Growth shares often have forfeit provisions so that if an employee leaves the company the provisions bite.

IHT planning

Family investment companies often use alphabet growth shares as an IHT planning option.

Let's consider a family investment company currently worth £2 million with shareholders in their mid-50s. In twenty plus years the company could be worth much more. As an investment company business property relief would not be available and so IHT could be a major issue.

Giving away the company early may not be an option, especially if the shareholders have built up the company with a view to it providing them with income in retirement.

Growth shares could be issued with a hurdle value of say £2.5 million, giving the share owners rights to capital when the company's value exceeds £2.5 million. These shares could be issued with or without voting and dividend rights. If they do have dividend rights then they should be independent of the main shares.

HMRC would be hard pushed to argue that these shares have any current day value. The company is worth £2 million and the shares only come into play when the company's value exceeds £2.5 million.

These growth shares can be issued to the parents and then gifted to their children or issued direct to the children. The shares have no initial value.

On death of the parent(s) any growth in the company value would be attributed to the growth shares and as such would be outside the parents' death estate as the shares would not be owned by them.

In summary the parents retain control of their company during their lifetime but freeze their IHT exposure at the approximate value of the company when the growth shares are issued.

Divorcing children

Where concerns exist about wealth potentially being passed to a child's spouse should they divorce, forfeit provisions may be included to prevent this happening.

Property incorporations

Growth shares are also used on property incorporations. This could be in conjunction with preference shares as incorporation relief is not dependent on the type of shares issued to the sole trader/partnership.

Using an expert

Secretarial agents are used to dealing with the creation of alphabet and growth shares. We would however be well-advised to seek advice from a share scheme specialist where we have clients that might benefit from such share issues.

Brief guide to ATED **(Lecture B1169 – 16.28 minutes)**

The Annual Tax on Enveloped Dwellings (ATED) is actually one of a package of measures which affect residential properties valued in excess of the threshold amount which are 'enveloped' i.e. held by non-natural persons.

The measures are:

- The ATED charge itself;
- A 15% SDLT charge on purchase;
- A CGT charge on disposal.

The CGT charge is longer be relevant from 1 April 2019 due to the introduction of wider measures taxing non-resident persons.

It is important to acknowledge that these are anti-avoidance provisions which often work in a very punitive way but this was in response to widespread avoidance of tax, particularly SDLT, by use of overseas property holding structures and HMRC are unapologetic about the way the provisions work. We are also seeing an increase in the compliance work being done by HMRC on ATED, mainly in relation to SDLT.

ATED's introduction

By way of context the following is an extract from the HMRC manuals explaining why ATED and the linked duties were introduced:

At Budget 2012 the Government announced a package of measures to counter arrangements to avoid tax by 'enveloping' high value residential property in the UK.

An example of the sort of arrangements targeted is:

- A wealthy individual Z is resident, but not domiciled, in the UK and is chargeable on the remittance basis. Z owns 100% of the shares in Company Y, which is not UK resident.

- Z arranges for company Y to buy a residential property in London for £5 million. Company Y has no other assets and the shares are worth £5 million. The property is 'enveloped' in company Y.

- After a few years the property has increased in value to £8 million, and so have the shares in Y. Z sells the shares for £8 million to another UK resident, non-domiciled individual X.

- Z has effectively realised a profit of £3 million on the London property, but –

    - *Z can ensure the gain on the shares in Y is tax-free by not remitting the gain to the UK;*

    - *X will not be liable to stamp duty land tax (SDLT) on acquiring the shares in Y, the 'envelope' sheltering the London property;*

    - *X will be able to repeat the process if and when X sells on the shares in Y.*

The basic principles of ATED

The chargeable interests

The basic charge relates to enveloped residential property, but the legislation is not expressed in quite such a straightforward way. There are exceptions from the basic charge where certain conditions are met.

ATED is charged where the following conditions are met:

- There is a chargeable interest which is a single-dwelling interest
- Beneficially held by a company, partnership with a company member or collective investment vehicle
- Which has a taxable value over the threshold.

It is payable for each year, or part year, for which the conditions are met.

ATED commenced on 1 April 2013 and the threshold at that time was £2m. This threshold reduced to £1m with effect from 1 April 2015 and further to £500,000 with effect from 1 April 2016.

Chargeable interests

A chargeable interest in land is defined as:

- An estate, interest, right or power in or over land in the UK or
- The benefit of an obligation, restriction or condition affecting the value of any such estate, interest, right or power.

This is very similar to the scope of SDLT.

This means in England, Wales and Northern Ireland chargeable interests include freeholds, leaseholds, undivided shares in land, rights in or over land such as easements, rent charges, the right to receive rent and the benefit of a restrictive covenant. In Scotland, it will include ownership of land, other heritable rights in or over land, the tenant's interest under a lease of land, a servitude and a life rent.

ATED applies to UK property only excluding the Isle of Man or the Channel Islands (but including dwellings or islands within the 12-mile limit).

Single-dwelling interest

This is an important principle as it is vital to be able to identify the entity which is potentially chargeable to ensure that the value is correctly ascertained.

It is a chargeable interest which consists of a single dwelling. Where a chargeable interest is made up of two or more dwellings and/or dwellings and non-residential land, then each interest is treated separately for the purposes of ascertaining liability to ATED.

A dwelling is a building or part of a building which:

- Is used or suitable for use as a single dwelling or
- Is in the process of being constructed or adapted for such use.

Land that is, or is at any time intended to be, occupied or enjoyed with a dwelling as a garden or grounds is taken to be part of that dwelling at that time.

Whilst this is, on the face of it, a relatively simple definition, there are some complications to this definition.

- Mixed use property will need to be separated out. If a dwelling is part of a larger property, only the residential part is subject to ATED. This may be easy in some cases. For example, a shop with a flat over can be easily separated out into its constituent parts. However, a large residential property which is part of an agricultural holding might be more difficult as it could be problematic to work out where dwelling starts or finishes.

- Since the definition looks at whether a property is suitable for use as a dwelling, it is irrelevant that a building is temporarily unavailable for use as a dwelling for any reason.

- If two or more chargeable interests that are single-dwelling interests in the same dwelling are held by the relevant person, those separate interests are treated as if they constitute one single-dwelling interest. This will be a rare situation.

- If there is more than one dwelling in a property (i.e. a main dwelling and an associated dwelling standing within the garden or grounds of the main dwelling) and they are owned by a person connected with the chargeable person, they are added together and looked at as a single dwelling where there is no separate access. Two dwellings in the same dwelling they are treated as one dwelling for ATED purposes where there is private access between them. This would apply to property in a terrace, semi-detached houses or flats in a single building.

- If two chargeable interests that are single-dwelling interests in the same dwelling are held separately by a non-natural person (NNP) and a person connected with that NNP, those separate interests are treated as if they were both held by the NNP. Where the NNP is a company and the person connected with the NNP is an individual, there is an exception which means the NNP is not treated as entitled to the individual's interest but this depends on the value of the relevant interests.

- Flat management companies cause some complications where the company owns the freehold of a block of flats whose shareholders are lessees of the flats in the block. There was concern that the aggregation provisions outlined above would apply on the basis that the individuals acting together control the company so the company and the leaseholders would be connected persons. However, HMRC have confirmed that the company would be run according to a comprehensive shareholders' agreement rather than being under the control of ongoing shareholders.

There are some specific exclusions from the definition of 'dwellings' being:

- Residential accommodation for school pupils;

- Residential accommodation for students other than halls of residence;

- Residential accommodation for members of the armed forces;

- A home or other institution that is the sole or main residence of at least 90% of its residents;

- A home or other institution providing residential accommodation for children;
- A hall of residence for students in further or higher education;
- A home or institution providing residential accommodation with personal care for persons in need of personal care by reason of old age, disablement, past or present dependence on alcohol or drugs or past or present mental disorder;
- A hospital or hospice;
- A prison or similar establishment; and
- A hotel or inn or similar establishment.

This is slightly different from the way in which this applies for SDLT purposes.

Valuation of single-dwelling interest

The valuation of land for ATED purposes is not very logical. At the point at which ATED was introduced, being 1 April 2013, any existing dwellings had to be valued as at 1 April 2012. The value then has to be re-evaluated every 5 years from that initial date. The value that we are looking at in all cases is the market value, being the price that could be expected to be achieved between a willing buyer and a willing seller.

This is true for all property held at that date even if the value was not sufficient to bring the property within the charge immediately.

Property held at that time will have been revalued at 1 April 2017 with the revaluation having an impact from 2018/19 onwards.

The date of a substantial acquisition of a chargeable interest, or the substantial disposal of a chargeable interest is also a valuation date. Substantial in this context means by reference to chargeable consideration of £40,000 or more.

Where a new dwelling is being or has been constructed, the valuation date is the earlier of the completion day (being the day on which the dwelling is treated as having come into existence for council tax purposes or equivalent) or the day on which the dwelling is first occupied.

Those to whom the charge applies will need to self-assess the value of the property. There is no obligation for the value to be established by a professional valuer but, of course, HMRC can challenge any ATED return and this includes being able to challenge the valuation. This has given some problems for property in places like London where the value has risen significantly.

It is important to remember though that it was the valuation of the property in 2012 which was initially relevant so there will be property which is demonstrably valued at over £500,000 now but was not in April 2012 so will not come into the regime until 2018. This will only apply if the property was held at 2012 since anything bought since then will be valued according to the purchase price.

Example

A property is valued at £750,000 on 1 April 2012. It is valued at £1.3m by 1 April 2015 and £2.2m by 1 April 2017.

Under the ATED legislation as originally enacted by FA 2013 (applicable only to properties with a value of £2m plus), there would have been no ATED before 1 April 2018.

