Tolley®CPD

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Autumn Statement (Lecture B1347 – 15.32 minutes)

Personal Taxes

Reduction to the additional rate band threshold

The additional rate threshold for income tax will reduce from £150,000 to £125,140 with effect from 6 April 2023.

The new threshold is £125,140 because the personal allowance is abated where the individual's taxable income is between £100,000 and £125,140 (ie £100,000 plus (£12,570 x 2)). Had the new additional rate threshold been £125,000, this would have led to an effective marginal tax rate of 67.5% for income between £125,000 and £125,140 due to the withdrawal of the personal allowance and the 45% tax rate.

This change affects the taxable income of English, Welsh, Northern Irish and non-resident taxpayers and the savings and dividend income of Scottish taxpayers. Scottish taxpayers pay income tax on non-savings non-dividend income (commonly referred to as 'non-savings income' in practice) in accordance with the Scottish income tax rates and bands. Although the Welsh Government has the power to vary the rate of income tax that applies to non-savings income of Welsh taxpayers (although no such changes to the rates have been implemented to date), it cannot vary the levels of the tax bands or create new tax bands.

The Scottish Budget is due to take place on 15 December 2022, but even if the Scottish Government decides not to mirror this change and retains the threshold for the top rate (the name for the Scottish additional rate) at £150,000, this does not mean that Scottish taxpayers with non-savings income between £125,140 and £150,000 in 2023/24 will pay less income tax than those in the rest of the UK. This is because the gap between the higher rate threshold that applies to Scottish taxpayers (£43,662) compared to the rest of the UK (£50,270) on which the difference in the tax rate is 21% (41% Scottish higher rate less 20% basic rate) outweighs the larger gap between the top rate and additional rate thresholds on which the difference in the tax rate is 4% (45% additional rate less 41% Scottish higher rate).

Individuals with income between £125,140 and £150,000 may wish to consider accelerating income or delaying income tax reliefs in order to increase their taxable income in 2022/23 and reduce their taxable income in 2023/24 to ensure more income is taxed at 40% rather than 45%.

Income tax, NIC, CGT and IHT allowances and thresholds

The following announcements were made in respect of allowances:

1. Personal allowance — the allowance was already frozen at £12,570 until 5 April 2026 and has now been extended to 5 April 2028. This also means that the transferable tax allowance (also known as the marriage allowance) is frozen at £1,260 until the same date.

2. Blind person's allowance — the allowance is £2,870 for 2023/24 (increased from £2,600 for 2022/23).

3. Married couple's allowance — the maximum allowance is £10,375 for 2023/24 and the minimum allowance is £4,010 (increased from £9,415 and £3,640 in 2022/23). The level of the taxpayer's adjusted net income determines whether the allowance is abated, but the threshold for 2023/24 has yet to be released.

The blind person's allowance and married couple's allowance are uprated by the consumer prices index (CPI) in line with the rules in s.57 ITA 2007. Note that this section is specifically disapplied to order to freeze the personal allowance.

The Chancellor also announced:

1. Dividend nil rate band or dividend allowance — reduced from £2,000 to £1,000 from April 2023, and to £500 from April 2024.

2. Income tax higher rate threshold — the higher rate threshold (which is the basic rate band plus the personal allowance) is frozen at £50,270 until 5 April 2028. This means that the basic rate band remains £37,700 for this period. The higher rate threshold applies to the taxable income of English, Welsh, Northern Irish and non-resident taxpayers and the savings and dividend income of Scottish taxpayers. A Scottish Budget announcement is expected on 15 December 2022 to clarify the position for Scottish taxpayers.

3. NIC for employed persons — the upper earnings limit for employees and the upper secondary threshold, apprentices' upper secondary threshold and veteran upper secondary threshold for employers will remain frozen at £50,270 until 5 April 2028.

   The lower earnings limit for employees will be frozen at £6,396 (the 2022/23 level) in 2023/24.

   The primary threshold for employees will remain frozen at £12,570 (ie the level of the personal allowance) until 5 April 2028.

   The secondary threshold for employers will be fixed at the current level of £9,100 from 6 April 2023 to 5 April 2028.

   The employment allowance available to most small employers which reduces their liability to secondary Class 1 NIC will remain unaffected at £5,000.

   The freeport upper secondary threshold will be fixed at £25,000, but it is unclear as to how long the freeze will remain in place.

4. NIC for self-employed persons — the Class 4 NIC lower profits threshold increases to £12,570 on 6 April 2023 and will remain frozen at this level until 5 April 2028.

   The Class 4 NIC upper profits limit will remain frozen at £50,270 (i.e., the same as the higher rate threshold) until 5 April 2028.

   The Class 2 NIC weekly contributions for 2023/24 will be £3.45 (increased from £3.15 per week in 2022/23).

   There is some confusion surrounding the Class 2 NIC small profits threshold as paragraphs 5.17 and 5.18 of the Autumn Statement contradict each other. The HMRC Press Office has been approached for clarification.

NIC voluntary contributions — the Class 3 weekly contributions for 2023/24 will be £17.45 (increased from £15.85 per week in 2022/23).

As expected, the Inheritance tax nil rate band and residence nil rate band are frozen for a further two years until 5 April 2028 at £325,000 and £175,000 respectively. The residence nil-rate band taper will continue to start at £2million.

Finally, then Chancellor announced that the CGT annual exempt amount will be reduced from £12,300 to £6,000 from April 2023 and to £3,000 from April 2024.

Car, van and fuel benefit charges

From 6 April 2023 car and van benefit charges will rise in line with the Consumer Price Index (CPI). The same will apply to car and van fuel benefit charges.

Company car tax

It is intended that there remains an incentive for the provision of electric and ultra-low emissions cars, and that taxpayers have long term certainty in this area. Therefore, it has been announced that the Autumn Finance Bill 2022 will set rates until April 2028.

From 2025/26 onwards appropriate percentages for electric and ultra-low emission cars with CO_2 emissions of less than 75g/km will increase by 1% per year until 2027/28. A maximum appropriate percentage of 5% will apply for electric cars and 21% for ultra-low emission cars

Rates for all other vehicles bands will also increase by 1% in 2025/26. A maximum appropriate percentage of 37% and will then be fixed in 2026/27 and 2027/28.

The state pension triple lock

The basic state pension generally rises by the greater of either:

1) the average annual increase in UK earnings; or

2) the annual increase in the cost of living, as calculated by the consumer price index;

3) 2.5%.

For 2022/23 only 1) above has been disregarded in determining the increase.

The government confirmed that it is increasing the state pension from April 2023 by inflation, in line with the commitment to the triple lock. Per week, a full basic state pension will increase from £141.85 to £156.20, and the new state pension will increase from £185.15 to £203.85.

The standard minimum income guarantee in pension credit will also increase in line with inflation from April 2023, rather than in line with average earnings growth.

Under s.27 Pensions Act 2014, the Government is required to review the state pension age every six years. The first review was published in March 2017 and the Chancellor announced that the next review will be published in early 2023.

Business Taxes

OECD Pillar 2 and the UK multinational top-up tax

The Government confirmed it will continue with the implementation of the OECD's Pillar 2 proposals as expected, but with a little more detail on expected timescales. In July 2022, draft legislation was published setting out the provisions needed for the UK's adoption of the Income Inclusion Rule (IIR), the main charging mechanism of the OECD's Global Anti-Base Erosion (GloBE) rules, by introducing a new multinational top-up tax in the UK. The new tax will apply for accounting periods beginning on or after 31 December 2023.

In today's announcement, the Government confirmed its commitment to implement the second charging mechanism of the GloBE rules, the Undertaxed Profits Rule (UPR), but with effect no earlier than accounting periods beginning on or after 31 December 2024. It has also been confirmed that a supplementary Qualified Domestic Minimum Top-up tax (QDMTT) rule will be introduced with effect for accounting periods beginning on or after 31 December 2023. This rule will require large groups, including those operating exclusively in the UK, to pay a top-up tax where their UK operations have an effective tax rate of less than a prescribed minimum of 15%. This would allow any top-up tax due under the Pillar 2 framework from UK economic activities to go directly to the UK Exchequer, rather than to another country. Draft legislation for the QDMTT has not yet been published, although the provisions will be included in Spring Finance Bill 2023 along with those referred to above for the IIR.

Research and development

The government announced changes to the rates of relief for research and development expenditure under the RDEC and SME relief schemes. The changes will apply to expenditure incurred on or after 1 April 2023 and will be included in the Spring Finance Bill 2023. The intention is to rebalance the reliefs available under the two schemes and is a step towards a single RDEC-like scheme for all companies. The new rates are as follows:

1. RDEC–20% (currently 13%)
2. SME additional deduction–86% (currently 130%)
3. SME tax credit–10% (currently 14.5%)

The government intends to consult on the design of a new single scheme and will work with industry to understand whether further support is needed for research intensive SMEs. The Spring Finance Bill 2023 will also include changes to R&D reliefs announced at the Autumn Budget 2021: expanding qualifying expenditure to include data and cloud costs, refocusing support towards innovation in the UK, and targeting abuse and improving compliance.

Anti-avoidance on share for share exchanges

The government will introduce legislation in the Spring Finance Bill 2023 to treat shares in a non-UK company held by an individual as located in the UK where the shares were acquired in exchange for shares in a UK company. In particular, the new rules are intended to prevent non-UK domiciled individuals from applying the remittance basis to gains realised on a subsequent disposal of the non-UK company shares and to dividends received in respect of those shares. The new rules will apply with immediate effect to share exchanges and schemes of reconstruction carried out on or after 17 November 2022.

The rules will apply only where both companies are close companies (or would be if they were resident in the UK). A UK company for this purpose is one incorporated in the UK and a non-UK company is one incorporated outside the UK. The individual must hold at least 5% of the shares in the UK company before the exchange and 5% of the shares in the non-UK company afterwards. Exchanges involving debentures also fall within the rules.

Where the conditions are met, the new holding of shares in the non-UK company is treated as located in the UK for CGT purposes, as a 'deemed UK holding'. Distributions in respect of such a holding are not foreign income for income tax purposes. Deemed UK holding treatment will continue following a disposal to a spouse or civil partner and to new holdings following further share exchanges. Additional shares acquired in the same non-UK company will also be treated as located in the UK.

It will be possible for an individual to opt out of deemed UK holding treatment by electing to disapply the CGT share reorganisation provisions on the exchange. The effect is that a capital gain will arise at the time of the exchange. An election must be made by the first anniversary of 31 January following the tax year in which the exchange took place.

Windfall taxes - energy profits levy and electricity generator levy

The Energy Profits Levy (EPL, also commonly referred to as the Oil and Gas Windfall Tax) will increase to 35% from 1 January 2023 and will apply until 31 March 2028 (ie it will not be phased out before then). This brings the headline tax rate for the oil and gas sector to 75%. The investment allowance will also reduce to 29% for all investment expenditure (other than decarbonisation expenditure), to maintain its existing cash value. Decarbonisation expenditure (such as installing bespoke wind turbines to power the production installation) will continue to qualify for the existing 80% investment allowance rate. Legislation for this is expected in the Autumn Finance Bill 2022 (with the decarbonisation expenditure changes to be included in the Spring Finance Bill 2023).

