Tolley®CPD

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Personal tax

Car benefits (Lecture P1262 – 21.17 minutes)

One of the best known benefits in kind relates to the provision of a car for a director or employee by an employer. The relevant part of S114(1) ITEPA 2003 states:

> 'This Chapter applies to a car . . . in relation to a particular tax year if in that year the car:
>
> (a) is made available . . . to an employee or a member of the employee's family;
>
> (b) is so made available by reason of the employment; and
>
> (c) is available for the employee's or member's private use.'

The three requirements quoted in (a), (b) and (c) above can be classified, respectively, as Condition A, Condition B and Condition C.

The First Tier Tribunal decision in Tim Norton Motor Services Ltd v HMRC (2020) deals with an important aspect of this legislation. The appellant company (TNMS) runs a Ford dealership. TNMS buys and sells cars and does some repair work. Several years ago, the company bought two rare (and expensive) high performance cars: a Maserati and a Ford GT40.

Following a PAYE audit in 2016, HMRC concluded that these two cars had been made available to the company's main director (Mr Norton) for periods longer than those in respect of which a benefit in kind had been declared. They therefore raised income tax assessments on Mr Norton for the tax years 2012/13, 2013/14, 2014/15, 2015/16 and 2016/17 in respect of the Maserati and the Ford GT40.

The company's premises were situated in Oakham, Rutland. There would generally be 25 – 30 new cars on the premises and about the same number of used cars which were for sale. In addition, the Maserati and the Ford GT40 were kept there.

Mr Norton and his wife (who was also a director of TNMS) lived some 10 miles from the company's showroom and drove to work, but neither the Maserati nor the Ford GT40 was used for commuting. The keys for the two cars were kept in a locked box in a safe in Mr Norton's office.

Because the two cars were only driven relatively infrequently, they were subject to a SORN (Statutory Off Road Notification) which meant that they did not need to be taxed or insured. In fact, both cars were insured (presumably because of their value), but, if Mr Norton wanted to take one of them on the road, duty had to be paid before it could be used and Mr Norton would have to check that the vehicle had a current MOT.

The Ford GT40 had the words 'Tim Norton' painted on its bonnet. In his evidence, Mr Norton said that the Ford GT40 'acted as an attraction to the dealership, both when at the premises and when taken to various shows'. He added – perhaps unsurprisingly – that 'it was a crowd puller and led to conversations and sales'. Mr Norton did not make similar statements about the Maserati.

The three conditions mentioned in S114(1) ITEPA 2003 were referred to above. By virtue of S117(1) ITEPA 2003, a car which has been made available to an employee is treated as having been made available by reason of the employee's employment. There are two exceptions to this rule, but neither of them is relevant in the present case. As a result, if Condition A is satisfied, Condition B will also be satisfied. This was the case with Mr Norton.

We therefore need to examine Condition C. An extract from S118(1) ITEPA 2003 states:

> 'For the purposes of this Chapter a car . . . made available in a tax year to an employee . . . is to be treated as available for the employee's . . . private use unless in that year:
>
> (a) the terms on which it is made available prohibit such use; and
>
> (b) it is not so used.'

Consequently, if Condition A is satisfied (i.e. by reason of the car being made available), Condition C will also be satisfied unless the taxpayer can show that both the let-outs in S118(1) ITEPA 2003 are in point.

Ss121 – 142 ITEPA 2003 deal with the computation of the car's taxable benefit. In this case, there was no dispute about how the figures for Mr Norton arose.

We now turn to S143 ITEPA 2003. The key part of this section states that 'a deduction is to be made from the amount (in the computation) if the car has been unavailable on any day during the tax year in question'. Subsection (2) goes on to say:

> 'For the purposes of this section a car is unavailable on any day if the day:
>
> (a) falls before the first day on which the car is available to the employee;
>
> (b) falls after the last day on which the car is available to the employee; or
>
> (c) falls within a period of 30 days or more throughout which the car is not available to the employee.'

The final subsection provides for a reduction in the taxable benefit on a pro rata basis by reference to the number of unavailable days. In other words, even though the legislation applies for a tax year, there is an appropriate switching on and off procedure where the car is not available for the whole of the year.

In addition to the fact that the two cars were subject to a SORN for much of the year, there was another constraint on their use. TNMS's staff handbook contained the following paragraph:

> 'It may be necessary to use a company vehicle in the course of your duties with the company. You may not use a company vehicle without the expression permission of management. At all times, all employees and officers of the company must ensure that any vehicle used is taxed unless covered for use by trade plates, has adequate insurance cover and (has) a valid MOT, if appropriate.'

In his evidence before the First-Tier Tribunal, Mr Norton confirmed that he regarded these restrictions as imposing clear obligations on officers and employees of TNMS in relation to both the business and the private use of a company car.

The company's barrister argued that cars were not 'available' when subject to a SORN declaration, given that their use would be illegal. During the times when the cars were under a SORN, driving them on the roads (other than with trade plates or to an MOT test) would be a criminal offence. It was wrong, he said, to equate potential availability – the potential to pay duty so as to make the car's use legal – with actual availability. One of the cases which he used in support of this contention was Golding v HMRC (2011) – this was won by the taxpayer before the First-Tier Tribunal, but HMRC have gone on record as saying that, although they did not appeal the finding, they considered that it 'does not set any precedent of any kind' (see 'Taxation', 22 September 2011).

Judge Charles Hellier dismissed the barrister's arguments. On the subject of the SORN, he asserted that the declaration did not prevent a car being available to an employee, in view of the fact that it could easily be remedied. As far as the need for management permission was concerned, he felt that this requirement did not represent an 'effective constraint' for Mr Norton, given that he was the owner of the business and that his wife, as a fellow director, would almost certainly acquiesce in his decisions to use the Maserati or the Ford GT40. He therefore decided that Condition C was satisfied and the benefit in kind charges were correct. As a result, Mr Norton derived no benefit from the reductions in S143 ITEPA 2003.

An intriguing side-issue was that this conclusion appeared to mean that, as well as the Maserati and the Ford GT40, the 40 – 50 cars in the TNMS forecourt would be equally available to Mr Norton and that he should be charged a benefit in kind tax on all of them! As a director of the company, Mr Norton certainly had the authority to make all of them available for his use. However, the judge said that 'such a charge would not arise unless in fact Mr Norton did use the cars for private use'.

Is there not some inconsistency here? Mr Norton did not make use of the Maserati and the Ford GT40 other than occasionally, but the judge confirmed that a benefit charge still arose in respect of them on the ground of availability.

In the end, the words in S114(1)(c) ITEPA 2003 state that the car 'is' available for the employee's private use. The test is not that 'the car, despite being unavailable, could easily be made available'.

Hopefully, the taxpayer may be allowed to take this case further.

Contributed by Robert Jamieson

Employment expenses lack evidence **(Lecture P1261 – 25.47 minutes)**

Summary –Employment related expenses were disallowed due to inadequate mileage records and lack of evidence to support other expenses claimed.

Derek Storey, trading as an employed scaffolder, submitted his Self Assessment tax returns for the years 2014/15, 2015/16 and 2016/17, claiming deductions against his employment income, totalling close to £32,000. The deductions related to mileage, subsistence, tools and related costs, and accountancy fees.

On 20 June 2018, HMRC opened enquiries into each of the three returns, with the taxpayer and his agent being asked to provide evidence of the expenses incurred and how they qualified as allowable expenses.

A month later, having received no response, HMRC sent a letter stating their intention to disallow the claim for employment expenses and add employment benefits which were not included in the 2015/16 tax return.

Derek Storey's agent responded on 8 August 2018, stating that their client drove a car for his employment. The response included a schedule of mileage and a schedule of expensed items for all years. Two weeks later, HMRC asked for more detail and supporting evidence. The agent stated that Derek Storey could not give any further information and that mileage was kept to the best of his memory. The Agent further explained that a van was also used in the period when mileage was claimed.

HMRC issued closure notices, making the following amendments:

- Car and fuel benefit were added to the 2015/16 return, as reported on the P11D;
- Mileage calculated using HMRC's Approved Mileage Allowance Payment rates were disallowed as there was insufficient evidence to support the figures claimed;
- The subsistence claims of £1,875 per annum were denied as no allowable travel had been established;
- A flat rate allowance of £140 per year in respect of tools was disallowed, as no receipts were provided;
- Accountancy fees were disallowed as they were not incurred in the performance of Derek Storey's duties.

Decision

The First Tier Tribunal agreed with HMRC's decision.

Evidence for the mileage claim was lacking. Derek Storey had use of a company vehicle so why was he claiming mileage for using his own car? Even if he was using his own car, Derek Storey's mileage 'log' recorded monthly totals, and not individual journeys and dates.

The First Tier Tribunal dismissed the appeal, disallowing every expense.

The penalty for carelessness was suspended, subject to the remaining tax liability being settled promptly. HMRC had not published detailed guidance on how to keep records and the types of supporting evidence that should submitted. Consequently, it would not have been acceptable to say that Derek Storey was careless as he may not have known the level of record-keeping expected.

In Taxation (3 June 20201) Andrew Hubbard commented:

> 'This is an odd case. In the first place, the taxpayer is described as having the trade of an employed scaffolder, which seems to be a contradiction in terms. Second, the tribunal suspended the penalty "subject to the condition that the remaining tax liability is settled forthwith". It is difficult to see how this can be reconciled with the requirement in FA 2007, Sch 24 para 14 that "HMRC may suspend all or part of a penalty only if compliance with a condition of suspension would help [a person] to avoid becoming liable to further penalties under para 1 for careless inaccuracy". It is not clear to me that payment of tax has any relevance to the prevention of any future careless inaccuracies.
>
> 'Finally, there are the strange comments about the urgent need for HMRC to publish "detailed guidance to assist and cater for employees who find themselves facing a lacuna of having submit to expenses by way of self-assessment returns where there has been no consideration of the same by their employer etc. in calculating an employee's tax liability". I do not really follow what that means. HMRC does publish guidance and, in any event, there was no evidence that the taxpayer's significant overclaims of expenses — he claimed for nearly double the total milage his vehicle actually travelled — had anything to do with his inability to find any HMRC guidance.'

Derek Storey v HMRC (TC8090)

£40 million was taxable income (Lecture P1261 – 25.47 minutes)

Summary – Payments totalling some £40 million were taxable income in the hands of the lawyer that received them. Furthermore, as the beneficial owner of stolen family jewellery, a capital loss of £1.6m was allowed.

Stephen Mullens, a lawyer, was for many years involved in the business affairs of Bernie Ecclestone and those of the Ecclestone family.

Between 1999 and 2013, he received some £40 million that he argued were not taxable income:

1. £2.25m was paid to induce him to resign from his then-partnership in a law firm and so enable him to provide his services uniquely to Formula 1;

2. Three payments totalling £36m were gifts made by or at the direction of Mrs Slavica Ecclestone by reason of a "personal relationship of friendship and affection" and nothing to do with any business relationship;

3. A payment of £187,000 was made by Mrs Ecclestone to cover a family holiday to Mauritius

HMRC argued that the sums were taxable.

Stephen Mullens appealed to the First Tier Tribunal.

Decision

The First Tier Tribunal found that the £2.25 million 'inducement' was received as consideration for future services and was held to be trading income.

The Tribunal questioned why would Mrs Ecclestone would have made three payments totalling £36 million to Stephen Mullens? The written submission explained:

> "Born in Croatia, Mrs Ecclestone became a woman of vast wealth with the habit, quite common among people of her class and type, of making what, to most, would seem to be huge payments for no particular reason, rather as a rich aunt might give big presents to her nieces, nephews and close friends."