The introduction (by FA 2014) of the reduced 'threshold amount' of £1m from 1 April 2015 would appear to bring it into charge from that date, but we are still working on the April 2012 value so it actually does not come into the charge until 1 April 2016. An ATED charge of £3,500 will apply for the 2016/17 year and 2017/18 (see below for rates). However, for 2018/19 it will move into a different band as its value at 1 April 2017 will be relevant.

It is possible for a taxpayer to ask HMRC to agree the valuation before the return is submitted by asking for a Pre-Return Banding Check. However, this is only available for those who believe that their property valuation falls within a 10% variance of a banding threshold. In fact, HMRC will only agree to the banding proposed and not comment on any formal valuation. It is also stressed by HMRC that this confirmation cannot be used for any other purpose by the taxpayer. HMRC can still also enquire into a return which is based on the PRBC.

Chargeable persons

The legislation applies to properties held by companies, partnerships with corporate members and collective investment schemes. Company and partnership are defined in FA2013 and the latter includes both regular partnerships and LLPs. A collective investment scheme is one which meets the definition in Financial Services and Markets Act 2000.

The legislation specifies who is actually liable to pay the charge and it depends on who meets the ownership condition:

- Where a company meets the ownership condition, the company is liable to the charge;

- Where a partnership meets the ownership condition, the responsible partner is liable to the charge being all the persons who are members of the partnership on the first day of the chargeable period on which the partnership meets the ownership conditions with all partners being joint and severally liable to pay the tax;

- Where a unit trust meets the ownership condition, the trustee of the scheme is liable to the charge;

- Where an open-ended investment company meets the ownership condition, the body corporate referred to in the FSMA provisions is liable to the charge;

- Where any other type of collective investment scheme meets the ownership condition, the person who has day-to-day control over the management of the property is liable to the charge.

There are specific provisions where interests are jointly held with others.

The charge

ATED is levied according to a banding system based on the value of the dwelling. The current charges are as follows (with last year's figures also shown):

Value of property	2019/20 charge	2018/19 charge
£500,001 to £1m	£3,650	£3,600
£1,000,001 to £2m	£7,400	£7,250
£2,000,001 to £5m	£24,800	£24,250
£5,000,001 to £10m	£57,900	£56,550
£10,000,001 to £20m	£116,100	£113,400
Over £20m	£232,350	£226,950

These charges apply for the whole year but can be pro-rated where the charge applies for only part of the year. So if a property is only acquired part way through the year, the charge will only apply for the period when the property is held.

Reliefs and exemptions

Since this is an anti-avoidance provision, HMRC acknowledged that there must be reliefs and exemptions from the charge in (what they consider to be) genuine commercial scenarios and so genuine businesses should be exempt from ATED.

Reliefs have to be claimed although the exemptions do not.

The reliefs

The reliefs are specified in FA2013 at s132 and this provides that for any chargeable period that includes one or more days that are relievable as a result of any of the listed provisions, the adjusted chargeable amount is to be calculated on the basis that the chargeable person is not within the charge on any relievable day. So the ATED is pro-rated if the relief does not apply for the whole year. Some changes to these reliefs applied from 1 April 2016.

The following are exempted from the charge:

- Property rental businesses
- Rental property being prepared for sale
- Dwellings opened to the public
- Property developers
- Property traders
- Financial institutions acquiring dwellings in the course of lending
- Regulated home reversion plans (from 2016)
- Occupation by certain employees or partners (changed in 2016)
- Caretaker flats owned by management company (from 2016)
- Farmhouses
- Providers of social housing

Property rental business

A business must meet two conditions to be a qualifying property rental business:

- The business must be a property rental business as defined in CTA2009 (although it is not relevant whether the business is chargeable to corporation tax) being (as per s205) every business which is carried on for generating income from land with the meaning of generating income from land (per s207) being exploiting an estate, interest or right in or over land as a source of rents or other receipts;

- It must be run on a commercial basis and with a view to a profit.

HMRC say that the following may suggest that a property rental business is not being run on a commercial basis:

- The property is not, and has never been, marketed to the public through an agent

- The property is not managed by an independent agent

- The property is not let on standard third party terms including charging less than commercial rent

- The landlord does not enforce its legal rights (such as where the property is altered by the tenant or damage is done and payment not enforced as compensation)

- There are long or repeated periods when the property is untenanted

- The business is funded by debt on terms or at levels which would not be available from an unconnected third party

Of course, it is a matter of fact whether a property rental business is being run on a commercial basis but evidence to support that fact may be needed if any of those factors are present. A person is carrying on a qualifying property rental business in respect of every day on which the dwelling is either let to a third party or steps are being taken to secure that the dwelling will, without undue delay, be let.

Evidence that a person was trying to let a property would include:

- appointing an lettings agent;

- re-decoration;

- more substantial alterations than simply re-decoration; and

- purchasing furniture.

These steps must be taken so as to ensure that the dwelling will generate rents without undue delay. A delay in generating rent will though be justified if that results from commercial considerations or was unavoidable, for example, if it is caused by factors wholly outside the control or influence of the owner of the property: for example, if it is severely damaged in a fire, or extensive works need to be undertaken to make the property inhabitable or to comply with legal requirements.

There may be a period of time when a property is not being occupied as it is being prepared for sale or other qualifying disposal. Relief is available in that case, assuming that the relevant conditions are met:

- on day X the dwelling is unoccupied and any of the conditions A to D are met (see below);

- day X is preceded by one or more days that are relievable because the property is used in a qualifying property development business (and at that time the current owner was entitled to the property interest); and

- the days (if any) between day X and the last of the qualifying days to precede day X are all relievable under this section.

Conditions A to D are as follows:

A. Steps are being taken to secure that the interest will be sold without undue delay

B. Steps are being taken to secure that the dwelling will be demolished without undue delay and if it is intended that a new dwelling will be constructed on the site of the existing dwelling, the intention is that it will be sued in a relievable way.

C. Steps are being taken to secure that the dwelling will be converted into a different dwelling without undue delay and it is intended that the new dwelling will be used in a relievable way

D. Steps are being taken to secure that the dwelling will be converted into a different dwelling without undue delay and it is intended that the new dwelling will be used in a relievable way.

In this context 'use in a relievable way' means relief would be available because it is used in a property business, it is a dwelling open to the public, it will be occupied by employees or partners of a relevant business or it is a farmhouse (i.e. it is not that it is relievable under any of the relief above; it is a more limited list).

One of the most important facets of this relief is that it is not available where a non-qualifying individual is in occupation. It is important to note that although refers to 'individual' it is not limited to individuals! The complete list of non-qualifying individuals is:

- an individual who is entitled to the interest (otherwise than as a member of a partnership),

- an individual ("a connected person") who is connected with a person entitled to the interest,

- if a person is entitled to the interest as a member of a partnership, an individual who is, or is connected with, a qualifying member of that partnership (a qualifying member being someone who is entitled to a 50% or greater share of the income profits of the partnership or the partnership assets),

- an individual ("a relevant settlor") who is the settlor in relation to a settlement of which a trustee is (in the capacity of trustee) connected with a person who is entitled to the interest,

- the spouse or civil partner of a connected person or of a relevant settlor,
- a relative of a connected person or of a relevant settlor, or the spouse or civil partner of a relative of a connected person or of a relevant settlor,
- a relative of the spouse or civil partner of a connected person or of a relevant settlor,
- the spouse or civil partner of a person falling within the above paragraph, or
- an individual who is a major participant in a relevant collective investment scheme or is connected with a major participant in a relevant collective investment scheme (a CIS being a scheme which means the ownership condition in respect of the interest and a major participant being a person who is entitled to a share of at least 50% either of all the profits or income arising from the scheme or of any profits or income arising from the scheme that may be distributed to participants or would in the event of the winding up of the scheme be entitled to 50% or more of the assets of the scheme that would then be available for distribution among the participants).

When looking at this legislation, the definition of connected party is that which is found in s1122 CTA2010 with the exception that the rules about those connected to partnerships are omitted so that you are connected if the following applies:

- A company is connected with another company if:
    - the same person controls both or
    - A has control of one company and persons connected with A have control of the other company or
    - if A has control of one company and A together with persons connected with A have control of the other or
    - a group of two or more persons has control of both companies and the groups either consist of the same persons or could be so regarded if either group were replaced by a person with whom the member is connected
- A company is connected with another person (A) if:
    - A has control of the company or
    - A together with persons connected with A have control of the company
- In relation to a company, any two or more persons acting together to secure or exercise control of the company are connected with one another
- An individual A is connected with another individual B if:
    - A is B's spouse or civil partner,
    - A is a relative of B,
    - A is the spouse or civil partner of a relative of B,

- A is a relative of B's spouse or civil partner or
- A is the spouse or civil partner of a relative of B's spouse or civil partner

- A person, in their capacity as trustee of a settlement is connected with:
- any individual who is a settlor in relation to the settlement,
- any person connected with such an individual,
- any close company whose participators include the trustees of the settlement,
- any non-UK resident company which, if it were UK resident, would be a close company whose participators included the trustees of the settlement,
- any body corporate controlled by a company in either of the two above categories,
- if the settlement is the principal settlement in relation to one or more sub-fund settlements, the person in the capacity as trustee of such a sub-fund settlement and
- if the settlement is a sub-fund settlement in relation to the principal settlement, a person in the capacity as trustee of any other sub-fund settlements in relation to the principal settlement.

Relative means brother, sister, ancestor or lineal descendant.

An interesting case has recently been seen about the relief relating to property rental businesses. Although the enquiry was on an SDLT return, the basic principles are the same. A company had acquired a flat in a large block which included the use of car parking space in the basement carpark. When they acquired the flat it had a tenant already in occupation who remained within the property for around a year after the purchase. The tenancy in place specifically excluded the use of the associated car parking space, although it was unclear why the previous owners had done this. The space was not used for anything else. HMRC were arguing that because part of the property acquired was not being used for the purposes of a qualifying property rental business that the higher rate applied to the whole of the property. The purchasers had not, in fact, realised that the prohibition existed and had done nothing to enforce it. However, HMRC were taking a very harsh line on this point and it is still being argued.