A new, temporary Electricity Generator Levy (EGL) will apply from 1 January 2023 at a rate of 45% to 'extraordinary returns' made as a result of the current high price of low-carbon electricity. The structure of the UK energy market means that cheap, low-carbon electricity is priced at a more expensive rate when oil and gas prices are high, leading to higher profits. 'Extraordinary returns' will be defined as 'the aggregate revenue that generators make in a period from in-scope generation at an average output price above £75/MWh'. The cumulative tax rate on earnings over £75Mwh will be 70%. The EGL will only apply to larger electricity generators and large returns, namely those generators whose output exceeds 100GWh across a period and returns exceeding £10 million. Legislation will be included in the Spring Finance Bill 2023.

The EGL technical note published alongside the Autumn Statement 2022 sets out some details of the design of the levy.

It will apply to companies that undertake electricity generation from nuclear, renewable and biomass sources in the UK and are either connected to a national grid or connected to local distribution networks.

It will not apply to electricity that is generated under a contract for difference entered into with the Low Carbon Contracts Company Ltd.

The levy will apply to 'Exceptional Generation Receipts' calculated at an aggregate level across a group in respect of a qualifying period.

The measure of revenue used in the EGL calculation will be the revenue received in the qualifying period irrespective of when the relevant contracts were entered into.

The qualifying period will be aligned to the accounting period of the company responsible for administering the levy for the group.

It will not be deductible for corporation tax purposes and will be administered in the same was as corporation tax (and so will need to be included in the responsible company's Corporation Tax Return and paid on its normal payment dates for corporation tax).

HM Treasury and HMRC are consulting with electricity generators to discuss how the EGL will be implemented in legislation.

The government will also launch a consultation as part of a review of the long-term tax treatment of the North Sea, with a report expected by the end of 2023.

Other business and enterprise measures

The following measures were also announced:

1. First year allowances on electric vehicle charging points—expenditure incurred on new plant or machinery to be used solely for electric vehicle charging points attracts 100% first year capital allowances. This relief was due to end in 2023 but will now be extended for expenditure up to 31 March 2025 for corporation tax and 5 April 2025 for income tax.

2. From April 2023 multinational businesses operating in the UK will be required to keep and retain transfer pricing documentation in a prescribed and standardised format as set out in the OECD's Transfer Pricing Guidelines.This would apply to both the master file and the local file.

   HMRC will continue to consult on a summary audit trail which is a questionnaire that businesses would be required to complete that covers the main steps undertaken in preparing the local file.

   These measures were previously announced at Legislation Day 2022 along with draft clauses to be included in the Spring Finance Bill 2023.

3. The annual chargeable amounts for ATED for the 2023/23 charging period will be increased by the September CPI figure of 10.1% and will be implemented, as usual, through Treasury Order.

Corporation tax rates

The government confirmed that the increase in corporation tax rates for financial year 2023 onwards will come into effect as planned following the reinstatement of the CT increase.

It was also confirmed that the bank surcharge and the diverted profits tax will also increase from this date. Therefore from April 2023, banks will be charged an additional 3% on profits in excess of £100 million and the diverted profits tax will be increased to 31%.

VAT and Indirect Taxes

VAT registration threshold frozen for further two years

The government announced that the VAT registration and deregistration thresholds will not change for a further period of 2 years from 1 April 2024. This measure maintains the VAT registration threshold at £85,000 and the deregistration threshold at £83,000 (thresholds which have been in place since 1 April 2017.

The Office of Tax Simplification (OTS) had previously identified that the VAT registration threshold may cause distortions, particularly given that the UK's VAT registration threshold is more than twice as high as the EU and OECD averages. The OTS set out that a lead option to deal with such distortions would be to lower the thresholds. However, it was acknowledged that reducing the thresholds could simply move the point at which the distortion takes place. Despite this background, the maintenance of the current VAT registration thresholds aims to provide businesses with certainty and allow them to make decisions in the knowledge that current thresholds will not change until at least 31 March 2026.

CCL main rates and discounts

The government will legislate in Spring Finance Bill 2023 for the following CCL main rates and discounts in 2024-25:

1. the main rate of CCL on gas to £0.00775/kWh in 2024-25 (from £0.00672/kWh in 2023-24)
2. the main rate of CCL on electricity will be frozen at £0.00775/kWh
3. the main rate of CCL on solid fuels will rise to £0.06064/Kg (from £0.05258 in 2023-24)
4. the main rate of CCL on LPG will remain at £0.02175/Kg
5. the percentage discount on CCL main rates available through the Climate Change Agreement scheme will remain at 92% for electricity and 77% for LPG
6. the percentage discount on CCL main rates available through the Climate Change Agreement scheme for gas and solid fuels will be adjusted to 89% (from 88% in 2023-2024)

These changes will fulfil a commitment from Budget 2016 to equalise the main rates of CCL on gas and electricity.

Two-year removal of tariffs on certain goods

Tariffs will be suspended on over 100 goods for two years.

Goods affected will include (but are not limited to):

1. aluminium frames used by UK bicycle manufacturers
2. ingredients used by UK food producers

Vehicle Excise Duty on electric vehicles

From April 2025, Vehicle Excise Duty (VED) will apply to electric cars, vans and motorcycles under legislation that is to be introduced in Autumn Finance Bill 2022.

Zero emission cars first registered between 1 April 2017 and 31 March 2025 will be liable at the standard rate, which is currently £165 a year.

New zero emission cars registered after 31 March 2025 will be liable at the lowest first year rate, which currently applies to vehicles with CO_2 emissions from 1g/km to 50g/km at the rate of £10 a year. From the second year of registration onwards the standard rate will apply.

Other measures

Stamp duty land tax-expiry of changes in the Growth Plan 2022

In the Growth Plan 2022, Kwasi Kwarteng announced that the stamp duty land tax (SDLT) nil rate threshold for residential property purchases in England and Northern Ireland would increase from £125,000 to £250,000 with effect from 23 September 2022. Where all buyers in the transaction are first-time buyers and the purchase price is £625,000 or less, the nil rate threshold is £425,000 from the same date.

These changes are retained and will be legislated in the Stamp Duty Land Tax (Reduction) Bill, but the Chancellor announced that these amendments to the thresholds (including the maximum purchase price for first-time buyer relief) will expire on 31 March 2025. The Bill will be amended to implement this sunset date.

As such, the pre-23 September 2022 SDLT rates and thresholds will apply to all residential property transactions, including those involving first-time buyers, with effect from 1 April 2025 onwards. This is forecasted to raise significant amounts for the Exchequer and it remains to be seen whether a rush to take advantage of these thresholds will bolster an otherwise slumping market as interest rate rises, the cost of living crisis and recession bite.

Online sales tax

Following consultation, the government has decided not to introduce an online sales tax (OST), an idea looked at as a means to rebalance the taxation of the retail sector between online and in-store. The government's decision reflects concerns raised about an OST's complexity and the risk of creating unintended distortion or unfair outcomes between different business models. A response to the OST consultation will be published shortly.

Audio-visual creative tax reliefs

Various tax reliefs are available for businesses in the creative sector which include film, animation, high-end TV, children's TV and video games tax relief. The Government is consulting on simplifying and modernising these reliefs. The consultation does not cover creative tax reliefs available to museums, orchestras and galleries.

Business rates and Council tax

Business rates will be based on updated property valuations from 1 April 2023. Targeted support will be offered to support businesses through the transition. The business rates multipliers will also be frozen in 2023/24.

A number of reliefs are being introduced or extended, namely:

1. the transitional relief scheme, which will cap bill increases caused by the 2023 revaluation;

2. retail, hospitality and leisure relief, which is extended and will increase to 75% business rates relief up to £110,000 per business;

3. the supporting small business scheme, which will cap bill increases for certain of the smallest businesses at £600 per year from 1 April 2023;

4. improvement relief, available between April 2024 and 2028, which means ratepayers will not have increased business rates as a result of improvements they make to a property they occupy for 12 months.

Local authorities in England are being given additional flexibility in setting council tax rates. The referendum limit for increases in council tax will be raised to 3% per year from April 2023 and local authorities with social care responsibilities will be able to increase the adult social care precept by up to 2% per year.

Tax Conditionality: Licensing in Scotland and Northern Ireland

Tax conditionality refers to a principle whereby businesses are granted access to Government awards and authorisations only if they can demonstrate good tax compliance. From 4 April 2022, firms applying for licences in England and Wales to drive taxis and / or private hire vehicles (PHVs), to operate a PHV business or to deal in scrap metal are only able to obtain or renew a licence to operate if they carry out a tax check.

The government had planned to extend the provisions to Scotland and Northern Ireland from April 2023 for access to, or renewal of, licences to drive taxis. In Scotland it will also apply for access to licences to operate a private hire booking office, or deal in scrap metal. These provisions will now come into force for license renewals from October 2023 rather than April 2023. This measure will be legislated for in Spring Finance Bill 2023.

National Living Wage (NLW) and National Minimum Wage (NMW) Uprating

Following the recommendations of the independent Low Pay Commission (LPC), the government will increase the NLW for individuals aged 23 and over to £10.42 an hour from 1 April 2023.

The government has also accepted the LPC's recommendations for the other NMW rates to apply from April 2023, as follows:

1. 21-22 year olds £10.18 an hour

2. 18-20 year olds £7.49 an hour

3. 16-17 year olds £5.28 an hour

4. apprentices £5.28 an hour

https://www.gov.uk/government/publications/autumn-statement-2022-documents

Adapted from the summary produced Tolley

Personal tax

Employee, worker or self-employed (Lecture P1346 – 18.07 minutes)

Summary – Using the Construction Industry Scheme was only one of the factors to be considered in determining the individual's correct status. Looking at the findings as a whole, the only proper conclusion was that the individual was an employee.

From 2010, Lee Richard worked as a skilled carpenter on a self-employed basis, receiving net payments under the CIS from the company that he worked for.

In 2018, the company he worked for reviewed its arrangements and sought to engage him under an employment contract. For most of the time that followed, he was on sick leave and later resigned.

Lee Richard appealed to an employment tribunal, claiming that he had been an employee throughout the period of engagement; not just from 2018.

The employment tribunal dismissed the appeal stating that both parties had agreed to pay him on a self-employed basis through the CIS.

Lee Richard appealed to the Employment Appeal Tribunal.

Decision

The appeal tribunal found that the employment tribunal had erred in finding, in a working relationship which had numerous indicators of employment status and only one in favour of self-employment, that the latter should determine the issue.

The Tribunal found that Lee Richard was an employee and remitted the appeal to the Employment Tribunal with an instruction that it had to proceed on that basis.

Justine Riccomini, head of tax (employment and devolved taxes) at ICAS, stated:

> 'Having read through both case transcripts, it occurs to me that the original employment tribunal (ET) judgment focused on the fact the appellant was registered for CIS purposes rather than the underlying facts of the working arrangements. This appears to have been a distraction. The facts described in the ET decision state that the appellant was a skilled carpenter who worked five days a week on an hourly pay rate for the same engager over the best part of a decade, with no other clients to his name, and that the arrangements were, in everything but name, providing for a contract of service
>
> 'To all intents and purposes, the appellant appears to have fallen within the definition of a "labour-only" subcontractor at Construction Industry Scheme Reform Manual CISR13030. Had this factor been considered by the ET, a different conclusion may have been reached.

