# Tolley®CPD

January 2020

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# Personal tax

## IR35 – IT consultant win (Lecture P1171 – 19.24 minutes)

*Summary - The hypothetical contracts satisfied the Ready Mixed Concrete tests, resulting in HMRC losing the case.*

Mr Alcock worked as an employee for Accenture from September 1998 until March 2008 when, having failed to gain promotion, he left to provide his services via RALC Consulting Limited, his personal services company. DWP had been a client of Accenture and Mr Alcock had worked on DWP engagements whilst at Accenture.

Between 6 April 2010 and 5 April 2015, RALC Consulting Limited contracted with Accenture and the DWP (the "end clients") through two agencies to provide Mr Alcock's services. While working on these engagements he undertook work for other organisations, although this was less than 10% of his total revenue.

HMRC claimed that the arrangements fell foul of the IR35 rules and issued determinations to collect income tax and NICs payable of £164,482 and £78,842 respectively.

RALC Consulting Limited appealed, arguing that the Intermediaries legislation did not apply because the hypothetical contracts with the end clients would have been contracts for services and Mr Alcock would have been self-employed.

*Decision*

The First Tier Tribunal concluded that there was insufficient mutuality of obligation between Mr Alcock and the end clients in the notional contracts to establish an employment relationship. There was no obligation within the contracts for Accenture or DWP to provide Mr Alcock with any minimum amount of work. Further, there was no obligation within the contracts for him to work on any given day or to make himself available for a minimum amount of work. The contracts were time limited with no obligation for them to be renewed on their conclusion. Mr Alcock's contract could be terminated on the spot if there was no work, with no guarantee of any further days even within the contract period and there was no contractual right for Mr Alcock to claim against his clients.

Under the contracts there was a right of substitution, but this was never exercised because Mr Alcock personally performed each contract. It was a fettered right subject to the approval of his clients. They had chosen him personally to provide the services. The only example of another person being considered was not to replace Mr Alcock but to assist in delivery of the project. The Tribunal concluded that this would have pointed towards the contracts being contracts of employment.

The Tribunal was satisfied that Mr Alcock had substantial control. He had reasonable autonomy when determining what and how to carry out his work. Although Accenture and DWP determined when and where he worked, this was required due to the nature and deadlines of the tasks to be completed and the quality of the service to be provided for the end clients.

Mr Alcock had a contractual right to work for other clients, and he exercised this right to a limited extent. However, this proved to be a neutral factor for the Tribunal due to his economic dependency on the contracts in question.

Mr Alcock was held to be operating in business on his own account with his own leased premises, website, email and professional indemnity insurance. He was not involved in any management, pastoral care, HR, training nor disciplinary responsibilities or obligations at either Accenture or DWP.

So, applying the three stages of the *Ready Mixed Concrete* case, including "painting the picture" and taking into account that Mr Alcock was in "business on own account", the Tribunal was satisfied that the hypothetical contracts with his end clients would be ones for services and therefore not caught by the IR35 legislation.

The appeal was allowed.

*RALC Consulting Limited v HMRC*

## Unauthorised payment charge (Lecture P1171 – 19.24 minutes)

*Summary - HMRC's documentary evidence was insufficient to demonstrate a connection between the specific pension fund and the loan and the appeal was allowed;*

Elizabeth Hughes wanted to consolidate three pension pots and sought advice from Mr Steve Cannon who had set up the occupational scheme at Moorcroft Pottery where she worked. At the time, she was not looking to release pension funds from her scheme before the age of 55 but was looking for some financial support whilst undertaking the third year of doctoral studies in urban regeneration at Staffordshire University.

On 26 October 2012, Fast Pensions wrote to Elizabeth Hughes to confirm that funds of just over £31,000 had been received into her new Plan (FP1), and that the Plan had started. At around the same time, she was offered and accepted a loan from another company, Blu Funding Corporation Limited and received £10,000 on 24 October 2012.

HMRC submitted that the loan to Elizabeth Hughes was an unauthorised payment under the FA 2004 and applied the relevant tax charges. They argued that the amount advanced to her of £10,000 was paid to her under one of two possible routes:

- Direct route: "the payment was a simple payment made to Miss Hughes via the bank accounts of FP1 and Blu Funding"; or

- Indirect route: "FP1 paid the money to Blu Funding Corporation Ltd as an investment, and Miss Hughes was paid out from the investment".

Elizabeth Hughes claimed that she was unaware that the loan was connected to her pension fund and appealed the charge.

*Decision:*

The Tribunal concluded that this was not a case, unlike some others, where a single payment could be readily and unequivocally identified moving to the pension fund, from the pension fund to the lender, and from the lender to the taxpayer. It appeared that Elizabeth Hughes' money moved as part of a larger sum making it difficult to identify exactly when the money was transferred.

From the evidence supplied, the Tribunal concluded that at best the loan was being made (24 October) before the Pension moneys had arrived (26 October). The Tribunal was not satisfied that the direct route applied and were not satisfied that Elizabeth Hughes received a payment from her pension scheme via a third party.

As for HMRC's second approach, the documentary evidence supplied was muddled and not clear-cut. The Tribunal stated that it was not their task to seek to unravel a documentary tangle that defeated even the Insolvency Service's investigators. (Interestingly, the Insolvency Service referred to the winding up of Fast Pensions Ltd and Blu Debt Management Ltd as "Rogue pension and finance companies closed down after abusing millions of pounds". The service had acknowledged that it had been impossible for Government investigators to determine the full extent of the companies' activities, the nature and value of the investments made, or the value of the members' pension funds).

Due to the inconsistent documents, the Tribunal could not be satisfied that the £10,000 loaned was connected to her pension fund under either the direct or the indirect route postulated by HMRC.

It was therefore not an unauthorised payment, and the charges could not stand. The appeal was allowed.

*Elizabeth Hughes v HMRC (TC07417)*

Earlier this year there was another case involving the same pension and loan companies (Gary West v HMRC -TC07385)

Gary West needed a loan as he was in financial difficulty due to his ill health. In August 2012, Blu Funding Corporation Limited offered him a loan for £11,650 and around the same time they asked him about his pension arrangements.

He believed the transfer of his pension to Fast Pensions to be a good idea because his current pension was not receiving any further contributions, it was not being managed and it was not growing. He was told the funds would be actively managed in the Fast Pensions scheme. His fund was transferred on 21 December 2012

Unlike in the Hughes case, there was a single credit identifiable on the bank statement showing the transfer from Gary West's pension to Blu Funding. The sum of £11,650 appeared on 25 January 2013 described as 'Transfer loan to Blu funding'. While in the Hughes case, it was not possible to trace the funds moving, in this case the matter was clear cut.

The First Tier Tribunal said the evidence proved 'on the balance of probabilities' that funds were moved from the FP1 account to Blu Funding and then to the taxpayer as a loan. The appeal was dismissed.

At the end of the Hughes case the Tribunal highlighted that there are some 520 people who were encouraged to transfer their pension savings from existing providers into schemes (including FP1) with Fast Pensions acting as the sponsoring employer. Only time will tell just how many of these will come before the Tribunal.

## EIS relief denied **(Lecture P1171 – 19.24 minutes)**

*Summary - EIS relief did not apply to a new issue of shares as the new shares had an excluded preferential right to dividend.*

Foojit Limited was incorporated on 22 January 2014 and provided hybrid mail solution services to businesses.

The company wanted to issue B shares in order to raise funds and to provide enhanced protection as compared to the existing A shares and shareholders

On 28 August 2014 Foojit Limited applied for advanced assurance in respect of the EIS. On 7 October 2014 HMRC confirmed that EIS authorisation would be provided if a satisfactory EIS 1 certificate was filed. This included certification that the shares complied with the requirements contained within ITA 2007.

On 18 November 2014 Foojit Limited amended its Articles of Association in order to facilitate the share issue following which 910 £1 B Shares were issued for a subscription of £400,000 and the company submitted form EIS 1 on 16 January 2015.

HMRC refused to grant authorisation on 30 January 2015 on the basis that the B Shares carried a preferential right to dividends as the B shares were entitled to 44% of the distributable profits in preference to the other shareholders.

The company appealed.

*Decision*

The First Tier Tribunal concluded that the B shares satisfied s173(2)(a) and (b) as they did not carry any preferential rights on a winding up or any rights of redemption.

The Tribunal found that the profit allocation did not disqualify the company from relief as the amount payable did not depend on a decision by the company, the shares did not carry a preferential right within s173(2A)(a). The right was fixed and could not be altered by a director or member

However, there is a second requirement within s173(2A)(a) that also needs to be satisfied. This states that the dates on which the dividends become payable is not dependent on a decision by the company, shareholder or any other person.

This was not satisfied as the Articles of Association did not provide that the dividends were payable on a certain date and suggested that payment in stages was possible and was dependent on the company making a decision or passing a resolution.

The Tribunal concluded that the date or dates on which the dividends were payable depended on a decision of the company, the holder of the share or any other person on the basis that once the audited accounts were completed, the distributable profits had to be identified and a declaration or resolution was required for the dividends to become payable. The B Shares carried a preferential right of the type which was excluded by s173(2A).

The appeal was dismissed.

*Foojit Limited v HMRC (TC07467)*

# Capital Taxes

## Who wants to be a millionaire? (Lecture P1173 – 14.41 minutes)

*Background*

The television game show known as 'Who Wants To Be A Millionaire?' was created in 1998 by David Briggs, Michael Whitehill and Steven Knight for ITV. The show took its title from a song written by Cole Porter for the 1956 film 'High Society' starring Frank Sinatra, Bing Crosby and Grace Kelly. Following the launch of the original version, several individuals made claims that they had conceived the idea behind the show and that the company producing it had breached their copyright. There were also allegations about unpaid or underpaid royalties. As a result, significant litigation followed. Since the show's debut, international variations have been aired in around 160 countries worldwide.

*The sale*

The three creators, together with the trustees of the Briggs Accumulation and Maintenance Trust, held all the shares in two UK-resident companies:

- Knight Whitehill Productions Ltd (KWPL); and
- River Studio Ltd (RSL).

KWPL and RSL owned the rights to the show, along with another company called Complete Communications Corporation Ltd (which was not otherwise involved). The sale of the KWPL and RSL shares in December 2006 has given rise to an intriguing First-Tier Tribunal case (Briggs v HMRC (2019)) about whether a gain can be backdated to the business asset taper era that would then allow that relief to apply.

The terms of the deal were as follows:

- The four parties sold their shares in KWPL and RSL in return for a cash sum of £106,000,000 and a right to receive a future 'pass through payment' (PTP) which was dependent on the outcome of litigation in the USA.
- The sale and purchase agreement stipulated that the vendors' entitlement to any PTP would be satisfied by the issue of guaranteed redeemable loan notes from the buyer.

As far as the taxpayers' 2006/07 returns were concerned, these disclosed gains based on the 2006 sale proceeds, in respect of which 75% business asset taper relief was deducted. It is understood that nothing was shown with regard to any PTP entitlement on the ground that relief was due under the automatic deferral rule in S138A TCGA 1992.

*The deed of variation*

Eventually, the USA litigation was settled and this resulted in a substantial sum being passed on to the vendors in satisfaction of the PTP. At this point, the vendors decided that they would prefer to receive their PTP in the form of cash rather than in the form of loan notes and so a deed of variation amending the sale and purchase agreement was executed in May 2013. A few days later, the vendors received cash payments in settlement of their PTP rights. It was the tax treatment of these 2013/14 payments that brought about this case.

Following the payment, the vendors argued that the source of the PTP was the original sale and purchase agreement. They said that the subsequent changes implemented by the deed of variation had to be read back to that agreement. Therefore, in 2006/07, the vendors had sold their shares in exchange for:

- an initial cash sum; and
- a future unascertainable amount (i.e.. the value of the PTP).