The First Tier Tribunal disagreed, finding that these arose from the business relationship between the parties and were in fact success fees relating to deals as well as dispute settlement work undertaken. Consequently, they were taxable income.

The Tribunal did accept that the £187,000 for a holiday was a genuine gift and was not taxable.

On another matter, Stephen Mullens accepted he had brought diamonds worth £2 million into the UK without declaring them or paying the relevant taxes due. The First Tier Tribunal accepted HMRC's argument that the assessment was not out of time due the fraudulent conduct admitted to by Stephen Mullens in the Contractual Disclosure Facility that he entered into.

Finally, Stephen Mullens had claimed a £1.6 million capital loss on jewellery that had been stolen from his home. HMRC had disallowed the claim, arguing that the jewellery was his wife's property, and was described as such in the police report. The Tribunal found that Stephen Mullens had bought the jewellery, it was a matrimonial asset and that he was the beneficial owner. Ownership of family assets is often unclear and relying on police statements made immediately after a crime was not appropriate.

Mr Stephen J Mullens v HMRC (TC08112)

High Income Child Benefit Charge and reasonable excuse

Summary – The taxpayer was held to have a reasonable excuse for failing to notify and pay a High Income Child Benefit Charge for six years and the penalties were cancelled.

As an employee, Austin Hurley had always paid tax through the PAYE system. He had never been registered as liable to file a Self Assessment return and believed his tax affairs were up to date.

He was surprised when, in 2019, HMRC wrote to him telling him he was liable to the high income child benefit charge (HICBC) for the years 2012/13 to 2017/18 and raised assessments and imposed penalties.

Having appointed an agent, he accepted the HICBCs but appealed the penalties, arguing that he had a reasonable excuse:

- His children were born before the introduction of the HICBC, so neither he nor his wife became aware of the charge through completion of a claim for Child Benefit.

- He stated that he never received the letter SA252 which HMRC's records indicated was sent in August 2013 but, had he done so he would have acted on it and he would have retained it as he retained every communication with HMRC concerning his coding.

- He stated that HMRC had had access to the information concerning his tax and his wife's claim for child benefit for six years so why had it taken until 2019 to commence communications.

Decision

The First Tier Tribunal stated that:

> "The HICBC is a novel form of tax. It is not income tax. Its operation can involve a charge to tax or a disclaimer of a benefit. The optionality is unusual and these features have resulted in misleading headlines and articles in the press …. even if the Appellant had chanced upon one of them."

The Tribunal concluded that Auston Turley did have a reasonable excuse. He was a PAYE taxpayer with no history of filing self-assessment returns and no way of identifying a liability to file a self-assessment return following the introduction of HICBC.

His children were born before the HICBC and so he and his spouse did not receive the information offered to new claimants of Child Benefit after the introduction of HICBC. He had kept meticulous records of his notifications of coding which he provided to an agent. His records did not include the SA252, which he never received. He could not reasonably have become aware of the obligation to file a return.

The First Tier Tribunal acknowledged that Austin Turley had cooperated fully and quickly as soon as he became aware of the HICBC and his appeal was allowed.

Austin Eric Turley v HMRC (TC08104)

Peer-to-peer lending – tax issues (Lecture P1263 – 9.52 minutes)

Introduction

People with a bit of spare cash have had a tricky time in recent years knowing where to put it in order to achieve some sort of noticeable return. With interest rates being as low as they are, letting savings relax contentedly in a building society account is probably costing money since rates of inflation are above the derisory rates which are on offer.

So it's hardly surprising that we have seen the rise in popularity of "peer-to-peer" lending which offers investors headline-grabbing returns.

But things are rarely as rosy as they seem. A peer-to-peer ("P2P") investment is not like putting your money into a building society. A more fitting analogy is that you are lending money to a guy in a pub who you've never met. In fact, your pub is the Rose & Crown while your borrower frequents the Red Lion and the only thing you have in common is that he wishes to borrow some money and you have some money sitting in a savings account earning pennies.

The borrower and the lender are duly introduced by a P2P lending platform (such as Funding Circle, Zopa and numerous others) and a deal is agreed.

The P2P platform therefore acts as a financial dating site or online money matchmaker putting together individuals or companies with borrowing requirements with investors looking for a reasonable return. The P2P platform takes a fee. The borrower gets a better deal that he would by approaching a bank. The lender can charge an interest rate of considerably more than is being currently achieved from his savings account. Unless you are the banking middleman who has been made redundant in this arrangement, it's a win-win.

The pub analogy is, of course, both flippant and inaccurate as the transaction is one of providing financial services and is therefore regulated by the Financial Conduct Authority (FCA). So it's not the Wild West. And once the investor has deposited his funds, the P2P platforms will select borrowers using investor-provided criteria, will carry out the required risk analyses and credit checks, will obtain security and complete all legal formalities.

The P2P platform may also spread the investor risk by lending the invested funds by way of a number of small sub loans (usually £25,000 or less) to a number of different borrowers (so each borrower will typically borrow a small amount from many different lenders to make up the full loan they need). This "eggs and baskets" approach spreads the risk and softens the blow in the event of default or non-recovery.

The FCA also protects investors by restricting their investment in P2P products to no more than 10% of their investable assets. [Albeit this is self-certified so not exactly watertight.]

That said, P2P lending is investment rather than saving. The contract for the debt is between borrower and lender (not lender and P2P platform) and while P2P has worked well for many investors, there always remains the possibility of the investment not being repaid if individuals or companies don't pay back their loans.

There is no "safety-net" in the form of a savings safety guarantee and the Financial Services Compensation Scheme (which protects the first £85,000 of savings per financial institution if that institution fails) does not apply to P2P lending. The investor could therefore lose every penny of his investment if the loans go bad. Caveat emptor.

On the plus side, if the P2P platform itself went bust, the loan remains in place and can still be enforced.

On balance, P2P lending is relatively safe (especially when investments are spread), provides relatively good liquidity and offers relatively good interest rates. It's an investment opportunity for risk-averse people who are wary of investing.

The tax side

Once a P2P investment has been made, the online platform will try and find a match. No interest will be paid by the P2P platform while the invested funds remain unmatched.

Once the matches are in place, the P2P platform will collect the repayments of interest and capital from each borrower and pass them to the lenders (after deducting a facilitator's fee). Interest will therefore flow from the borrower, via the P2P platform, out to the lender. Since 2017, the interest is paid without deduction of tax at source by the P2P platform. This is savings income and, like all savings income, is taxable at the point of receipt.

The taxable amount is the amount paid to the investor by the P2P platform and is therefore net of any fees which the platform deducts. The investor will typically receive a statement showing the interest and the fee deducted and should enter the amount received on his self-assessment return. Any repayments of the principal investment are not taxable or disclosable.

The savings allowance (£1,000 for basic rate taxpayers, £500 for higher rate taxpayers) will apply to P2P income as will be £5,000 starting rate band (if applicable).

There are "Innovative Finance ISAs" on the market which allows P2P loans to be held within an ISA wrapper. Interest from P2P loans can therefore be converted into tax free income (the usual £20,000 per tax year ISA cap will apply). "Contact your IFA for further information".

Irrecoverable loans

The COVID crisis has impacted on the P2P lending sector. As borrowers find it increasingly difficult to make the required loan repayments to the platform, many investors are having trouble accessing their cash. These are not normal times.

The P2P platforms will normally provide an option (via a secondary market) whereby an investor can sell his loan to a fellow investor. The sales price will depend on the probability of full recovery and the interest rate attaching to that loan.

However, this is only an option if there are fellow investors who want to take another debt on board and that is a big "if" in the current climate.

The P2P platform will do all it can to recover the full debt, but if a loan becomes wholly or partly irrecoverable, the investor will lose money.

Tax relief on irrecoverable loans

As a debt is not a chargeable asset for CGT, there is no question of taxpayers being able to treat the irrecoverable loan as a loss on a capital asset which is available for relief against capital gains.

There are provisions in the CGT legislation (S.253 TCGA 1992) for a loan to a trader which has become irrecoverable to be treated as a capital loss for CGT, but this requires the defaulting borrower to have used the money for trading purposes which isn't always the case.

Thankfully income tax relief is available for P2P loans which have become wholly or partly irrecoverable. The relief has applied since 6 April 2015, but COVID is now shining a light on its usefulness.

If a P2P loan is not repaid (or not fully repaid), the lender can set the loss suffered on the loan against the interest they receive on other P2P loans in the same tax year. This relief is automatic and does not ned to be formally claimed. The lender will then be taxed on the interest received less the bad debt relief.

Conditions for bad debt relief

Relief for bad debts on P2P loans can only be set against interest on other P2P loans. It cannot be used against “general” interest or against any other form of income. It cannot be transferred (for example, to a spouse).

Bad debt relief is given against interest from the same P2P platform in priority to income from a different platform. But this is procedural, and it all comes out in the wash.

If the bad debt exceeds the P2P interest for the tax year, the excess is carried forward against future P2P income. There is no carry back option.

Carry forward relief is only available against interest received from loans made through P2P platforms in the 4 years following the tax year in which the debt became irrecoverable. Therefore, if carried forward, relief for the outstanding amount of the irrecoverable loan must be used against P2P interest received in the earliest year first, up to a maximum of 4 years. This means that for an irrecoverable loan in 2016/17, any unused relief will have lapsed on 6 April 2021.

The bad debt must have arisen from a loan made via a P2P lending platform that is authorised by the FCA. This includes platform operators based elsewhere in the EEA who have been granted equivalent permissions under the law of that jurisdiction.

Relief is only available if:

1) The lender is subject to UK Income Tax on their P2P income;

2) The loan is made on commercial terms, at market rates and conditions and on an arm’s length basis; and

3) The loan is not part of a scheme or arrangement to obtain a tax advantage.

Condition 1) will still be met if the lender has no tax to pay, for instance because the amount of interest paid is covered by the lender’s personal allowance or falls within the 0% starting rate band or is taxed at 0% under the savings allowance. This condition will not however be met if the loan is held within an ISA (as the lender would not then be subject to income tax on the income).

If the loss arises in the hands of a company, relief for the loss should be available under the loan relationships rules.

Relief can be claimed at the point at which there is no reasonable prospect of the P2P loan being repaid. Whether a loan has become irrecoverable should be judged on a case-by-case basis. As the loan will be managed by a P2P platform, the platform would usually be in a position to determine when a loan has become irrecoverable (as they have a relationship with the borrower). The platform would then inform the lender that the loan had become irrecoverable.

Loans that a lender has acquired by way of assignment (for example by purchase from another investor via the P2P platform) are treated in the same way as loans that are made as an original lender and are therefore eligible for bad debt relief.

The amount of relief available is the P2P loan still outstanding from the borrower at the time it became irrecoverable (being the loan less capital repayments already received).

If a lender has received relief for a bad debt on a P2P loan that is repaid at a later date (for example if the borrower manages to pay late, or if there is some recovery of assets by the P2P platform), the amount recovered is treated as P2P income of the lender in the year of receipt. In essence, amounts recovered once bad debt relief has been claimed will come back into the income tax computation as taxable income.

Where an irrecoverable P2P loan would have been eligible for CGT as a capital loss under the S.253 TCGA 1992 "loans to traders" rules, it will no longer be eligible for that relief (because S.2(3) TCGA 1992 specifically gives priority to income tax reliefs).

Compliance procedures

P2P interest should be entered on the "Additional Information" pages (form SA101) as "Other UK income, Interest from gilt-edged and other UK securities, deeply discounted securities and accrued income profits". The interest will be "Box 3" income.