> 'Usually, for employer's liability insurance purposes, labour-only subcontractors are treated as employees, and HMRC generally expects that labour-only subcontractors should be paid under deduction of PAYE through the payroll rather than being paid under the CIS scheme (see CIS340, section 1.8 – tinyurl.com/ hmrccis340), where HMRC says:
>
> '“For a contract to be within the [CIS] scheme, it must not be 'a contract of employment'. This means that the scheme applies to workers who are self-employed under the terms of the contract, and not employees subject to PAYE.
>
> '“Employment status depends on general law and it's for the contractor to decide on the individual's employment status when the subcontractor is first engaged. The fact that the subcontractor has worked in a self-employed capacity before is irrelevant in deciding on their employment status — it's the terms of the particular engagement that matter.”

This case illustrates how employment legislation and tax legislation are sometimes misaligned and decisions can be skewed as a result. Had this case been heard at the tax tribunal, it is likely the CIS guidance would have been considered.

Lee Richard v Waterfield Homes Ltd and Unity Build & Repairs Ltd, EAT

Working from home – expenses and tax (Lecture B1348 – 9.41 minutes)

Employees who work from home for some or all of the week have a limited range of expenses available to claim. This article Looks at the key points to remember.

Travelling Expenses

Where the employer offers to reimburse travelling expenses for trips to the main office this is very unlikely to attract tax relief. This is because any journey with the employee’s home at one end can only be tax free if the other end of the journey is a temporary workplace. Where the employee works form home for part of the week and at the office for the remainder, this is travel between home and the permanent workplace and is therefore regarded as ‘ordinary commuting’ which is not allowable for tax.

This means that if the employer reimburses this travel or contributes towards it, the amount is taxable as pay (not a benefit in kind) and should therefore be processed through the payroll and be subject to PAYE and NIC in the same way as any other pay.

Temporary workplace

A temporary workplace is somewhere the employee goes to perform the duties of the employment but attends the place to perform a task of limited duration or for some other temporary purpose.

When working from home for part of the week, trips to the office are neither to perform a task of limited duration, nor for another temporary purpose, the journey is merely made to perform the duties of the employment.

Once it has been established that a workplace is a temporary workplace, this is then subject to the limitation of the 24-month rule.

24-month rule

When an employee works at a temporary workplace, if they spend a substantial amount of their time there (at least 40% of their working time) for a period which is expected to exceed 24 months, the workplace is no longer a temporary workplace, and journeys from home lose their tax-free status.

The key part of this test is that tax free status is lost as soon as it is expected that the period will last more than 24 months rather than at the point it exceeds that time period.

Expenses at home

Employees can receive £6 per week tax free from their employer to contribute to heat and light and other household expenses. In the absence of a payment by the employer it is very unlikely that most employees would be able to claim any other form of tax relief on household expenses.

Telephone / internet expenses

If payments are made towards the cost of telephone or internet this can be made in addition to the £6 per week, but the payments will have to exclude private use by the employee. Although HMRC's guidance does recognise that in some cases, additional internet costs might be incurred due to home working, it is unlikely in current times that additional costs would be incurred over and above what an employee would incur privately, so no tax relief would be available. In any event if the contract is in the name of the employee this can give rise to a national insurance liability, as the employer is meeting liabilities which strictly belong to the employee.

Mobile telephone

The employer could provide a mobile phone to the employee for work use. Even if the employee makes significant private use of the phone, it is an exempt benefit giving rise to no tax charge provided the contract for the phone is in the name of the employer.

Contributed by Rebecca Benneyworth

Trivial benefits exemption and directors (Lecture B1350 – 12.03 minutes)

Background

There are some useful and well-known exemptions from an income tax charge on employment income. A useful income tax exemption is for 'trivial' benefits provided by employers. The exemption is perhaps more helpful and wide ranging than some employers and their employees might assume. For example, the exemption applies to benefits provided to the employee or to a member of the employee's family or household. It also applies where the benefit is provided by a third party on the employer's behalf (e.g., by a related management services company).

There are no Class 1A National Insurance contributions (NICs) on benefits which are exempt from income tax (in SSCBA 1992, s 10(1)(a)). In addition, there is an exception from Class 1 NICs for non-cash vouchers (in SI 2001/1004, Sch 3, Pt V, para 6(da)).

Exemption conditions

The trivial benefits exemption is subject to various conditions contained in ITEPA 2003, s 323A).

- Conditions A to D apply to employees, and
- Conditions A to E apply if the employee is a director or other office holder (or a family or household member) of a close company employer.

The conditions are as follows:

- Condition A is that the benefit is not cash, or a 'cash voucher' as defined in the legislation (in ITEPA 2003, s 75).
- Condition B is that the benefit cost does not exceed £50. The 'benefit cost' is simply defined as the cost of providing the benefit. Alternatively, if the benefit is provided to more than one person and it is impractical to calculate the cost per person (e.g., due to the nature of the benefit, or the scale of its provision) the benefit cost is the average cost per person of providing the benefit. So, the total cost of providing the benefit is divided by the number of persons to whom the benefit is provided. HMRC's Employment Income manual (at EIM21865) features several useful examples of the exemption and benefit calculations.
- Condition C is that the benefit is not part of 'relevant salary sacrifice arrangements' or other contractual obligations. The term 'relevant salary sacrifice arrangements' is defined for these purposes as arrangements whereby the employee gives up the right to receive an amount of general earnings or specific employment income in return for the benefit (ITEPA 2003, s 323A(8)).
- Condition D is that the benefit is not provided in recognition of particular employment services performed by the employee as part of their duties, or in anticipation of such services.
- Condition E (which applies to close company employers where the employee is a director or other office holder or a member of their family or household) is that the benefit cost of the benefit provided to the employee (or the amount allocated to the employee, where the benefit is provided to a family or household member who isn't an employee) does not exceed an 'available exempt amount'.

A useful feature of the trivial benefits exemption is that the £50 limit in Condition B applies per benefit, not per tax year.

Available exempt amount

For Condition E, the individual has an available exempt amount of £300.

The benefit cost of 'eligible' benefits (i.e., within conditions A to D) provided by or on behalf of the employer earlier in the tax year are aggregated, together with any eligible benefits earlier in the tax year allocated to the employee in respect of any member of the individual's family or household who are not employees, in calculating the 'available exempt amount'.

If the cost of an additional trivial benefit results in a total cost exceeding the annual cap of £300, none of the benefit that results in the cap being exceeded is exempt (see EIM21869).

Family and household members

A useful feature of the trivial benefits exemption is that members of the office holder's family or household who are employees of the close company are each subject to their own annual eligible benefits exemption of £300 (ITEPA 2003, s 323B(4)). So, there is a potential attraction in employing family members, such as adult children. 'Eligible benefits' in this context are those benefits which satisfy Conditions A to D mentioned earlier.

Many close companies are family companies (i.e., the directors, other office holders and/or employees of a company are members of the same family). Whilst each employed individual is entitled to their own available exempt amount of £300, the company might also have provided benefits to one or more members of the employee's family or household who aren't employed by the company. In those circumstances, the cost of that benefit is divided between those members of the non-employee's family or household who are directors or office holders, or members of that director's or office holder's family or household, or former directors or office holder of the company or members of their family or household.

Recurring or contractual benefits?

If an otherwise qualifying trivial benefit is made on a recurring (e.g., annual) basis, could HMRC contend there is effectively a 'contractual obligation' to it, such as under an informal agreement, which fails Condition C?

This possibility cannot be ruled out; each case will depend on the particular circumstances. However, HMRC apparently accepts that just because a gift is provided each year does not necessarily mean that the employee has a contractual entitlement to it; so Christmas or birthday gifts shouldn't normally be challenged (see EIM21867).

What about regular gifts other than at Christmas or on birthdays, or more frequent gifts? HMRC guidance states (at EIM21868): '…if an employer provides their employees with benefits on a regular or frequent basis you should consider whether they are linked to the employee's services.' So it would seem that employers who are regularly or continually generous potentially risk breaching Condition D for exemption purposes.

Even if gifts are non-contractual and non-recurring, they need to be separate benefits to avoid the possibility that they will be aggregated for the purposes of the £50 limit per benefit.

Deductions for trivial benefits

What is the tax position for the employer who provides trivial benefits? The general rule is that the cost of business gifts is not an allowable trading deduction. However, this general rule is subject to certain exceptions.

One such exception is where gifts are provided for employees of the business, unless gifts are also provided for others, and the provision of gifts for the employees is incidental to the provision of gifts for those other persons (ITTOIA 2005, s 47(4); CTA 2009, 1300(4)).

Accordingly, provided the gifts are predominantly provided for employees (as will usually be the case) rather than non-employee family or household members, the provision of benefits within the trivial benefits exemption will generally be tax-deductible for the self-employed, trading partnerships and trading companies.

Contributed by Mark McLaughlin

Contributions to EBT not repayable during liquidation (Lecture P1346 – 18.07 minutes)

Summary - Contributions made by a company to an EBT under an avoidance scheme had been found to be taxable employment income. The director who benefited from the payments made was not liable to repay these sums after the company went into liquidation.

The case was brought by Asertis Limited on behalf of the liquidator against Dale Heathcote, the sole director of Servico Build Tec Limited.

Servico Build Tec Limited had entered an employee benefit trust scheme, with sums totalling £520,000 paid to the trust and used to buy gold. This was provided to the beneficiary, who in this case was the company's sole director. He could keep or sell the asset as he so wished.

The Scheme was designed to allow Dale Heathcote to obtain rewards from the company without tax becoming payable either by the company or by him. However, HMRC enquired into the company's tax returns, concluding that the EBT scheme did not work and that the sums represented taxable employment income.

Later, following the loss of a big contract with Next plc and the announcement of the 2019 Loan Charge, Servico Build Tec Limited went into voluntary liquidation. Asertis Limited claimed that the sums paid to the EBT were repayable by Dale Heathcote as the rewards:

- were neither authorised nor justifiable as remuneration to Mr Heathcote for his services as director and had no other proper basis and, thus, made in breach of his duties to the Company as its director; and/or
- represented transactions at an undervalue defrauding creditors under s.423 of the Insolvency Act 1986; and/or
- were made in breach of what is commonly referred to as the insolvency or creditors' interests duty.

Decision

The High Court found in favour of Dale Heathcote concluding that the payments made represented Dale Heathcote's year-end bonus and were linked to the company's profitability. Dale Heathcote and the company's accountant had entered into the transactions on the basis that if the EBT was found not be tax effective, there would be sufficient funds available, either from the company's profits or Dale Heathcote's own assets, to be able to settle any PAYE or NICs that fell due.

Although the scheme was found to be ineffective for tax, this did not render them recoverable payments. The rewards were always intended to be a form of bonus for services rendered. This fact was included in the company's board minutes. There was no evidence that Dale Heathcote's rewards were excessive or unreasonable as director's remuneration or that they were disguised gifts of capital rather than genuine awards of remuneration.

Asertis Ltd v Mr Dale Heathcote and Servico Contract Upholstery Limited [2022] EWHC 2498

Tenancy deposit scheme nudge letters

Landlords letting property to tenants under assured shorthold tenancies are required to protect tenant deposits by using a government-approved Tenancy Deposit Scheme.

HMRC has compared Tenancy Deposit Scheme information to check consistency with rental income reporting on their 2020/21 Self Assessment tax returns.

Where deposits were made into such a scheme, but rental income declared appears to be lacking, HMRC has sent out nudge letters, giving them 30 days from the date on the letter to submit any amendments.

A template of the letter is available on the CIOT's website.

HMRC has:

- Advised that CGT may be due where such a property has been sold.
- Asked taxpayers to check their 2021/22 return is correct

https://www.tax.org.uk/latest-hmrc-nudge-letters-for-landlords

OTS property income report (Lecture P1346 – 18.07 minutes)

The OTS has published a report on the Income Tax rules for residential property income. The key findings are summarised below.