Dwellings opened to the public

There are two conditions, one of which has to be met for this relief to be available:

1. The dwelling is being exploited as source of income in the course of a qualifying trade in the normal course of which the public are offered the opportunity to make use of, stay in or otherwise enjoy the dwelling as customers of the trade on at least 28 days in any year

2. if the intention is that the property will be exploited, that steps are being taken to secure that this will commence without delay except so far as delay is justified by commercial considerations or cannot otherwise be avoided.

To be qualifying, the trade must be carried on on a commercial basis and with a view to profit. Persons are not taken to be enjoying the dwelling unless the areas that they are permitted to utilise are a significant part of the interior taking into account the size, nature, and function of the areas to which they have access.

One important point to note here is that the condition that a non-qualifying individual must not occupy the dwelling is absent. This is intentional and logical since it is likely that the occupant in these types of situations will be connected with the owner.

Property developers

Relief is available where a person is carrying on a property development trade, being a trade that consists of or included buying and developing for resale residential or non-residential property and which is run on a commercial basis with a view to profit. Development also means re-development.

Relief is also available for property developers who have acquired the property as part of a qualifying exchange unless the property is occupied by a non-qualifying individual. The acquisition is part of a qualifying exchange only if:

- it was made by way of transfer,
- the person from whom the acquisition was made itself acquired (by way of grant or transfer) a chargeable interest in or over a new dwelling from the relevant person,
- each of those acquisitions was entered into in consideration of the other.

Finally, care needs to be taken where a property developer allows a non-qualifying individual to occupy the dwelling. If that happens, no previous or subsequent day in the current chargeable period is relievable by virtue of their being a property development trade or any of the subsequent three chargeable periods assuming there is continuity of ownership of the asset.

Property traders

If a person is carrying on a property trading business and the interest in a dwelling is held as stock in the business and for the sole purpose of resale in the course of the business then no ATED charge arises. It will not be treated as held for the sole purpose of resale at any time when it is occupied by a non-qualifying individual and this taints the relief for the entire of the current and subsequent three chargeable periods.

A property trading business is one which consists of or included activities in the nature of a trade of buying and selling dwelling, carried on on a commercial basis and with a view to profit.

Financial institutions acquiring dwellings in the course of lending

No ATED charge arises where the following conditions are met:

- A financial institution carrying on a business that involves the lending of money is entitled to the interest in the dwelling;

- The financial institution has acquired the interest in the course of that business and in connection with those lending activities ;and

- The interest is held with the intention that it will be sold in the course of that business without delay (except so far as the delay is justified by commercial consideration or cannot be avoided). This condition cannot be met at any time when a non-qualifying individual is permitted to occupy the dwelling and, as with above reliefs, this taints the relief for the current and future 3 chargeable periods.

Regulated home reversion plans

Relief is available in relation to a property held by a person who is an authorised plan provider who has entered into a regulated home reversion plan relating to the dwelling and the occupation condition is met.

The occupation condition is that a person who was originally entitled to occupy the dwelling under the regulated home reversion plan is still entitled to do so. If a qualifying termination event has occurred, the occupation condition is that the interest is being held with the intention that it will be sold without delay (other than that caused by commercial considerations or cannot be avoided) and no non-qualifying individual is permitted to occupy the dwelling. Qualifying termination event is interpreted in accordance with the provisions relating to such qualifying home reversion plans and means that the person who is entitled to occupy the property becomes a resident of a care home, dies or a period of at least 20 years has passed since the home reversion plan was entered into.

The definition of a qualifying home reversion plan is governed by the relevant regulatory provisions in relation to such financial products and arrangements entered into before 6 April 2007 will qualify if they would have qualified if entered into now.

Returns and payment

Where tax is charged on a person for a chargeable period will respect to a single-dwelling interest, the person must deliver a return for the period. A claim for relief must be made in the return or by amending the return.

However, for chargeable periods beginning on or after 1 April 2015, there is new type of return called a relief declaration return for those persons holding properties eligible for a relief from ATED. For each type of relief being claimed a relief declaration return must be filed in respect of one or more properties held for that chargeable period: no details are required of the individual properties eligible for that relief. A separate return is required where a property is acquired during the year that qualifies for different type of relief. Where such a return for a chargeable period has been delivered to HMRC with respect to one or more single-dwelling interests and there is another property falling within the same exemption acquired, the existing return is treated as also made with respect to that other single-dwelling interest.

A return will be required in respect of any property which ceases to qualify for a relief i.e. where ATED becomes due. Overall this will offer considerable time savings for those with large portfolios of exempt properties.

The ATED return must generally be delivered by the end of the period of 30 days beginning with the first day in the period on which the person is within the charge with respect to the interest.

So for a person within the scope of ATED, the annual return will normally be due within 30 days of the start of the chargeable period (1 April in a year): the filing date will be 30 April. However, if the dwelling is first acquired during a chargeable period (for example, by purchase from a third party), the filing date will be 30 days from the date of acquisition.

Where a taxpayer has disposed of the dwelling during the course of a year and had previously claimed a relief (so that there is no repayment due to them) in relation to that dwelling they should still submit an amended return showing the disposal of the dwelling.

There is one further issue to consider. Where the ATED charge relates to the acquisition of a newly constructed single dwelling interest or a dwelling produced from another dwelling, the return is due 90 days from the earliest date on which the dwelling is deemed to come into existence for Council Tax purposes or the day on which the dwelling is first occupied.

Tax charged for a chargeable period must be paid not later than the filing date for the ATED return required to be made for that period.

As noted above, the annual return will normally be due within 30 days of the start of the chargeable period (1 April in a year): the filing date - and so the payment date - will be 30 April. If the dwelling is first acquired during a chargeable period (for example, by purchase from a third party), the filing date - and payment date - will be 30 days from the date of acquisition.

Contributed by Ros Martin

Administration

Individual voluntary arrangement

Summary – Unsurprisingly, having entered into a five- year individual voluntary arrangement (IVA), additional tax liabilities arising during that five year period remained payable and did not simply disappear at the end of the IVA.

Barbara Rowland was a medical practitioner who worked as a GP, and for other periods she worked for South Western Ambulance Service NHS Foundation Trust.

This was an appeal against penalties imposed for late payment of income tax in respect of tax years 2012/13 to 2015/16 respectively. Barbara Rowland did not dispute the amount of tax to which she was liable, nor did she dispute that the payments made by her were made on the dates and in the amounts claimed by HMRC. She also accepted that she did not specify to HMRC to which liability the various payments were to be allocated.

Barbara Rowland had entered into an IVA between 2008 and October 2013. She said that during this period, there were annual reviews of her payments into the IVA. At these annual reviews, the insolvency practitioner supervising her IVA would look at her annual income and expenditure, and consider how much she could currently afford to pay into the IVA.

During the period that she made these required payments into the IVA, she believed that her additional year's tax liabilities would be added to her debt and at the end of the 5 year period, these would be cleared and she would emerge debt free. She claimed that she had never imagined that when the IVA ended in in October 2013, she would emerge with a tax liability in respect of the 5 year period from October 2008 to October 2013. That was not the case and so, when she made payments for her 2012/13, 2013/14 and 2015/16 tax, she did not realise that HMRC was allocating these payments to earlier years.

HMRC issued penalties for late payment for 2012/13 to 2015/16 against which Barbara Rowland appealed.

Decision

The First Tier Tribunal concluded that Barbara Rowland had not shown that she had a reasonable excuse for the late payments on the ground she thought she had no liability to pay for the earlier years.

It was 'more likely than not that she was well aware' that her tax liabilities would continue to accrue during the IVA and even if she had been under that impression, a reasonable taxpayer should have checked 'exactly what the effects and consequences of the IVA' would be.

The appeal was dismissed.

Barbara Rowland (TC07338)

Adapted from the case summary in Taxation (17 October 2019)

Arrangements notifiable under DOTAS

Summary – The reward arrangements were notifiable arrangements under DOTAS: the steps were pre-planned with the main benefit being to obtain a tax advantage.

EDF, offered tax advice to clients on certain reward arrangements, referred to as the Delta arrangements.

In a letter to clients 'Delta Rewards' were described as a 'flexible platform' which allowed the company to set aside funds for rewarding employees immediately but deferring the choice of actual reward until after the year end. The letter stated the company had a range of options to reward its employees, such as cash bonuses, pension contributions, shares, health club membership, cars, loans and employee trusts. The next few pages advised on the tax consequences of each method. Properly understood, the letter advised the recipient to set up an EBT and to later implement a deed of variation in respect of it in order to implement the Delta rewards platform.

The company denied that these arrangements were disclosable under DOTAS. The company produced two brochures that they claimed were the only marketing material available to potential users of the arrangements and argued that these documents talked about advising on rewarding employees generally with Delta delivering 'a platform to deliver flexible employee rewards'. EDF also maintained that the steps taken by users were not pre-determined. EDF ceased trading on 31 January 2017 and entered into creditors' voluntary liquidation.

On 23 October 2017, HMRC made an application that the Delta arrangements were notifiable arrangements within the meaning of s306(1) FA 2004 and that the company was a promoter of the arrangements.

Decision

The First Tier Tribunal stated that letters from EDF to clients and their marketing materials supplied superficially suggested that EDF was advising on different reward options and their related tax implications for employees generally. However, the letters immediately advised on the creation of an employee benefit trust. The Tribunal believed that it was likely that EDF gave oral advice to users at the outset so that the letters 'were actually a part of the scheme, designed to convey an impression that there was no advance planning and that each step was spontaneous'. There was no evidence that the documentation was tailored to different clients' circumstances.