The P2P interest figure to be reported is interest received less any bad debt relief from all platforms. There is therefore no separate box for the bad debt relief as the relief is automatic and simply reduces the taxable amount.

Any excess relief for P2P bad debts available to carry forward does not need to be included on the tax return, but the lender should keep records of any carry forward relief in order to make a correct and complete claim in a tax return for a future period.

Lenders who do not submit a tax return can simply report their P2P income separately for the tax year by contacting their local tax office and providing the annual tax statement from the P2P lending platform. The reportable figure is the interest less any bad debts suffered via the same platform.

Any claims to set relief for P2P bad debts from one platform against P2P interest received through another platform, or to carry relief forward against P2P interest received in future years, must be made through a tax return.

Contributed by Steve Sanders

Pensions: In specie contributions (Lecture B1263 – 8.45 minutes)

Tax relief for pension contributions

The legislation on tax relief for registered pension schemes (FA 2004, Pt 4, Ch 4) states (at FA 2004, s 188(1)):

'188 Relief for contributions

> (1) An individual who is an active member of a registered pension scheme is entitled to relief under this section in respect of relievable pension contributions paid during a tax year if the individual is a relevant UK individual for that year.'

HMRC considers that 'paid' in this context generally means that contributions to the registered pension scheme must be a monetary amount, such as cash, cheque, direct debit, or bank transfer.

In specie contributions

However, HMRC's guidance in its Pensions Tax manual (at PTM042100) broadly states that in certain circumstances it is possible for pension contribution involving an asset to retain its monetary form for tax purposes. Unfortunately, HMRC's guidance on this point in PTM042100 has been the cause of some confusion and dispute with HMRC.

In Revenue and Customs v Sippchoice Ltd [2020] UKUT 149 (TCC), a pension scheme administrator company claimed income tax relief at source in respect of a net contribution of £68,324 made by an individual (C) to a self-invested pension plan (SIPP) in March 2016. HMRC refused the claim. The point in dispute was whether the contributions made by C to the SIPP were 'paid' (within FA 2004, s 188(1)) and therefore qualified for tax relief.

The Upper Tribunal (UT) accepted that, when viewed in isolation, 'paid' was broad enough to encompass non-monetary payments. However, the UT concluded that the expression 'contributions paid' in FA 2004, 188(1) was restricted to contributions of money. As 'contributions paid' in section 188(1) meant 'paid in money', it couldn't include settlement by a transfer of non-monetary assets, even if the transfer was made in satisfaction of an earlier obligation to contribute the money. Tax relief was therefore denied.

HMRC: "We told you so! "

In HMRC's Pension Schemes Newsletter 126 (December 2020), HMRC stated that it was 'clarifying' its 'long-standing approach' on in specie pension contributions following Sippchoice. HMRC acknowledged that its guidance in PTM042100 had 'created some uncertainty', and stated:

'In light of the UT's comments, we've clarified the "Giving effect to cash contributions" guidance at PTM042100 to try to help customers better understand HMRC's long-standing approach to pension contributions made pursuant to a contractual offset agreement. This is a clarification and HMRC's position remains unchanged.'

HMRC's amended guidance at PTM042100 affirms that contributions to a registered pension scheme by a member or an employer must be a monetary amount, and that where an asset is transferred to a registered pension scheme in satisfaction of an earlier obligation to contribute money, the resulting contribution is not a monetary amount and therefore the requirements for tax relief are not met.

However, where a contribution obligation exists and the pension scheme has separately agreed to purchase an asset from the scheme member (or employer) for consideration, the parties may enter into a contractual offset agreement in relation to the payment of the contribution and the asset sale consideration. HMRC acknowledges that 'in certain circumstances' it is possible for a contribution effected in this way to retain its monetary form for tax relief purposes.

HMRC’s current guidance states:

‘For a contribution to retain its monetary form, there must be:

- a clear obligation on the contributing party to pay a contribution of a specified monetary sum, say, £10,000. This needs to create a recoverable debt obligation;

- a separate agreement between the scheme trustees and the contributing party to sell an asset to the scheme for market value consideration, and

- a separate agreement whereby the scheme trustees and the contributing party agree that the cash contribution debt may be offset against the consideration payable for the asset.’

Where are we now?

Whether HMRC’s amended guidance at PTM042100 is clarification or possibly just setting more onerous requirements, Sippchoice has at least resulted in more specific instructions on how pension contributions and arrangements involving assets can be undertaken in a way capable of obtaining tax relief.

Contributed by Mark McLaughlin

Capital tax

No entrepreneurs' relief for partnership (Lecture P1261 – 25.47 minutes)

Summary – Preparing to carry on an activity was held not to be trading and so gains on partnership assets sold during this time were ineligible for Entrepreneurs' Relief.

John Wardle was one of three partners who, in January 2014, established a partnership to develop, construct and operate renewable power plants at three locations in the UK.

On 1 May 2014, the Partnership commenced pre-trading activities. In 2015, prior to commencing trading and once the projects had reached the stage where construction could begin, it sold two plants to a third party.

John Wardle declared his share of the gains in his 2015/16 tax return and claimed entrepreneurs' relief.

HMRC refused the claim, arguing that under s.169S TCGA 1992, the partnership needed to be 'a business' and 'a business' <u>is</u> a trade, profession or vocation, and <u>is</u> conducted on a commercial basis and with a view to the realisation of profits.

John Wardle appealed arguing that a partnership's business disposed of during the pre-trading period came within the definition of 'a business' under s 169S(1). He argued that the legislation explicitly stated that a disposal of shares could qualify for relief where the company was conducting pre-trading activities. He argued that the legislation should be interpreted to allow the same treatment to partnerships.

Decision

The First Tier Tribunal preferred a straightforward reading of the definition in the legislation, concluding that the legislation was written in the present tense. The Tribunal found that 'is a trade' and 'is conducted on a commercial basis' suggested that the trading activity should already have started, and that preparing to carry on an activity was not the same.

The Tribunal pointed out that parliament 'had the tools available to make commencement of trading a pre-condition … but chose not to do so'. There was therefore no reason to adopt an interpretation to ensure the same treatment for partnerships

Wanting to keep details of the disposals out of the public domain, John Wardle requested that the decision remain anonymous. Although he lost this request on appeal, the details are not included in the case summary, on the grounds that he might appeal the case. It seems he may well have achieved his goal anyway.

John Douglas Wardle v HMRC (TC08105)

Guarantee rights (Lecture P1261 – 25.47 minutes)

Summary – The disposal of the beneficial interest in guarantee rights in a company resulted in a gain for the taxpayer but that gain did not qualify for entrepreneurs' relief as no ordinary shares had been sold.

Incorporated before changes in company law, Monarch Assurance Holdings Ltd was limited by both share capital or guarantee (or distribution) rights with the company's articles of association providing for two classes of member in the company: shareholder members and investor members. The rights carried the voting rights, rights to surplus assets after repayment of share capital, and a right to share in profits. Further, the shares could be transferred but there was no provision for the transfer of distribution rights.

In July 2008 John Tenconi became a director of the company and, in June 2009, became an investor member, acquiring four "distribution rights" for £100 each.

In 2015, another company, Soogen Holdings Limited wished to purchase the shares of a subsidiary of Monarch Assurance Holdings Ltd. At the time, Monarch Assurance Holdings Ltd had issued eight distribution rights such that John Tenconi held 50% of those rights and so also 50% of the voting rights in Monarch Assurance Holdings Ltd. It was accepted that the approval of the investor members would be required for the shares of the subsidiary to be sold, so Soogen Holdings Limited either needed to acquire such approval from a majority of the existing investor members or alternatively acquire distributions rights to enable it to provide such approval.

John Tenconi assigned a beneficial interest in his rights to Soogen Holdings Limited, in exchange for cash. Following completion he held the rights as nominee and trustee for Soogen Holdings Limited and would exercise the voting and other rights on their behalf. He also undertook to account to Soogen Holdings Limited for dividends or other receipts. Of particular importance to the deal, John Tenconi agreed to vote in favour of Soogen Holdings Limited's acquisition of the subsidiary.

John Tenconi initially claimed entrepreneurs' relief in respect of his disposal of the distribution rights but HMRC refused the claim. He then argued that there was no disposal or, alternatively, no capital sums were received which derived from assets so any sums received were not taxable.

Decision

The First Tier Tribunal found that the rights were an asset. John Tenconi had made a disposal to Soogen Holdings Limited of his beneficial interest in the rights (s21 TCGA 1992) and a chargeable gain arose as calculated by John Tenconi in his tax return.

The Tribunal found that the distribution rights were not shares and did not form part of the issued share capital of Monarch Assurance Holdings Ltd. The articles of association specifically stated that investor members were not required to contribute to the company's capital. The Tribunal stated that if it had been intended that entrepreneurs' relief should include gains relating to guarantee rights, the legislation would have stated this.

The appeal was dismissed and the closure notice upheld in full.

Although not required, the First Tier Tribunal stated that if there had been no actual disposal, there would have been a deemed disposal under s22 TCGA 1992 as exercising rights, including voting rights, as instructed by a third party would be the use or exploitation of those rights by the owner.

Mr John Tenconi v HMRC (TC08088)

Refurbishment costs (Lecture P1261 – 25.47 minutes)

Summary – HMRC restricted the deduction for refurbishment costs on the sale of a property and, due to lack of supporting evidence, this was restricted further on appeal.

In 2003, Babatunde Iginla owned a residential property on Fulham Palace Road, which he sold in 2015. His 2015/16 tax return included a chargeable gain, having allowed nearly £100,000 that had been paid for refurbishing the Property.

When asked for evidence to support the refurbishment costs, his accountants supplied an undated invoice on the contractor's letter headed paper. The payment was made in Nigeria by the taxpayer's father who was now deceased as this 'was the only place at that point in time where additional finance could be sourced because the mortgagor could not extend any further loan for such enhancement. Additionally, the contractor was willing to accept payment in Nigeria at a pre-agreed exchange rate." No bank statement was supplied supporting the payment as the accountant stated that "a bank statement is a confidential document which belongs to the account holder and in this instance [the Appellant] was not privy." The accountant went on to say that no payment had yet been made to his father's Estate as "the administrators were resolving many post-testamentary issues"

HMRC reduced the refurbishment deduction to £23,500 and issued a closure notice to reflect this new figure, as well as a number of matters/ corrections that had been made.

Babatunde Iginla accepted these other amendments as correct but appealed the refurbishment costs that had been disallowed.

Decision

The First Tier Tribunal found Babatunde Iginla to be a "less than straightforward witness" and concluded that HMRC were within their rights to request more evidence.

Having worked through the refurbishment costs on a line-by-line basis, the Tribunal allowed only £11,263 of costs, just about half of what HMRC had allowed. Babatunde Iginla's CGT liability was increased accordingly.

Babatunde Iginla v HMRC (TC08081)

Gifts and gift relief: Some pitfalls (Lecture B1264 – 11.44 minutes)

Gift relief: Background

Where an individual makes a gift of chargeable assets (e.g. land and buildings or shares), they are generally treated as having received disposal proceeds equal to the market value of the asset for capital gains tax (CGT) purposes (TCGA 1992, ss 17, 18).

However, the effect of relief for gifts of business assets in TCGA 1992, s 165 (where the relief conditions are satisfied and a claim is made) is broadly to hold over all or part of the CGT liability that would otherwise arise on the gift of a chargeable asset, normally until a later disposal by the recipient of the gift.