Furnished holiday lettings (FHL)

Despite the tax benefits offered, the report stated that the FHL regime is not widely used but adds complexity to the tax rules.

If abolished, the OTS acknowledged that this might place pressure on the distinction between whether let property is a trade or a business, with taxpayers seeking the benefits of the trading rules. The OTS recommended that it would be appropriate to introduce a statutory ‘brightline’ test to define when a property trading business was being carried on.

If the regime was retained, the OTS recommends the government consider restricting the relief to commercial lets and changing the rules to cover either just UK or worldwide properties.

Deductibility of repairs, replacements, and improvements

This is a confusing area for taxpayers who find it difficult to decide if costs are immediately deductible as repairs and replacements or, are they disallowable capital improvements.

The OTS recommends that either:

- guidance in this area should be enhanced to include clear examples of common situations; or

- income tax relief should be available on all property costs, except for where the work is part of the capital cost of the building, such as the initial fit-out of properties bought in a dilapidated state or structural work such as extensions to the property. This would make it simpler to administer and support the policy objective of improving the standards of rental property.

Jointly owned property

To bring things in line with all unmarried co-owners, the OTS report recommended that the automatic 50:50 taxation split for spouses and civil partners should be changed so that the split reflects the underlying ownership.

The report also suggested that the government may also wish to consider removing the ability for joint owners to decide on a split other than this ownership.

Making Tax Digital for Income Tax

The OTS report identified several potential areas for improvement, including:

1. allowing joint owners to file one return between them;

2. increasing the minimum threshold for reporting; and

3. delaying the introduction until the system has been improved and tested.

Diversified agricultural-based businesses

in order to make their business viable, the report stated that around 66% of agricultural businesses are diversified and their income may well include property-related income.

The report explains the challenges faced by such businesses in the way the tax system disaggregates streams of income for reporting, availability of reliefs and losses. The review recommends that a 'rural business unit' should be established for tax, to simplify obligations on diversified agricultural-based businesses.

Non-UK residents

Unless a non-UK resident landlord registers to file and pay with HMRC, the Non-Resident Landlord Scheme requires the deduction of tax at source from rents paid to them. This obligation falls on letting agents or, if there are none, on tenants and it is not widely understood. The report highlighted the low compliance with the tax withholding regime and recommended that the government consider reviewing this policy.

If tenant withholding is retained, the government could consider raising the threshold, making the withholding obligation on tenants clearer in guidance and finding ways to raise awareness, and clarifying the process to rectify matters if tenants initially do not withhold.

https://www.gov.uk/government/publications/ots-review-of-residential-property-income

Denial of loss arising under gilt strips scheme

Summary - The taxpayer was denied a substantial tax loss, which purportedly arose in connection with a disposal of gilt strips under a tax avoidance scheme.

The gilt strips scheme broadly involved the following steps:

- the acquisition of gilt strips with a value of circa £1.5m by the taxpayer using borrowed funds;
- the grant of an option to buy the gilt strips to an interest in possession (IIP) trust, of which the taxpayer was the settlor and life tenant for a premium of circa £1.3m, with an exercise price of circa £150,000;
- the assignment of the option in respect of the gilt strips to a bank (Investec) for a payment to the trustee of the IIP trust of circa £1.3m; and
- exercise of the option by Investec with the corresponding payment of the exercise price of circa £150,000 by Investec to the taxpayer.

The taxpayer claimed an income tax loss of circa £1.35m in their self-assessment return.

The taxpayer claimed the income tax loss pursuant to Sch 13 para 14A FA 1996 with the amount of such loss being calculated as the difference between the amount that the taxpayer paid to acquire the gilt strips (circa £1.5m) and the exercise price of the option paid to the taxpayer by Investec (but excluding the premium paid by Investec for the assignment of the option).

The appeal focused on the central issue of whether the transactions in question, applying a Ramsay analysis, entitled the taxpayer to tax relief in light of:

- the fact that a corresponding substantial commercial and economic loss was not suffered by the taxpayer;
- the pre-ordained and composite nature of the component transactions of the scheme; and the fact that the taxpayer had only directly received the exercise price from Investec (with the IIP trust receiving the assignment premium).

Decision

Noting that it was bound by the decision of the Upper Tribunal in Berry v HMRC [2011] UKUT81 (TCC), the First Tier Tribunal held that the concept of 'loss' in the relevant legislation was a legal concept (i.e. it bore the legal meaning conferred by statute) by virtue of the formulaic approach to quantifying the quantum of the loss; however, it also held that 'the amount payable on the transfer' of the gilt strips was a commercial concept deriving its meaning from the 'real world'.

The First Tier Tribunal concluded that there was a single transaction relating to the transfer of gilt strips from taxpayer to Investec. Accordingly, giving the word 'transfer' a wider practical meaning (which encompassed not only the exercise of the option by Investec but also the preceding grant of the option and its assignment), the 'amount payable on the transfer' included the exercise price and the premium paid by Investec to the IIP trust trustee for the assignment (having the effect of reducing the taxpayer's tax loss to a negligible amount).

Timothy Watts v HMRC (TC08634)

Adapted from the case summary in tax Journal (18 November 2022)

Capital taxes

Difficulties with UK property returns (Lecture P1347 – 14.04 minutes)

Recent CGT statistics show that some 137,000 UK property returns were submitted in respect of disposals in 2021/22 and it is estimated that approximately 26,500 of these were filed late (i.e. 19.3% of the total). The position for 2020/21 was even worse, but there were perhaps two reasons for this:

1. The FA 2019 legislation, which introduced the shorter deadline for UK property returns, only took effect from the start of 2020/21. Given that HMRC initially provided minimum publicity and very little detailed guidance about what was then the new CGT reporting system, it was hardly surprising that so many people were unaware of these rules in their first year of operation. 28.1% of that year's returns were filed late.

2. The start of the COVID-19 pandemic which had reached the UK in March 2020 and was the main cause for the lower volume of property disposals in 2020/21.

One of the important side-effects of the FA 2019 30-day time limit, which was increased to 60 days from 27 October 2021 by virtue of FA 2022, is that the system doubled the reporting effort required by the taxpayer and their adviser and doubled the risk of a late filing penalty. Since the UK property reporting service is not connected to the Self Assessment regime, virtually all taxpayers must report the same gain twice: firstly, on the UK property return and secondly, on the individual's normal self-assessment tax return. Only in the rare circumstance when a UK property deal completes towards the end of the tax year and the self-assessment tax return is submitted within 60 days (as it now is) of the completion date, will the taxpayer be able to sidestep the obligation to file a UK property return.

An annoying feature of the legislation is that, where taxpayers report their gains in the wrong order, i.e. on their self-assessment tax return first, they will still be saddled with penalties for submitting a late UK property return. The penalties due for a late UK property return are imposed on the same basis as apply for a late self-assessment tax return. HMRC are currently chasing up those individuals who failed to file a UK property return within the 30-day deadline for 2020/21 and are demanding that they file a paper version of the return (known as PPDCGT) to stop late filing penalties from accruing further. This paper form cannot be downloaded from HMRC's website – it can only be obtained by telephoning HMRC to request a copy.

Because the late filing property penalties for 2020/21 were not issued as promptly as they should have been, the sums involved are substantial and it is anticipated that many taxpayers will be appealing against their imposition. The problem should not be as serious for 2021/22.

Technical guidance on the details of the UK property account, which first appeared in late 2021, can be found in Appendix 18 at the back of HMRC's Capital Gains Manual.

Contributed by Robert Jamieson

Market value and shares listed on AIM (Lecture P1348 – 18.12 minutes)

There was an interesting case heard earlier this year under the name of Close v HMRC (2022) by the First Tier Tribunal on the meaning of 'market value', the meaning of which one might have thought was relatively well settled.

In 2003/04, a Mr Close (C) and two others gifted their shares in Readybuy plc to a charity and claimed income tax relief under what is now S431 ITA 2007 based on the market value of the shares on the date of the gift. The company had recently been the subject of a placing and admission to AIM. On the date of C's gift, the shares were dealt in at a price of 53.25p each. Accordingly, that was the figure used by C and one of the others in calculating their relief. The third individual made a gift some three months later and used a share value of 50p for his relief. One would have assumed that all this was reasonably conclusive, but unfortunately that was not the case.

The legislation states that, to be eligible for relief, it is necessary for the taxpayer to donate an interest in a 'qualifying investment'. This term is understood to include shares or securities which are listed or dealt in on a recognised stock exchange. It was common ground that the shares in Readybuy plc were dealt in on a recognised stock exchange (i.e. AIM) and so were regarded as qualifying investments. However, AIM shares are not treated as 'quoted' or 'listed' – they count as 'unquoted' for all tax purposes – and the relevant valuation criteria for these purposes are set out in S273 TCGA 1992. In other words, the market value of such a share is 'the price which the asset might reasonably be expected to fetch on a sale in the open market'.

HMRC opened enquiries into the 2003/04 tax returns of C and the other two appellants on various dates in 2005. Remarkably, closure notices were not issued until 2017 and 2018 in respect of the three parties. The closure notice for each taxpayer amended their relevant self-assessment to show relief based on a market value of the shares at the date of gifting of 14.66p per share. The obvious effect of these closure notices was that the income tax relief available to the three individuals was significantly reduced – hence their appeals.

Prior to issuing the closure notices, HMRC had obtained a report from a professionally qualified member of their Shares and Assets Valuation Department which concluded, as mentioned above, that the value of each share in Readybuy plc at the relevant valuation date 'cannot be more than 14.66p'.

Subsequently, another valuation expert – an independent chartered accountant – valued the shares at 8.05p each. He arrived at this figure using conventional valuation bases involving all the artificial assumptions required to value unquoted shares for tax purposes. Interestingly, he was unable to explain why the AIM prices were so high since such a value could not be justified by the normal analysis of turnover, profits and so on. As a result, HMRC readjusted the three taxpayers' income tax relief to this lower figure. In C's case, this process gave rise to the following results:

Shares gifted	123,000
Date of gift	8 September 2003
Relief claimed	£65,497
Adjusted relief	£18,032
HMRC's readjusted relief	£9,901

In the event, the First Tier Tribunal broadly agreed with the conclusions reached by the second valuation expert. However, the judge felt that this person had not given sufficient weight to one key piece of evidence. As a result, he summarised his decision with these words:

> 'Taking into account all the evidence and submissions, in my judgment the highest price a reasonably prudent purchaser would have paid for the shares in Readybuy plc . . . would have been 12.1p per share.'

This was the market value which the judge fixed for C and the other two parties and gave a final relief figure for C of £17,343. It might be worth noting that such a figure was very close to the acquisition price which the parties paid for their shares at the time of the placing!

One eminent tax expert has made the following comment about this valuation:

> 'The . . . odd thing is that this conclusion was reached in the face of a value on AIM of 53.25p. When looking at the definition in S273 TCGA 1992, we must look at the price which the shares might reasonably be expected to fetch on a sale in the open market. When the shares are sold on AIM at 53.25p each, it is difficult to see why this is not the relevant price.
>
> The only conclusion which makes sense is that the (Tribunal) did not trust the AIM price to be sufficiently genuine to override the value which would apply if there were no such AIM transactions.'

In the speaker's view, an important point to be aware of is that a flotation on AIM does not – per se – cause the value of a company to increase.