The First Tier Tribunal concluded that the Delta arrangements amounted to a scheme involving a series of pre-planned transactions that fell within the meaning of 'arrangements'. The Tribunal found that the main benefit of the arrangements was to obtain a tax advantage and that EDF was clearly a 'promoter' of the scheme.

HMRC's application was allowed.

HMRC v EDF Tax Ltd (in creditors' voluntary liquidation) (TC7381)

Penalties for late filed corporation tax returns

Summary – The First Tier Tribunal were unable to conclude that HMRC had given valid notices to file a company tax return for any of the periods under appeal.

Mr Corrick, a scaffolder had been employed and self-employed for many years. In 2015 he incorporated his business because one of his main 'employers' wanted to treat him as an independent contractor, not an employee.

Whilst self-employed, Mr Corrick had looked after his tax affairs himself but around July 2014, as those tax affairs became more complicated as a result of him getting more business, he engaged an accountant to deal with the tax and accounting affairs of his company and passed any communications from HMRC to him.

No company tax returns were filed so HMRC issued penalties and eventually it was struck off the register of companies. The taxpayer appealed against the penalties on the grounds that neither he nor his accountant had received notices to file returns from HMRC.

HMRC provided computer print outs bearing the appellant's name, tax reference number and national insurance number. There was a column with the words "Return Issued Date" alongside which appeared "06/04/xx". HMRC argued that this was evidence that a Notice to File was sent to the appellant's correct address because it would have been sent to the address for the appellant which HMRC held on file by way of another computer record headed "Individual Designatory Details".

Decision

The First Tier Tribunal said that it was for HMRC to prove it had sent the notices and in this instance, it relied on three computer printouts.

The First Tier Tribunal concluded that it was not possible to infer from the printouts provided by HMRC that valid notices to file had been issued to the taxpayer. The Tribunal was confident that the return issue date of 06/04/xx was fiction as that is the date which appears alongside every person's Return Summary alongside the words "Return Issued Date". They stated that it is equally well known that HMRC sends out Notices to File on a staggered basis because, it simply could not hand over to the Royal Mail the huge volume of letters which it would need to send if every relevant taxpayer was sent a Notice to File on the same day of each year. They concluded that the print out was 'inherently improbable and unreliable.'

The Tribunal concluded that:

- they could not infer from the printouts a positive finding of fact that valid notices to file for the periods under appeal were given to the appellant as claimed by HMRC. It would be speculation to do so.

- HMRC had not established on the balance of probabilities that they had given valid notices to file company tax returns to the appellant for the years under appeal.

The appeal was allowed.

Tillzane Scaffolding Limited (TC07369)

Legality of automated notices

A number of recent cases have seen Tribunal's consider whether computer generated penalty determinations are valid.

On 31 October 2019, HMRC published a Technical Note stating that in the next Finance Bill it will legislate to put beyond doubt the legal basis for HMRC's use of large-scale automated processes for issuing assessment and penalty notices.

The following functions will be covered:

- Notice to file a return in relation to individuals, trustees and partnerships;
- Correction of a personal or trustee's return;
- Notice to file a return in relation to corporate bodies; and
- Charging penalties under TMA 1970 s 100 and FA 2003 Sch 14 (SDLT).

This legislation will have retrospective effect and would specify that such notices are equally valid whether automated or issued by an officer of HMRC. HMRC has confirmed that where taxpayers have received settled judgments before 31 October 2019, they will not be subject this retrospective legislation.

https://www.gov.uk/government/publications/securing-the-tax-base-affirming-the-legislative-framework-for-hmrc-to-use-automated-processes

Penalties for inaccuracies in return

The taxpayers were involved in a property development business in Poland. They claimed relief in their UK tax returns for losses incurred with the business. HMRC considered a company controlled by the taxpayers but incorporated in Poland incurred the losses and refused the claim. It imposed penalties for careless inaccuracies in the taxpayers' returns.

The First Tier Tribunal dismissed their appeal. At the hearing the taxpayers were represented by their accountant, Mr Weissbraun who acknowledged he was not an experienced litigator, but specialised in giving tax advice.

Shortly before the First Tier Tribunal hearing, HMRC amended its statement of case on penalties. The taxpayers were given the opportunity to object but they chose not to.

Further, Mr Weissbraun asked to give oral evidence during the hearing that would confirm the taxpayers ran a partnership and that the company held its assets on trust for the taxpayers. However, the tribunal refused permission on the basis that the evidence was hearsay.

Decision

The Upper Tribunal found the First Tier Tribunal had erred in refusing to permit the proposed evidence on the ground it was hearsay and introduced without notice. However, it too would have refused because it had not been presented in accordance with rule 2 of the First Tier Tribunal Rules. In any event, it would not have affected the outcome of the appeal.

On the penalties, the Upper Tribunal said the taxpayers had been 'unwise' not to supplement their witness statements but the First Tier Tribunal had been entitled to find the returns contained inaccuracies. Mr Weissbraun emphasised he had given the taxpayers professional advice and that his firm had submitted the returns. The judges accepted this but said, had the taxpayers given evidence to the First Tier Tribunal that they had checked the position with their adviser before the returns were submitted, that they had given him all the necessary information and that Mr Weissbraun had told them they were entitled to losses, the First Tier Tribunal would have been likely to accept that. However, it was not obliged to 'speculate' on what the evidence might have been. The First Tier Tribunal had been entitled to conclude the taxpayers were careless.

The Upper Tribunal dismissed the taxpayers' appeal.

H Wiesenfeld, A Strom v CRC, Upper Tribunal (Tax and Chancery Chamber)

Adapted from case summary in Taxation (7 November 2019)

Deadlines

1 December 2019

- CT due for SMEs with years ended 28 February 2019 not liable to pay by instalments

7 December 2019

- VAT returns and payment for 31 October 2019 quarter (electronic payment)

14 December 2019

- Quarterly CT instalment for large companies (depending on accounting year end)
- Monthly EC sales list — paper returns

19 December 2019

- Non-electronic PAYE, NIC, CIS, student loan liabilities for month to 5 December 2019
- File monthly CIS return

21 December 2019

- File online monthly EC sales list
- Submit supplementary intrastat declarations for October 2019

22 December 2019

- PAYE, NIC, CIS and student loan liabilities should have cleared to HMRC

30 December 2019

- Online SA returns if underpayments are to be collected by a PAYE coding adjustment

31 December 2019

- Accounts to Companies House for private companies with 31 March 2019 year ends
- Accounts to Companies House for public companies with 30 June 2019 year ends
- CTSA returns filed for companies with accounting periods ended 31 December 2018
- End of CT61 quarterly reporting period
- Year end for taxable distance supplies to UK for VAT registration
- Non-EC traders claim recoverable UK VAT in year ended 30 June 2019

News

Corporation tax cut cancelled (Lecture B1166 – 15.28 minutes)

We were expecting the rate of corporation tax to be reduced to 17% from April 2020.

However, at the CBI conference held on Monday 19th November, Boris Johnson announced that this planned reduction will not go ahead and is being postponed.

Instead, the money, around £6 billion, will be used to support the NHS and other public spending priorities.

Invalid VAT surcharge notice

It has been brought our attention that HMRC has issued a letter to a taxpayer stating that a Surcharge Liability Notice that was issued to them between 23 Aril 2018 and 31 January 2019 was invalid as it was undated.

The letter confirms that as the Surcharge Liability Notice was undated, any linked Surcharge Notice extensions and surcharges are also invalid and that the surcharge Notice and extensions will be removed from their records.

One would assume this is not an isolated incidence and other taxpayers should expect the same treatment when HMRC issues undated notices.

OTS: Tax reporting and payments review

The OTS has published its report on options for simplifying the process of reporting and paying tax for the self-employed and landlords of private residential property. Broadly, the report makes recommendations for further work, falling into three main areas:

Recommendation 1

The government should invite the OTS to, or HMRC should, explore the potential for HMRC to offer a fully integrated Individual Tax Account, providing an end-to-end tax reporting and payment service, and the key steps and timescales that would be involved.

This Individual Tax Account, would merge the present personal and business tax accounts so that taxpayers could see information about all their different types of income separately in one place.

HMRC would:

- be able to receive and display data from taxpayers about their self- employment or rental income;

- offer a running calculation of the additional tax that the individual may need to pay in relation to the year to date, looking across all the information held in the individual's tax account;

- offer the facility for the taxpayer to make payments (whether of the calculated amount, or other amounts chosen by the taxpayer) to HMRC towards their overall liability, and to display information about amounts paid;

- be able, in time, to receive and display data from third parties in selected sectors who have a significant role in relation to the individual's self-employment or rental business.

Recommendation 2

The government should invite the OTS to, or HMRC should, explore and identify in more detail:

- the sub-sectors of the economy where third parties play a significant role in relation to a group of taxpayers, in particular where the majority of a taxpayer's activity can involve third parties who would have sufficient information to support effective reporting; sub-sectors to consider further could include the taxi/private hire market and holiday lettings market;

- the information it would be natural for such third parties to hold and any additional information (such as the National Insurance number) that might need to be gathered to support effective and helpful reporting;

- the extent to which it is usual for such intermediaries to handle money relating to the business;

- the key steps and timescales that would be involved in requiring them to report such information.

Recommendation 3

The government should invite the OTS to, or HMRC should, explore in more detail:

- which types of self-employment business or rental business would most benefit from being able to report data periodically and pay tax through an integrated Individual Tax Account;

- what data individual taxpayers would need to be able to send to HMRC for this to work effectively (whether through MTD or in other ways);

- the key steps and timescales that would be involved.

https://www.gov.uk/government/publications/ots-tax-reporting-and-payment-arrangements-review

Business Taxation

Undeclared income (Lecture B1166 – 15.28 minutes)

Summary – Regular bank deposits and invoices settled through an informal value system represented undeclared income.