Under the principle in Marren v Ingles (1980), the value of this future amount should have been brought into account when computing the chargeable gain which arose in 2006/07. The resulting gains would have been significantly larger, but they would have benefited from 75% business asset taper. Thus further CGT was due (plus, of course, some interest), but at a relatively modest rate.

On receipt of the cash in 2013/14, the vendors contended that there had been a second CGT disposal, based on the amount by which the cash received exceeded the valuation of the PTP right in 2006/07. Accordingly, they:

- amended their CGT computations for 2006/07 to include the value of the CGT rights; and
- submitted returns for 2013/14 showing their capital gains or losses on the disposal of those rights.

It should be emphasised that any 2013/14 gains would not qualify for entrepreneurs' relief (which had by now replaced the business asset taper relief code).

*HMRC's arguments*

Ignoring all this, HMRC raised CGT assessments on the vendors for the full amount of the cash sums received in 2013/14.

As HMRC's barrister pointed out, the difficulty with the vendors' approach lies in the words of S138A TCGA 1992. This provision is designed to address the situation where a right (such as we have here) is received in the form of – typically – loan notes and the Marren v Ingles (1980) principle would otherwise operate to charge CGT on the vendor, notwithstanding that there has been no actual cash receipt at the time.

S138A TCGA 1992 applies automatically where a right is received on a sale of shares (known as 'old securities') and that right consists of an entitlement to be issued with shares or loan notes in another entity (known as 'new securities'). It is also a requirement that, in these circumstances, it must be impossible to ascertain the value of the shares or loan notes at the time when the right is conferred.

It is open to a taxpayer to disapply the operation of S138A TCGA 1992 by making an irrevocable election under S138A(2A) TCGA 1992. In this case, none of the vendors had made a disapplication election.

As a result, under S138A TCGA 1992, the vendors were treated as having disposed of their shareholdings in 2006/07 partly for cash (on which a CGT charge immediately arose) and partly for a new asset, i.e.. the future right to proceeds from the PTP arrangement. The share exchange provisions applied so that the 'new' asset (the PTP right) represented the same asset as the 'old' asset (the shares for which it was exchanged). This new asset was extinguished in 2013/14 on the execution of the deed of variation. The cash received was thus a capital sum derived from that asset and was taxable under S22 TCGA 1992.

*The decision*

Judge Guy Brannan was emphatic that the taxpayers' arguments were 'wrong in every respect'. They had a right to receive loan notes until May 2013 and that right was clearly an asset for CGT purposes. However, the deed of variation in May 2013 had expunged that asset and had replaced it with a right to receive a cash sum which was satisfied a few days later. CGT was chargeable by reference to that sum. The original CGT computations for 2006/07 therefore stood and additional gains arose in 2013/14. HMRC won the case.

*Conclusion*

If the vendors had been successful in having the value of the PTP right taxed at the time of the share disposal in 2006/07, the gains would have been subject to business asset taper relief at 75%, as has already been mentioned, which would have produced an effective 10% CGT rate. This position could have been achieved by electing to disapply S138A TCGA 1992 by the first anniversary of 31 January next following the tax year in which the earn-out right arose, i.e.. by 31 January 2009. But this was not done. As the judge observed:

> 'It surely cannot be the case that, by executing a deed of variation in 2013 (and receiving cash in lieu of loan notes shortly thereafter), the appellants can replicate the tax position that would have prevailed if they had made an election within the time limit specified by S138A(5)(b) TCGA 1992. That would make the time limit meaningless.'

Although this case concerned business asset taper relief, similar issues arise under the entrepreneurs' relief rules. The question of whether or not to make an election under S138A(2A) TCGA 1992 always requires careful consideration.

*Contributed by Robert Jamieson*

## Entrepreneurs' relief for a partnership (Lecture P1171 – 19.24 minutes)

*Summary – The couple were in partnership but entrepreneurs' relief was denied as no trade ceased when the premises were sold.*

Stephen Reneaux worked as a self-employed MOT tester and mechanic. His wife worked as a hairdresser but she was also employed by her husband's business to deal with the administration and accounts.

The couple acquired two business units. Between 1993 and 2003, Stephen Reneaux traded at the premises under the name Trucktest as an MOT tester and HGV vehicle mechanic.

In 2003, the Trucktest business was sold to a Mr Robertson, who leased the premises from that date until 2011 when his business failed. The premises were unoccupied for a short period.

The couple considered running the premises as an MOT centre and in May 2012 contacted the Vehicle and Operator Services Agency ("VOSA") to apply for appointment as an Authorised Examiner. However, this plan was shelved when Stephen Reneaux was approached by Chalvey Car Service, a dealer in classic cars, with a view to hiring out Unit 2 to provide secure storage for their stock of cars. Chalvey Car Service paid him £10,000 to store their cars at the Premises from 1 November 2012 until 31 March 2013.

Stephen Reneaux continued to work as a freelance MOT tester at customer locations. He occasionally made use of the workshops in Unit 1 to carry out vehicle maintenance work, as well as for the storage of some of his heavier tools, but he acknowledged that this was at most "a couple of times a month". Most of the tools of his trade were kept in a garage at his home address.

All the income from his work as a freelance MOT tester and vehicle mechanic was returned on his income tax returns for the period. None of this income was returned on the tax returns of his now, ex-wife.

All the income from the letting of the storage facility in Unit 2 and the workspace hire facility in Unit 1 was split 50/50 between them and reported on their respective tax returns as rental rather than trading income.

On 9 May 2013 the units were sold for £600,000 to the owner of Chalvey Car Service. They both reported gains on their tax returns and claimed entrepreneurs' relief, which HMRC denied.

*Decision*

The First Tier Tribunal stated that there were two trades that they needed to consider:

1. Stephen Reneaux's trade as a freelance MOT tester and vehicle mechanic;

2. The couple's provision of storage facilities and workshop hire at the premises.

The Tribunal concluded that Stephen Reneaux's trade as a freelance MOT tester and vehicle mechanic did not cease when the premises were sold. The condition in s169I TCGA 1992 that requires the premises to be used at the time that a business ceased to be carried on, were clearly not met.

The Tribunal also concluded that the leasing of the storage space for cars was a single transaction that constituted the simple lease of property rather than trading activity. The workshop hire might have had the necessary frequency to be treated as a trade but the Tribunal did not hear any evidence that this was a substantial activity. Without a business, the premises could not have been in use for the purposes of a business at the time the business ceased to be carried on and so entrepreneurs' relief was denied.

Clearly it was not necessary to consider whether the taxpayer and his former wife were carrying on a business in partnership. However, the Tribunal did look at this point.

Even though they were divorced they agreed on a joint course of action, which was designed to realise income from the Premises. S1(1) Partnership Act 1890 says a "Partnership is the relation which subsists between persons carrying on a business in common with a view of profit." On this basis, the Tribunal concluded that the couple were in partnership despite there being no partnership agreement and income being declared to HMRC on an individual rather than partnership basis.

*Stephen Reneaux & Lynne Reneaux-Smith V HMRC (TC07441)*

## Reversal of a main residence relief decision (Lecture P1172 – 19.26 minutes)

The Court of Appeal's decision in Higgins v HMRC (2019) concerns the availability of principal private residence relief under Ss222 and 223 TCGA 1992. It is another in the long line of main residence tax cases which have come before the Tribunals and Courts in recent years and will be of particular interest to those practitioners advising clients about the sale of off-plan properties. The Court of Appeal has reversed the finding of the Upper Tribunal in 2018.

In 2004, the taxpayer (H) paid a reservation deposit of £5,000 for a two-bedroom apartment which was being created out of the former St Pancras Station Hotel but which, at that time, had yet to be built.

On 2 October 2006, when issues relating to the site's title had been resolved, H entered into a contract with the seller for the grant of a 125-year lease over the apartment (which had still not been started) for a total consideration of £575,000. This was to include two further deposits which, if not paid, would have allowed the seller to rescind the contract. A final payment was due on completion.

H sold his previous residence in July 2007 and, from then until he obtained possession of his new apartment, he stayed with his parents and also occupied a rental flat which he owned where the tenant had moved out. HMRC accepted that all these arrangements were temporary, i.e.. there was no other dwelling which H regarded as his main residence.

Work finally began on the construction of H's apartment in November 2009 following delays over funding issues that affected the seller but, by mid-December 2009, H was informed that the property had been substantially completed.

H, although allowed access to the building to look round, had no right to occupy his property until 5 January 2010 when his purchase went through.

Exactly two years later, i.e.. on 5 January 2012, H completed the sale of this apartment to a new owner. He had exchanged contracts with the buyer on 15 December 2011.

HMRC did not challenge the amount of H's gain on the disposal in 2011/12 and they accepted that principal private residence relief was available as a result of S223(1) TCGA 1992 which states that no part of a gain is chargeable to tax where the property has been the taxpayer's only or main residence throughout his period of ownership. Where the two sides differed was over the period of ownership for which relief was due. In other words, HMRC were arguing that there should be a restriction on the principal private residence relief which resulted in a CGT liability of more than £60,000 becoming payable, on the ground that there was a period of time during H's ownership when he had not occupied the apartment as a main residence. This, in turn, came down to a question of when H's occupation of the property was deemed to commence for CGT purposes.

HMRC's argument was that the qualifying period of ownership should not necessarily be confined to periods when H could first occupy the property. In their view, the period of ownership commenced on the date when the contract to acquire the lease was signed (2 October 2006), and not on 5 January 2010 when H actually took up residence. HMRC considered that relief from CGT should be limited to increases in value during the period of occupation as a residence. Any increase in value before H occupied the apartment should not, they said, be covered by principal private residence relief. ESC D49, which is soon to become a statutory provision, allows a period of up to two years in exceptional circumstances to be treated as a period of occupation, but the delay in H's case comfortably exceeded this time limit and so ESC D49 was not in point – see Paras CG65003 and CG65009 of the Capital Gains Manual.

Newey LJ, who delivered the leading judgment, began by highlighting the fact that, under HMRC's interpretation (see above), very few people would qualify for full main residence relief, given that exchange and completion do not normally take place on the same day. HMRC had argued that S28 TCGA 1992, which identifies the acquisition and disposal of a chargeable asset by reference to contract dates, should determine the meaning of 'period of ownership' in the context of the availability of principal private residence relief. The judge did not accept HMRC's contention that any resulting anomaly which this caused was effectively remedied by the fact that only small liabilities would typically arise and that, in practice, short delays are ignored. There was a strong likelihood, he felt, that HMRC's interpretation was incorrect.

HMRC's understanding of the phrase 'period of ownership' ran counter, Newey LJ said, to the normal meaning of the words, since a purchaser would, as a matter of ordinary language, only be described as the owner of the property once completion had taken place. Moreover, he continued, it was hard to see how ownership could have commenced before completion of the building work as H's apartment did not exist in 2006 (and this could be distinguished from the purchase of a plot of land and the subsequent construction of a dwelling – catered for by ESC D49 – since, in that case, the land had existed throughout).

The Court of Appeal agreed with the First-Tier Tribunal that the period of ownership for main residence relief purposes did not begin until the completion of the contract for building the apartment and so the three judges allowed the appeal against the Upper Tribunal's decision.

There is likely to be considerable relief at this outcome, as the use of completion dates in this situation:

(i) ensures that most taxpayers will obtain full relief; and

(ii) avoids the need to rely on unpublished HMRC practice.

However, it remains to be seen whether there will be an appeal to the Supreme Court.