Foreign-controlled companies

Gift relief is subject to various restrictions and anti-avoidance provisions, one of which was amended by legislation published in Finance Act 2021. This amendment concerns gifts to foreign-controlled companies (TCGA 1992, s 167).

Prior to the above amendment, the legislation provided that gift relief was not available (subject to an exception for gifts of direct or indirect interests in UK land to non-residents) if the transferee was a company '…controlled by a person who, or by persons each of whom—

a) is not resident in the United Kingdom, and

b) is connected with the person making the disposal.'

In Reeves v HMRC [2018] UKUT 293 (TCC), the Upper Tribunal concluded that attributions of interests in this context are limited to connected persons who 'control' the recipient company, essentially by being able to exercise direct or indirect control over the company's affairs, and/or by possession or entitlement to acquire the greater part of the share capital, voting power or assets and distributions on winding up. The existence of non-resident relatives who were otherwise not involved in the company was held not to preclude the availability of the relief.

The effect of the amendment is that gift relief is denied if the company is controlled by the same individual who made the disposal. Consequently, for disposals from 6 April 2021, a non-UK resident individual with a UK trade would be unable to incorporate by transferring the trade to a wholly-owned UK company and claiming gift holdover relief on a gain arising from the disposal of the goodwill. This measure effectively blocks gift relief in similar circumstances to the Reeves case.

The A/B reduction

In certain instances involving gifts of shares, a held over gain may be reduced or completely eliminated. This can arise if the company's assets include chargeable non-business assets.

If the donor of the shares was able to exercise at least 25% of the company's voting rights in the 12 months prior to the disposal, or if the donor is an individual and the gifted shares were in a company which was the individual's personal company within that 12-month period, the held over gain is reduced by the fraction A/B, where:

- A = market value of the company's chargeable business assets at the time of the share disposal; and

- B = market value of all chargeable assets of the company (TCGA 1992, Sch 7, para 7).

Example: Business and investment assets

Adam gave his 100% shareholding in Widgets Ltd to his adult daughter, Brenda. The shares were acquired for £100 and are now worth £1 million.

At the date of disposal, the market value of Widgets Ltd's assets are:

Trading premises - £600,000;

Quoted share investments - £200,000; and

Cash - £200,000.

Applying the formula A/B, Adam's held over gain (ignoring the £100 base cost of the shares, and the cash as it is not chargeable to CGT) is:

£1 million x £600,000/£800,000 = £750,000

Adam therefore has a chargeable gain of £250,000.

A further problem arises if (say) the company's business commenced after the introduction of the intangible fixed assets provisions from 1 April 2002. Suppose that in the above example, Adam's company was a consultancy business set up in 2010, and instead of the company owning business premises of £600,000, it had goodwill with a market value of £600,000.

Applying the formula A/B, the held over gain reduction becomes:

£1 million x £0/£200,000 = £1 million

This position might be prevented if the company sold its chargeable investment assets for cash some time prior to the gift of shares, such that the company would have had no chargeable assets at the date of the share disposal. Hence, holdover relief would not be subject to restriction.

Gifts and interest relief

Individuals can claim income tax relief in respect of interest paid on commercial loans borrowed for various purposes. One such purpose is to buy shares in a close company, where certain conditions are satisfied (ITA 2007, ss 392-393). Those conditions include that when the interest is paid, the company is not a 'close-investment holding company', and the individual meets a 'capital recovery' condition and either a 'full-time working' or a 'material interest' condition.

The 'capital recovery' condition is broadly that between the making of the loan and the payment of the interest, the individual has not recovered any capital from the company (other than to repay their own borrowing, as the loan interest would be reduced in any event). If this condition is not met, the individual is treated as if they had used the capital recovered to repay their borrowing, whether or not it was actually repaid. The eligible interest paid is reduced by an amount equal to interest on the capital recovered and ceases to qualify for income tax relief from the date the capital was recovered.

There is a potential trap here for gifts or sales at undervalue. If the shares are sold and the disposal proceeds are not at arm's length, the proceeds are treated as being equal to the market value of those shares (ITA 2007, ss 406-407). In HMRC's view, this market value rule applies even if the shares are gifted (see HMRC's Savings and Investment manual at SAIM10250).

Thus if (say) the market value of gifted shares exceeds the amount of the outstanding loan, interest relief thereafter will be lost entirely.

Contributed by Mark McLaughlin

Capital Gains Tax Review - second report

The second report published by the OTS considers a wide range of areas covering practical, technical and administrative CGT issues. In total, it makes 14 recommendations, highlighting the following areas.

Integrating CGT into the Single Customer Account

There are three main ways of reporting a capital gain: through Self Assessment, the UK Property tax return for disposals of UK residential property, and the 'real time' Capital Gains Tax service. The OTS recommends that HMRC integrate these into the new Single Customer Account, removing the need for people to fill in a Self Assessment return to report a gain.

UK Property tax return

The OTS considers that 30 days to report property gains is a challenging deadline, even if it were integrated into the Single Customer Account. Consequently, the OTS recommends extending the reporting and payment deadline for the UK Property tax return to 60 days, or mandate estate agents or conveyancers to distribute HMRC provided information to clients about these requirements.

Private Residence Relief nominations

At present, where taxpayers have more than one home, there is insufficient awareness of the nomination procedure whereby taxpayers can choose which home they wish to benefit from this relief. The OTS recommends a review of the Private Residence Relief nominations process, and for the Government to look for ways to raise awareness of how the rules operate, and in time enable nominations to be captured through the Single Customer Account.

Divorce and Separation

Given the length of time it can take for divorcing couples to finalise settlements, the OTS recommends that the current no gain no loss rule continues beyond the end of the tax year of separation. They suggest extending it to the later of:

- the end of the tax year at least two years after the separation event;
- any reasonable time set for the transfer of assets in accordance with a financial agreement approved by a court or equivalent processes in Scotland.

Treatment of deferred proceeds when a business is sold

In situations where proceeds are deferred, such as on the sale of a business or land, the OTS recommends considering whether CGT should be paid at the time that cash is received.

https://www.gov.uk/government/publications/ots-capital-gains-tax-review-simplifying-practical-technical-and-administrative-issues

Access to communal garden (Lecture P1261 – 25.47 minutes)

Summary – The purchase of a London property with a right to access a communal garden did not make the property purchase liable to mixed use SDLT rates.

In August 2018, Nael Khatoun acquired the freehold interest in a London property for a consideration of £9,375,000. On the same day, he signed agreements giving him access to a communal garden in return for an annual rent.

Initially, Nael Khatoun submitted an SDLT return, applying the residential rates to the property. Later, he amended the return on the basis that an equitable interest in a communal garden was not residential property and so the lower mixed-use rates applied, generating a repayment of £861,750 of SDLT.

HMRC raised an enquiry into the SDLT return and later issued a Closure stating that SDLT was due at the residential rates and the refund claim was disallowed.

The taxpayer appealed arguing that the right of access to the garden was a separate property interest which was not residential property.

Decision

The First Tier Tribunal agreed with HMRC.

Nael Khatoun's right to enter and use the communal garden was a licence to use land as permission to enter and use the garden was revocable on three months' notice. Whilst there was clearly a connection between the right being granted to Nael Khatoun to use the garden and his ownership of the property, the right did not itself pertain to the property; it pertained to the communal garden.

The purchase of the London property with access to a communal garden was subject to SDLT at the residential rates and not mixed-use rates.

Nael Khatoun v HMRC (TC08085)

Properties joined by glass conservatory (Lecture P1261 – 25.47 minutes)

Summary – Multiple Dwellings Relief was denied as the annex to the main property was not capable of being 'lawfully let as a dwelling"

Michael And Anthea Mullane acquired a house with an annex in August 2018. The property had originally comprised two separate buildings with the annex being a coach house. They were separated by a wrought iron frame through which one could walk to reach the garden.

The previous owner joined the two buildings by creating a “T” shaped glass conservatory style area five feet wide. Separate doors allowed entrance to the annex and to the main house via the kitchen and lounge. The annex door had no lock when then property was acquired but one has been added since.

The couple were considering letting out the annex. The ground floor of the annex comprised a large room and bathroom. A photo of the living room in the annex showed a microwave on a stool or low table. The first floor of the annex has a kitchen sink, drainer, and small work top and a fridge. At the time of completion, there was no cooker or washing machine or place designed to accommodate a washing machine in the annex. At the time of purchase, the property was advertised as a single dwelling with the rooms in the annex described as bedroom 3/study and bedroom 4. Finally, there were no separate council tax bills or utility bills for the annex.

Michael And Anthea Mullane initially submitted an SDLT return on the basis that this was a residential property but three months later they submitted an amended return claiming Multiple Dwellings Relief, reducing the SDLT to £16,400. Following an enquiry, HMRC declined the relief.

Decision

The First Tier Tribunal found that the fact that there was a conservatory linking the two properties did not indicate that there was only one dwelling. The main problem was the lack of a proper kitchen. The cooker and sink were too close together for safe use, and the open plan kitchen posed a fire risk.

The Tribunal concluded that the annex was capable of separate occupation, but not of safe, separate occupation. It could not lawfully be let as a dwelling.

The appeal was dismissed.

Michael And Anthea Mullane v HMRC (TC08100)

Administration

No repayment by HMRC (Lecture P1261 – 25.47 minutes)

Summary – HMRC’s request to strike out an appeal was dismissed as a dispute relating to box 20.1 in the tax return was within the scope of the enquiry and therefore was within the scope of the tribunal's jurisdiction.

Richard Cochrane submitted his 2003/04 tax return in July 2004. As part of that return he gave details of an arrangement that he entered into involving an IIP settlement of which he was settlor and life tenant and an option that was sold by the trustees of that trust. Following the subsequent exercise of that option by the purchaser, Investech Bank (UK) Ltd, Richard Cochrane believed that he had suffered an income tax loss of £1,052,800, allowable under para 14A Schedule 12 to Finance Act 1996. He claimed relief in his tax return and claimed a tax repayment of £415,079.16.

At box 20.1 of his return and in response to the question “Have you already had any 2003/04 tax refunded or set off by your Inland Revenue Office …?” he responded “yes” and disclosed a repayment as £20,000.

Following a long enquiry into this return, it was agreed that the loss had arisen as a result of an ineffective tax avoidance scheme. HMRC wrote stating that Richard Cochrane owed some £25,000, which included the £20,000 previously been repaid to him.

Richard Cochrane claimed that he had made an error on his return and had never received this refund. He wrote to HMRC stating:

> “I have reviewed considerable amounts of information in an attempt to reconcile the entry within your computations described as ‘Tax already refunded in the year’ in the sum of £20,000. I’m afraid that I have not been able to identify any repayment of 2003/4 income tax overpaid to Mr Cochrane. Please can you send me details of this entry, including the dates, amounts involved and the manner in which they have been repaid.”

HMRC were unable to produce any evidence to support the £20,000 repayment and replied stating:

> “of course this does not mean that a repayment was not made, simply that no records for it can now be traced.”

Richard Cochrane concluded that as neither party could identify the £20,000 it was reasonable to conclude that the sum had not in fact been repaid. He submitted an amended tax return, having removed the box 20.1 entry.

HMRC did not accept the amendment and issued a closure notice for the full amount.

Richard Cochrane appealed.

HMRC applied to the First Tier Tribunal to strike out the appeal on the grounds that the box on the tax return that Richard Cochrane had ticked (in error) was not part of the return and so could not be the subject of an appeal to the tribunal.