Contributed by Robert Jamieson

Investment bonds in trust (Lecture P1349 - 13.29 minutes)

We see investment bonds in trust in various circumstances. Here we are talking about a single premium investment bond of the type which falls within the chargeable event gain regime. They can be used in certain IHT planning tools such as discounted gift trusts or gift and loan trusts, but they can also be a way of getting funds out of a person's estate into a trust where there is no automatic income generated by the investment such that there is no tax liability or reporting of the income. The ability to withdraw 5% of the initial capital without an immediate tax charge is often utilised in the tax planning ideas referred to above but the income does not have to be drawn. Any growth in value of the asset is outside of the estate of the settlor unless the trust is settlor-interested.

The taxation of these products falls within the chargeable event gain regime, but the legislation is complex, mainly because it does not follow the usual rules of trust taxation. The trust will always be subject to the trust rate of taxation (even if it is an interest in possession trust) but any gains will be taxed on the settlor of the trust during their lifetime unless they are no UK resident. In fact, that treatment applies up to the end of the tax year in which the settlor dies. The only deviation from this would be if it was a bare trust since the beneficiary would always be taxable on the chargeable event gain in that situation.

If there is a tax charge on the settlor, it will be assessed as if the settlor owned the bond, so it is possible to claim top slicing relief and the basic rate tax credit will attach to the bond if it is an onshore insurance company. The settlor has the right to reclaim any tax paid from the trustees.

Once the end of the tax year of death of the settlor has passed, the gain will be taxed at the trust rate of tax (other than on the first £1,000 in some cases) with the tax credit still being available. However, trustees cannot use top slicing relief to reduce the tax payable on such gains.

This gives rise to an interesting planning opportunity. The assignment of this type of bond for no consideration to a beneficiary would not create a chargeable event for the purposes of this legislation. The beneficiary would then be treated as holding the bond since commencement and would be able to claim top slicing relief, if beneficial, for the whole lifetime of the bond. Of course, the appointment of capital would also be a chargeable event for IHT purposes and so any potential IHT liability would need to be considered, although the transfer of cash out of the trust after the bond was encashed would also be caught.

Example

A single premium insurance policy is taken out; no withdrawals have been made. This is held in a discretionary trust.

On the death of the settlor, the bond is standing at a gain of £50,000, with total value of £150,000.

The bond has been in place for five complete years.

There is a single beneficiary of the trust who has income of £40,000 before allowances.

What is the tax position:

(a) For the trust if they encash?

(b) If the bond is assigned to the beneficiary before encashment?

For the trust

The trust gain of £50,000 is taxed as follows:

1,000 x 20%	200
49,000 x 45%	22,050
Total	22,250
Less tax credit	(10,000)
To pay	£12,250

If this was an offshore bond, then no tax credit would be available, so the tax would be £22,250.

Assignment to the beneficiary

No tax on assignment but the individual's gain is £50,000.

Their other income is £40,000 so £10,270 of the basic rate band is still available, with the balance taxed as follows:

10,270 x 20%	2,054
39,730 x 40%	15,892
Total	17,946
Less tax credit	(10,000)
To pay	7,946

If top slicing was claimed (£50,000/5), all of the gain would be within the basic rate band so no additional tax to pay. This would clearly be a much better situation that if the trust encashed the bond.

Discounted gift trust (DGT)

This is a lump sum investment into a single premium life assurance bond or capital redemption bond held subject to a special trust that gives the right to regular cash payments to the settlor for life with the balance of the trust fund being held for the benefit of the trust beneficiaries.

In particular:

- As the underlying investment in normally a single premium bond, the settlor's regular annual cash entitlement under the trust will typically be equal to 5% of the single premium to utilise the partial surrender rules
- A DGT can be used by joint settlors so that income can continue through both lifetimes
- The DGT can be used with a discretionary trust or a bare trust.

The tax analysis is as follows:

- The DGT involves a 'discounted gift' so the value of the gift for IHT purposes is less than the physical cash introduced into the trust because it is discounted for the income stream due to the settlor. HMRC have set out their view on how such gifts should be valued so there is some certainty about their attitude.
- There is no value remaining within the estate as the retained right has no value at death.
- Cash payments are capital so will be free of tax in the hands of the settlor.

- The initial gift falls out of the estate entirely if the settlor survives for 7 years.

- If the DGT is a discretionary trust, then it will be a chargeable lifetime transfer; if it is a bare trust then it is a potentially exempt transfer.

- If the DGT is a discretionary trust, then there are periodic and exit charges but the value of the assets continues to be discounted for the income stream so that if the initial value was less than the nil rate band (and assuming growth in value is not high) then there is unlikely to be any charge arising.

- No income tax is payable if withdrawals from the bond are within the 5% limit.

- The gift with reservation rules do not apply because the trust carves out the settlor's retained interest from the remaining property from which he cannot benefit.

There are disadvantages however:

- It is only appropriate for those who want a regular cash withdrawal as the amount to be withdrawn must be set at the time the trust is set up and cannot be varied. The investment also cannot be varied.

- The investor must be less than 90 and in good health or there is no discount.

- The investor should spend the cash received as if it is retained then no IHT advantages are received. This is rarely a problem as these types of trusts are typically established because the donor needs to retain income. If the settlor no longer needs the payments once the DGT has been established, they could simply gift the money away to a suitable recipient or waive the right to receive the money (although this will depend on the terms of the trust).

- There will be a gain accruing for the trust on encashment due to the 5% withdrawals being taken and there is no rebasing of the asset at the date of death.

Loan trusts

A loan trust would involve an individual loaning money to a trust of which he is settlor. The loan is typically interest free and repayable on demand. The trustees invest the loan in a single premium bond and can take encashments from this to fund the repayment of the loan.

The way that this operates:

- The settlor would have no ongoing rights under the trust other than the repayment of the loan and the growth of value of the assets are outside the estate.

- Loan repayments are capital and free of tax. As with the DGT, this needs to be spent or given away to give a permanent IHT advantage.

- Some flexibility is possible as loan repayments can be deferred if there is no requirement for income (although the repayment of the loan which is then spent is the key to getting the IHT advantages).

- No gift is made so there are no initial IHT implications.

- There is no gift with reservation as there is no benefit to the settlor under the trust other than the repayment of the loan.

- It would be usual to have a discretionary trust which means that there are 10-year charges but the value of the trust is always reduced by the loan so there is rarely any IHT to pay. No exit charges arise as the money is distributed not as capital but to the settlor as a creditor of the trust. A bare trust could be used if any of these are problematic.

Problems with these types of arrangements are as follows:

- The loan is an asset of the estate and so the planning is only effective over time as the loan is repaid so the settlor must live for a reasonable time.

- The loan will have to be repaid by the trustees and this might cause a problem if the value of investments has fallen as the trustees would then be personally liable. There are mechanisms for limiting this problem by restricting the amount repayable to the value of the underlying assets but there are issues with this type of restriction and so specialist advice should be taken.

- The total amount of income that can be paid to the settlor is limited to the amount of the initial loan so the repayment period must be matched to the age and health of the settlor.

Contributed by Ros Martin

Public right of way and mixed use **(Lecture P1346 – 18.07 minutes)**

Summary – A public footpath maintained by the owners, which ran across the rear of their property, did not make a property mixed use and so the lower non-residential SDLT rates did not apply.

On 28 August 2020, James and Charlotte Averdieck jointly purchased a property for £2,999,000 and shortly after filed a stamp duty land tax return on the basis that the property was residential and that £258,630 of SDLT was payable.

Just over three months later, their agent wrote to HMRC stating that the property had been misclassified and should have been classed as "mixed use" arguing:

> "The public footpath which runs across the rear of the property is classed as a public highway by the local highway agency and our client is responsible for keeping the footpath safe for all users who pass through their land. The public

> footpath restricts the use of the land acquired by our client and as such, the public footpath does not contribute to the reasonable enjoyment of the dwelling.”

Further, the couple argued that the land that the path was on was used for a separate commercial purpose, as it granted access to a farm, disturbing their use as a residential property.

The couple amended the return and sought repayment of £119,180 with interest.

In August 2021 HMRC opened an enquiry and later issued closure notices on the basis that the transaction was not mixed use.

Decision

The First Tier Tribunal confirmed that the right of way was used by the couple to access the property, as well as by other property owners and a farm further down the lane.

The use of the path by a farm did not make it a place where business was conducted. No one conducted their business on the lane.

Further, the fact that they had statutory obligations to maintain the path did not change the fact it was used as part of the residential property.

The appeal was dismissed.

James and Charlotte Averdieck v HMRC (TC08623)

GAAR opinion on SDLT arrangements

HMRC has published a new GAAR Advisory Panel opinion on SDLT arrangements relating to the sale and purchase of a residential property involving an alternative finance agreement and a lease agreement.

The taxpayers (a married couple) purchased a residential property for just under £1m. They took advice on a scheme which, the promoter contended, would save them SDLT on the purchase. The scheme used a series of steps involving trusts settling an amount equal to the purchase price, and the acquisition of the property by the taxpayers under an alternative finance agreement where the property was acquired 'absolutely for the lender' rather than directly by the taxpayers. At that point, any acquisition by the lender was treated as an exempt 'security interest' rather than a land transaction, with no SDLT due. The property was then leased to the taxpayers at a peppercorn rent. The intended effect was to replace the £1m consideration with the peppercorn amount, meaning that no SDLT would be due on the transaction.

The Panel found that the enablers had 'devised and implemented a contrived way of circumventing the clear aim of the tax legislation' and that the arrangements were not a reasonable course of action.

This is the Panel's first opinion under the provisions of F(No.2)A 2017 Sch 16 which introduced penalties for enablers of defeated tax avoidance schemes.

Tax Journal (14 October 2022)

Repayment of SDLT

Summary – SDLT was not repayable in respect of a substantially performed contract that was never fully performed as it was outside the 12-month window.

On 9 August 2012, Christian Candy entered into two separate contracts with the Commissioners of the Royal Hospital Chelsea and other persons as intermediate landlords:

1. The first contract was an agreement for a lease of the property for a term of 25 years for a premium of £20 million (the initial lease). This contract was accompanied by a deed governing the development of the property by the taxpayer. On 10 August 2012, the taxpayer's building contractors commenced construction work at the property. The initial lease was granted on 1 October 2012.

2. The second agreement was for the assignment of a separate lease (the contracted-out lease) of the property for a term of 201 years from 1 October 2012 for a price of £48 million, payable in four instalments. The first instalment of £7.39 million was paid on 1 October 2013 by Christian Candy.

In October 2012, the appropriate SDLT was paid over to HMRC:

- on the full consideration of £20 million; and

- on the £48 million, which had been triggered as a result of the building contractors starting work on the property. This constituted taking of possession of the property, amounting to "substantial performance".

Roughly two years later, Christian Candy gave both leases to his brother. A deed of novation was signed, discharging Christian Candy from his remaining instalment payments.

No further SDLT was payable on the assignment of the initial lease because, as a gift, there was no chargeable consideration on which SDLT could be assessed.

The Court of Appeal summarised the SDLT position on the second lease by saying that:

> "the effect of the deed of novation was that the brother became liable to perform the remaining obligations under the agreement of the contracted-out lease, namely the payment of the three remaining instalments (£40.61 million) of the £48 million purchase price. However, the chargeable consideration for SDLT purposes for this transaction remained the full £48 million purchase price. This was because the subject-matter of the deed of novation was an uncompleted contract and, since there was a gift between two brothers, special charging rules in Schedule 2A, paragraphs 12 to 14 FA 2003 applied."