*Contributed by Robert Jamieson*

## No PPR for flat (Lecture P1171 – 19.24 minutes)

*Summary – Lack of reliable evidence to show that the taxpayer had ever lived in a property meant that Principal Private Residence (PPR) relief did not apply on the sale of a flat*

On 18 December 2001 and following her divorce, Cornelia Simpson bought Coleherne Court for £825,000 and moved into the flat with her daughter. She claimed that when her daughter married in 2013 this property was to become her daughter's marital home and so she looked to buy a smaller flat in the same area of London. In June 2013, she bought a flat in Earl's Court Square that she claimed she had moved into it on her return from her daughter's wedding that summer. She argued that having bought the flat that she had furnished it, moved in and had lived in it while the refurbishments were being undertaken as her main residence.

Later that year in November 2013, she sold the flat, having undertaken the substantial improvements at the property and claimed PPR relief that HMRC denied.

*Decision*

Interestingly, the daughter and her French husband never moved to London, choosing to live in Paris where he worked. The First Tier Tribunal stated that they were not satisfied that the daughter and new husband ever intended to move to London.

Throughout, all correspondence had continued to be addressed to Cornelia Simpson at her Coleherne Court address and she had continued to claim the 25% single person council tax discount in relation to that property.

As for the new flat, it had been sparsely furnished and no contents insurance had been taken out. Utility suppliers confirmed that they had had no contact with Cornelia Simpson and so the Tribunal concluded that she did not tell them that she was the new occupant of Earl's Court Square.

The Tribunal found that the flat was never occupied as a residence and PPR relief was denied.

The appeal was dismissed.

*Cornelia Simpson v HMRC (TC07476)*

## UK Residency and the sale of property (Lecture P1175 – 13.34 minutes)

The following is a case study that looked at residency within the UK for tax purposes. It was particularly pertinent in this case as the individual had sold a property in the UK which would have resulted in a tax bill if she had been treated as resident during 2018/19 but would have been covered by reliefs if taxed under the Non-Resident CGT provisions.

*Basic provisions of legislation*

The statutory residency test is used to determine residence. There are three stages:

1. Is the individual automatically not resident? If the answer is yes, then that is conclusive and you have to go no further;

2. If not, are they automatically resident? If the answer is yes again you go no further;

3. If not, consider the number of ties and days in the UK and this determines residence.

If the answer to the above is that the individual is resident, then you may be able to claim split year treatment so that the person becomes resident for part of the year only and there are rules that govern:

a) if you can claim it ;and

b) the date at which you become resident. In this case, the property was sold after the individual returned to the UK so if split year treatment applied, then tax would have been payable.

The automatic NR tests are:

- Working FT overseas – this has to be judged over a whole tax year and if you leave part way through the year, you cannot meet this test;

- Spending insufficient time in the UK – it is either less than 46 days if you have not been resident in any of the previous 3 years or less than 16 days if you have been resident in one of the previous three years.

The automatic residency tests are

- Working FT in the UK – this is judged over a 365-day period of which at least one day must be in the tax year;

- Spending more than 183 days in the UK;

- Having a home in the UK and no home outside the UK (this is a complex test and has to consider a number of steps).

The connections that have to be considered if neither of the above apply are:

1. Family tie (if you have a spouse or minor children resident in the UK);
2. Available accommodation (basically somewhere to live);
3. Working for at least 40 days;
4. Spending at least 90 days in the UK in either of the two previous years.

There is a fifth connection which is whether you spend more time in the UK than any other country but that only applies for individuals who have been resident in at least one of the previous three tax years.

There is a table that then tells you whether you are resident or non-resident depending on the number of days you are present in the UK. There are actually two scales – one where someone is outbound (i.e. has been UK resident in at least one of the previous three years) or inbound (not UK resident in at least one of the previous three years).

*Outbound individuals*

| Days in the UK | UK ties needed to be resident |
|---|---|
| 16 – 45 | At least 4 |
| 46 – 90 | At least 3 |
| 91 – 120 | At least 2 |
| Over 120 | At least 1 |

Inbound individuals

| Days in the UK | UK ties needed to be resident |
|---|---|
| 46 – 90 | All 4 |
| 91 – 120 | At least 3 |
| Over 120 | At least 2 |

*Facts*

Our taxpayer, Barbara, returned permanently to the UK on 20th December 2018. Her days in the UK in 2018/19 were:

| Month | Days |
|---|---|
| April (from 6th) | Nil |
| May | Nil |
| June | Nil |
| July | 2 |
| August | 26 |
| September | 30 |
| October | 4 |
| November | Nil |
| December | 12 |
| January | 31 |
| February | 28 |
| March | 24 |
| April (to 5th) | 5 |

The property was purchased in 1999. Barbara lived there until September 2010 when the family emigrated to Australia and the property was sold. It was sold on 28th January 2019. She worked in Australia up until December 2018 but has not worked since returning.

It should be noted that we do not need to consider the temporary non-residence rules which would bring the gain into charge to UK tax even if she was non-resident in 2018/19. These only apply if she was out of the UK for less than 5 years.

*Analysis*

Barbara is not automatically non-resident as she stopped working part way through the tax year so cannot meet the test relating to overseas employment. She has spent too many days in the UK to meet the other test.

If we look at the automatic residency tests, Barbara did not fall within (a) or (b) so it hinges on where she is living in the UK. This is a complex test and the one which is most often misunderstood.

To meet the second automatic UK test, the individual has to meet the following conditions:

- He spends at least 30 days in his UK home during the relevant tax year; and
- There is at least a 91-day period which the individual has that home, at least 30 days of which are in the relevant tax year, and throughout that 91-day period either the individual has no overseas home or, if the individual does, the individual spends less than 30 days in the relevant tax year in each overseas home.

It is important to accurately understand this test. In particular:

- The 30-day period referred to in the first test does not have to fall within the 91-day period in the second test;

- In the second test, although the individual has to have a home in the UK on at least 30 days in the relevant tax year, he does not have to have any presence in during that 30-day period;

- If the individual meets the first condition and there is a 91-day period when he had no overseas home which meets the second set of conditions, it will not matter that the individual had over 30 days presence in an overseas home at another time during the relevant tax year.

Without going into detail, Barbara had not rented or bought a property in the UK as she had stayed with family and friends (but none for an extended period) or in hotels or been travelling abroad. She also retained a property in Australia which she spent time in during the year. As such she did not meet the home test because she had no home in the UK. If she had chosen to rent a property, then it would have been a different outcome.

We then have to look at the ties test. Barbara would need to have 2 ties to be resident in the UK based on the number of days she has been here. She definitely has available accommodation but as long as she was not in the UK in 2017/18 or 2016/17 for more than 90 days then she will be treated as non-resident on the basis that she has not worked.

*Would split year have applied?*

If it had not been possible to confirm that she was not resident, it is interesting to speculate whether split year treatment would have applied. For someone returning to the UK, there are five possible scenarios (with additional conditions needing to be met for each to apply):

- Case 4: where the individual does not meet the only home test at the start of the tax year but at some point in the tax year that ceases to be the case and then the individual continues to meet the only home test until the end of the tax year. The overseas part of the tax year starts of the beginning of the tax year and ends on the day before the earliest point at which the individual meets the only home test. The UK part of the tax year is the period from the end of the overseas part until the end of the tax year.

- Case 5: if they start to work full time in the UK and then meet the third automatic UK test over a period of 365 days. The overseas part of the tax year starts at the beginning of the tax year and ends at the point at which the third automatic UK test is met by working full-time in the UK and the UK part of the tax year is the period from the end of the overseas part until the end of the tax year.

- Case 6: if an individual is not resident in the previous tax year due to working full time overseas but full time work overseas ceases in the tax year. The overseas part of the tax year will be from the beginning of the tax year until the last day of the latest period for which the sufficient hours test is met and the UK part of the tax year is the period from the end of the overseas part until the end of the tax year.

- Case 7: if they come to the UK with a partner who is returning or relocating to the UK after a period of working full-time overseas. The deemed arrival day is the later of the date that is the first day of the UK part of the year for the partner under Case 6 and the date on which the individual moves to the UK so that they can live with their partner. The overseas part of the tax year is the period from the beginning of the tax year until the deemed arrival day and the UK part of the tax year is the part of the year beginning with the deemed arrival day and ending at the end of the tax year.

- Case 8: if an individual has no home in the UK but at some point during the tax year the individual starts to have a home in the UK. The UK part of the tax year starts on the date that the individual has a home in the UK and continues until the end of the tax year and the overseas part of the year is from the beginning of the tax year to the start of the UK part of the year.

Cases 5, 6 and 7 are not applicable as Barbara did not work in the UK or return with a partner. Cases 4 or 8 could have applied and she could have been caught by these if she had acquired a home in the UK before she had sold the other property – importantly of course that could have included a rented property.

*Contributed by Ros Martin*

## Farming business eligible for APR and BPR (Lecture P1171 – 19.24 minutes)

*Summary – The deceased occupied the house and other buildings at Woodlands Farm for agricultural purposes for two years up to his death and the business carried on by him did not consist "wholly or mainly of...making or holding investments".*

Thomas Gill lived at Woodlands Farm in Lancashire and on death, he owned the freehold to 11 properties which broadly included the house where he lived; a yard, brick barn and other outbuildings and 21.19 acres of bare agricultural land (permanent pasture).

During the relevant period Mr Gill did not own any livestock. He allowed farmers to graze their livestock on his agricultural land under annual grazing licences. HMRC allowed the executors' claim for APR on the land on the basis that the land was agricultural property at the date of Mr Gill's death and that he had the right to obtain vacant possession within 12 months as the grazing licences had less than 1 year left to run,

On 1 November 2017 HMRC issued a Notice of Determination refusing the claim for:

- APR in respect of the value of the house, the brick barn and all other outbuildings at Woodlands Farm; and

- BPR in its entirety.

The APR claim in respect of the buildings was refused on the basis that the house was not a "farmhouse" and thus did not constitute "agricultural property" and neither the house nor the other buildings were occupied by Mr Gill "for the purposes of agriculture" throughout the period of two years ending with Mr Gill's death.

The BPR was refused on the basis that the business carried on was not "relevant business property" as it consisted of "wholly or mainly of...making or holding investments" (i.e. the land owned by Mr Gill).

The taxpayers appealed, arguing that the land, farmhouse and buildings were agricultural property as they were occupied by Mr Gill for agriculture purposes for the relevant period. It was wrong to break down the farm into various discrete elements and that HMRC should consider the claim based on the overall nature of the farm. They argued that under the licences, Mr Gill retained possession, overall control and occupation of the land. Although not his livestock, Mr Gill would move the animals depending on the state of the land through the seasons; some of the fields were best for grazing, others had shelter for the animals and there was a shed in the yard in which the animals could be penned. He maintained the hedges, fencing, ditches, drains, control of weeds, topping, harrowing, rolling and preventing 'poaching' by animals; his vehicles and equipment, stored in the outbuildings, were used for and in connection with working the land; he received the Single Farm Payment from the Rural Payments Agency payable to farmers.

*Decision*

There was no dispute that Mr Gill occupied the house until his death or that the house was "of a character appropriate to the property". But was his property used "for the purposes of agriculture"?

The Tribunal stated that the activities carried out by Mr Gill were those of a farmer, working an active farm. In their view his significant maintenance and keeping the land in good order were part and parcel of running a working farm. The outbuildings were used as farm buildings, for storing equipment used for agricultural activities. He ran a farming business and occupied the main farmhouse on a farm where he was an active farmer.

The Tribunal concluded that these activities were not carried out to obtain income and could not be regarded as a business of holding investments; the farming work was done to maintain the business of an active working farm.

The Tribunal were satisfied that Mr Gill's occupation had always been as a farmer and although the manner in which he farmed was modified with time and age, he did not cease to be a farmer, his activities did not cease to be "for the purposes of agriculture" nor did they become those of an investor.

The appeal was allowed.