In Adelekun v HMRC [2016] UKFTT 107 (TC), the Tribunal concluded that Mr Adelekun carried on two separate trades. The first was the provision of project advisory services and the second was the leasing of oil water separation plant. In June 2016, HMRC wrote asking that he submit revised tax returns to reflect this decision as losses incurred in the leasing trade could not be carried forward and set against the profits of the advisory trade.

This case concerns Andrew Adelekun's sole trader business of providing project and business advisory services. Although based in the UK, his clients are located around the world, particularly in Nigeria and South Africa. A key part to his business is his network of contacts around the world that he is able to use to provide advice to his clients. He does not provide these services personally.

At the hearing Andrew Adelekun stated that, sometimes he helps his clients with their own business dealings or personal matters as a gesture of goodwill. He confirmed that this money goes into his own bank account and is not included in his business accounts. There was no written evidence supporting these actions. He may agree to set off these amounts with amounts that his clients owe him for his actual work.

There were no entries on Mr Adelekun's bank statements corresponding to the payment of his local representatives' invoices, and there was no evidence supplied linking entries to particular invoices. HMRC assumed that these must have been paid out of unrecorded business income.

However, HMRC noted regular payments described as rent into his bank account. With no satisfactory explanation, HMRC assumed that this was business income. Similarly with various payments from the account being unsupported, HMRC assumed that these payments were not allowable business expenses,

On 16 January 2017, Andrew Adelekun appealed against HMRC's closure notice dated 21 December 2016 in respect of an enquiry into his self-assessment tax return for 2014/15 that resulted in HMRC demanding additional tax and class 4 NICs of £40,000.

On 30 January 2017, Mr Adelekun filed a further tax return for 2014/15, claiming bad debt relief of £111,067.

On 10 February 2017, Mr Adelekun wrote to HMRC claiming an increase in his direct costs, and submitting revised invoices addressed to him for work done by his agents relating to 2014, but only dated in January 2017. There was no evidence that these invoices were paid from his bank account, and so HMRC assumed that they were paid through the informal value transfer system out of unrecorded business income. There would therefore be no change to the assessed profit.

Decision

The First Tier Tribunal did not regard Mr Adelekun's evidence as at all credible.

The Tribunal concluded that it was highly unlikely that some £90,000 of income, amounting to approximately one-third of his overall economic activities, could have related to errands undertaken on a goodwill basis. With no credible evidence supplied supporting this claim, the Tribunal concluded that the deposits made into his accounts were trading income, and withdrawals were not trading expenses. Further, as the discharge of his overseas agents' invoices could not be reconciled to payments out of his bank accounts, they must have been paid from undeclared income via an informal value transfer system.

Finally, in Adelekun v HMRC [2016] UKFTT 107 (TC), it was found that Mr Adelekun had instructed his accountants to review aged debtors on 10 February 2016. Consequently, the bad debt relief claim for 2014/15 could not be allowed.

The appeal was dismissed

Andrew Adelekun v HMRC (TC07397)

Claiming Structures and Buildings Allowance (Lecture B1166 – 15.28 minutes)

As we have previously reported, from 29 October 2018 the new structures and buildings allowance was introduced.

HMRC have stated that their Corporation Tax online service will not be updated to support this new relief until April 2020.

If a company needs to submit a Structures and Buildings Allowance claim online before April 2020 it is possible to do this using existing capital allowance boxes. For CT600, boxes 725, 750 and 775 can be used until the online service and new boxes are available.

- Use box 725 to report Structures and Buildings Allowances relating to a trade until the new boxes are available;

- Use box 750 to report Structures and Buildings Allowances not relating to a trade until the new boxes are available;

- Use box 775 to record qualifying expenditure for Structures and Buildings Allowances until the new boxes are available.

Companies using the HMRC free filing service (CATO) wishing to claim the new Structures and Buildings Allowance will only be able to file when the Corporation Tax online service is updated in April 2020. Businesses needing to file their Company Tax Return urgently before April 2020 should contact HMRC for further advice.

https://www.gov.uk/government/publications/corporation-tax-service-availability-and-issues/corporation-tax-service-availability-and-issues

Time limit for a capital allowances claim? (Lecture B1167 – 15.45 minutes)

The rules which apply to capital allowances claims are somewhat different from those which govern other types of claim in the tax system. As a general principle, capital allowances have to be claimed as part of a tax return – free-standing claims are not permitted, unlike the position with certain other reliefs.

For income tax purposes, there is no express statutory guidance about the time limits for making or amending a capital allowances claim, although HMRC argue that, if a claim has to be made as part of a tax return, it follows that 'the time limit for making a claim or amending a claim is the normal time limit for making or amending a tax return' (see Para CA11130 of the Capital Allowances Manual).

For income tax purposes, the time limits for filing and amending a tax return for a given tax year are respectively:

- the first 31 January after the end of that tax year; and
- the following 31 January.

Thus a capital allowances claim for 2018/19 must normally be made in a tax return filed on or before 31 January 2020 and, once made, that claim can be amended at any time up to 31 January 2021. In practice, HMRC seem to take the view that the initial capital allowances claim can be made at any time up to 31 January 2021. However, if a taxpayer files his 2018/19 return later than 31 January 2021, it is thought that he has missed an opportunity and that he cannot claim capital allowances for that particular tax year.

For companies, the law is more specific. Para 82(1) Sch 18 FA 1998 states that 'a claim for capital allowances may be made, amended or withdrawn at any time up to whichever is the last of the following dates'. FA 1998 then lists four dates, of which the first two are:

- the first anniversary of the filing date for the tax return of the company making the capital allowances claim (this will normally be two years after the end of the relevant accounting period); and
- where a notice of enquiry has been given into that tax return, 30 days after the enquiry is completed.

Dundas Heritable Ltd was a company with a 31 March year end which carried on the business of running public houses and bars. The recent Upper Tribunal decision in HMRC v Dundas Heritable Ltd (2019) is concerned with the company's tax returns for the year to 31 March 2012 and for the year to 31 March 2013. The filing date for the company's tax return for the year ended 31 March 2012 was 31 March 2013. It was received by HMRC on 3 February 2015. The filing date for the company's tax return for the year ended 31 March 2013 was 31 March 2014. This one was received by HMRC on 26 November 2015. Both returns contained claims for capital allowances (which for each year totalled more than £300,000 but which were otherwise uncontroversial) and both claims were submitted more than 12 months after the relevant filing date (i.e.. after the date specified in Para 82(1)(a) Sch 18 FA 1998). Because of this, HMRC opened enquiries into these returns, restricted to the capital allowances claims. The company contended that both claims had in fact been made in good time, given that they were made within the 30-day time limit following

completion of HMRC's enquiries (i.e.. before the date specified in Para 82(1)(b) Sch 18 FA 1998).

The company's argument was rejected by HMRC and, on 16 September 2016, closure notices were issued, amending the company's returns by deleting the claims for capital allowances. In 2018, the company appealed to the First-Tier Tribunal which allowed their appeal. The gist of the judge's reasoning was unequivocal: a claim is timeous if it is lodged before the last of the dates stipulated in Para 82(1) Sch 18 FA 1998. This was not accepted by HMRC – they continued to assert that the company's claims were made out of time.

Before the Upper Tribunal, the company said that the plain wording of Para 82 Sch 18 FA 1998 provided that, in a case where there has been an enquiry, a claim for capital allowances is made in a timely manner if it is made at an earlier date than the '30 days after the enquiry is completed' time limit. This was the case for each of the company's capital allowances claims and so the claims were in time and should be allowed.

Having lost before the First-Tier Tribunal, HMRC developed their line of argument further. The key point, they asserted, was that the validity of a claim had to be determined at the time when it was made and by reference to the time limits which were then applicable. Nothing which subsequently took place could, they said, operate to 'post-validate' a claim which was invalid when made. It should be noted in passing that, in order to remove a late capital allowances claim, HMRC must first open an enquiry. At the Upper Tribunal hearing, the judges summarised the HMRC viewpoint as follows:

> 'An analysis which permitted an out-of-time claim to be validated by the very process required for corrective action was entirely circular and rendered the initial time limit in Para 82(1)(a) Sch 18 FA 1998 otiose.'

This sounds like a very fair point, but the Upper Tribunal again sided with the company, reasoning that the words of the legislation are quite clear.

One commentator has summarised the position thus:

> 'The decision is surprising. The effect seems to be to allow a company to make a capital allowances claim in any tax return, regardless of how late the tax return is made. For, in such a case, the claim can be challenged only by the making of an enquiry into the return and the very fact of the making (or, at least, completing) of the enquiry retrospectively extends the time limit for making the claim: a sort of Catch-22 against HMRC.
>
> This can hardly have been the result that Parliament envisaged when enacting the provision.'

However, unless and until the law is changed or the case is reversed on appeal, that is how things now stand. Remember that a decision of the Upper Tribunal creates a legally binding precedent.

Contributed by Robert Jamieson

Capital allowances on hydroelectric scheme

In the SSE Generation appeal case, the UT dismissed HMRC's appeal, finding that all the items qualified for capital allowances.

SSE was involved in the generation, transmission, distribution and supply of electricity, and the production, storage, distribution and supply of gas and various associated energy services. It had constructed the first large-scale hydroelectric scheme with a conventional hydraulic head feed built in the UK in the last 50 years. This appeal was concerned with expenditure incurred in both the original construction of the scheme and the subsequent remedial works.

The issue was the availability of capital allowances on each of the items comprised in the scheme; the question was whether they fell within CAA 2001 s 21 list A or s 22 list B (excluded items), or s 23 list C (items unaffected by the exclusions in lists A and B). The dispute was in relation not to the generator turbine (which was accepted as being eligible for allowances) but to works of civil engineering which enabled water to be taken into and from a dammed area and channelled under high pressure to the turbine to generate electricity and for the used water to be discharged into Loch Ness.