Decision

The First Tier Tribunal concluded that as box 20.1 was in the return, any dispute as to its effect was within the scope of the enquiry and the closure notice, and therefore within the scope of the tribunal's jurisdiction.

The Tribunal stated that it would expect to see bank account information from Richard Cochrane to prove there was no repayment received from HMRC.

The Tribunal concluded by saying that it was astonished that HMRC had no record of payments made, "if indeed a repayment was made."

HMRC's application to strike out the appeal was refused.

Richard Cochrane v HMRC (TC08078)

Code of Practice 8 investigations (Lecture P1265 – 12.56 minutes)

What is Code of Practice 8?

Historically, there was a clear demarcation between HMRC's Codes of Practice 8 and 9. Whereas Code of Practice 9 dealt with cases of suspected (serious) fraud, Code of Practice 8 was used to tackle tax avoidance, over a wide range of risk areas. HMRC's current guidance refers to Code of Practice 8 as "Specialist investigations for fraud and bespoke avoidance".

The current version of Code of Practice 8 covers "civil investigations in certain cases where the Code of Practice 9 is not used". The document goes on to say that it will cover cases where a taxpayer has "deliberately" tried to pay less than the correct amount of tax. Advisers will be aware that, absent an admission by a taxpayer, the onus is on HMRC to demonstrate deliberate behaviour.

Code of Practice 8 investigations are undertaken by HMRC's Fraud Investigation Team, and will be used where there may have been a "significant" loss of tax.

Particular care is required when dealing with this type of investigation, as, if HMRC suspect or find evidence of fraud, they can switch to Code of Practice 9, or commence a criminal investigation. The taxpayer does not, at the start of the investigation, have the protections afforded by Code of Practice 9 if there has been fraud. It should be noted that Code of Practice 8 does not give HMRC any additional statutory powers.

What type of cases are investigated under Code of Practice 8?

The investigations cover a broad range of taxpayers, and include individuals, partnerships, limited liability partnerships (LLPs), companies and trusts.

Cases conducted under this Code of Practice cover a broad range of issues. As well as tackling cases involving bespoke avoidance, as noted above, other cases investigated by HMRC using this process include offshore matters, domicile and complex issues. For example, one of the cases I dealt with recently involved a taxpayer's property transactions over a 20-year period.

The investigation process

The investigation will start with notification in writing that HMRC are using the Code of Practice 8 procedure. The Fraud Investigation Service investigator may take over an existing compliance check, or there can be a stand-alone investigation.

The opening letter will, usually, contain a request for the information and documents that the investigator wants to see. The request is usually extensive, and may cover a long period. The letter may also include a request for a meeting with the taxpayer, and/or a visit to the business premises. Requests for information, or meetings, should be considered on their merits, and in the context of the case, to determine what is reasonable.

When the inspector's queries have been dealt with, the case will, usually, be settled by a contract settlement, where there are additional liabilities. The position regarding penalties will need to be considered, and the normal rules apply. In other cases, including where agreement cannot be reached, the case may be concluded via a formal route. Where the inspector's enquiries have not identified additional liabilities, the case should be closed (unless the adviser has established that there is a disclosure to make).

Use of a specialist adviser

HMRC use specialist investigators for Code of Practice 8 cases. It is prudent for advisers to seek specialist assistance where they do not have the relevant experience. Typically, the specialist adviser will work with the existing accountant.

A Code of Practice 8 investigation can have a significant impact on an adviser's resources, particularly given the extensive, and complex, information requests that typically accompany such cases. There is usually a large amount of data to be gathered, together with extensive analysis, which can place a disproportionate strain on the adviser, especially in smaller firms.

Specialist advisers can conduct a case review, to determine the best response to a Code of Practice 8 investigation, and whether any challenges are necessary to the HMRC queries. A specialist can also help to identify whether it is necessary to seek the client's voluntary inclusion in the Contractual Disclosure Facility (Code of Practice 9) where fraud is established (helping to reduce the risk of a criminal investigation, where HMRC identify the fraud). The specialist adviser can help to protect the client, and the regular adviser.

Contributed by Phil Berwick (Director, Berwick Tax)

Deadlines

1 July 2021

- Corporation tax for periods ended 30 September 2020 if not paying by instalments

5 July 2021

- Application for a PAYE settlement agreement for 2020/21
- Report non-cash benefits not from a registered pension scheme

6 July 2021

- File Forms P9D, P11D, P11D(b) for 2020/21
- File taxed award scheme returns.
- Details of 2020/21 redundancy packages exceeding £30,000 to HMRC
- File Forms 42

7 July 2021

- Electronic filing and payment of VAT liability for 31 May 2021
- Election to aggregate beneficial loans in 2020/21
- File Forms EMI40

14 July 2021

- CT61s for quarter ended 30 June 2021

19 July 2021

- PAYE liabilities for month ended 5 July 2021 if by cheque
- PAYE for quarter to 5 July 2021 if average monthly liability is less than £1,500

21 July 2021

- Online monthly EC sales list (businesses based in Northern Ireland selling goods)
- Supplementary intrastat declarations for May 2021
  - arrivals only for a GB business
  - arrivals and dispatch for a business in Northern Ireland

22 July 2021

- PAYE liabilities if paid online

31 July 2021

- Companies House should have received accounts of
  - private companies with 31 October 2020 year end
  - plcs with 31 January 2021 year end
- Second 5% surcharge for unpaid 2019-20 balancing payments
- 2020-21 second instalment self-assessment liabilities
- Tax credits claims to be renewed

News

Finance Act 2021 receives Royal Assent

Royal Assent to Finance Act 2021 was notified in the House of Lords at 12pm on 10 June 2021.

The Act incorporates a number of UK government amendments that were made to the Bill during its passage through Parliament, which include the insertion of the following four new clauses and one new Schedule at Report Stage:

Clause 95 (Distance selling: Northern Ireland)

Clause 96 (Distance selling: power to make further provision)

Clause 97 (Supply of imported works of art etc)

Clause 98 (Continuing effect of principle preventing the abuse of the VAT system)

Schedule 18 (VAT and distance selling: Northern Ireland)

Sourced from Tolley Guidance

G7 global tax agreement

It was widely reported in the press that the G7 has agreed to the idea of a minimum corporation tax rate of at least 15% in all countries, so creating a more level playing field for all firms while also cracking down on tax avoidance.

Further, G7 Finance Ministers have agreed to target multinational (tech) giants with a global tax reform to ensure that such companies pay their fair share of tax in the countries where they trade. "These rules would apply to global firms with at least a 10% profit margin and would see 20% of any profit above the 10% margin reallocated and subjected to tax in the countries they operate and not just where they have their headquarters.

https://www.g7uk.org/g7-finance-ministers-agree-historic-global-tax-agreement/

Year end on the move?

The Office of Tax Simplification (OTS) is reviewing the possibility of moving the tax year end to the end of March each year. Already the UK government's financial year end and the date to which corporation tax rates apply, a 31 March year end would fit well with calendar quarters.

In carrying out its review, the OTS will take into account the implications of any change in relation to tax credits and benefits and consider the implications for the Exchequer, the tax gap and compliance generally, in particular in relation to income tax, PAYE, NICs, capital gains tax and inheritance tax.

In addition, the OTS will outline the main additional broader issues, costs and benefits that would need to be considered if the end of the tax year were moved instead to 31 December.

A report will be published this summer.

https://www.gov.uk/government/publications/ots-to-explore-potential-for-moving-the-end-of-the-tax-year

Business Taxation

Taxpayer loses IR35 appeal **(Lecture B1261 – 23.09 minutes)**

Summary - A project manager contracting through an intermediary personal service company was subject to the IR35 legislation and so liable to income tax and NICs as an employee.

Robert Lee worked almost continuously for seven years as a project manager for Nationwide through his personal service company, Northern Light Solutions Limited (NLS). The terms of the various contracts were all similar, requiring him allocate tasks to the project team and to determine the costs and timescales for delivering projects. Under each of the contracts, he worked for a fixed term, with fixed hours and a fixed day rate. There was no holiday or sick pay. Included in his contracts was an unexercised right of substitution that would have required Nationwide's consent.

Believing that the arrangements fell foul of the IR35 rules, HMRC issued Income Tax determinations and NIC notices in respect of three tax years.

On appeal, the First Tier Tribunal had found that had a hypothetical contract existed between Robert Lee and Nationwide, it would have been one of employment. Robert Lee was subject to the kinds of controls that were consistent with being a highly skilled employee.

NLS appealed to the Upper Tribunal arguing that the First Tier Tribunal had erred in their decision relating to mutuality of obligation, the level of control exercised by Nationwide and that the company's ability to provide a substitute was not hypothetical.

Decision

The Upper Tribunal concluded that sufficient mutuality of obligation existed. It did not matter that there would have been no obligation on Nationwide to offer work or indeed, for Robert Lee to accept work, if a project ended early. What mattered was that until the contract ended, there was clearly an obligation to pay for work done and an obligation to do the work provided.

On the issue of control, the Upper Tribunal found that, although Nationwide could not insist that Robert Lee work on a project other than the one in his contract, Nationwide had sufficient control over when and where he worked. Under his contracts he was required to work a 7.5 hour day and Nationwide could require him to work from a particular office.

Based on the case facts, although there was a right of substitution on the contracts, the Upper Tribunal concluded that it was unlikely that NLS would be able to provide a satisfactory substitute with the right experience, security clearance and familiarity with the project. Following the decision in the *Pimlico Plumbers case,* the dominant feature of the contract was an obligation for Robert Lee to perform the role himself.

The First Tier Tribunal's decision was upheld.

Northern Light Solutions Limited v HMRC [2021] UKUT 0134 (TCC)

Ghost account to conceal income (Lecture B1261 – 23.09 minutes)

Summary – A sole trader had under-declared income from his business for six tax years, receiving customer payments into a bank account in his mother's maiden name.

In 2005 Roger Whitlock commenced his self-employed business of removing household and garden rubbish from domestic properties, builders and other businesses.

On 9 March 2017, HMRC opened an enquiry into his Self Assessment tax return for the tax year 2015/2016. This was prompted by the fact that all figures were reported in round thousands, his expenses seemed very high compared with other businesses and his profits chargeable to tax were always just above or occasionally just below the personal allowance limit.

Roger Whitlock claimed that he usually worked alone, he did not issue invoices to his customers and that all cash received from customers was banked the following day and that he did not retain any cash.

HMRC:

- established that expenses claimed were more than had been withdrawn from his bank account;
- showed him reviews of his "team" on social media in 2014 and 2015 and were able to prove that he had insured multiple vehicles;
- identified a bank account in his mother's maiden name which recorded payments to and from Roger Whitlock's bank account.

He accepted that not all receipts had been banked and that he did indeed have a team of people working for him, meaning that his business was in fact larger than he had made out.

As for the bank account, he claimed that these were loans from his mother to assist him financially. However, the sum of the payments from him to his mother's bank account was greater than the sum of the payments from his mother's bank account to him. Furthermore, in some transactions the same amount of money was transferred back and forth between the accounts in the same amount on the same day. He claimed that his mother used telephone banking to make her transfers but none of the bank statements showed any sign of telephone banking having been used. He was unable to explain payments from her account for commercial vehicle insurance and payday loans. Further, there was no evidence supporting the fact that she used the account for her own income and expenses. He denied that the account was in fact a ghost account that he operated for the purposes of his business. HMRC included all payments to him from his mother's bank account as additional trading income.

Finally, having flagged that there was no sign of any 'ordinary household' expenses coming out of his bank account, HMRC added a further figure of £100 per week to his turnover to represent the fact that he was likely to have paid for his ordinary household expenses in undeclared cash generated by his business.