*Charnley & Hodgkinson as Executors for Thomas Gill (Deceased) v HMRC (TC07425)*

## Making tax easier for trusts and estates **(Lecture P1174 – 4.46 minutes)**

In FA 2016, the requirement to deduct basic rate tax on income from banks, building societies and National Savings and Investments was removed and interest from these sources has been paid gross with effect from 6 April 2016.

As a result, trustees and personal representatives now have increased reporting requirements. For example, trustees of an interest in possession settlement would normally have had no tax to pay on any interest which they received from trust investments up to 2015/16, given that the basic rate tax deducted at source franked their income tax liability. For 2016/17 onwards, this interest has been subject to a 20% tax charge and, of course, the personal savings allowance is not available to these taxpayers.

HMRC therefore introduced an interim arrangement under which trustees and personal representatives do not have to submit returns or make payments where their only source of income is savings interest and the resulting tax liability would be less than £100.

It was announced in the HMRC Trusts and Estates Newsletter for August 2019 that this arrangement has been extended to cover 2019/20 and 2020/21, with HMRC committing to review the situation in the longer term.

*Contributed by Robert Jamieson*

# Administration

## HMRC choose payment allocation

*Summary - Late payment penalties were charged in accordance with legislation and there was no reasonable excuse for failure to pay tax on time, nor by the date the penalty arose.*

Kuriakos Kritikos filed his tax return for 2010/11 on time and believed that he had settled the related tax liability. However, he had not specified that the payment was to be allocated against his 2010/11 liability.

HMRC allocated the 2010/11 tax payment against outstanding penalties relating to previous years, meaning that the 2010/11 liability was unpaid on HMRC's system and further penalties arose.

The taxpayer appealed.

*Decision*

The First Tier Tribunal acknowledged that HMRC's allocation of money paid by the taxpayer towards his tax liability was done in a way that was detrimental as it resulted in additional penalties.

However, in the absence of any allocation by the taxpayer, they were within the law, and could allocate the payments made toward the tax liability as they saw fit. The allocation was not unreasonable.

The appeal was dismissed.

*Kuriakos Kritikos v HMRC (TC077452)*

## CIS – deductions on account

*Summary – Having accepted that he should have made deductions under the Construction Industry Scheme (CIS), the taxpayer failed to have HMRC's determinations reduced.*

Peter Ormandi carried on business as a painter and decorator who also installed flooring, kitchens and bathrooms.

In April 2017, HMRC opened an employer compliance check into his records and, during this time, Peter Ormandi acknowledged that he was not aware of the Construction Industry Scheme. In 2013/13 to 2017/18, he had made payments to sub-contractors and as the sub-contractors were not registered to receive payments gross, he should have deducted tax at source from the payments made, but he failed to do so.

On 22 March 2018, HMRC issued two determinations under Regulation 13(2) of the CIS Regulations for periods from 6 June 2013 to 5 July 2018:

1) 10,829.20 (deductions should have been made at 20%); and

(2) £11,595.00 (deductions should have been made at 30%).

HMRC also notified Peter Ormandi that he would be liable to penalties in respect of his failures to file monthly returns and account for amounts deducted under the Scheme for the relevant periods.

Peter Ormandi appealed against the determinations. He argued that the result was grossly unfair. He accepted that he failed to operate the CIS but has since cooperated with HMRC and paid all the related penalties. The sub-contractors have now submitted their tax returns and accounted for tax on the relevant income and profits which includes the payments made by him. If he was now charged on amounts which should have been deducted from those payments, the effect would be "double taxation and a windfall for HMRC".

*Decision*

The First Tier Tribunal stated that the wording of Regulation 13(2) requires HMRC to make a determination of an amount equal to its best judgment of the amounts that a contractor is liable to pay under the CIS Regulations. This is what HMRC did.

Under Regulation13(3), HMRC are only required to exclude from a determination amounts included in a direction which has actually been made before the time of the determination. It would be possible for the existing determinations to be withdrawn and revised determinations made but this would be at HMRC's power and discretion. The Tribunal stated that they have no jurisdiction to supervise the exercise of these powers. If Peter Ormandi wanted to challenge the determinations made by HMRC on the grounds that he raised, he could only do so by way of an application for judicial review and the Tribunal stated that this Tribunal has no jurisdiction to consider such an application.

The appeal was dismissed.

*Peter Ormandi v HMRC (TC07442)*

## Notices to file returns and PAYE

*Summary – HMRC had been entitled to issue a notice to file a return even though the amount of the tax due was known to them.*

David Goldsmith was an employee whose income tax was collected through the PAYE system.

However, for 2011/12 and 2012/13, the PAYE deductions did not cover the full amount of income tax due and he received a PAYE calculation (a P800) advising him that he had underpaid tax for each year. This was due to an incorrect personal allowance being used. He failed to settle the amounts due with HMRC.

HMRC issued David Goldsmith notices requiring him to file self-assessment returns. HMRC said they needed a return to collect the tax that the taxpayer had started to pay off but then stopped doing so. The notices were served in order to create a debt due from David Goldsmith under s59B TMA. He delivered both of these returns late and HMRC issued the relevant penalties.

David Goldsmith appealed against the penalties issued by HMRC in respect of his failure to deliver the relevant income tax returns by the due date. He argued that the notices to file had been invalid, given that the tax due was already known to HMRC.

The First Tier Tribunal looked at the relevant wording in s8(1)(a) TMA:

*"... for the purpose of establishing the amounts in which a person is chargeable to income tax and capital gains tax for a year of assessment, and the amount payable by him by way of income tax for that year...."*

The First Tier Tribunal concluded that HMRC did not need a return to establish the income or the amount of tax payable, as the PAYE system had done that, and the P800 had "assessed" it in the ordinary sense of that word. They allowed the appeal.

*Decision*

The Upper Tribunal concluded that the First Tier Tribunal did have jurisdiction to consider whether the notice to file had been issued for the statutory purpose. However, they disagreed with the First Tribunal's conclusion.

The Upper Tribunal agreed with Judge Mosedale's interpretation of 'establishing' taken from the Crawford case. Here, Judge Mosedale rejected the First Tier's interpretation of 'establishing' reached in the Goldsmith case. Instead, Judge Mosedale stated that one needed to look at the word in its context, so in other words, one needed to look at what a notice to file does. He stated that a notice to file requires a person to make a return that includes a self-assessment. A person is not merely required to make a calculation of the tax that he owes, but to assess himself to that tax as well. The effect of a self-assessment is to create a debt to HMRC (s 59B TMA).

Consequently, the Upper Tribunal concluded that, even though HMRC knew the amount of tax due from David Goldsmith, they did serve a valid notice to file to establish the amounts chargeable as they served the notice to file in order to create a debt due from David Goldsmith pursuant to s59B TMA.

*HMRC v David Goldsmith [2019] UKUT 0325 (TCC)*

# Deadlines

*1 January 2020*

- Corporation tax for periods to 31 March 2019 for SME companies not paying instalments.

*7 January 2020*

- VAT returns and payment for 30 November 2019 quarter (electronic payment)

*14 January 2020*

- Forms CT61 to be submitted and tax paid for the quarter ended 31 December 2019

*19 January 2020*

- PAYE, NIC, CIS, student loan liabilities for month to 5 January 2020 if not electronic
- File monthly construction industry scheme return
- PAYE for quarter to 5 January 2020 if average monthly liability is less than £1,500

*21 January 2020*

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

*22 January 2020*

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

*31 January 2020*

- Online deadline for 2018/19 personal, partnership and trust SA tax returns
- Balance of 2018/19 SA liabilities due
- First instalment of 2019/20 SA liabilities including class 2 NICs
- Deadline for 2017/18 SA tax returns to be amended
- Private company accounts to Companies House with 30 April 2019 year ends
- Public limited companies accounts to Companies House with 31 July 2019 year ends
- Corporation tax SA returns for periods ended 31 January 2019

# News

## Secretary of State confirms pensions tax arrangement for clinicians

Matt Hancock, Secretary of State for Health and Social Care has stated:

"I have agreed to support this proposal from NHS England and NHS Improvement for reasons of urgent operational necessity.

The scheme involves employers making binding contractual commitments to be given to every affected NHS clinician so as to ensure that this commitment is honoured. Full details of the terms of the payment arrangements are set out in letters that are being sent to each affected clinician by their employer including the terms and conditions of the offer.

This contractual commitment contains the provision that in order for it to be operative, the affected clinician must make a Scheme Pays election in relation to the tax charge for 2019/20 only relating to accrual in the NHS Pension Scheme excluding 2019/20 additional voluntary contributions (AVCs) that is accepted by the NHS Business Service Authority.

These binding contractual commitments will provide for payment to be made when the clinician takes their pension, at which point the employer (or its successor) will be liable for the payment. NHS England has undertaken to provide funding to the employer (or its successor) in respect of those liabilities as the payments are made.

There are long-standing precedents for how the liabilities of NHS bodies are met and the government will act in accordance with these.

Should the NHS trust or foundation trust employing the clinician cease to exist, there are statutory provisions to ensure its liabilities, including commitments to staff, would be transferred to one or more existing NHS bodies, or the Secretary of State. The Secretary of State ultimately takes responsibility for the liabilities of NHS bodies including NHS England and NHS Improvement.

Legislative changes to NHS structures by successive governments have previously made provision for the liabilities of organisations that cease to exist to transfer to successor bodies or the Secretary of State. The commitment to make these payments will be contractually binding and if either (a) there is no employer or other NHS body to make this payment at the time the clinician retires or at any later time when a payment falls to be made, or (b) any NHS body to whom these liabilities are transferred does not have sufficient assets to make the payment, the Secretary of State undertakes responsibility for making the payment, or securing that it is made.

Therefore, these payments will be honoured even if the NHS body no longer exists in the future. In order to provide the same level of assurance to clinicians who are TUPE transferred outside the NHS, NHS England undertakes to ensure that the financial responsibility for meeting any employer's liabilities in relation to this commitment is transferred or remains with an NHS body as part of a future transfer process.

Clinicians are therefore now immediately able to take on additional shifts or sessions without worrying about an annual allowance charge on their pensions."

*https://www.gov.uk/government/publications/statement-from-the-secretary-of-state-on-the-clinician-pension-tax-scheme*

## The Queen's Speech

The Queen's speech confirmed the government's plans to:

- raise the NICs threshold to £9,500 from April 2020;
- increase R&D tax credit rate from 12% to 13%;
- leave unchanged the rates of VAT, income tax and NICs;
- provide a measure of relief from employer's NICs when employing former armed forces personnel;
- review alcohol duty to ensure the system supports Scottish whisky and gin producers;
- devolve corporation tax to Northern Ireland once the Assembly and Executive are restored in the province and consider devolution of short-haul air passenger duty;
- introduce a plastic packaging tax through the Environment Bill;
- double the maximum prison term to 14 years for individuals convicted of serious tax fraud; and
- establish the independent Trade Remedies Authority in the Trade Bill.

*www.gov.uk/government/publications/queens-speech-december-2019-background-briefing-notes*

*Tolleys Guidance 20 December 2019*

## Loan charge U turn **(Lecture P1171 – 19.24 minutes)**

The 2019 disguised remuneration Loan Charge was introduced to tackle contrived schemes where a person's income is paid as a loan that does not have to be repaid. The government is clear that disguised remuneration schemes do not work and that their use is unfair to the 99.8 per cent of taxpayers who do not use them.

However, in its present form, the Charge seeks to retrospectively tax a significant number of freelance workers for employment arrangements used over the last twenty years and affects many thousands of workers across all sectors.

There were serious concerns that the tax bills being issued were causing widespread distress and that the rules should not be applied retrospectively. Consequently, in September 2019, it was announced that Sir Amyas Morse, the former Comptroller and Auditor General and Chief Executive of the National Audit Office (NAO), would lead an independent review of the Loan Charge to consider whether the policy is an appropriate way of dealing with disguised remuneration loan schemes.