The FTT had found that the expenditure incurred on a considerable number of the items was allowable as expenditure incurred on the provision of plant or machinery but that the expenditure on a number of the items was not so allowable. HMRC appealed against the findings in respect of the most substantial items so that the appeal turned upon questions of statutory interpretation of a number of words used in CAA 2001, which were 'ordinary words of the English language'; 'aqueduct', 'tunnel', 'pipeline' and 'installation'.

The UT observed that the function of list B was to 'draw the line in the sand' between expenditure on those assets which have the character of real estate or buildings or structures, which, subject to the exception for industrial buildings, are not to be regarded as 'plant' for capital allowance purposes and other assets which do qualify (with a further exception, as set out in list C). It added that the provisions of s 22(1)(a) and s 22(1)(b) were mutually exclusive.

As a result, the correct approach when considering whether expenditure on a structure or other asset (other than land) was not qualifying expenditure was to consider first whether the structure or asset fell within the scope of any of the specified structures or assets in list B. If the structure or asset answered to the description of any of those items (for example because it was a 'tunnel' or an 'aqueduct' as in this case) then the expenditure was disallowed (unless s 22 was disapplied because the expenditure was incurred on any of the items specified in list C).

The UT found that the structure was neither a 'tunnel' nor an 'aqueduct' for the purpose of list B, so that all the expenditure in relation to the structure was allowable (save for one exception) on the basis that the expenditure was on the provision of an industrial building falling within the scope of the exception in item 7(a) of list B. This was because the 'provision' of a structure included all of the costs of construction, including the necessary preparatory work in excavating the land before the structure was built, its building in situ and its subsequent covering over.

Like all capital allowances cases, this decision is highly dependent on the facts. However, it will be of wider interest to all who advise on capital allowances because of the very careful analysis undertaken by the tribunal of the relationship between the various elements in the definition of buildings for capital allowances purposes and also because of the discussion of the meaning of the word 'installation' in this context.

The UT accepted that there had been 'a recent tendency in both the Supreme Court and the Privy Council to rely on Parliamentary debates on a Bill not as an indication of legislative intent on resolving an ambiguity as to the meaning of a particular word or phrase but rather to supply context or identify the nature or extent of the mischief at which the legislation was aimed.' Referring to Parliamentary debates enabled the UT to establish that the purpose of s 22 et seq. had been to clarify the boundary between buildings and structures, on the one hand, and plant on the other.

HMRC v SSE Generation Ltd UKUT 0332 (TC)

Contributed by Joanne Houghton and taken from Tax Journal (13 November 2019)

Tax treatment of cryptoassets for businesses

HMRC has published guidance on the potential liability to CGT, CT, IT, NICs, stamp duty, SDRT and VAT on transactions companies and other businesses (including sole traders and partnerships) may undertake involving cryptoasset exchange tokens, such as Bitcoin. The guidance does not cover transactions involving security tokens and utility tokens. HMRC published guidance for individuals on the treatment of cryptoassets in December 2018.

Exchange tokens are intended to be used as a method of payment and encompasses 'cryptocurrencies' like bitcoin. They utilise some form of 'digitalised ledger technology' and typically there is no person, group or asset underpinning these, instead the value exists based on its use as a means of exchange or investment. Unlike utility or security tokens, they do not provide any rights or access to goods or services. HMRC does not consider cryptoassets to be currency or money.

The type of activities which will be subject to tax and which involve exchange tokens would include:

- buying and selling exchange tokens
- exchanging tokens for other assets, including other types of cryptoassets
- mining (see more details on this below)
- providing goods or services in return for exchange tokens

The normal tax rules will apply to the income, expenditure, profits, gains and losses on such exchange tokens with these amounts being calculated under generally accepted accounting standards. The guidance provides more information on specific issues that arise from the utilisation of exchange tokens which are summarised below.

Currency of the tax return

The tax return for the business must be completed in sterling and so transactions involving exchange tokens must be translated at an appropriate exchange rate at the time of each transaction.

Does buying and selling exchange tokens constitute a trade?

As with other activities of a business, whether an activity constitutes a trade will be determined by the badges of trade such as the frequency of transactions and intention etc.

What is 'mining'?

Mining is essentially the work performed which ensures that the transactions are secure and it also documents a history of the exchange token and the transactions. This is required because exchange tokens do not have a central controlling authority. The persons who do this work are rewarded with more exchange tokens.

> Whether mining is a trade will also depend on a review of the badges of trade but if there is deemed not to be a trade any cryptoassets awarded to the miner will generally be taxed as miscellaneous income and also be subject to tax on any chargeable gains in the future.

Treatment for corporation tax purposes

As detailed above the transactions involving exchange tokens may be treated as trading amounts and therefore subject to corporation tax. Otherwise they could be treated as:

Loan relationships: A loan relationship arises if there is a money debt that has arisen from a transaction for the lending of money. HMRC state that as there is no counterparty to an exchange token and they are not money an exchange token do not create a loan relationship or a deemed loan relationship. There could however be a loan relationship where loans are backed by exchange tokens as securities.

Intangible assets: Where exchange tokens have been accounted for as intangible assets, or would be had GAAP compliant accounts been prepared, then they will be taxed under the intangible fixed asset rules. as long as they have been created or acquired by a company for use on a continuing basis. HMRC note that exchange tokens which are simply held by the company, even when held in the course of its activities, will not meet this definition.

Capital asset: If the activity does not fall to be treated as trading, a loan relationship or an intangible then it will be a chargeable gain.

It should be noted that as exchange tokens are not money the foreign currency rules do not apply to them.

Specific points that arise when exchange tokens treated as chargeable assets

Generally the calculation of any chargeable gain or loss would apply the normal tax rules but the guidance highlights some specific points.

Pooling of exchange tokens: TCGA 1992, s 104 provides for pooling of share and securities and any other assets where they are of a nature to be dealt in without identifying the

particular assets disposed of or acquired. Therefore, exchange tokens must be pooled with each type of token having its own pool.

Gifts of exchange tokens: HMRC's guidance advises that if a company gives away exchange tokens to another company which is not a member of the same group, or to an individual or other entity, the company making the disposal must work out the market value of what it gave away. It must then use this to calculate any chargeable gain. Similarly, the recipient is treated as having acquired the cryptoassets at their market value at the time of the gift.

Allowable costs: The costs of mining activities cannot be allowable costs in the gain calculation as they were not wholly and exclusively to acquire the exchange tokens.

What about VAT?

VAT is due in the normal way on any goods or services sold in exchange for cryptoasset exchange tokens. The value of the supply of goods or services on which VAT is due will be the pound sterling value of the exchange tokens at the point the transaction takes place.

Exchange tokens received by miners will generally be outside the scope of VAT as they do not constitute an economic activity for VAT purposes and there is no customer. When exchange tokens are exchanged for goods and services no VAT will be due on the supply of the token itself.

Charges made over and above the value of the exchange tokens for arranging any transactions in exchange tokens will be exempt from VAT.

Venture capital schemes and tax reliefs

The determination of whether a company qualifies for the tax reliefs available for venture capital schemes and schemes such as EIS, SEIS, BPR and gifts of business assets is determined by the standard conditions of the scheme including the relevant trading requirements and excluded activities list.

Paying employees in exchange tokens

If an employer 'pays' exchange tokens as earnings to an employee, those exchange tokens count as 'money's worth' and are subject to income tax and NICs on the value of the asset.

When providing a notional payment in the form of a readily convertible asset, for example an exchange token, to an employee, the employer will need to establish if that notional payment constitutes a payment of employment income. If it does constitute employment income, the employer will need to apply a valuation to that readily convertible asset using their best estimate and then subject it to the appropriate PAYE income tax and Class 1 NICs deductions.

If the exchange token is not a readily convertible assets, the employer does not have to apply PAYE income tax and Class 1 NICs deductions. However, the employee must declare any amount received in the form of exchange tokens on their tax return. In addition, the employer should treat the payment as being a benefit in kind and pay and report any Class 1A NICs arising to HMRC.

Stamp duty and stamp duty reserve tax (SDRT)

HMRC's view is that the transfer of existing exchange tokens would not be likely to meet the definition of 'stock or marketable securities' or 'chargeable securities' and so would be outside the scope of stamp duty and SDRT but this would be considered on a case by case basis.

Exchange tokens could be given as consideration for purchases of 'stock or marketable securities' and/or 'chargeable securities'. If exchange tokens are given as consideration, this would count as 'money's worth' and so be chargeable for SDRT purposes. Tax will be due based on the pound sterling value of the exchange tokens at the relevant date. They would still be outside the scope of stamp duty.

Stamp duty land tax (SDLT)

HMRC does not consider transfers of exchange tokens to be land transactions. This means that SDLT will not be payable on such transfers.

Chargeable consideration for the purposes of SDLT comprises anything given for the transaction that is 'money or money's worth'. As a general rule, any non-monetary consideration should be valued at its market value on the effective date of the transaction.

Accordingly, if exchange tokens are given as consideration for a land transaction, these would fall within the definition of 'money or money's worth' and so be chargeable to SDLT.

HMRC guidance on tax on cryptoassets

Contributed by Joanne Houghton

Offshore receipts in respect of intangible property (ORIP)

From 6 April 2019, unless an exemption applies, a person is subject to an income tax charge of 20% if they are not resident in the UK or a full treaty territory and UK-derived amounts arise to them in the tax year.

A UK-derived amount is an amount (whether capital or revenue in nature) made in respect of the enjoyment or exercise of intangible property rights where the enjoyment or exercise of those rights (or rights derived directly or indirectly from those rights) enables, facilitates or promotes UK sales.

'UK sales' means any services, goods or other property either provided in the UK, or to persons in the UK.

The legislation which effected the charge to income tax was introduced in FA 2019 and this allowed for subsequent regulations to be made to deal with any required amendments. HMRC have issued final draft regulations and some of the amendments will have effect for 2019/20 tax year. They have also issued draft technical guidance.