In total, HMRC added approximately £38,000 as under-declared income for 2015/16. Given his business had not varied in size in the previous five years and the figures were again rounded, based on the ‘presumption of continuity’, it could be inferred that similar under-declarations had occurred in earlier tax years. HMRC issued discovery assessments for the five years before.

Although he disputed the figures in HMRC’s discovery assessments and the closure notice, Roger Whitlock could not put forward any reliable alternative figures. He had very little in the way of business records and, apparently, no method of recording the receipt of cash. He had offered HMRC £20,000 to settle his liabilities and could not understand why this was not acceptable.

Roger Whitlock appealed to the First tier Tribunal against the Closure notice for 2015/16 and the discovery notices for the previous five years.

Decision

With Roger Whitlock unable to offer any evidence to the contrary, the First Tier Tribunal agreed with the evidence that HMRC had presented.

He had deliberately under-declared his income and the appeal was dismissed.

Roger Whitlock v HMRC (TC08136)

No loss relief as not trading (Lecture B1261 – 23.09 minutes)

Summary - Participants in a tax avoidance scheme designed to create losses were denied sideways relief as they were not trading and there was an absence of economic loss.

Anthony and Ross Outram were brothers whose cases were heard together due the similar nature of the facts involved.

As part of a criminal investigation involving a search of the scheme provider, Montpelier Tax Planning, HMRC became aware of the brother’s involvement in that scheme.

The brothers sought no advice before entering into the scheme, stating that they both relied on Montpelier Tax Planning for everything, who in turn reassured them that their involvement in the tax planning scheme was trading activity, and that this was confirmed by counsel. Consequently, the brothers claimed that they were self-employed options traders and claimed trading losses for 2005/06 against other income in that year and by carrying it back.

Suspecting fraud, HMRC opened a COP 9 enquiry, believing that the brothers had submitted incorrect tax returns containing loss claims believed to be knowingly incorrect. The brothers chose not to make a contractual disclosure and HMRC issued discovery assessments that disallowed most of the losses, arguing that their behaviour had been deliberate.

The brothers appealed.

Decision

The Tribunal found that there was no trade and they had not suffered an economic loss. Choosing not to use a trading platform, the brothers engaged the tax planning services of Montpelier. Knowingly, they had entered into a tax avoidance scheme with the sole aim being to create a significant loss, enabling them to claim substantial tax repayments. The brothers knew when they filed their Self Assessment returns that they were not carrying on a trade entitling them claim loss relief.

The Tribunal stated:

> 'This was not a question of the appellants turning a blind eye. They did not ask questions or read documents because they knew precisely what they were doing.'

The appeal was dismissed.

Anthony Outram and Ross Outram v HMRC (TC08107)

Premises or plant? **(Lecture B1262 – 13.08 minutes)**

Cheshire Cavity Storage 1 Ltd v HMRC (2021)

The Upper Tribunal have recently clarified the meaning of 'plant' for capital allowances purposes in Cheshire Cavity Storage 1 Ltd v HMRC (2021). The appellant and a fellow group member were both companies in the EDF Energy Group whose business comprised energy generation and supply.

This appeal concerned the availability of plant or machinery allowances under CAA 2001 on expenditure incurred in connection with underground cavities for gas storage in Cheshire. The cavities were formed by injecting water into naturally-occurring salt rock which, when the salt rock dissolved, left a hole filled with saltwater. Gas was then pumped into the hole and the saltwater in it expelled. The rock around the hole created an impervious barrier so that the gas could not escape. The cavity was connected by pipes to the national transmission system for gas owned by the National Grid which supplies gas to end users.

The First tier Tribunal decision

In 2019, the main issue before the First-Tier Tribunal was whether the cavities met the common law definition of 'plant'. The First-Tier Tribunal concluded that the cavities were not 'plant' which resulted in the taxpayer companies' appeals being dismissed. As is well known, case law distinguishes between the premises in which the business is carried on and the plant with which the business is carried on. The question was whether the items functioned as premises and therefore could not qualify for capital allowances or, alternatively, as plant which could.

With regard to immovable property structures used for storage, the First-Tier Tribunal noted that providing shelter and protection for plant, stock and customer possessions was regarded as a premises function.

Where premises had both plant-like and premises-like

functions, the question was which of the functions predominated. The First-Tier Tribunal was prepared to accept that the cavities did have a plant-like function similar to that of a pump or compressor, but the judge determined that the premises function of storage was the predominant factor. This meant that the cavities were not plant so that the relevant expenditure could not qualify for capital allowances treatment.

The Upper Tribunal decision

The companies therefore appealed to the Upper Tribunal on the ground that the First-Tier Tribunal had erred in law in its approach to the common law meaning of ‘plant’. A considerable number of cases were cited in this context. In chronological order, these were:

- Yarmouth v France (1887);
- Jarrold v John Good & Sons Ltd (1963);
- CIR v Barclay Curle & Co Ltd (1969);
- Cooke v Beach Station Caravans Ltd (1974);
- Schofield v R&H Hall Ltd (1975);
- Benson v Yard Arm Club Ltd (1979);
- Wimpy International Ltd v Warland (1989);
- Carr v Sayer (1992);
- Bradley v London Electricity plc (1996); and
- Attwood v Anduff Car Wash Ltd (1997).

Principles derived

The starting point is that plant is the apparatus used for the carrying on of a business (Yarmouth).

Even though premises are normally regarded as the setting in which the trade is carried on (and are therefore not plant), premises and plant are not mutually exclusive, with each case depending on its facts. There are cases where an item is excluded from being classified as plant on the basis that it is more part of the setting than part of the apparatus (Jarrold).

The function of an item is an important consideration. The functional test is a preliminary to the assessment of whether a particular item is apparatus. A structure can be plant if it fulfils the function of plant in a trader’s operations. However, not every structure which fulfils the function of plant will be regarded as plant if there is a good reason to exclude such a structure (Barclay Curle and Benson).

A decision on whether an item is plant is a decision on a question of fact and degree and there are a number of cases which, on the facts, are capable of being decided either way (Schofield and Anduff).

Although the premises in which a business is carried on can accurately be described as being provided for the purposes of the business, it is not enough for that reason alone to be held to be plant (Benson).

Where premises also perform a plant-like function, the question is whether it is more appropriate to describe the item as having become part of the premises rather than retaining a separate identity. If the item functions as part of the premises, it cannot be plant (Wimpy and London Electricity).

Equipment does not cease to be plant merely because it discharges an additional function such as providing the place in which the business is carried on (Sayer).

The question in each case is whether the item functions as premises or plant. To answer this may involve deciding whether it is more appropriate to describe the item as apparatus for carrying on the business or as the premises in which the business is conducted (Wimpy and Anduff).

The decision

The judges in the Upper Tribunal disagreed with the taxpayer company. They held that the First Tier Tribunal had applied the correct test, although its terminology could perhaps be said to be inconsistent with case law. The correct approach in the view of the Upper Tribunal is to consider which function is *more appropriate* (the author's emphasis) rather than which function predominates. It was more appropriate to classify the cavities as premises, based on the facts of the case. The expenditure was not therefore eligible for capital allowances.

Contributed by Robert Jamieson

A taxpayer's appeal on reconstruction relief (Lecture B1265 – 10.56 minutes)

Euromoney Institutional Investor plc v HMRC (2021) is a First-Tier Tribunal case heard in May last year but where the decision was only published on 4 March 2021. It concerned a taxpayer company (E) appealing against an amendment to its corporation tax return for the year ended 30 September 2015 which had the effect of increasing its tax liability by nearly £10,500,000.

The amendment related to a transaction between E and a company called Diamond Topco Ltd (D) whereby E exchanged its shareholding in a third company (C) for ordinary and preference shares in D.

HMRC's amendment was made on the basis that E was liable to corporation tax on a gain following the disposal of its preference shares in D. This was because the tax authorities contended that the share-for-share exchange took place as part of a scheme or arrangement, of which one of the main purposes was the avoidance of a liability to corporation tax on a chargeable gain. This in turn meant that the 'no disposal' rule in S135 TCGA 1992 was disapplied by S137(1) TCGA 1992.

E is a UK-resident company, founded in 1969 by Sir Patrick Sergeant (a former financial journalist), which provides news, data and analysis to various business markets. It is listed on the London Stock Exchange and is a member of the FTSE 250 Index.

As part of the negotiations for the sale of the shares owned by E, that company initially agreed to receive ordinary shares and cash from D. Subsequently, the cash element was replaced by preference shares. Cash proceeds would have generated an immediately taxable gain on E, but an exchange of preference shares brought the provisions of S135 TCGA 1992 into play. It was anticipated that the preference shares would, in due course, be redeemed, in which case any gain was free of tax under the substantial shareholding exemption as long as the shares had been held for at least 12 months.

On 17 January 2016, the preference shares were duly redeemed. This was some 14 months after the deal was done.

On 8 September 2016, E filed its CT600 for the year ended 30 September 2015, along with supporting tax computations which were prepared on the basis that there was no chargeable gain on the disposal of the C shares because of the share-for-share exchange rules. Advance clearance from HMRC under S138 TCGA 1992 had been sought by E, but the transaction was completed before a response was received.

HMRC opened an enquiry into this return on 2 November 2016 which ultimately led to the hearing before the First-Tier Tribunal.

Before the First-Tier Tribunal, HMRC denied the availability of reconstruction relief on the ground that one of the main purposes of the arrangements was tax avoidance. Note that there was no dispute between the parties about the exchange of shares being effected for bona fide commercial reasons.

When considering the nature of the arrangements, the First-Tier Tribunal decided that they must be considered as a whole and that they were not limited to arrangements which only concerned the acquisition of the preference shares. This follows from a principle established by the House of Lords in Brebner v CIR (1967).

Avoiding a liability to tax was held by the judge to be a purpose of the arrangements, but it was not a main purpose. He said:

> 'I . . . accept that a more than trivial purpose is not necessarily a "main" purpose. A main purpose will always be a more than trivial one, but the converse is not the case. A purpose can be more than trivial without being a main purpose. "Main" has a connotation of importance.'

He went on:

> 'Whether a tax purpose is one of the "main" purposes of the arrangements is a matter of subjective intention, involving a careful analysis of all the reasons the taxpayer had for carrying them out (see Versteegh Ltd v HMRC (2014) and Brebner v CIR (1967)).
>
> The witness evidence in this appeal, which I accept, is that E's main subjective purposes were commercial and the tax considerations were not important in this context.'

The e-mail and the verbal evidence in this case showed that the taxpayer company would not have substituted preference shares for cash if that change would have endangered the deal. The tax at stake was not significant, compared with the overall transaction value, and the taxpayer's advisers did not invest much effort in exploring the tax outcomes.

The anti-avoidance rules did not deny reconstruction relief and E's appeal was upheld.

Contributed by Robert Jamieson

Entitlement to relief for US withholding tax

Summary - A UK company was allowed to claim unilateral relief against US withholding tax despite being refused treaty relief by the US Internal Revenue Service.

The taxpayer, a wholly owned subsidiary of Aozora Bank Ltd and incorporated in the UK, received interest payments, net of withholding tax, from its US subsidiary.

The US Internal Revenue Service did not accept its application to access benefits of the UK-US double tax treaty on the ground that Aozora UK was not a qualified person within the meaning of Article 23 of the treaty.