In his review, Sir Amyas concluded that:

> "…the loan charge should not apply to loans entered into by either individuals or employers before December 9 2010, being the point at which the law became clear."

Following this review, HMRC has now announced that:

- the charge will now only apply to loans taken out from 9 December 2010 (rather than 1999). This was the date that the rules were announced;
- loans taken out between 2010 and 2016 and declared will be exempted; (This seems somewhat unfair on those who were advised not to disclose or that they did not need to disclose).
- taxpayers can defer filing their returns and paying their liability until September 2020 and they will be able to split the balance over three tax years;
- taxpayers earning less than £50,000 and without disposable asset, can agree Time to Pay arrangements for a minimum of 5 years, extended to 7 years for those earning less than £30,000, we will agree a minimum of 7 years. Those needing longer to pay, will need to provide HMRC with detailed financial information. There is no maximum time limit for a Time to Pay arrangement.

The Government is expected to introduce legislation to implement the changes early next year. Once this has happened, HMRC will refund qualifying voluntary payments already made to prevent the loan charge applying.

*https://www.gov.uk/government/publications/disguised-remuneration-independent-loan-charge-review/guidance*

## Revised advisory fuel rates for company cars

HMRC has published revised advisory fuel rates for company cars, applying from 1 December 2019.

The rates are to be used only where employers either reimburse employees for business travel in their company cars, or require employees to repay the cost of fuel used for private travel.

| *Engine size* | *Petrol - amount per mile* | *LPG - amount per mile* |
|---|---|---|
| 1400cc or less | 12 pence | 8 pence |
| 1401cc to 2000cc | 14 pence | 9 pence |
| Over 2000cc | 21 pence | 14 pence |

| *Engine size* | *Diesel - amount per mile* |
|---|---|
| 1600cc or less | 9 pence |
| 1601cc to 2000cc | 11 pence |
| Over 2000cc | 14 pence |

Hybrid cars are treated as either petrol or diesel cars for this purpose.

The Advisory Electricity Rate for fully electric cars is 4 pence per mile.

Electricity is not a fuel for car fuel benefit purposes.

*https://www.gov.uk/government/publications/advisory-fuel-rates*

# Business Taxation

## Suppressed takings (Lecture B1171 – 23.36 minutes)

*Summary – The company had deliberately suppressed cash takings to reduce the amount of Corporation Tax and VAT payable arguing that a card to cash sales ratio was typically 90:10.*

Exotic Spice (Sprotborough) Limited was formed in 2008 and registered for VAT on 1 July 2009. It operates an Indian restaurant and takeaway business near Doncaster that is run by Mr Ala Uddin who is a director of the company. It is open 7 days a week.

On 1 March 2013, HMRC opened an enquiry into the company's corporation tax return for the accounting period ending 30 June 2011. In April 2014 the enquiry was extended to cover the company's VAT returns as well. By the time of the trial, the enquiries had been extended to a number of periods.

A key part of the enquiry involved a covert visit on Saturday 10 May 2014. On this date, two groups of two HMRC officers dined at the restaurant. At the end of the evening the officers observed the cashing up procedure. In evidence, HMRC stated that takings on 10 May 2014 showed one of the lowest card : cash sales ratios identified during their enquiry. The presence of the HMRC officers meant that there was no opportunity for Mr Uddin to suppress the takings. HMRC calculated that the ratio of card payments to cash payments on this date was 55:45. From their analysis of the company's records the declared card to cash ratio was consistently around 90:10

This ratio discrepancy indicated a substantial suppression of restaurant takings resulting in understated corporation tax and VAT liabilities. HMRC sought to recover £138,000 of corporation tax covering the accounting periods 30 June 2011 to 2014, and £73,000 of VAT for the returns from March 2012 to March 2015 as well as penalties totalling £150,000.

*Decision*

Having reviewed all of the evidence, the First Tier Tribunal agreed with HMRC.

The company had deliberately suppressed its takings in order to reduce the amount of VAT and corporation tax for which it would be liable to and they agreed that the extent of that suppression should be calculated by reference to HMRC's card:cash ratio of 55:45.

*Exotic Spice (Sprotborough) Limited v HMRC (TC07436)*

## Enterprise Zone Allowance (Lecture B1171 – 23.36 minutes)

*Summary – Two limited liability partnerships had been carrying on a business with a view to profit and could claim enterprise zone allowances on part of their investments, some of which was due on the basis of legitimate expectation.*

On 4 / 5 April 2011, two limited liability partnerships acquired, among other assets, an assignment of rights under a construction contract known as the "Golden Contract". The LLPs paid consideration of £153 million and £110 million respectively.

The "Golden Contract" related to construction works to be undertaken at the Cobalt Business Park that was within an enterprise zone. The amounts paid were considered to be advance payments for construction works to be undertaken. Two large data centres were subsequently constructed, but no tenants were ever found.

The LLPs claimed Enterprise Zone Allowance on the price that they paid but this was denied by HMRC.

The LLPs considered that, in denying the allowances that had been claimed, HMRC were acting contrary to their published practice which gave them a legitimate expectation that Enterprise Zone Allowances would be available and they therefore also instituted judicial review proceedings.

*Decision*

The Upper Tribunal found that the LLPs were carrying on business with a view to a profit as partnerships under s863 ITTOIA 2005 and so liable to income tax on the profits shared between its members. If s863 ITTOIA 2005 had not applied, it was common ground that the LLPs would have been corporate bodies subject to corporation tax. The distinction was important because the expenditure had been incurred on 4 and 5 April 2011 and the Enterprise Zone Allowance regime had been repealed from 1 April for corporation tax purposes and from 6 April for income tax purposes. Being liable to income tax meant that Enterprise Zone Allowance was potentially available. On the basis of examples and modelling prepared at the time of the transactions, the Upper Tribunal found that the LLPs had believed that making a profit was reasonably achievable.

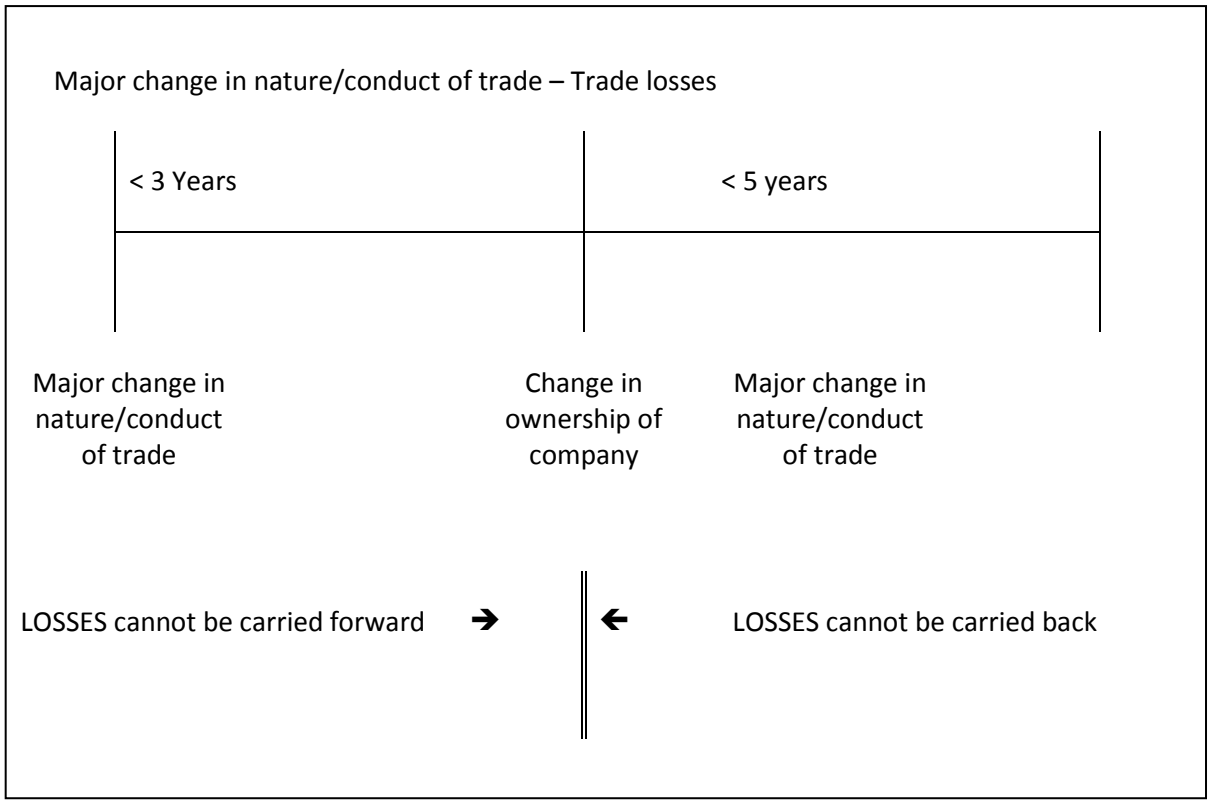
So in theory, the expenditure qualified for Enterprise Zone Allowances. However, the sums paid were not paid wholly for the relevant interest in the sites and so some expenditure, including the arrangement fee and rental support agreement fees, did not qualify for relief.

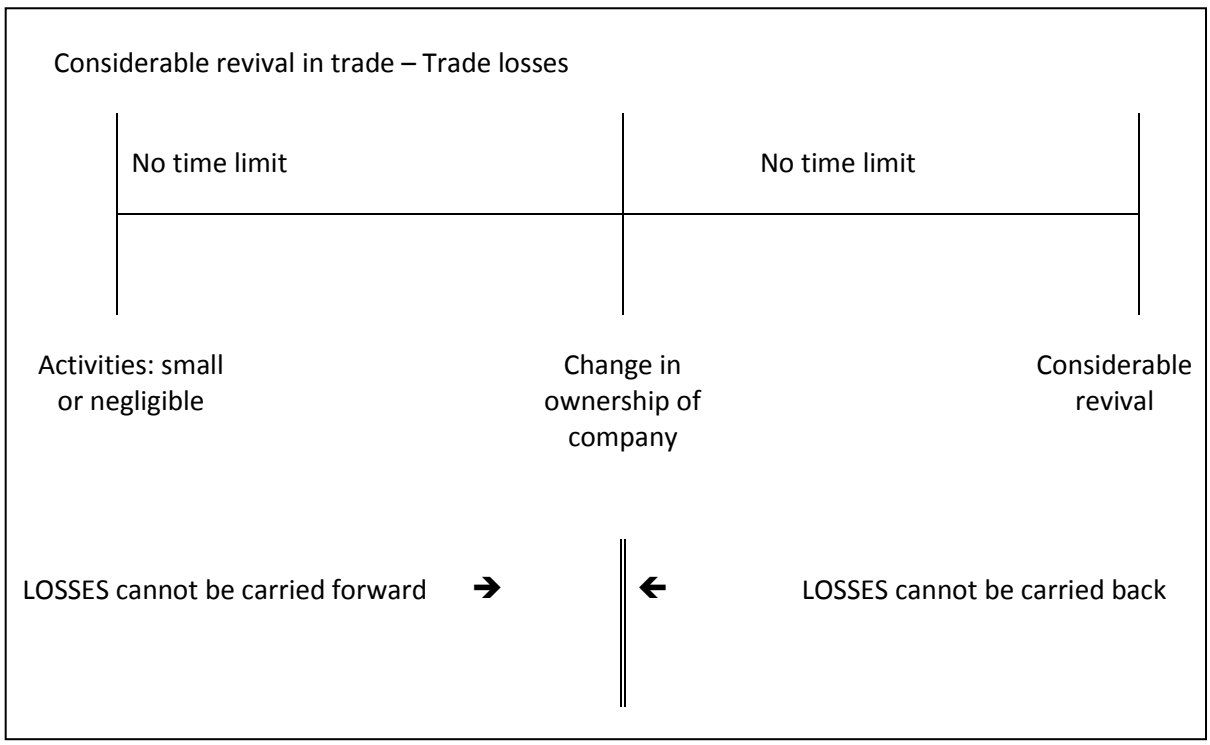
However, HMRC had explained its position on Enterprise Zone Allowances in correspondence with an industry committee, which the Upper Tribunal concluded HMRC knew would be relied on by investors. The LLPs had understood that HMRC would not deny Enterprise Zone Allowances on the purchase price that was paid for rental support agreements. The Upper Tribunal held that the LLPs had a legitimate expectation that such expenditure would qualify and found no good reason to allow HMRC to resile from its guidance.