On 10 April 2014, the taxpayer applied for repayment of the SDLT he had paid on 8 October 2012 in respect of the second lease, by submitting an amendment to his 8 October 2012 land transaction return.

HMRC rejected this amendment stating it was made outside the 12-month amendment window.

The First Tier Tribunal allowed the amendment, finding that the 12-month window was overridden where an amendment is made relating to a contract that has been substantially performed, but ultimately was never completed.

The Upper Tribunal disagreed and overturned the decision.

Christian Candy appealed to the Court of Appeal.

Decision

Agreeing with the Upper Tribunal, the Court of Appeal confirmed that the general 12-month time limit for amending a land transaction return applied in this case.

The Court of Appeal did not see the result in this case as unfair. It stated that tax is 'charged on two different people by reference to different periods as a natural incident of the SDLT scheme'. A sale of this lease to an unconnected party for consideration would have given rise to SDLT charges on two people, with no repayment. The Court of Appeal saw no reason why the taxpayer should be entitled to a refund in the circumstances and went on to state:

> “Moreover, if his argument is correct, he could enjoy the property for 20 years, never completing and leaving a small balance outstanding, then novate the uncompleted contract to someone else and still reclaim the SDLT.”

This is clearly not what the legislation intended.

The Court of Appeal confirmed that where SDLT is paid because of the contract being substantially performed but the contract is never carried into effect, the SDLT is only repayable if the taxpayer submits an amended return within 12 months.

Christian Peter Candy v HMRC [2022] EWCA Civ 1447

Administration

Human, not computer error (Lecture P1346 – 18.07 minutes)

Summary – An error by the person submitting a CT return for the wrong year was not a reasonable excuse for the late filing of a return.

On 21 October 2018 HMRC issued a notice to file a return for the period to 30 September 2018, with a filing date of 30 September 2019.

On 6 November 2019, the company filed a return for the period to September 2019, not September 2018.

Later, having established that the company's 2018 return had not been submitted, it submitted the missing return on 13 January 2021, electronically. This was 836 days late, resulting in a penalty of £4,343.70,

The company challenged the penalty stating:

> "There seems to be some sort of clerical issue as the return for the year ended 30.9.18 was originally submitted on 6.11.2019."

HMRC replied that it did not consider that the company had a reasonable excuse for the late filing of the CT return for the 2018 return because the submission receipt dated November 2019 properly related to the period ended 30 September 2019.

The case moved to the First Tier Tribunal.

Decision

The Tribunal found that the issue arose due to human error. The likely explanation was that the person who submitted the return had clicked a wrong button and filed the wrong year's documents. Unfortunately, this was not checked until some 11 months later.

The company was "aware of the risks of filing the wrong documents. It should have checked that the correct documents had been sent, and it should have done so far more timeously than it did so." Such a human error did not provide a reasonable excuse.

The company's appeal was dismissed, and the penalty assessment upheld.

T. PA Accountancy Services Limited v HMRC (TC08601)

Information request not reasonable

Summary – HMRC's information notices were considered onerous and not reasonably required for the purpose of checking the taxpayer's position.

Barry Davies and Rupinder Mahil, a married couple, ran a property investment business in partnership. In 2018, partnership business was transferred to a company with its property portfolio valued at £8.8 million.

The couple claimed this was financed by their own funds, loans from other people, refinancing properties once they had been refurbished/increased in value, and bridging loans and mortgages from financial institutions.

The couple bought their home, Bracken Hill House, in March 2016 for £1.7 million with a bridging loan that was replaced with a mortgage of £1.25 million and by refinancing other properties owned. Further refinancing was carried out to refurbish the property at a cost of £395,000.

In a book and articles that he had written, Barry Davies claimed to have made profits of £50,000 and £91,000 on two properties and that their five biggest properties were earning profits of £145,000. HMRC believed that this all related to the period between September 2014 and February 2015 when the taxable household income was said to be £12,500.

In May 2019, HMRC opened an in-time enquiry into the couple’s individual tax returns for 2017/18. The letter also requested 21 pieces of information. In February 2020, HMRC issued formal Schedule 36 information notices for the documents. There was therefore “reason to suspect” there was undeclared income.

The couple provided a good deal of information and documents on a memory stick as well as a box of paper records but appealed the information notices.

Decision

The First Tier Tribunal stated that the burden of proof as to whether the information was reasonably required for the purpose of checking the taxpayer's position fell on HMRC.

It found that the list of documents would have been ‘onerous' to provide. HMRC requested a great deal of detailed information including all the records of every refinancing transaction in relation to the property portfolio and Bracken Hill House since 6 April 2014, statements for all bank accounts for 2016/17 and all sources of money used to finance the property portfolio or themselves and the costs of the building improvements which were not from refinancing properties from 6 April 2014.

The First Tier Tribunal noted that HMRC’s own guidance to its staff in its Business Income Manual which: “indicates that it is impractical to look at every entry in the borrowing account. It refers to bank borrowings, but it would apply equally to other types of borrowing, e.g. from private investors.”. Indeed, HMRC’s manual directs officers to use “a reasonable basis as an approximation”.

The First Tier Tribunal found that the documents were not reasonably required and directed HMRC to issue a closure notice within 90 days of the date of the decision.

The taxpayers' appeal was allowed.

Barry Davies, Rupinder Mahil and Davies Mahil Partnership v HMRC (TC08619)

Paper repayment notifications to end in December

HMRC's Stakeholder Digest (10 November 2022) includes the announcement that income tax Self Assessment and corporation tax paper repayment notifications are to end on 16 December 2022.

Going forward, agents must use online services to review transactions on behalf of their clients, including details of BACS repayments.

https://www.tax.org.uk/hmrc-stakeholder-digest-10-november-2022

Non-compliance with an 'unless' order

Summary – Despite missing the deadline of an 'unless' order, the taxpayers were able to have their appeal reinstated as seven hours was not a 'serious or significant' breach.

In October 2018, Alan and Diane McFarland were directed to submit a hardship application. The direction included an 'unless' order, so that unless the couple substantiated their application to HMRC within a specified time, the appeal would be struck out.

Having failed to comply with the order, their appeal was struck out.

The couple applied to have their appeal reinstated but HMRC resisted.

Decision

Not surprisingly, the First Tier Tribunal found that Alan and Diane McFarland had breached the 'unless' order.

It was the couple's responsibility to justify hardship to HMRC, not to the tribunal. Unfortunately, the email that the McFarland's had sent went solely to the tribunal. This was a breach of the order.

However, the intention had been to send the email to HMRC and the couple remedied this shortly afterwards, albeit seven hours after the deadline. This, the tribunal decided, was not a 'serious or significant' breach.

Further, the reasons for replying at the last minute were because of problems in collating the required information. The 14-day period for responding was 'quite tight' and, in the tribunal's experience, 'when a deadline is imposed, it is often the case that things go right down to that deadline'.

The tribunal concluded that the prejudice to the taxpayers to lose the opportunity of appealing was greater than the prejudice to HMRC were the appeal not reinstated.

Alan and Diane McFarland's application was allowed.

Alan and Diane McFarland v HMRC (TC8608)

Adapted from the case summary in Taxation (3 November 2022)

Offshore Corporates owning UK property **(Lecture P1350 – 9.43 minutes)**

This session will consider the HMRC campaign targeting offshore corporates owning UK property. The campaign is due to start in November 2022. This session will consider how advisers should respond if HMRC approach one of their clients under this campaign.

Background

HMRC are starting another campaign in November 2022. This campaign is focussed on tackling non-compliance linked to non-resident corporates that own UK property. HMRC have identified potential offenders following a review of various data, including from the Land Registry. The review identified offshore corporate owners that may not have met particular UK tax obligations. The targets of the campaign will be the latest in a long line of recipients of HMRC nudge letters, which are issued outside, and without the protection of, the normal enquiry process.

Overview

Under the Campaign, HMRC may issue one of two “nudge” letters, depending on the circumstances. Advisers should note that HMRC may not necessarily restrict themselves to the issue of one of the letters where they suspect non-compliance, and may take a different approach to that outlined in this session.

When one of the letters, considered further, below, is issued, they will be sent to the corporates, and will be accompanied by a Certificate of Tax Position and a Notice of Intention to Disclose. The companies will be expected to complete the relevant document, and make the appropriate disclosure to HMRC, where one is necessary. There will be follow-up action by HMRC if a response isn’t sent to the letter.

The HMRC letters

The letters will, as noted above, be sent to the corporates. However, HMRC recommend that the companies should ask connected UK-resident individuals to ensure their personal affairs are up to date in respect of their tax position, including in relation to the relevant anti-avoidance provisions.

The recipient is given 40 days (from the date of the letter) to respond, otherwise HMRC state that they make an assessment of what they believe the company owes, and may open an investigation and consider charging additional penalties. In addition to the documents noted above, the letters will also be accompanied by various HMRC factsheets, including those relating to the Human Rights Act and penalties.

The first letter will be issued by HMRC to non-resident companies that own UK property and may need to disclose income received as a non-resident corporate landlord. The letter may also be issued where such companies may have a liability to the Annual Tax on Enveloped Dwellings (ATED).

The company is asked to contact any UK-resident individuals who have any interest in the income or capital of the company, whether directly or indirectly, to ensure that their tax affairs are up to date with the Transfer of Assets Abroad regime.

The second letter will be issued to non-resident companies that appear to have made a disposal of UK residential property between 6 April 2015 and 5 April 2019 without filing the relevant, Non-Resident Capital Gains Tax (NRCGT), return.

Additionally, the corporate is asked to consider whether they have any other UK tax liabilities, including on rental profits, income tax under the transactions in land rules and/or ATED.

HMRC state that they will need to consider whether, for properties purchased by the company before April 2015, any part of the gain may relate to UK-resident participators. The company is asked to ensure that any such participators make sure that their tax affairs are "updated" if the relevant legislation (Section 13, TCGA 1992, now relocated to Section 3, TCGA 1992) could apply.

How to respond to a letter

The key message when a client has received one of the nudge letters under this campaign is to ensure it is not ignored. HMRC will not go away, and follow-up action will be taken, although perhaps not immediately. Advisers need to proceed with caution, as the safeguards associated with a formal enquiry do not apply when replying to a nudge letter.

Although the nudge letter will be issued in response to information received by HMRC, it may be that basic checks have not been undertaken before the letter is sent to the taxpayer. Advisers should establish the position with the client, and, if a disclosure is needed, determine the appropriate response.

When there is a disclosure involving a significant liability, or there are aggravating factors, as per HMRC's criminal investigation policy, consideration should be given to use of the Contractual Disclosure Facility. Where this is being contemplated, you should consider seeking expert advice from a specialist adviser in this area before approaching HMRC. Whatever the outcome of the discussion with the client, they should not be allowed to sign the forms sent by HMRC with the nudge letters.