The changes which will apply to income arising from 6 April 2019 are summarised as follows:

- for determining UK sales, resellers will be looked through and the provision of online advertising services will be a UK sale to the extent that the advertising is targeted at persons in the UK;

- a new exemption for persons in specific territories with which the UK does not have a tax treaty, the territories will be listed in further regulations but are likely to be high tax jurisdictions;

- a new disregard for amounts derived from third party UK sales where the intangible property makes an insignificant contribution to the sale, allowing a reduction in administrative burden in tracing sales;

- a new exemption to ensure that two companies in a group cannot be subject to a double charge on the same income

- a new exemption for companies that are incorporated in a full treaty territory and which are tax transparent in that territory, the entity must be wholly owned by residents in that tax territory throughout the year. Without the exemption, these entities will fall into the rules because they do not meet the technical criteria of being tax resident in the non-low tax jurisdiction, even though the relevant IP income will be subject to tax there.

Amendment which will only apply to amounts arising after the regulations come into effect are as follows:

- an extension to the scope of the income tax charge to low tax jurisdictions in circumstances where the non-UK person is resident in a jurisdiction with which the UK has an appropriate double taxation agreement but where the provisions of the agreement mean that there is no tax relief available to the person. This may be because the person (or the income) is excluded under the terms of the double taxation agreement;

- entities that are resident in a full treaty territory but only liable to tax there on a source or remittance basis remain within the scope of the income tax charge; and

- a new exemption where UK-derived amounts arising to certain partnerships are fully taxable at a partnership level which ensures that an income tax charge under these provisions does not apply in respect of the same UK-derived amounts at the level of the partners where the partnership is chargeable in a full treaty territory on the amounts.

The regulations clarify that there is no duty to withhold income tax in payments which are also subject to the ORIP rules.

Therefore the full list of exemptions is now as follows:

- Limited UK sales
- Resident in specified territory
- Business undertaken within territory of residence
- Foreign tax at least half of UK tax
- Opaque partnership in full treaty territory
- Certain bodies corporate that are transparent in a full treaty territory
- Double taxation on amounts within same control group

Note that the exclusion of sales where the intellectual property makes an insignificant contribution is described as a disregard rather than an exemption in the legislation.

The draft regulations will now be laid before the House of Commons.

http://www.legislation.gov.uk/ukdsi/2019/9780111190500

Contributed by Joanne Houghton

Updated OECD guidance on Country-by-Country reporting

The OECD/G20 Inclusive Framework on BEPS has released additional interpretative guidance to give greater certainty to tax administrations and MNE Groups on the implementation and operation of Country-by-Country (CbC) Reporting (BEPS Action 13).

The new guidance includes questions and answers on, amongst other topics, the treatment of dividends received, the operation of local filing, the use of rounded amounts in Table 1 of an MNE Group's CbC report and the information that must be provided with respect to the sources of data used.

They have also released a summary of common errors made by multinational enterprises in preparing CbC reports, which include:

- an MNE's CbC report should be completed in the functional currency of the Ultimate Parent Entity. Information on all Constituent Entities must be converted into this currency when completing the CbC report. A CbC report should never contain information in more than one currency;

- full numbers must be used in completing Table 1, without decimals. The use of shortened numbers (for example, by deleting the final three or final six digits, as may be done in completing consolidated final statements in thousands or millions of currency units) is not permitted;

- other than with respect to the number of employees, the rounding of amounts in Table 1 is not specifically provided for in the BEPS Action 13 report. Jurisdictions may permit reasonable rounding of amounts, so long as this does is not distortive;

- dividends from Constituent Entities are included in Profit (Loss) Before Tax in jurisdictions where this is not permitted. To date, jurisdictions have applied different requirements on this issue. Going forward, interpretative guidance makes clear that Profit (Loss) Before Tax does not include dividends from Constituent Entities;

- an MNE's Constituent Entities include, among others, separate business units that are not included in its consolidated financial statements on size or materiality grounds, as well as permanent establishments of Constituent Entities for which separate financial statements are prepared for financial reporting, regulatory, tax reporting, or internal management control purposes. CbC reports have been filed that do not include these "non-consolidated" Constituent Entities, which is not permitted.

OECD update guidance on CbC reporting

Contributed by Joanne Houghton

OECD Pillar 2 update paper

As part of the ongoing work of the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS), the OECD is consulting until 2 December 2019 on three aspects of the Global Anti-Base Erosion (GloBE) proposal under 'pillar two'.

This follows the OECD's consultation on the 'pillar one' proposal for digital economy taxation which closed on 12 November 2019 with a consultation meeting being held on 21 and 22 November 2019.

'Pillar one' addresses the allocation of taxing rights between jurisdictions and considers various proposals for new profit allocation and nexus rules. 'Pillar two' involves seeking to protect against profit shifting to low-tax jurisdictions (BEPS issues). Although these proposals have been born out of concerns about the international taxation of the digital economy, the OECD concedes that is very difficult to ring-fence the digital economy and therefore the scope of GLoBE is not limited to highly digitalised businesses.

The GLoBE proposal is intended to operate as a top up to a fixed rate (that is yet to be agreed, albeit that 15% is used for the purposes of some of the examples). The proposal is based around four rules:

- an income inclusion rule that would tax the income of a foreign controlled entity or permanent establishment (PE) where that income was subject to tax at below the minimum rate

- an undertaxed payments rule that would deny a deduction or impose source-based taxation (e.g. withholding tax) for a payment to a related party if that payment was not subject to tax at or above the minimum rate

- a switch-over rule to be introduced into tax treaties that would permit a residence jurisdiction to switch from an exemption to a credit method where the profits attributable to a PE or derived from immovable property (which is not part of a PE) are subject to an effective rate below the minimum rate, and

- a subject to tax rule that would subject a payment to withholding or other taxes at source and adjust eligibility for treaty benefits on certain items of income where the payment is not subject to tax at a minimum rate (the intention is that this would complement the undertaxed payment rule (which is limited to related party payments))

These rules would be implemented by way of changes to domestic law and tax treaties and would incorporate a co-ordination or ordering rule to avoid the risk of double taxation that might otherwise arise where more than one jurisdiction sought to apply these rules to the same structure or arrangement.

The three aspects on which comments are invited during this consultation are:

- whether financial accounts should be used as a starting point for determining the tax base

- the extent to which income and taxes from different sources can be combined or blended to arrive at the effective tax rate, and

- possible carve-outs and thresholds for the GloBE rules, e.g. a de minimis level and sector approaches

A public consultation meeting on the proposal will be held on 9 December 2019.

Public consultation document Global Anti-Base Erosion Proposal (GloBE) – Pillar Two

Contributed by Joanne Houghton

VAT

Flat Rate Scheme capital expenditure (Lecture B1166 – 15.28 minutes)

Summary - The props and rooms used by an escape room company were capital items under the flat rate scheme. The Invoices related to supplies of finished installed rooms and that these were single supplies of goods and so input tax was recoverable

The Great Escape Game Limited operates escape room games whereby players are locked in a themed room and must navigate various puzzles and tasks in order to unlock the room and "escape".

The rooms have panels attached to stud walling. Fibreglass parts then go into the panel to act as part of the puzzles or as sets and props to support the theme. Screens are fitted into the panels to act as monitors for playing visual and audio media and giving instructions. Other sets and props are located within the room, again as puzzles or to support the theme and to immerse the players in the game. There may be doors, gates or suspended ceilings. Speakers and lighting are in the ceilings and can be triggered at various points during the game. Other interaction is provided using electronics. An example of a Room was called "Mad Scientist" in which there was a periodic table with LED lights, cabinets of bubbling liquids and Bunsen burners.

In principle, the rooms (including the panels) could be dismantled and reinstalled elsewhere. The Great Escape Game Limited purchased a number of finished installed rooms from another company and (where it was not the whole Room being purchased) sets and props installed in a room.

The Great Escape Game Limited claimed that all of the invoices related to supplies of capital expenditure goods and so input VAT was recoverable as it exceeded the £2,000 threshold. They argued that the rooms, sets and props were used to generate income over a number of years and that the majority of the cost and value was the manufacture of the assets. Further, the rooms, sets and props were not part of the building and were not consumed by Great Escape. Finally they argued that the invoices should be analysed by reference to what they were providing as a whole rather than the individual items on them and so all exceeded the £2,000 threshold.

HMRC disallowed the input tax claimed arguing that the invoices related to the design and installation of the themed rooms and so were a supply of services. The Great Escape Game Limited was not purchasing a room, but the services of designers, manufacturers, and labourers to design and install the rooms. The supplies of building materials in relation to the rooms were not capital expenditure goods, although they may have be used to create something capital in nature.

So the issues to be determined were:

- Whether or not Great Escape's purchases were of supplies of goods.
- To the extent that the supplies were of goods, whether or not they were capital expenditure goods.
- To the extent that the supplies were of capital expenditure goods, whether or not they were of a value of more than £2,000.

Decision

The First tier Tribunal concluded that The Great Escape Game Limited bought finished installed rooms They gave designs to Norse Sky and, in return for payment, received the rooms in situ. The Tribunal also found that the purchases in respect of the prop invoices were supplies of finished installed sets and props and that these were single supplies of goods.

The Tribunal disagreed with HMRC's view that the majority of Norse Sky's work was in the design and installation of the room, with the supply of the goods themselves being ancillary. The majority of the design work was carried out by The Great Escape Game Limited. The design worked by Norse Sky was considered to be ancillary to the supply of the rooms. Similarly, the process of installing the rooms was incidental to the supply of the rooms because that is how they were to be supplied. Any services involved in the design and supply were ancillary to the principal supply of the rooms.