*Cobalt Data Centre 2 LLP and Cobalt Data Centre 3 LLP v HMRC [2019] UKUT 0342 (TCC)*

## Change in ownership of a company- part 1 (Lecture B1172 – 12.40 minutes)

In principle, when there is a change in ownership (i.e. > 50% control), the company's trading losses are still available to be carried forward and set against the future profits of the company's trade. However, in practice, relief for the losses is likely to be denied under s.673 et seq CTA 2010. This applies in the following circumstances:



Major change includes:

- type of property dealt in; or
- services or facilities provided; or
- customers; or
- outlets; or
- markets

SP10/91 provides more detail

- 'technological improvements' and 'efficiency improvements' OK

Note that HMRC do not give advance clearance on the s.673 provisions.

*Contributed by Kevin Read*

## Change in ownership of a company- part 2 (Lecture B1173 – 14.31 minutes)

F(No.2)A 2017 increased flexibility in the use of b/fwd corporation tax losses arising on/after 1 March 2017, including:

- trading losses no longer needing to be 'streamed'
- b/fwd losses being available for group relief

However, there is lots more anti-avoidance to stop abuse of the new rules, including changes to the 'major change in nature of conduct of trade or business (MCINOCOTOB) rules.

*F(No.2)A 2017 provisions*

As676AA – AL apply where both the:

- the change in ownership, and
- MCINOCOTOB of the company, occur after 31 March 2017.

New legislation on changes in ownership seeks to prevent:

- Non-trading losses being carried forward against the profits of a trade which has undergone a major change in its nature or conduct, and
- Trading losses being carried forward against the profits of an investment business which has undergone a major change in nature or conduct.

In both cases, the losses concerned aren't disallowed in full; instead, they can no longer be offset against profits affected by the major change, where those profits arise within 5 years of the end of the AP in which the change in ownership occurred.

'Affected profits' are those which can fairly and reasonably be attributed to the trade or business in which there has been a major change.

The usual definition of 'major change' applies for these purposes, but is extended to include:

- a major change in the scale of any trade or business carried on, and
- beginning or ceasing to carry on a particular trade or business.

*Group relief: 5-year restriction on use of losses on acquisition*

Target group cannot surrender pre-acquisition carried forward losses as group relief to the acquiring group until the 5th anniversary of the end of the accounting period of Target in which the change in ownership occurs.

The aim is to prevent loss buying. There is no restriction on group relief for carried forward losses within the Target group.

In contrast, the acquiring group can surrender brought forward losses as group relief to the acquired group. However, ss676CF to CH restrict this where there has been a MCINOCOTOB within the acquired group. Losses cannot be deducted from "affected profits", which are:

- profits arising within 5 years of the end of the AP of the acquired group in which the change of group occurred
- that can fairly & reasonably be attributed to the trade or business in which there has been a major change.

*Change in ownership of company with investment business*

Where there is:

- no major change in the nature or conduct of that business,
- nor significant increase in the capital of the company

the old rules still prevent brought forward non-trade losses being set against capital gains arising on assets transferred into the company within 3 years of the change in ownership. (s171 TCGA or s775 CTA 2009).

As post 31.3.17 trading losses can be carried forward against total profits, ss 676BA to BE extend these rules to brought forward trading losses. Both sets of rules now apply for 5 years post change in ownership and also apply to gains elected into Target under s171A. A similar extension prevents Buyer transferring assets to Target with the aim of sheltering gains on sale of those assets by using carried forward losses group relief surrenders from companies within Target group.

*Due diligence*

You should consider all these matters when valuing losses if acting for the purchaser of a company. The logical conclusion is that there is so much risk about the availability of the losses to reduce future taxable profits that no value should be attached to them (although, in the end, this may be a matter for commercial negotiation).

Also, remember that if there has already been a MCINOCOTOB in the 3 years before the acquisition, this might also cause a bar on the use of the losses of the acquired company.

*Contributed by Kevin Read*

## Losses carried forward on transfer of trade **(Lecture B1171 – 23.36 minutes)**

In the *Spring Capital* case, the FTT found that losses could not be carried forward between the predecessor trade and the successor trade under ICTA 1988, s 343.

The FTT had released its decision in relation to Spring Capital's (SC) appeal in February 2015 but had adjourned the appeal in relation to one issue. This issue was whether SC was entitled to utilise carried forward losses, which arose on the transfer of trade from Spring Salmon & Seafood (SSS), a company under common ownership with SC.

SC claimed to be entitled to carry forward losses of SSS under what was then (ICTA 1988, ss 343 and 344) (now chapter 1 of Part 22 of CTA 2010). These rules apply where a company transfers a trade to another company under the same ownership, and effectively permit the successor company to step into the shoes of the predecessor company with respect to trading losses and capital allowances.

The losses that can be transferred are restricted if the predecessor company is left with liabilities that exceed its assets. The liabilities and assets that are left in the predecessor company after the transfer are referred to as relevant assets and relevant liabilities. Under ICTA 1988, s 343, when determining whether this restriction applies, the predecessor company's assets and liabilities are compared immediately before it ceased to carry on the trade.

The FTT accepted that the gradual closing down of a trade could be a 'process' rather than an overnight event, but it noted that the legislation required the identification of a point in time immediately before the cessation of the trade. This had to be the end of the process; when the trade actually ceased rather than when it started to wind down. The trade of SSS had therefore ceased on 11 November 2004, as this was the date of the last invoice issued by SSS to its customers. Consequently, the cash comprising the £1m interim dividend paid on 1 November 2004 could not be counted as a 'relevant asset' of the appellant; the dividend had been paid by SSS before its trade had ceased. In addition, the disputed sum of £2.8m, which was originally shown in the appellant's July 2002 loan account, had not been substantiated by evidence. It was therefore not a 'relevant asset' of the appellant.

The FTT concluded that the 'relevant liabilities' of the appellant exceeded its relevant assets by £1,579,574 and thus exceeded the losses that could potentially be carried forward (£424,544), so that no losses of the predecessor company (SSS) could be carried forward, under s 343, to the successor company (the appellant).

The tribunal observed that ss 343(4) and 344(5) and (6) had been introduced expressly as restrictions on the relief contained in s 343. Their purpose was to prevent insolvent companies from being transferred with their tax losses (in circumstances where there was no major change in the nature or conduct of the underlying trade). The FTT concluded: 'Accordingly, this appeal – which has lasted more than five years – is finally dismissed.'

It should be noted that the wording in the equivalent current provisions at CTA 2010, s945 is different to the wording in ICTA 1988, s 344 as now the reference to the date when relevant assets and liabilities are reviewed is the date immediately before the transfer of trade rather than immediately before the cessation of trade as was the case under s 344.

*Spring Capital Ltd v HMRC* (TC07471)

*Adapted by Joanne Houghton from Tax Journal, 4 December 2019*

## OECD support for tax transparency in developing countries

The EU has provided the OECD global forum with €2m to support developing countries in implementing international standards on tax transparency and information exchange.

The funds are intended to support the Global Forum in providing quality technical assistance to developing countries in implementing international standards on Exchange of Information on Request (EOIR) and Automatic Exchange of Information (AEOI). The technical assistance provided by the Global Forum to developing countries will play an important part in efforts to fight tax evasion and avoidance and generate revenues that are needed to achieve the Sustainable Development Goals.

*https://ec.europa.eu/taxation_customs/news/eu-provides-€2-million-global-forum-support-tax-transparency-and-exchange-information-developing-countries_en*

*Tolley Guidance News*

# VAT

## Matchmaking services (Lecture B1171 – 23.36 minutes)

*Summary – In a split decision, the provision of matchmaking services went beyond the provision of consultancy services so that article 59(c) Principal VAT Directive did not apply.*

Gray & Farrar International LLP ran a well-established, exclusive matchmaking business providing its services to clients in many jurisdictions.

Each client had a face to face meeting making it more difficult for a person to present themself differently so enabling a better match. After the interview Gray & Farrar International LLP would prepare a brief describing the client and the characteristics of the person that they were seeking. The brief was sent to the client for approval. Gray & Farrar International LLP also conducted some vetting of clients from publically available data.

After the brief had been agreed, Gray & Farrar International LLP identified possible matches for clients. The matching suggestions were not done by a computer program or by any sort of algorithm; they were individually selected.

Regularly, after suggestions had been made, clients were telephoned by the liaison team to gain feedback as to whether the date was successful, gather information that might give rise to amendments to their brief, or to arrange further introductions. During the telephone calls, advice or coaching could be given to the client.

The LLP argued that its services fell within the description in Article 59(c) Principal VAT Directive as being:

> "the services of consultants, engineers, consultancy firms, lawyers, accountants and other similar services, as well as data processing and the provision of information",

As a result, they believed that when it supplied its services to non-taxable persons who reside outside the EU, its supply should to be treated as made outside the EU and is thus outside the scope of VAT.

HMRC disagreed arguing that the services supplied were not services "principally and habitually" provided by a consultant.

*Decision*

The First Tier Tribunal agreed that the supply was a single composite service and to decide whether that service fell within Article 59 (c) they needed to look at the principal components of that supply and ask whether they all fell within that provision.

The Tribunal agreed that the clients sought a person for a long-term relationship and that Gray & Farrar International LLP supplied information about carefully selected individuals but the service went further.

Judge Wilkins concluded that the material elements of the supply consisted of the provision of information and expert advice, and that the supply fell within Article 59(c).

Judge Hellier, with his casting vote, accepted that an individual could be an expert at matchmaking. However, he stated that the support provided by the liaison team was support in the developing of a relationship and provided a form of ready-made confidante with whom the client could discuss a relationship. This was support in addition to the use of the information and expert advice received and, as it was not shown to be sufficiently inconsequential, it could not be ignored. He concluded that the services provided went beyond the provision of consulting expert advice covered by article 59(c).

The appeal was dismissed.

*Gray & Farrar International LLP v HMRC (TC07457)*

## School holiday camps (Lecture B1171 – 23.36 minutes)

*Summary – The holiday camps provided a single composite supply where the predominant element was childcare, as opposed to the provision of activities, and were therefore exempt supplies under item 9 of Group 7 Schedule 9 VATA 1994.*

RSR Sports Limited traded under the name of Get Active Sports and among other things they provided school holiday camps.

The company was registered with OFSTED as a private welfare institution or agency and was recognised by both parties as a "state-regulated private welfare institution or agency" for the purposes of construing and applying item 9 of Group 7 of Schedule 9 VATA 1994.

Both parties agreed that the Holiday Camp Services amounted to a single composite supply of services and not multiple supplies of services because the goods and services supplied in the course of providing the Holiday Camp Services were so closely linked that they formed objectively, from an economic point of view, a single supply which it would be artificial to separate into its constituent elements for the purposes of applying VAT law.

In order to decide the correct VAT treatment, the predominant element of the service had to be determined from the point of view of the typical consumer and having regard to the qualitative and not merely quantitative importance of the elements.