HMRC later refused the taxpayer's claim for unilateral relief by way of credit against the UK tax due on the interest it received, on the basis that s793A(3) ICTA 1988 applied (note that this section has since been repealed by TIOPA 2010. S793A is the provision which provided that where a tax treaty contains specific limitations on double taxation relief, unilateral relief [s790 ICTA 1988] will no longer be available as a fall back.

The taxpayer appealed.

Decision

The First Tier Tribunal said the key to unlocking the construction of s 793A(3) was the use of the adjective 'express' to qualify 'provision'. Its meaning was 'definitely formulated, definite, explicit, specifically designated, or specially intended'. So, the treaty would need to be explicit as to when credit was not available. However, this was not the case here — Article 23 did not expressly provide that relief by way of credit should not be given.

The First Tier Tribunal disagreed with HMRC that the purpose of s 793A(3) was to ensure that the reciprocal provisions agreed between two states in a double tax agreement were respected in domestic law. The reason that the UK entered into double tax arrangements was 'to limit the exposure of its residents to the taxes of the counterparty territory'. They were not carried out with a view to determining how the UK would tax its own residents.

Indeed, the UK-US treaty acknowledged the possibility that a taxpayer may have a smaller tax burden under domestic law than under the terms of the treaty.

The taxpayer's appeal was allowed.

Aozora GMAC Investments Limited v HMRC (TC08082)

Adapted from the article in Taxation (20 May 2021)

State aid: Luxembourg wins Amazon case but loses Engie case

Summary – The EU General Court annulled the European Commission's 2017 decision that Luxembourg had granted Amazon €250m in state aid, finding that the Commission's transfer pricing analysis was incorrect.

The Luxembourg tax authorities had granted a tax ruling to two Luxembourg subsidiaries of the Amazon group concerning the method of calculating a royalty to be paid by those subsidiaries in respect of intellectual property rights.

The Commission decided that the royalty was too high and that to this extent, the ruling constituted state aid. Luxembourg was ordered to recover the illegal aid of €250m.

Luxembourg and Amazon both brought actions seeking annulment of the Commission's decision.

The General Court upheld their arguments and annulled the decision in its entirety. The Court examined the methodology used by the Commission to determine whether the royalty had been set at an arm's length rate and identified a number of fundamental errors. As a result, the Commission had failed to establish that the Amazon companies had received an advantage in comparison with the situation that would have prevailed under 'normal' taxation rules, in the absence of the contested ruling.

On the same day, in Luxembourg v Commission; Engie, Engie Global LNG Holding Sarl and Engie Invest International SA v Commission (Cases T-516/18 and T-525/18), the General Court upheld the Commission's 2018 decision that tax rulings by the Luxembourg authorities in favour of companies in the Engie group (formerly GDF Suez) resulted in illegal state aid of €120m.

In Engie, the Luxembourg authorities had granted tax rulings on the group's internal financing arrangements. The Commission concluded that the rulings gave Engie a significant competitive advantage: they endorsed inconsistent tax treatment of the same financing structure within the same group; categorised transactions between subsidiaries as both debt and equity and led to non-taxation at all levels. The General Court agreed, finding the rulings had led to preferential tax treatment of Engie through not applying the normal Luxembourg tax rules. Luxembourg has been ordered to recover the €120m of illegal aid.

The Commission welcomed the decision in Engie and will 'reflect on possible next steps' in relation to Amazon.

According to PwC's EU direct tax group, the decision in Amazon provides 'important clarifications regarding the scope of the EC's burden of proof in establishing the existence of an advantage where the level of taxable income of an integrated company belonging to a group is determined by the choice of the transfer pricing method. 'Engie’ confirms for the first time that the EC can determine the existence of a selective advantage for state aid purposes on the grounds of non-application of a local concept of abuse of law by the local authorities'. It remains to be seen whether either judgment will be appealed.

https://curia.europa.eu/jcms/upload/docs/application/pdf/2021-05/cp210079en.pdf

Adapted from the case summary in Tax Journal (21 May 2021)

Loan relationship – anti-avoidance rules (Lecture B1264 – 19.49 minutes)

Non-market loans (s446A CTA 2009)

Where:

1. the amount recognised initially is less than the transaction price and the balancing credit is not treated as a LR credit, and

2. The lender is

   - Not a company, nor

   - Is a company resident or effectively managed in a non-qualifying territory

No LR debit is allowed for the initial discount.

Corporate lenders are taxed on P&L amounts credited in respect of the discount, even though their initial debit to 'investment in subsidiary' is not deductible.

Look for unusual additions to capital in the balance sheet and identify if it was caused by discounting loans payable, then check if lender is in a non-qualifying territory (tax havens, broadly) or is an individual.

Example

A Jersey parent lent £1,000,000 interest free to a subsidiary on 1 April 2018 when the market rate was 5% per annum.

The loan is repayable on 31 March 2023. The company has a 31 December year end.

The accounts have been properly prepared in accordance with FRS 102/IFRS (see the table below).

Calculate the adjustments needed in the CT600s for the accounting periods from 31 December 2018 to 31 December 2023.

Initial booking 1 April 2018

- Dr Bank account £1,000,000

- Cr Loan (1m ÷ 1.05^5) £783,526

- Cr Equity (other shareholder reserves) £216,774

•

		Balance	**New loan**	**Revised**	**Interest**	**Bal**
Year ended		**b/fwd**	**1.4.2018**	**balance**	**expense 5%**	**c/fwd**
31-Dec-18		0	783,526	783,526	* 29,202	812,728
31-Dec-19		812,728	-	812,728	40,636	853,364
31-Dec-20		853,364	-	853,364	42,668	896,032
31-Dec-21		896,032	-	896,032	44,802	940,834
31-Dec-22		940,834	-	940,834	47,042	987,876
31-Dec-23		987,876	-	987,876	**12,124	1,000,000
					216,774	

9 months' interest rate $(1.05^{0.75} - 1)$	*3.7270%			
3 months' interest rate $(1.05^{0.25} - 1)$	**1.2272%			

Analysis

Because the initial credit of £216,774 was not brought into account under the LR rules, the interest expense each period is also disallowed

- £29,202 should have been disallowed in the year ended 31 December 2018
- £40,636 disallowed in the year ended 31 December 2019
- £42,668 will be disallowed in the year ended 31 December 2020
- Etc….

Interest-free loans between UK companies

If an interest-free term loan is made between two UK companies in an AP beginning on or after 1 January 2016, both will initially discount the loan under FRS 102.

The lender will unwind the discount to recognise interest income each period and the borrower will unwind the discount to recognise interest expense each period.

The interest income is taxable on the lender and the interest expense is deductible for the borrower.

If the loan was granted in an accounting period beginning before 1 January 2016, ‘amortised cost’ for tax purposes used to be defined as booking the loan initially at the amount lent (net of any transaction costs).

This initial amount is then be amortised (if necessary) to the amount payable on redemption.

If the loan has been amortised in the accounts because of the requirements of FRS 102 or IFRS, this needs adjustment for both the borrower and lender to ensure the CT600 and tax computation reflects the tax definition.

Example

A UK parent company lent a UK subsidiary £1,000,000 on 1 April 2015, interest free and repayable on 31 March 2025.

The company could have borrowed at a market rate of 6%. There were no issue costs

The loan has been recorded in accordance with FRS 102/IFRS as set out below.

Year ended	**Bal b/fwd**	**Accounts Interest 6%**	**Amortised cost c/fwd**
31-Mar-16	558,395	33,504	591,899
31-Mar-17	591,899	35,514	627,413
31-Mar-18	627,413	37,645	665,058
31-Mar-19	665,058	39,903	704,961
31-Mar-20	704,961	42,298	747,259
31-Mar-21	747,259	44,836	792,095
31-Mar-22	792,095	47,526	839,621
31-Mar-23	839,621	50,377	889,998
31-Mar-24	889,998	53,399	943,397
31-Mar-25	943,397	56,603	1,000,000

For tax purposes, the amortised cost is the amount lent of £1m. The amount repayable is £1m, so for tax purposes it is treated as a no interest loan.

All of the accounting interest expense must be disallowed. If the loan was granted in an accounting period beginning on or after 1 January 2016, the interest would be deductible for the borrowing company and taxable on the lending company.

Imputed (notional) interest – s446A

Transfer pricing rules (Part 4, TIOPA 2010) can lead to tax adjustments on loans made other than on arm's length terms.

Imputed interest income on non-arm's length loans gives rise to taxable LR credits. Any compensating adjustments (s174 TIOPA 2010) of interest by the borrower are allowable LR debits.

But if the loan had been discounted by the borrower, ensure that the correct amount of interest is deducted in the CT600.

Check if transfer pricing adjustments are needed when looking at related party borrowings. Quantify the amounts involved and consider if a compensating adjustment can be made in the borrower company.

Example

A UK subsidiary borrowed £1,000,000 from its UK parent company on 1 April 2018. The loan is interest free, repayable on 31 March 2023 and the market rate at which the UK subsidiary could borrow externally is 5% per annum

The provisions of Part 4, TIOPA apply so that the parent has notional interest income of 5% of £1m, i.e. £50,000 which is taxable.

The subsidiary can make a claim for a compensating adjustment of £50,000 in its CT600.

The amounts booked by each company are the same as in the previous example:

		Balance	**New loan**	**Revised**	**Interest**	**Bal**
Year ended		**b/fwd**	**1.4.2018**	**balance**	**expense 5%**	**c/fwd**
31-Dec-18		0	783,526	783,526	* 29,202	812,728
31-Dec-19		812,728	-	812,728	40,636	853,364
31-Dec-20		853,364	-	853,364	42,668	896,032
31-Dec-21		896,032	-	896,032	44,802	940,834
31-Dec-22		940,834	-	940,834	47,042	987,876
31-Dec-23		987,876	-	987,876	**12,124	1,000,000
					216,774	

9 months' interest rate ($1.05^{0.75} - 1$)	*3.7270%			
3 months' interest rate ($1.05^{0.25} - 1$)	**1.2272%			

Adjustments to the CT600 will be the tax interest amount minus the accounts interest

- 2018: (37,500 – 29,202) £8,298
- 2019: (50,000 – 40,636) £9,364
- 2020: (50,000 – 42,668) £7,332
- Etc…

Late paid interest (s373 – 378 CTA 2009)

Where the lender is not within scope of corporation tax, they are only taxed on interest when received (e.g. individual, trust, pension fund).

The borrower company generally gets relief on accruals basis, so could get relief without the lender being taxed until much later.

Relief for interest debits is denied, in certain circumstances, until paid where

- The interest is not paid within 12 months of the end of the period to which it relates, an
- It is not brought into account by the lender under the loan relationship rules

When calculating tax provision, current year interest won't be paid 12 months late. Check if any prior year interest remains unpaid and check if within disallowable categories in s375 (or s378).

s.375:

- Borrowing company is a close company
- Lender is a participator, associate of a participator or a company controlled by the participator (or the participator has a major interest in the company)
- Includes where a non-resident property business is close

s.375(4A)

- The lender is resident for tax in a non-qualifying territory at any time in the accrual period, or
- It is effectively managed in a non-taxing, non-qualifying territory
- Non-qualifying territories include Jersey, Guernsey, the Isle of Man, Hong Kong, the Cayman Islands and the British Virgin Islands

s.378

- The lender is an occupational pension scheme (s.378)

Other anti-avoidance rules

Loans for unallowable purposes (s441)

Loan relationship debits are disallowed where the loan is financing activities not within the scope of UK corporation tax, or used in an arrangement where one of the main purposes is tax avoidance

Always ask how the money raised for loans has been used. It is important for this, but also for the trading/non-trading distinction.