On the second point, the Tribunal concluded that the supplies of goods in respect of the room and prop Invoices were of capital expenditure goods. Both the rooms and the props were used as fixed assets in its business to generate income on an on going basis; neither were consumed.

Finally, the Tribunal held that the supplies of capital expenditure goods in respect of both the room and prop invoices had a value, together with the VAT chargeable, of more than £2,000. As the rooms and props were supplied in situ as finished articles, it would be artificial to treat the different components of the charges making up the rooms and props as individually priced goods.

The Great Escape Game Limited v HMRC (TC07375)

Retrospective Flat Rate registration **(Lecture B1166 – 15.28 minutes)**

Summary - HMRC cannot use their discretion to back a request for a Flat Rate Registration in order to provide funds for a struggling business.

The Holy Cow! Ice Cream Company Ltd, owned by Ms Gutane and Mr Sutton, its two directors began trading in 2016 and registered for VAT in that year. However, the Directors over-estimated the Company's turnover and profits, and it began to make losses.

In August 2017 the company applied to enter the VAT Flat Rate Scheme (FRS), backdated to 1 January 2017. The backdating was requested to enable the company to recover a further £2,000, which would have covered its losses for a three month period

However, HMRC granted the application on 10 November 2017, but only with effect from 1 July 2017. This was because HMRC's guidance states that backdating is not allowed for VAT periods for which a trader has already calculated its liability. The purpose of the FRS is to "simplify the recording of sales and purchases for small business by removing the need to keep detailed records of sales and purchases". It was not designed "as a means of increasing/ensuring the financial viability of a business".

The company appealed against the refusal to backdate for the first two quarters, on the basis that it was within the "exceptional circumstances" part of HMRC's guidance (FRS3300).

This states that the backdating policy may be disapplied in "exceptional circumstances" such as where "the survival of the business" is in issue. HMRC argued that the facts showed that the company's survival was not at risk, and the requested repayment of just over £2,000 was too small to have prevented the redundancies that occurred.

Decision

The First Tier Tribunal stated that FRS implements Article 24 of the Sixth Directive, which states that Member States can apply "simplified procedures such as flat-rate schemes for charging and collecting the tax provided they do not lead to a reduction".

In this case, the company had already filed its VAT returns for the earlier periods and was seeking backdating in order to obtain a cash refund. This would have been ultra vires HMRC's discretion to backdate. The Tribunal concluded that HMRC do not have the legal power to backdate in order to provide a cash refund to a struggling business.

Even if HMRC did have the power to backdate the registration, this was not possible in this case as the company's survival was ensured by:

- the personal loan obtained by the Directors
- one of the wife's working without pay for four months.

Holy Cow! Ice Cream Company Ltd v HMRC (TC07400)

Sports club pavilion (Lecture B1166 – 15.28 minutes)

Summary – A community amateur sports club (CASC) that wished to take advantage of the tax benefits of being a charity could deregister as a CASC and register as a charity, but it could not be both a CASC and a charity. Zero rating was not applicable.

Eynsham Cricket Club built a pavilion for the use by members and the local community. As a charity, the Club believed that it was eligible to receive zero-rated building services from its contractor (Sch 8 Group 5 VATA 1994)

Although it was a community amateur sports club (CASC), it was not registered with the Charity Commission and so HMRC refused the claim.

The First-tier Tribunal dismissed the Club's appeal, and the matter progressed to the Upper Tribunal.

Decision

The Upper Tribunal said it was common ground that a purpose of Charities Act 2006, s5(4) was to absolve CASCs from having to comply with the requirements of registering as a charity. A sports club could choose to be a CASC and exempt from registration, or a charity and access more generous tax reliefs, but not both.

The taxpayer's appeal was dismissed.

Eynsham Cricket Club v HMRC [2019] UKUT 0286 (TCC)

Adapted from the case summary in Taxation (24 October 2019)

Annexe to church

Summary – The construction costs of building an annexe to an existing church were held to be zero rated.

The initial planning application submitted by Immanuel Church, Bournemouth, provided for the construction of a new extension/annexe on the left-hand side of the existing church building, substantial renovations to the hall at the rear of the church building, and the construction of two flats above the hall for the accommodation of theological students.

The building works that were the subject of this appeal related only to the new extension/annexe constructed on the left-hand side of the church building, a self-contained area intended to be used for meetings. The new building was connected to the hall at the rear of the church by a covered corridor area that ran along the back of the church and the new building. In addition, the new building shared a dog-leg wall with the church along one side.

The issue was whether the construction works fell under Sch 9 Group 5 VATA 1994 qualifying for zero rating which would be the case if the building was an independent annexe. HMRC accepted that the building could be an annexe capable of functioning independently. However they argued that it was in fact an enlargement/ extension of an existing building, rather than a new annexe.

Decision

The First-tier Tribunal found that the existence of the corridor was not sufficient to render the new building an extension of the church and that the wall clearly linked the new building to the church.

However, the First-tier Tribunal considered the tests from Cantrell v HMRC to be important and so looked at the appearance, layout and function of the new building:

1. It was built in an different style to the existing church;

2. It was clearly not suitable for use as a church;

3. It could not be used as an extension of the church as the only access between the two buildings was through a single set of fire escape doors which could only be opened from the church side.

The Tribunal concluded that the new building was an independent annexe making the construction works zero-rated.

Immanuel Church v HMRC (TC07384)

VAT Group rules reformed **(Lecture B1166 – 15.28 minutes)**

Prior to 1 November 2019, only corporate bodies, limited companies or LLPs which have a business establishment in the UK, have been able to join a VAT group.

In 2015, the CJEU's decision in two cases (C-108/14 and C-109/14) meant that HMRC had to extend the eligibility to comply with EU law and so, from 1 November 2019 the rules as to who can be a member of a VAT group have been expanded. From this date partnerships, sole traders and trusts can join a VAT group provided that the they:

- are entitled to register for VAT as a stand-alone business;
- control all of the corporate bodies in the group.

As has always been the case, when forming a VAT group the benefits to consider are cashflow and reduced administration:

- old registrations are cancelled by deregistration;
- the new group obtains its own VAT number issued by HMRC;
- supplies between group members are outside the scope of VAT;
- a single VAT return will be completed for the group as a whole;
- all group members are jointly and severally liable for any VAT debts of the group.

http://www.legislation.gov.uk/uksi/2019/1348/made

http://www.legislation.gov.uk/ukpga/2019/1/schedule/18/enacted

New rules for refunds and extra payments (Lecture B1170 – 11.38 minutes)

Even though it is now 46 years old, there are still some basic flaws in our VAT system that occasionally need sorting out with a change in the law. One such change took effect on 1 September 2019, relating to VAT adjustments that are made when prices change. The new measure is aimed at ensuring that the regulations cannot be abused by only allowing VAT to be adjusted on a return if the price is reduced when refunds are actually made to customers.

Law change (Revenue and Customs Brief 6(2019))

Regulation 38 of the 1995 VAT Regulations deals with situations where a business has charged and declared output tax on a supply of goods or services but then the price subsequently changes in the future. In practical terms, this price movement is more likely to be downwards. The new brief addresses these issues by making amendments to Part 3 and Part 5 of the regulations.

Example

Let's imagine that a builder does some work for a client and charges £100,000 plus VAT as an advance fee in October 2019 – he receives this payment and accounts for output tax on his December 2019 VAT return.

However, the job goes wrong and the builder agrees to reduce the job to £60,000 plus VAT, issuing a credit note (with a current date) for £40,000 plus VAT. The new regulations make it very clear that he can only reduce the output tax on his VAT return by £8,000 if he makes an actual refund of £48,000 to the customer or other person entitled to receive the payment. And the customer (if he is VAT registered and able to claim input tax) is only obliged to reduce his input tax if he receives the refund. So, if the builder raises a credit note on 14 March 2020, and pays a £48,000 refund to the customer on the same day, he will reduce his output tax by £8,000 on his March 2019 VAT return.

Timing

A supplier has 14 days to issue a credit note from the date that the refund is made, which must be adjusted in the same VAT period as the refund is given or received. In the case of upward price movements, the supplier must issue a debit note within 14 days of when the change is agreed with the customer. The failure to issue a debit or credit note within these time limits is a mistake that needs to be corrected under the error correction procedures. (VAT Notice 700/45)

Credit note for VAT registered customer

An opportunity that is sometimes forgotten is that VAT does not need to be adjusted on a credit note if both the supplier and customer agree to this outcome. This will only be relevant where the customer is fully taxable, i.e. the VAT on the original invoice was claimed as input tax and was not a cost to the customer. That outcome is still available with the new procedures (*VAT Notice 700, para 18.2.1).*

Finally, Regulation 38 does not apply when the price is adjusted in the same VAT period as the original VAT was declared.

Tribunal case won by HMRC

In the case of Inventive Tax Strategies Ltd (In Liquidation) [2019] UKUT0221 plus three others (herein referred to as ITS), the company received advance payments for a tax planning scheme and accounted for output tax. The scheme then failed, so customers were entitled to a full refund and a credit note was therefore raised by ITS, but no refund was ever made because the company went into liquidation. The case was originally heard in the FTT back in 2017, and the judge concluded that the reduced output tax claimed by the taxpayer on their VAT returns had been rightly disallowed by HMRC because there had been no refund paid for the supplies in question. Any doubt about the above decision is removed with the change in law from 1 September 2019. The change in law reflects HMRC's view in this case that in order for ITS to reduce its output tax, there had to be "an actual transfer of that consideration" to the customer – in other words, no refund means no output tax credit. The commercial reality was that ITS had provided tax services and received a fee, and there was no entitlement to reduce the output tax paid on this fee because the company had received consideration which they never repaid.

Conclusion

The aim of the new rules is to stop a business making a price reduction to gain a VAT advantage without refunding customers. The new rules "put it beyond doubt" that Regulation 38 can only be used to reduce VAT paid to HMRC when a refund is actually made.

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