Contributed by Phil Berwick, Director at Berwick Tax

Deadlines

1 December 2022

- Corporation tax for periods ended 28 February 2022 (SMEs not paying by instalments)

7 December 2022

- VAT returns and payment for 31 October 2022 quarter (electronic payment)

14 December 2022

- Quarterly corporation tax instalment for large companies
- Monthly paper EC sales list –businesses in Northern Ireland selling goods only

19 December 2022

- File monthly CIS return

21 December 2022

- File online monthly EC sales list - businesses in Northern Ireland selling goods only
- Submit supplementary intrastat declarations for October 2022
    - arrivals only for a GB business
    - arrivals and despatch for businesses in Northern Ireland

22 December 2022

- PAYE, NIC, CIS and student loan liabilities cleared into HMRC bank account

30 December 2022

- Online tax return deadline for underpayments collected by a PAYE coding adjustment

31 December 2022

- Companies House should have received accounts for:
    - private companies with 31 March 2022 year ends
    - public limited companies with 30 June 2021 year ends
- CTSA returns filed for companies with accounting periods ended 31 December 2021
- End of CT61 quarterly reporting period
- Year end for taxable distance supplies to UK for VAT registration

News

Rates rise again

Following the Bank of England's decision to increase the bank base rate once more, HMRC has followed suit.

With effect from 22 November 2022:

- for most taxes and payments, the late-payment interest rate became 5.5%; and
- the repayment rate 2%,

From 14 November 2022, interest charged on underpaid quarterly instalment payments of corporation tax is 4% and 2.75% is paid on overpaid quarterly instalment payments and on early payments of Corporation Tax not due by instalments.

https://www.gov.uk/government/publications/rates-and-allowances-hmrc-interest-rates-for-late-and-early-payments/rates-and-allowances-hmrc-interest-rates

Possible ATED penalties

HMRC is writing to taxpayers to remind them about the annual tax on enveloped dwellings (ATED) valuation deadline that is fast approaching.

ATED properties must be revalued every five years, with the valuation dates being 1 April in 2012, 2017, 2022, 2027 and so on.

The new property valuation takes effect for the ATED reporting year starting on the following 1 April. This means that the 2023/24 ATED return and payment will be based on the value of the property as at 1 April 2022.

HMRC has reminded taxpayers that they need to revalue their properties at 1 April 2022 using an open-market value. Failure to revalue at on this date could lead to penalties. Properties could move up an ATED band, more than doubling the ATED charge due for year.

HMRC’s letter will not be sent to those below the lowest £500,000 threshold as they are not currently registered for ATED. It is important to warn clients of this potential new charge.

HMRC will impose penalties for both late filing and failure to pay the correct ATED charge on time.

Business Taxation

Enterprise Zone Allowance – contract outside 10-year period

Summary - Two LLPs were not entitled to Enterprise Zone Allowance (EZA) as the relevant expenditure was incurred under a new, self-standing agreement entered into outside the relevant statutory window.

Two SPVs were formed to develop land in an enterprise zone. One (the developer) held a lease of part of the site, and the other (the contractor) was to carry out the building works. The day before the ten-year period for the enterprise zone expired, they entered into a 'golden contract' with the intention of enabling allowances to be claimed on buildings constructed in the following ten years while retaining flexibility on the type of development. The contract therefore allowed for a choice of different developments ('works options'), each linked to a specific part of the overall site. No work had to be done under the contract unless and until the developer issued a notice to proceed for one of the work options. Subsequently, under the terms of a 'change order', a data centre (which was not within the scope of the existing works order options) was constructed. Following the assignment of the lease held by the developer to the two LLPs, two further data centres were constructed under further change orders and the LLPs claimed enterprise zone allowances.

For the claim for allowances to succeed, the data centres had to have been built under the golden contract, but HMRC argued that this was not the case.

Decision

Their first argument was that the golden contract was not a contract within the terms of the legislation because it did not create a legal liability within the ten-year period for the developer to pay anything and it did not identify the building to be constructed. The Court of Appeal rejected this argument because the legislation did not mandate any particular type of contract.

Their second argument was that the data centres were not constructed under the golden contract at all; the effect of the change orders was so radical that they were not variations but amounted to a new and self-standing contract.

The Court of Appeal agreed with HMRC. The LLPs argued that the change orders providing for the later data centres gave effect, by variation, to works option 1 in the golden contract. But the contract only permitted the selection of one project under a particular works option and works option 1 had already been selected in constructing the first data centre.

Further, the work described in the change orders was 'radically different in kind' from that described in the works option – they provided for a different building on a different site for a different price. These features led 'inexorably' to the conclusion that the data centres were not constructed under the golden contract and therefore were not constructed under a contract entered into within the ten-year period. The expenditure did not qualify for allowances.

Cobalt Data Centre 2 LLP and another v HMRC [2022] EWCA Civ 1422

Adapted from the case summary in Tax Journal (11 November 2022)

Incorporation advice in 2023/24 **(Lecture B1349 - 8.54 minutes)**

Corporation tax rate increase

The announcement that we are to press ahead with the increase in corporation tax – main rate increasing to 25% - as legislated for in Schedule 1, Finance Act 2021 means that advice regarding incorporation of small businesses – and indeed advice regarding remaining a small company is changing from April 2023.

Small profits rate of corporation tax

Section 7 and Schedule 1 set out the details of the small profits rate and related marginal relief. The rate of corporation tax applying profits in a company subject to the small profits rate will be 19% from 1 April 2023. The legislation also specifies a standard 'marginal relief fraction' of 3/200ths.

The small profits rate will apply to the chargeable profits of a company where:

- The company is UK resident;
- The company is not a close investment holding company, and
- The company's 'augmented profits' do not exceed the lower profit limit which is set at £50,000.

Augmented profits

The adjustment for augmented profits arises because UK dividends are not part of chargeable profits, but a company in receipt of substantial amounts of UK dividends would not be regarded as one with 'small profits'. The augmented profits are arrived by taking the chargeable profits of the company for the accounting period and adding any exempt distributions of a qualifying kind (exempt from corporation tax under Chapter 9A CTA 2009) received by the company that are not excluded.

Dividends that are excluded for this purpose are those paid by 51% subsidiaries or fellow subsidiaries in a group.

Marginal relief

Marginal relief is available if:

- The company is UK resident;
- The company is not a close investment holding company;
- The company's 'augmented profits' exceed the lower profit limit; and
- The company's augmented profits do not exceed the profit upper limit which is set at £250,000.

In this case, the corporation tax charge on the profits is calculated as the chargeable profits multiplied by the main rate less marginal relief, where the marginal relief is calculated using the following formula:

> Marginal relief fraction x (Upper profit limit – augmented profits) x total taxable profits / augmented profits.

A company with taxable profits of £75,000 in receipt of £5,000 of UK dividends and with no associated companies would be liable to:

> 75,000 x 25% - 3/200 x (250,000 - 80,000) x 75,000/80,000 = £16,359.38 or 21.81%

The effective marginal rate for a company with no dividend income and profits between the relevant upper and lower limits will be 26.5%.

Profit limits

The lower limit is £50,000 for the 2023 financial year and the upper limit £250,000. However, these are annual limits and should therefore be time apportioned if used in an accounting period of less than 12 months.

The limits are also adjusted for the number of associated companies – the limits are divided by 1 + N where N is the number of associated companies.

Close investment holding company

A close company is a close investment holding company unless throughout the accounting period it exists wholly or mainly for on the following permitted purposes:

- for the purpose of carrying on a trade or trades on a commercial basis;
- for the purpose of making investments in land, or estates or interests in land, in cases where the land is, or is intended to be, let commercially (not to connected persons);
- for the purpose of holding shares in and securities of, or making loans to, one or more companies each of which—
    - (i) is a qualifying company (controlled by candidate company or parent thereof), or
    - (ii) falls within subsection (4)*,
- for the purpose of co-ordinating the administration of two or more qualifying companies;
- for the purpose of the making of investments as mentioned above:
    - (i) by one or more qualifying companies, or
    - (ii) by a company which has control of the candidate company, or
- for the purpose of a trade or trades carried on on a commercial basis—
    - (i) by one or more qualifying companies, or

(ii) by a company which has control of the candidate company.

Dividend taxation

The rates applying to dividends increased in April 2022 at the same time as the NIC rates were increased. However, it is not now intended to reduce the rates of dividend tax, so these will remain at 1.25% over those for 2021-22.

The rates are:

- Basic rate 8.75%
- Higher rate 33.75%
- Additional rate 39.35%

In addition, as announced in the 2022 Autumn Statement, the dividend nil rate band is to reduce from £2,000 to £1,000 in April 2023, and to £500 in April 2024.

Incorporation comparison

The table below considers the relative tax burden on various levels of profit based on the following assumptions.

For a sole trader, the tax, Class 2 and Class 4 National Insurance contributions are calculated.

For the limited company, a salary of £12,570 (the tax and primary NIC threshold) is assumed, and the profits then taxed at the relevant rate of corporation tax. There will be secondary NIC on earnings in excess of £9,100 at a rate of 13.8%. I have assumed that no Employment Allowance is available as it is a single director company. There is tax relief on the employer NIC paid.

All of the post tax profits are extracted by way of dividend, by a director shareholder who has no other sources of income.

Profit	Self Employed	Ltd company	Tax Saved
20,000	2,334	2,205	129
30,000	5,234	4,814	420
40,000	8,134	7,423	711
50,000	11,034	10,032	1,002
60,000	15,199	12,669	2,530
70,000	19,399	17,239	2,159
80,000	23,599	22,370	1,228
90,000	27,799	27,501	297

100,000	31,999	32,632	- 634

Marginal rates on dividends

When corporation tax is 19%, the marginal rate of tax on dividends distributed is 26.09%.

Dividends reach the higher rate bracket when the profits reach £59,592. While the corporation tax rate remains 19% the marginal rate is 32.93%, but the small profits marginal rate is reached at £63,049 at which point the marginal rate becomes 51.31% (as against 42% for the sole trader).

For the limited company, taper of personal allowance starts at profits of £126,899 and the marginal rate is then 63.71%. The sole trader has moved to 47% marginal rate.

Contributed by Rebecca Benneyworth

Dividend not accessible by creditors (Lecture B1346 – 12.44 minutes)

Summary – A large dividend paid at a time when the company was solvent was lawfully made and not accessible to the company's creditors following a subsequent insolvency.

In 2009, the directors of AWA distributed €135 million as a dividend to its only shareholder, Sequana SA, extinguishing most of a larger debt owed. At the time, looking at both the company's balance sheet and on a cashflow basis, the company was solvent. However, there were long-term pollution-related contingent liabilities meaning that there was a risk of insolvency in the long term, but the risk was not imminent nor probable,

Roll forward nearly 10 years, and AWA went into insolvent administration. BTI 2014 LLC, as the assignee of AWA's claims, sought to recover the amount of the May dividend from AWA's directors. It argued that, when paying the dividend, the directors had failed in their 'creditor duty' as there was a real risk of, insolvency. This duty is also known as the "rule in West Mercia" after the leading case of West Mercia Safetywear v Dodd.

Both the High Court and the Court of Appeal rejected the creditor duty claim. The Court of Appeal had stated that:

> "the creditor duty did not arise until a company was either actually insolvent, on the brink of insolvency or probably headed for insolvency."

At the time of the dividend payment, AWA was not insolvent or on the brink of insolvency and so the appeal failed. BTI 2014 LLC appealed to the Supreme Court.

Decision

The judges confirmed that, under Companies Act 2006 there is a duty for directors to act in good faith to promote the success of the company for the benefit of its members.

The Supreme Court found that, in certain circumstances, this duty was modified by the common law rule that the company's interests are taken to include the interests of the company's creditors.

Creditors have an economic interest in the company and that interest increases where the company is insolvent or nearing insolvency. Where this is the case, directors should manage the company's affairs in a way which takes creditors' interests into account.

The key issue in this case was whether the creditor duty was engaged at the time the dividend was paid. The Supreme Court found that it was not.