Loans to participators in a close company (s321A)

No loan relationship debit is allowed for the release or write off of the loan.

Contributed by Malcolm Greenbaum

VAT and indirect taxes

R&C Brief 6 (2021): Juice cleanse programmes

Following the Upper Tribunal's decision in The Core (Swindon) Ltd UT/2019/0049, Revenue and Customs Brief 6 details HMRC's position on the VAT treatment of supplies of juice cleanse programmes.

When deciding how to treat supplies, HMRC accepts that products designed specifically as complete meal replacements can be zero-rated as food, rather than being treated as a standard rated beverage.

In deciding the correct treatment, the Upper Tribunal confirmed that the manner in which a product is marketed is potentially relevant. Each case must be decided on its own facts.

https://www.gov.uk/government/publications/revenue-and-customs-brief-6-2021-vat-liability-of-juice-cleanse-programmes

R&C Brief 7 (2021): Charging of electric vehicles (Lecture B1261 – 23.09 minutes)

Revenue and Customs Brief 7 confirms that supplies of electric vehicle charging through charging points in public places are standard rated and that a reduced rate of VAT applies for 'de minimis' supplies if the supply is ongoing to a person's house or building, and less than 1000 kilowatt hours a month.

The Brief also explains that businesses can recover the input tax for charging electric vehicles as follows:

- Sole traders can recover the input tax for charging an electric vehicle at home or at other places where the charging is for business use;

- VAT when employees charge an electric vehicle at home for business use cannot be recovered as the supply is made to the employee and not to the business;

- VAT on employees charging an employer's electric vehicle used for business and private use at the employer's premises can be recovered on the business element of the input tax suffered in one of two ways, provided the employee keeps a record of business and private mileage:

    1. Recover the full amount of VAT for the supply of electricity used to charge the electric vehicle and record an output tax charge (deemed supply) on the amount for private use; or

    2. Recover VAT on the business element only.

https://www.gov.uk/government/publications/revenue-and-customs-brief-7-2021-vat-liability-of-charging-of-electric-vehicles

R&C Brief 8 (2021): public funds received by further education institutions

R&C Brief 8 (2021) has been issued following the Upper Tribunal's decision in Colchester Institute Corporation v HMRC [2020] UKUT 368 (TCC) that concerned the treatment of money received from government funding agencies to fund the provision of education to 16–19-year-old students.

Although HMRC is not appealing this part of the decision (because it won on other grounds), it has not changed its policy view that that monies received by these institutions are grants and the activity funded is a supply that is outside the scope of the VAT. HMRC is seeking to challenge the decision through another appeal.

In the meantime, HMRC will not impose the decision on any other education providers, but institutions can choose to apply it by submitting error correction notices. Such institutions should be aware that HMRC will protect its position to secure tax revenues pending the outcome of the new appeal.

https://www.gov.uk/government/publications/revenue-and-customs-brief-8-2021-vat-treatment-of-public-funds-received-by-further-education-institutions

Land and property exemption simplification

HMRC is seeking opinions on the existing VAT rules relating to land and property and their simplification. The call for evidence closes on 3 August 2021.

As well as the proposal set out by HMRC, other suggestions are welcome, including those that have become possible following Brexit.

The OTS had previously highlighted a number of potential options for simplifying the VAT treatment of land and property. However, problems were identified with each of these options, and as a result they were rejected by the OTS in the report. Nevertheless, HMRC is still seeking views on these options:

- Removing the ability to opt and making all relevant transactions exempt;
- Removing the option to tax and making all land and property taxable at a reduced rate;
- Making all commercial land and property taxable at the standard rate with an option to exempt.

Further, HMRC are considering making all short-term interests in property taxable and simplifying VAT on land by making most supplies subject to VAT, while exempting specific supplies.

VAT Liability linked to Land Registry

A further option which could provide certainty for businesses is to link the VAT liability of supplies of land and property interests to those that have been registered with the relevant Land Registries in England, Scotland, Wales and Northern Ireland:

If it was decided that interests registered in a Land Register were to be exempt from VAT, then any interest in land not registered with a relevant Land Registry would be taxable by default.

Alternatively, interests registered with the relevant Land Register could be taxable, thereby making any interests in land that are not so registered exempt from VAT.

Either of the above could still be subject to exceptions to ensure certain interests always remained taxable or exempt.

This would provide greater certainty of the VAT liability of land transactions, by reference to an independent and publicly accessible record and reduce the scope for disputes.

https://www.gov.uk/government/consultations/call-for-evidence-simplifying-the-vat-land-exemption/simplifying-the-vat-land-exemption-call-for-evidence

Management charges to foreign subsidiaries (Lecture B1261 – 23.09 minutes)

Summary – A holding company recharging management services to its subsidiaries through a loan account that remained unpaid was an economic activity supplied for consideration.

Tower Resources plc is a UK holding company. Its business is to acquire licences to explore for and produce oil and gas in Africa. These operations generally take up to 10 years before the first production of oil and are far from certain to succeed, with only about 20% of ventures operating on a commercially viable basis.

The activities are operated through local foreign subsidiaries, with the parent company funding the subsidiaries management, logistical and technical services. Tower Resources plc suffered input tax on invoices from UK companies which were passed on to its subsidiaries with a 5% mark up as part of their management fees.

Tower Resources plc believed that these management charges fell under the general B2B rule for services, making them outside the scope of VAT as the services were provided outside the UK. The management services invoiced were charged through intercompany loan accounts, that were technically repayable on demand, but at the time of the appeal had not been repaid.

Input tax suffered by Tower Resources plc on supplying the management services was reclaimed on the basis that the services would be subject to VAT if they had been supplied to a UK based entity. HMRC accepted that the UK invoices to Tower Resources related to genuine supplies and that there an economic activity existed but disallowed £1.45m of input VAT, arguing that the company was not making taxable supplies for consideration to its subsidiaries.

On appeal, HMRC provided an alternative argument that if Tower was making taxable supplies, then it was not doing so in the course of an economic activity.

The First Tier Tribunal had found that the management services were supplies for consideration and that those supplies were an economic activity and so the company was able to recover the input tax claimed.

HMRC appealed to the Upper Tribunal.

Decision

The Upper Tribunal concluded that there was a genuine business activity and that a parent funding its subsidiaries' activities through debt was normal commercial practice. It did not matter that the loans remained unpaid.

The Upper Tribunal disagreed with HMRC, concluding that the supplies were made for consideration. The fact that both parent and subsidiaries knew that the loans would only be repaid if the subsidiaries had the funds did not break the direct link between supply and consideration. In fact, the Upper Tribunal stated that, in their view, there was nothing that stated that there could be no consideration if the payment of contractual consideration was subject to any contingency at all.

Further, the Upper Tribunal confirmed that a holding company providing administrative, financial and technical services to its subsidiaries for consideration constituted economic activity.

HMRC's appeal was dismissed.

Tower Resources plc v HMRC [2021]UKUT 123 (TCC)

Charity cancels registration **(Lecture B1261 – 23.09 minutes)**

Summary – The charity was making exempt supplies of education or vocational training and supplies made by the restaurant were closely related to that exempt supply. Registration could be cancelled.

Step By Step (Northern Ireland) Limited is a registered charity which had registered for VAT back in 2011.

The charity provides training for people with learning difficulties and was funded by grant payments from Southern Regional College. No fees were charged to students. As part of this training, the charity runs a restaurant on its premises that is open to the public and is staffed by students. On the website of the Charity Commission for Northern Ireland, it states "Step by Step NI Ltd operates the One Eighty Degrees Restaurant as a not-for-profit social enterprise. The restaurant is used as a training environment for young people with learning disabilities to give them the qualifications, skills and experience to gain meaningful employment in the hospitality industry…".

In 2018, the charity applied for its VAT registration to be cancelled on the basis that it did not make any taxable supplies, but rather exempt supplies of education.

HMRC refused the application, on the basis that the supplies of education and vocational training made were outside the scope of VAT, and not exempt, as the supplies made were not closely related to any supply of education or vocational training in any event.

Decision

The First Tier Tribunal stated that, under Sch 9 Group 6 VATA 1994, supplies of education and vocational training are exempt from VAT if provided by an 'eligible' body. A charity is an eligible body in this context.

In Brockenhurst College(C-699/15) [2017] STC 1112 it was decided that restaurant meals produced by students for the public qualified as exempt from VAT if the main supply of education was also exempt, making the meals 'closely linked' to the education.

The First Tier Tribunal concluded that the provision of training by Step By Step (Northern Ireland) Limited was an exempt supply of education or vocational training. Further, the supplies made by the restaurant were closely related to that exempt supply and so were accordingly exempt.

The charity no longer needed to be registered for VAT and HMRC's refusal to cancel that registration was unreasonable.

The appeal was allowed.

Step By Step (Northern Ireland) Limited v HMRC (TC08038)

Assessments out of time but penalties upheld (Lecture B1261 – 23.09 minutes)

Summary – Assessments for VAT periods 10/15 to 04/17 were within the statutory time limit but the assessments for periods 08/10 through to 07/15 were made more than one year after evidence of facts, and so were out of time. However, all penalties were upheld.

Albany Fish Bar Limited runs a fish and chip shop and Waseem Akhtar is the Company's director and shareholder.

Having visited the company's premises in July 2016, HMRC established that the Company had been systematically excluding lunchtime sales from its VAT returns. Consequently, in August 2017, HMRC issued "best judgement" assessments under s73(1) VATA 1994, charging the Company VAT of nearly £110,000 for VAT quarters 08/10 to 04/17,

In the same month, HMRC issued the Company with a penalty of just under £88,000 on the basis that the behaviour had been deliberate and concealed. Later, in January 2018, HMRC issued a personal liability notice making Waseem Akhtar liable for 100% of the penalty on the basis that the inaccuracies were attributable to him.

The Company appealed the assessments and the penalty, and Mr Akhtar appealed the personal liability notice. The appeals were joined by the Tribunal on 18 March 2018.

Decision

The First tier Tribunal agreed that the company had been deliberately suppressing its lunchtime sales for VAT periods 08/10 to 04/17; that this behaviour was deliberate and concealed, and that the inaccuracies were attributable to Mr Akhtar.

The First Tier Tribunal considered whether the assessments had been made in time. Under s73(1) VATA 1994 assessments “shall not be made later than” the time limits set out in VATA s 73(6), namely:

> “(a) 2 years after the end of the prescribed accounting period; or
>
> (b) one year after evidence of facts, sufficient in the opinion of the Commissioners to justify the making of the assessment, comes to their knowledge.”

The Tribunal concluded that in relation to VAT periods 10/15 to 04/17, the assessments were within the time limit but that the assessments for periods 08/10 through to 07/15 were made more than one year after evidence of facts, and so were out of time.

Moving on to the penalties, the First Tier Tribunal did not reduce the penalties relating to the out-of-time periods. The Tribunal stated that a penalty is payable if a person gives HMRC a VAT return which “contains an inaccuracy which amounts to or leads to…an understatement of a liability to tax”. The Company was liable to a penalty under Sch 24 because it had deliberately submitted VAT returns which contained inaccuracies for all periods from 08/10 through to 04/17. The Tribunal went on to say that it is well-established that “liability does not depend on assessment” (see Whitney v IRC [1926] AC 37), so the fact that some of those correcting assessments had been set aside did not change the Company’s liability to a penalty.

Finally, the Tribunal found that Waseem Akhtar was responsible for the inaccuracies and that 100% of the penalty so calculated was payable by him.

Albany Fish Bar Limited and Waseem Akhtar v HMRC (TC8083)