RSR Sports Limited considered that these supplies constituted supplies of "welfare services" within the meaning of item 9 of Group 7 of Schedule 9 to the VATA 1994 and so were exempt. By contrast, HMRC considered that these supplies did not fall within these provisions and were properly treated as standard-rated taxable supplies for VAT purposes. So the issue to be decided was whether the predominant element of the supply was the provision of childcare or the provision of activities.

*Decision*

The First Tier Tribunal confirmed that the Holiday Camp Services provided included both an activities element and a childcare element. In order to make the Holiday Camp Services attractive to potential consumers the company was keen to emphasise to those potential consumers the activities element of the relevant services.

Staff supervised the activities at the holiday camps but there was no coaching or teaching of the relevant skills and the staff were not required to have any coaching or teaching qualifications or experience. In addition, there was no external standard to which the activities were being provided. The only qualifications that needed to be held were the appropriate DBS checks required by OFSTED, a child safeguarding certificate from the NSPCC and a first aid certificate. Parents looking for childcare could choose a either a passive or active provider. The former would have children sitting in front of a television or allowing the relevant children to entertain themselves. An active provider, such as RSR Sports Limited , would offer a more active approach to childcare in the form of supervised activities. In the First Tier Tribunal's opinion, a more active provider should not be disqualified from falling within the VAT exemption. They added that with the present focus on obesity in children, a childcare provider adopting an active approach is "surely doing more for the welfare of the children in its care than the passive childcare provider" and should be " more deserving of the exemption."

The appeal was allowed.

*RSR Sports Limited v HMRC (TC07453)*

## Hay making business **(Lecture B1171 – 23.36 minutes)**

*Summary – haymaking and the sale of buildings did not constitute operating as a business during the relevant period and so input tax recovery was denied*

Babylon Farm Ltd had been registered for VAT since 1991 and had previously carried out more extensive farming activities whilst under the ownership of Mr McLaughlin and his wife.

Mr and Mrs McLaughlin owned land and other buildings on a farm, while Babylon Farm Ltd owned and had control over some outbuildings on the farm that were occupied by Mr and Mrs McLaughlin. The company produced hay and maintained the outbuildings.

Babylon Farm Ltd claimed £19,765 of input tax, the majority of which related to the construction of a new barn. No output tax was reported in this period and HMRC denied the claim, arguing that the scale of the business was not of a kind that could be argued to be a business venture

Babylon Farm Ltd claimed that its farming activity had been carried on uninterrupted since 1989 and that the haymaking was the remains of its original farm business. The company claimed that its activities had always been run on sound business principles and its activities as a whole were not negligible. During the relevant period, the company's only income, apart from an exempt property sale, was just over £400 per annum for selling hay to Mr McLaughlin for his livery business.

*Decision*

The First Tier Tribunal stated that the mere fact that Babylon Farm Ltd was registered for VAT did not constitute an acceptance by HMRC that a person was operating as a business. Whether or not company was carrying on business and making taxable supplies needed to be determined on the facts.

The Tribunal looked at the six factors from the case *CCE v Lord Fisher* to determine whether an activity constitutes a business, and considered was:

1. the activity a serious undertaking earnestly pursued?

2. there a certain measure of substance?

3. an occupation or function actively pursued with reasonable or recognisable continuity?

4. the activity conducted in a regular manner and using sound and recognised business principles?

5. the activity predominantly concerned with the making of taxable supplies for consideration?

6. the supply of a kind that, subject to differences of detail, commonly made by those who seek to profit from it?

The Tribunal concluded that Babylon Farm Ltd was hay making seriously, but with Mr McLaughlin doing the work, using the company's equipment and machinery. The customers of Mr McLaughlin's livery business were the end-users for the hay.

However, they concluded that it was a very modest activity carried out on a casual, non-commercial basis. The company's activities did not give rise to any staff or other costs. Mr McLaughlin fixed the price that he paid for the hay and decided what costs were borne by Babylon Farm Ltd. Mr McLaughlin appeared to carry out some or all of the activity himself without charge. The profitability of the company's hay making activities was entirely dependent on Mr McLaughlin's subjective judgement as to where costs and revenue should be allocated between his various activities. The Tribunal concluded that the company's activity was not predominantly concerned with making a profit as the business generated less than £500 per year, with no invoices raised until HMRC questioned the input VAT recovery

The First Tier Tribunal found that haymaking and the sale of buildings had not been conducted on a basis that followed sound and recognised business principles or on a basis that was predominantly concerned with the making of taxable supplies for consideration. As a consequence the company was not operating as a business during the relevant period.

The appeal was dismissed.

*Babylon Farm Ltd v HMRC (TC07356)*

## Supply to profit making parent (Lecture B1171 – 23.36 minutes)

*Summary - Applying the Halifax doctrine, the supply by a non-profit making company was redefined as a supply by its profit-making parent and so made taxable supplies.*

Snow Factor Limited operated a large leisure and adventure complex promoted as a family entertainment destination described as an "indoor snow sport resort" with two slopes and an ice wall. It includes a licensed café/bar.

Snow Factor Limited's Managing Director set up Snow Factor Training Limited, a company limited by guarantee, with no shareholders or staff, to provide training and tuition in relation to snow sports.

Having set up the new company, Snow Factor Limited's transferred its snow training and education business as a transfer as a going concern for £1. The company never registered for VAT as it was argued that it provided exempt supplies as it qualified as an "eligible body" for the purposes of Note 1 Group 6 Schedule 9 VATA 1994.

An agreement between the two companies provided that 100% of Snow Factor Training Limited's income would be paid to Snow Factor Limited, plus the costs incurred.

HMRC argue that the use of two companies whereby the tuition services were supplied by SFTL and all of the other supplies were made by SFL, amounted to an abusive tax avoidance arrangement liable to redefinition under the Halifax doctrine.

*Decision*

The First Tier Tribunal observed that very little changed following the creation of Snow Factor Training Limited. Customers were attracted to the Snow Resort by Snow Factor Limited's marketing. There was no mention that a separate company, Snow Factor Training Limited, provided the tuition services.

The Tribunal concluded that the set up between the companies was 'wholly artificial' and abusive and that any non tax savings were merely incidental compared to the VAT savings that applied. Indeed little evidence was put forward to support these non-tax benefits. The Tribunal concluded that the tuition supplies should be treated as if supplied by Snow Factor Limited. In any event, Snow Factor Training Limited did not qualify as an eligible body as the main aim of setting up the company was to enrich Snow Factor Limited.

They concluded that the commercial and economic reality was that at all material times Snow Factor Training Limited was part of a single integrated commercial organisation trading under the brand "Snow Factor". Nothing at all was at arm's length and it was not an eligible body.

The appeal was dismissed

*Snow Factor Limited and Snow Factor Training Limited v HMRC (TC07439)*

## Loan administration services (Lecture B1171 – 23.36 minutes)

*Summary - Loan administration services were not exempt financial services under Article 135(1)(d) PVD but should be treated as taxable supplies of debt collection.*

Target Group Limited provided outsourced loan administration services to banks and building societies including Shawbrook Bank Limited, a provider of a range of mortgages and loans.

On 21 May 2015, Target Group Limited wrote to HMRC requesting a non- statutory clearance of the proposed VAT treatment of supplies it made to Shawbrook Bank Limited, following changes to their supply agreement. Target Group Limited believed its supplies were composite supplies of payment processing and so were exempt. As an undisclosed

agent of Shawbrook Bank Limited, it established loan accounts, liaised with borrowers, dealt with their payments, and so on.

In July 2015, HMRC notified Target Group Limited of their decision that the supplies to Shawbrook Bank Limited were composite supplies of the management of loan accounts and were therefore taxable.

Target Group Limited appealed to the First Tier Tribunal where they lost their appeal with the Tribunal finding that the loan administration services supplied were standard rated as debt collection stating:

> "the essence of what is being acquired, and the main objective [of Target's supplies], is the collection of debts as they fall due ..." and the predominant nature of the services supplied by Target to Shawbrook is debt collection."

Target Group Limited appealed to the Upper Tribunal.

*Decision*

The Upper Tribunal upheld the First Tier Tribunal's decision.

Article 135(1)(d) PVD that requires Member States to exempt "transactions, including negotiation, concerning deposit and current accounts, payments, transfers, debts, cheques and other negotiable instruments, but excluding debt collection…"

Although the transactions were transfers concerning payments, Target Group Limited's role was to recover the interest and principal from borrowers. However, the actual payments were processed between the borrower's bank and Shawbrook Bank Limited. Target's supply was limited to passing on information to enable the transfer or debt collection. As debt collection is specifically excluded form exemption, their supply was taxable at the standard rate.

*Target Group Limited v HMRC [2019] UKUT 0340 (TCC)*

## B2B supply chain operators - '4 quick fixes' (Lecture B1171 – 23.36 minutes)

With effect from 1 January 2020, EU member states have agreed four changes to the Business To Business VAT rules on intra-community supplies'. These changes aim to simplify EU VAT compliance and will be in use provisionally until 1 July 2022, when a new definitive VAT system is planned.

*Call-off stock*

Call off stock refers to the situation where a supplier moves stock to a known customer's warehouse in another EU country but the supply only takes place when the customer removes or 'calls off' the goods from storage.

Under current EU rules, the supplier must:

- register for VAT in the country of destination, reporting the stock movement in both their domestic return and foreign return as a self-supply;

- record a domestic sale when the customer removes the goods and also report it on their foreign VAT return.

Some countries (including the UK) operate their own 'call off stock relief' and so do not require the suppler to register for VAT in the foreign country. Here, the customer accounts for VAT on the acquisition under normal rules.

Under the new rules, provided that the relevant conditions are met, VAT registration in the storage country will not be required. The supplier must record the stock movement in their EC Sales Listing and both parties must maintain a register of the goods.

If the goods are not 'called off' within 12 months of dispatch, the stock should be returned, or the transaction be recorded as an intra- community supply.

*Cross border chain transactions*

Cross border chain transactions are supply chains involving at least 3 parties, making it hard to identify when the zero-rated cross border supply step occurs. Under the new rules, where there are more than three parties involved, is will be important to identify the intermediary who is responsible for the transport of the goods.

From 1 January 2020, new rules will apply when the parties are located in three different EU countries, with the goods moving between the supplier and customer's countries only.

1. Intermediary provides a VAT number from another EU state:

- supplier zero-rates the sale - cross- border supply to the intermediary;
- intermediary
    - transports the goods from supplier's to the customer's country;
    - reports a domestic supply with the customer in their country.

  Triangulation would be available to the intermediary in this instance.

2. Intermediary presents a non-resident VAT number in supplier's country where the goods are dispatched:

- supplier charges VAT to the intermediary as a domestic transaction in their country;
- intermediary
    - transports the goods to the customer's country
    - reports a zero- rated cross-border supply to the customer.

*Proof of cross-border transportation*

B2B goods sold cross border within the EU are exempt from VAT provided that the supplier holds evidence that the goods left their country.

From 1 January 2020, the evidence required will depend on who is responsible for the movement of goods.

- supplier responsible: they must keep 2 pieces of evidence that the goods where transported;

- customer responsible: supplier must obtain written evidence of the transport from the customer, supported by two pieces of evidence as detailed above.

*Customer VAT number*

Despite what many believe, currently for zero rating to apply to Cross Border EU supplies, a customer does not have to provide a valid VAT number issued by another Member State. This was only a formal rather than substantive requirement.

However, from 1 January 2020 customers must provide a valid VAT number for zero rating to apply and these must appear on suppliers' invoices as well as their EC Sales list. Without this information, the supply will be subject to VAT in the EU state of dispatch. The new rules do not require the supplier to validate the customer's VAT number, although it would seem sensible to do so in order to avoid becoming involved in any VAT evasion.