The judges confirmed that the creditor duty was only engaged when the directors knew, or ought to have known, that the company was insolvent or bordering on insolvency, or that an insolvent liquidation or administration was probable. When the 2009 dividend was paid, AWA was not actually or imminently insolvent, nor was insolvency even probable.

The Supreme Court unanimously dismissed the appeal.

BTI 2014 LLC v Sequana SA & Ors [2022] UKSC 25

Unavailable information **(Lecture B1346 – 12.44 minutes)**

Summary – The taxpayer, a charity, should be issued with the closure notice requested, with HMRC deciding the outcome based on the data already in its possession.

Newpier Charity Limited submitted its corporation tax return claiming charity tax relief on payments made by the charity to its creditors. HMRC raised an enquiry to check the claim and asked the taxpayer for more information.

The charity provided some information, but said it was unable to obtain anything further. It said that because the transactions had taken place more than 20 years ago, it was 'unreasonable' to expect the information relevant to them to be available. Further, it was not in HMRC's power to assess for such periods so the documents could not be reasonably required before the enquiry was closed.

However, HMRC continued to seek information and said that the enquiry could not be closed without it. The charity applied to the First Tier Tribunal for a direction that HMRC close the enquiry. HMRC said that it still had concerns about whether the income had been used for charitable purposes and without further information would be unable to reach a conclusion.

Decision

The First Tier Tribunal accepted that some of HMRC's concerns as to the legitimacy of the claim were reasonable and might justify the continuation of the enquiry.

However, the judge said the taxpayer's assertion that the information requested was 'not available due to the effluxion of time' or because it had never existed had been 'definitively stated in two witness statements which contain a statement of truth', which made it subject to the Perjury Act 1911.

As a result, the First Tier Tribunal directed HMRC to make an 'informed judgment' based on the information it held and then to close the enquiry.

The charity would be entitled to appeal against the closure notice if it wished and the tribunal would then decide – on the evidence already held – whether relief was due.

The charity’s application for a closure notice was allowed.

Newpier Charity Limited v HMRC (TC08622)

Adapted from the case summary in Taxation (3 November 2022)

Fiat State Aid case

Summary - An advance transfer pricing agreement entered into by the company with the Luxembourg tax authority constituted state aid.

The company (FFT) was a member of the Fiat/Chrysler group and provided treasury services and financing to group companies in Europe.

It operated from Luxembourg where its head office was located. FFT entered into an advance pricing agreement with the Luxembourg tax authority in 2012 which was to last for five years.

The European Commission investigated the agreement and ruled that it amounted to an unnotified state aid. It concluded that the methodology used in the agreement did not lead to a reliable approximation of a market-based outcome and so deviated from the arm's length principle. As such, it gave a selective advantage to FFT compared to a stand-alone company.

Decision

The EU General Court upheld the Commission's decision. It held that the arm's length principle was a general principle of equal tax treatment and necessarily formed part of the examination of tax measures under the state aid rules. The CJEU has now overturned that decision.

Its decision focused on the requirement for there to be a selective advantage to FFT. The case law showed that the Commission was required to decide as to whether, under a particular national regime, the tax measure at issue favoured certain undertakings over others in a comparable legal and factual situation. To do this it had to identify a 'reference system', i.e. the normal tax system of the member state concerned and then demonstrate that the tax measure was an unjustified derogation from that system. The Commission and General Court had failed to do this. Instead, an arm's length principle different to that defined by Luxembourg law had been applied and the way in which that principle had been incorporated into that law had not been considered. This failure also infringed the autonomy of member states in direct taxation; in the absence of harmonisation, the fixing of methods for determining an arm's length outcome was within the discretion of member states.

The CJEU therefore upheld the appeal and set aside the General Court's decision.

Fiat Chrysler Finance Europe and others v European Commission (Cases C-885/19 and C-898/19)

Adapted from the case summary in tax Journal (18 November 2022)

VAT and indirect taxes

Delayed input tax claim denied (Lecture B1346 – 12.44 minutes)

Summary – Although the late claim for input tax recovery was within time, there was a lack of evidence to support the amount of the claim made.

Between 1974 and 1997, NHS Lothian Health Board operated a number of scientific labs which undertook both business and non-business activities. NHS Lothian Health Board did not reclaim the input VAT paid in respect of those years until after the enactment of s.121 FA 2008. This provided that input tax recovery claims for accounting periods ending before 1 May 1997 could be made without time limit, provided the claim was made before 1 April 2009.

NHS Lothian Health Board submitted their claim in-time, but the issue was with the amount of the input tax reclaimed. The Board had insufficient records to show exactly how much input VAT had been paid for the work done in the labs, or to support the split of that work between business and non-business activity over the claim period. As a result, the Board calculated and applied a baseline percentage of 14.7%, adjusted for each year, to the total amount of VAT incurred for each year. The percentage used was their estimate of activity that was business activity in 2006/2007.

NHS Lothian Health Board’s claim for repayment of the overpaid tax was rejected by HMRC, who argued that the Board had not established that the method of valuing the claim was reasonable. In particular, they challenged using the 14.7%.

Both the First Tier and Upper Tribunal had dismissed the appeal, but the Inner House of the Court of Session had allowed the appeal. HMRC appealed to the Supreme Court.

Decision

The Supreme Court found that it was not enough to merely show that input tax had been suffered for the period; it was also necessary to be able to quantify the amount accurately through invoices or by using an alternative credible method.

The First Tier Tribunal had not found that the proportions of NHS Lothian Health Board 's business and non-business activities were pretty much the same across the claim period. The First Tier Tribunal had found there was insufficient evidence to establish what the proportion was and whether, and if so, how it varied through the claim period.

Further, the EU principle of effectiveness prohibits national laws which make claims based on directly effective EU law “virtually impossible or excessively difficult” to enforce. The Supreme Court held that the EU principle of effectiveness was not infringed. This principle did not require the ordinary rules on evidence and the burden and standard of proof to be changed, just because the taxpayer could not comply with these rules. The rules in this case were no different to other historic claims.

The Supreme Court held that the First Tier Tribunal's decision, as upheld by the Upper Tribunal, was correct. HMRC's appeal was allowed.

HMRC v NHS Lothian Health Board [2022] UKSC 28

Hospital car parking fees (Lecture B1346 – 12.44 minutes)

Summary – An NHS Trust was acting as a taxable person when providing car parking facilities and that not charging VAT would lead to a significant distortion of competition.

Northumbria NHS Foundation Trust provides goods and services for the purpose of the health service in England and is required to ensure that its sites and services are accessible at reasonable cost. This obligation includes the provision of parking for patients and visitors at a reasonable price.

Operating in a largely rural area, with public transport often limited or non-existent, around 80% of visitors to the Trust's main hospital sites travel by car.

The Trust provided free parking to certain hospital users and at certain local health centres; reduced rate parking for staff but at other sites a fee was charged to deter people from using the car parks for non-hospital related reasons.

Some sites made a loss on the provision of parking, but the Trust made a small surplus at three of its four major sites, which it used to improve the provision of healthcare at the Trust.

HMRC considered that the charges should be subject to VAT because the taxpayer was a taxable person.

The trust argued that the fees should be treated as non-business as it was not a taxable person in relation to the supply and was operating as a public authority under a special legal regime. It also argued that this would not be a distortion of competition, even though commercial operators are required to charge VAT on car parking.

The First Tier Tribunal had found against the Trust, so it appealed to the Upper Tribunal.

Decision

There was no dispute that the Trust was a public authority for the purposes of s.41A VATA 1994. The issue was whether when providing car parking facilities, it met the two conditions for treatment as a non-taxable person:

1. The car parking facilities must have been supplied in the course of the activities in which the Trust was engaged as a public authority;

2. The supply must not lead to a significant distortion of competition.

The Upper Tribunal stated that for the provision of car parking facilities to be subject to a special legal regime it was necessary to show that the pursuit of that activity involved or was closely linked to the exercise of rights and powers of the public authority. The Upper Tribunal found that the Trust was not subject to such a special legal regime.

The Upper Tribunal found that the First Tier Tribunal was entitled to conclude that competition existed between the trust's car parks and other private operators. This would result in a distortion if the trust was able to provide cheaper parking or obtain higher profits by not charging VAT on their parking. The potential difference 'could not be described as negligible'.

Northumbria NHS Foundation Trust v HMRC [2022] UKUT 00267

Power to delay a VAT refund (Lecture B1346 – 12.44 minutes)

Summary - HMRC had raised its VAT assessment in time and had the power to refuse a repayment while it was checking the validity of the claim.

DCM (Optical Holdings) Limited, trading as Optical Express, supplied:

- taxable frames and lenses for glasses;
- exempt supplies of eye tests and dispensing services.

On 20 October 2005, HMRC raised an assessment for VAT but the company argued that the assessment was out of time as HMRC was time barred under s.73 VATA 1994 that required HMRC to raise their assessment by one year after evidence of facts came to HMRC's knowledge.

DCM (Optical Holdings) Limited argued that HMRC knew that "something was wrong" by January 2004 and so should have raised their assessment within 12 months of that time. October 2005 was too late.

Secondly, the company argued that HMRC did not have an implied power to refuse an input tax claim made on its VAT return.

Decision

The Supreme Court unanimously held that the October 2005 assessment was not time-barred as HMRC had only obtained the last items of evidence during a visit on 1 September 2005. Before this time, HMRC did not have evidence of facts sufficient to justify that assessment.

On the second point, the Supreme Court found that it is implicit in s. 25(3) VATA 1994 that the obligation on HMRC to pay a VAT credit arises only once it has checked that the VAT credit is due. The Supreme Court stated:

> "The obligation to pay does not depend solely on the say-so of the taxable person".

The Court went on to say:

> "This implied power is consistent with the purpose of ensuring that the taxable person pays the right amount of VAT or receives the right amount of VAT credit".

DCM (Optical Holdings) Ltd v HMRC [2022] UKSC 26

R&C Brief 11 (2022): 'VAT and children's face masks'

Following a review, HMRC now accept that face masks are items of clothing. This means that where face masks are specifically designed and held out for sale to children under the age of 14, they are zero rated under Group 16, Schedule 8 VATA 1994.

VAT Notice 714, covering young children's clothing and footwear, has been updated accordingly.

https://www.gov.uk/government/publications/revenue-and-customs-brief-11-2022-vat-and-childrens-face-masks

VAT repayments – new online information form

Where HMRC queries a VAT repayment return and requests supporting documentation, businesses and their agents are now able to use an online form to upload the requested documents. Previously, this information would have been submitted by post, or by email, with the business accepting the risk of sending sensitive information electronically.

To use the form, the business will need:

- its VAT registration number;
- the CFSS reference number from the letter HMRC sent;
- details of its main business activities;
- the date it started trading;
- the VAT rates that apply to its sales;
- details of any VAT schemes used;
- its detailed VAT account;
- its five largest purchase invoices; and
- any additional specific information requested by HMRC.

Depending on the circumstances, additional information may also be requested including:

- bank statements;
- export sales invoices or supporting documents;
- import VAT documents;
- hire purchase or lease agreements;
- completion statements and proof of transfer of funds for the purchase of land or property;
- planning reference and postcode of sites if supplying construction services;
- sales invoices where non-standard VAT rates were charged.

HMRC state that they aim to review and respond to the information within 7 working days.

If HMRC does not reply within this timeframe, the business or its agent can contact HMRC using the telephone number quoted on the CFSS letter.

https://www.gov.uk/guidance/send-details-to-support-your-vat-repayment-claim