*Avalara – 2020 Guide: EU VAT Four Quick Fixes*

## Building and annexe

*Summary – Although the new school hall qualified as an annexe, zero rating was denied as the hall was not designed solely for use for a relevant charitable purpose.*

The College in this case is a registered charity that operates a residential, selective, Islamic faith school near Kidderminster. Pupils pay £300 per month as boarders or £170 per month as day pupils. Admission of students is not based on their ability to pay; students who are unable to pay are not obliged to do so; where arrears of fees were unpaid for good reason, the College would usually forgive the debt and allow the student to continue. The running costs of the College exceed the payments received from pupils. The balance (40 – 50%) is met by donations from the wider faith community.

One wing of the College's existing buildings was demolished and a new hall erected. Planning permission was granted for, "Demolition of existing halls to rebuild new multi-functional examination & lecture hall with recreational facilities within and the erection of perimeter fencing." The planning permission restricted use to the educational activities of the College; use for general public worship, prayer or assembly was forbidden; events where family and guests were invited (graduation ceremonies, induction days and open days) were limited to ten per annum.

The new hall is a steel framed structure, roughly the same size an Olympic swimming pool. The Hall abuts the retained adjacent College buildings on one side; the separating wall has five fire doors that were added after consultation with the Fire Officer; the fire doors would normally be closed and can be opened only from the Hall side by push-bar mechanisms. The Hall has a dedicated entrance from the outside car parking area. The Hall is serviced by its own electrical supply and heating/ventilation system. Toilet and welfare facilities are located externally to the Hall, for cultural and religious reasons.

Under Group 5 sch 8 VATA 1994 Item 2 (a) services can be zero rated if the supply is in the course of the construction of a building, intended for use solely for ... a relevant charitable purpose but under Note 6, not if used in the course or furtherance of a business.

Those services must be related to the construction other than the services of an architect, surveyor or any person acting as a consultant or in a supervisory capacity.

Under Note 17, a new annexe will qualify if it can function independently from the existing building; and the only access or main access to the annexe is not via the existing building; and similarly, the existing building is not accessed via the annexe.

HMRC argued that:

(1) The Hall was not designed solely for use for a relevant charitable purpose; the College operated in the course or furtherance of a business for the purposes of VAT; and

(2) The works did not qualify as they constituted the conversion, reconstruction, alteration, enlargement or extension of an existing building; and

(3) Even if the works created an annexe, they did not meet the specific tests in Note 17.

Finally, even if the College were successful in its appeal, HMRC would be unable to repay any VAT incorrectly charged to the College; as a third party appealing the rate charged for services undertaken by a supplier, the College will be required to liaise with its contractor and, subject to time limits for VAT error corrections, may need to submit a s 80 claim to protect its position.

The two questions for the Tribunal needed to address were whether the Hall is:

1. used solely for a relevant charitable purpose;

2. a qualifying annexe within Note 17.

*Decision*

The First Tier Tribunal found that the fees charged by the College to students constituted consideration received for a supply of education services. The building works to the Hall did not qualify for zero-rating and the appeal was dismissed. The College was a “business” within note 6 group 5 sch 8 VATA, and so the relevant charitable purposes test was not met. The sole activity of the College was the provision of education to its fee-paying students and the fees charged were significant, both in respect of each student and in aggregate and make a significant contribution to the cost of providing the education of the students paying the fees. The fees charged were similar to other schools and were not calculated by reference to the cost of providing the education. Nor are they calculated by reference to the means of the students or their families.

Although now not relevant to this appeal, the Tribunal did go on to consider the second issue. They concluded that:

- Architecturally, there was little similarity between the demolished buildings and the Hall. The Hall was designed to function differently from both the demolished buildings and the retained buildings… as a dedicated single, large, open space for recreational use and for holding events such as graduation ceremonies.

- The building is a self-contained structure to the existing building, and with the exception of the fire doors, operates independently from the other buildings. It constitutes an annexe to the existing building.

The Tribunal stated that they considered that HMRC had placed incorrect emphasis on the existence of the fire doors in the wall between the hall and the existing buildings; these were a fire officer requirement but would not be used for access or except in emergency.

*Madinatul Uloom Al Islamiya v HMRC (TC07433)*

## Input tax on business entertaining (Lecture B1174 – 12.10 minutes)

*Basic rules*

The starting point with business entertainment is that input tax can only be reclaimed on the cost of hospitality provided to staff. Entertainment given to non-staff members, such as customers, suppliers or the spouses of staff, are blocked and the input tax can't be recovered. Input tax can be claimed on staff entertaining because it is deemed to be a reward for good work and to improve staff morale (VAT Notice 700/65, para 3.1).

*Example 1.*

Mike is the managing director of ABC Ltd. He has decided to have a big Christmas party at his local Chinese restaurant. The guest list will comprise 20 staff plus one guest each, plus some important suppliers and customers. The total party will comprise 50 people. The company can claim 40% of the VAT on the final bill as input tax – i.e. 20/50 based on the ratio of staff to total guests.

Note - a condition of reclaiming input tax on the staff meals is that the staff must not be acting as host to the guests. This is unlikely to be the case with a staff Christmas party where the aim is for everyone to have a good time to celebrate (hopefully) a good trading year but it might be the case where the primary function of an event is to increase goodwill and potential orders from customers.

Exclusions from the definition of an employee include pensioners (even if they are being paid a company pension as a retired employee) and former employees, as well as shareholders who are not also employees. It is all about people who are currently involved with the business. A self-employed person, such as a contractor, is not an employee for the purposes of business entertainment but there is no problem claiming input tax on subsistence expenses as long as the arrangements are the same as for employees e.g. working on the same project away from base.

*Charge to guests*

A token charge to guests can produce big VAT savings. This is because a charge to guests means that the input tax block on entertaining is no longer relevant because you are not providing "free" hospitality. The charge can be less than the cost of the food and drink provided to the guests i.e. the output tax declared on the charge is less than the input tax claimed on the costs of the event.

*Example 2.*

The cost of the Christmas party for ABC from Example 1 is £75 per head plus VAT. Mike has decided to charge the 30 guests a token amount of £6 each – with no charge to the 20 staff.

The company will account for output tax of £30 on the money collected from the guests i.e. £6 x 30 x 1/6. But it can then claim all input tax on the costs of the party - there is no apportionment needed for entertainment of non-employees. So, the token charge has produced a VAT saving of £14 per guest – i.e. input tax of £15 less output tax of £1.

Key point - the charge to the guests needs to be compulsory and properly collected in all cases.

Note - for VAT purposes, there is no monetary limit on the cost of hospitality provided to employees to enable input tax to be claimed. The restriction to £150 per head including VAT (this figure also includes the cost of the spouse/partner meals) only applies for income tax purposes.

*Business owners*

There can sometimes be a problem with claiming input tax on the cost of directors' meals (or sole trader and partner meals in the case of an unincorporated business). But there is no problem if an event is open to all staff. And there is no problem if the business owners are away from base on company business and incur subsistence expenses.

In the case of, say, a trip for a 'directors strategy meeting' including a weekend hotel and food, input tax would be blocked as well.

*Overseas customers*

There is a window of opportunity to claim input tax on the cost of entertaining overseas customers but only if the entertaining relates to a business meeting, and the hospitality is not deemed to be excessively lavish – the phrase used by HMRC in the notice below is 'reasonable in scale and character' e.g. sandwiches and soft drinks provided during a meeting. But this is not relevant to a Christmas party, which is clearly a social function. The term 'overseas customer' means any customer not ordinarily resident or carrying on a business in the UK or Isle of Man.

If the entertainment is excessively lavish, then a private use charge will apply i.e. output tax is payable on the cost of the meal/function, effectively cancelling any input tax claimed on the expenditure.

*VAT Notice 700/65, para 2.6.*

*Corporate boxes and golf days*

The cost of corporate boxes at e.g. sports functions, or the cost of golf days which involve a round of golf and food and drink afterwards, follows the same rules for business entertainment as the cost of the office Christmas party in the example above. So, if it is a staff event, it can be claimed as a 'team building' day but if it is for customers or non-employees (including staff acting as host) then input tax is blocked.

*Contributed by Neil Warren*

## Cosmetic or medical treatment? (Lecture B1175 – 11.53 minutes)

The aesthetics market in the UK is apparently worth nearly £4billion a year, so it is understandable that HMRC is interested in the VAT issues. It is therefore a good time to ensure that clients are getting things right and a recent First Tier Tribunal case that against the taxpayer has given some useful tips.

*The law*

In order to qualify for VAT exemption, a medical service or treatment supplied to a patient needs to go through three different hurdles:

1. It is carried out by a registered health professional;

2. It is carried out in the field for which the professional is registered; and

3. The treatment is linked to the protection, maintenance or restoration of the patient's health.

*VATA1994, Sch 9, Group 7, Items 1 and 2.*

*Example*

If I visit my dentist and have a filling in one of my teeth, this service Is exempt from VAT because good teeth are an important part of my health. But if he has a look at my eyes during the same visit, and charges me £50, this fee would be subject to VAT because he is only registered as a dentist and not an optician.

*Tribunal case won by taxpayer*

As a general principle, cosmetic operations and procedures are standard rated because they are not carried out in order to improve or maintains a patient's health. VAT Notice 701/57, para 4.4.

It has always been a bit of a grey area as to whether some medical supplies are carried out for medical purposes (exempt) or cosmetic reasons (standard rated), and the VAT liability of Botox and other injectable treatments was one of the two key issues considered in the case of Skin Rich Ltd (SRL) (TC7310). HMRC decided that the services were standard rated because "clients sought treatment principally for cosmetic reasons." The taxpayer argued for exemption on the basis that Botox is a "medical procedure" and treatments "enhance their self-confidence and influence their quality of life."

After a very detailed analysis, the court agreed with HMRC that the procedures were given for cosmetic reasons and were standard rated: "SRL has not satisfied us that the principal purpose of the injectable treatments is to protect, restore or maintain the health of the individual rather than for cosmetic reasons." (Author underlining).

In a historic case from 2009, Ultralase Medical Aesthetics Ltd (TC00142) claimed its services of providing facelifts, hair removal and anti-cellulite treatment were standard rated and therefore claimed input tax on its costs and accounted for output tax on its receipts. HMRC claimed that the services were exempt and disallowed the input tax, the company said its services were taxable as cosmetic treatments. The taxpayer's appeal was allowed.

*Registered health professionals*

How could nail fungal treatment not qualify as a medical service? The answer in the SRL case is because the treatments were not carried out by a registered health professional. Miss Cleaver (director and company shareholder) carried out the treatments using a laser process that attacked the fungus but she was not a registered medical professional, even though SRL had a medical liability insurance policy. The taxpayer accepted this but the alternative argument that the premises of SRL qualified for exemption as a "hospital or state-regulated institution" (Item 4, Sch 7, Group 9, VATA1994) was also rejected by the court.

*VAT returns*

The SRL problem was first identified because the turnover declared on the company's corporation tax return exceeded the sales recorded on VAT returns for the same period. The reason for this discrepancy was because the company had omitted all of the sales it considered to be exempt from Box 6 of its returns. This was incorrect – all supplies of goods or services need to be included in Box 6, including those that are exempt (VAT Notice 700/12, para 3.7).

*Conclusion*

It is recommended that medical businesses that claim VAT exemption for services that might be questioned by HMRC should keep very clear and thorough client files to illustrate the medical rather than cosmetic purposes and an analysis of why VAT has not been charged. Doctors are often reluctant to divulge the information in these files but the alternative is to probably play safe and charge 20% VAT in borderline cases. It is important to be clear that exemption only applies if the 'principal purpose' of a process is to protect, maintain or restore good health.

*Contributed by Neil Warren*