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CONTENTS

Personal tax

Employee or self-employed? (Lecture B1256 – 16.27 minutes)

Summary – Determining his own working practices and remunerated on a commission basis, the taxpayer was not an employee but rather, in business on his own account.

C&G is a broker providing niche bespoke insurance products. Having worked at developing a medical malpractice product with an unrelated company, in May 2010 C&G decided to develop the product itself. This involved identifying an insurer who was prepared to underwrite the scheme and reach a binding authority agreement (a "binder") with that insurer as to the relevant terms. When a surgeon purchased a policy, C&G would receive a commission on that policy.

C&G did not have the contacts or experience themselves to identify potential insurers or negotiate the terms of a binder and so the company engaged with Gareth Phillips, who had both the experience and contacts required and had been involved with the project from the start.

Gareth Phillips had identified Newline as an insurer interested in underwriting the scheme. He negotiated the terms of a binder with them months and notified C&G that he had secured an agreement with Newline, which C&G signed off on. C&G only became involved once the terms were largely agreed. The terms included a key man clause, which provided that Newline had the right to terminate the contract if Gareth Phillips ceased to be an employee or director of C&G.

No business was written under this binder with Newline and in March 2011 Newline terminated the agreement. Gareth Phillips negotiated a binder with another insurer, AmTrust. Some business was written under that scheme, that generated commissions for C&G in early 2012. However, around May 2013 AmTrust terminated the agreement and C&G and Gareth Phillips parted company.

Although there was a draft Contract for Services and an Employment Contract, there was no signed written contract between Gareth Phillips and C&G. A number of possible relationships between the two parties were considered at various times.

This case relates to the period from 28 May 2010 to May 2013. On 10 October 2011, Gareth Phillips wrote to HMRC stating that he had experienced difficulty in obtaining his P60 from his previous employer, C&G, which he needed to complete his self-assessment return.

HMRC wrote to C&G who responded by stating that Gareth Phillips had never been employed by them. On 9 December 2011 HMRC notified Gareth Phillips that the matter had been passed to a "Status Inspector" to consider his employment status. Later, C&G confirmed that Gareth Phillips had been self-employed, paid on a tiered commission basis with no salary entitlement.

Gareth Phillips made a claim for unfair dismissal, breach of contract, holiday pay and unlawful deductions. That appeal was heard by the Employment Tribunal and was struck out. He was found to be neither an employee nor a worker of C&G.

HMRC subsequently assessed him as self-employed.

Gareth Phillips appealed to the First Tier Tribunal.

Decision

The First Tier Tribunal acknowledged that Gareth Phillips had expertise and experience in the insurance industry, and in developing medical malpractice insurance products.

The Tribunal found that although C&G were prepared to offer an employment contract to Gareth Phillips, he did not accept the contract. In fact, he was reluctant to commit to any option. An email exchange in December 2010 contained the terms which were agreed between the parties and those terms (commissions, bearing a share of operating costs, recovery of amounts already paid, retention of IP rights) were consistent with self-employment. The agreement did not include a separate or additional right to salary on top of the commission arrangements. He did not receive regular wages, but rather irregular payments without payslips.

Gareth Phillips had argued that FSA rules required that he could only operate in this field under the umbrella of C&G's authorisation as an employee of C&G. However, with no sight of these FSA rules, the Tribunal rejected this argument.

The Tribunal considered the key man clause requiring that Gareth Phillips be an employee or director of C&G but rejected its relevance. There was no evidence provided that the binder with Newline was signed and further, no business was ever entered in to under that binder.

Although Gareth Phillips did not have PII in his own right and appeared to be within the scope of that of C&G, again no evidence as to the terms of C&G's coverage was provided. The Tribunal placed little weight on this factor.

The Tribunal found that Gareth Phillips was self-employed:

- He set his own working hours, arranged appointments with insurers and potential clients. There was little reporting back to C&G and what was reported was on an irregular basis;
- He negotiated the terms of the binders with insurers;
- He was remunerated on a commission basis and had received advance payments on account of future expected commissions. He did not receive regular payments by way of salary, or any payslips;
- He retained the IP rights in the insurance product.

Gareth Phillips was performing his activities as a person in business on his own account.

Gareth Phillips v HMRC (TC08074)

No PAYE credit

Summary – The First Tier Tribunal had no jurisdiction to determine whether the taxpayer was entitled to a PAYE credit. Further, the transfer of assets abroad provisions did not apply as the individual's income from abroad was nil.

Stephen Hoey is a UK-based IT contractor who operated through intermediaries based offshore, initially in the Isle of Man and later through a second company based in Guernsey. These employers provided Stephen Hoey's services to UK end users, paying him a basic wage for this work, with tax paid in full by the employers. In addition, the employers made contributions to Employee Benefit Trusts which in turn made interest free loans to Stephen Hoey and other employees. These arrangements were disclosed to HMRC under the DOTAS legislation.

HMRC issued discovery assessments for 2008/09 and 2009/10 and a closure notice for 2010/11, exercising their discretion under s.687(7A) to transfer the PAYE tax burden from the employers to Stephen Hoey.

Following the Supreme Court's decision in the Rangers case (RFC 2012 Plc (in liquidation) (formerly The Rangers Football Club Plc) v Advocate General for Scotland [2017] UKSC 45), shortly before the First Tier Tribunal hearing, Stephen Hoey conceded that the payments into the trust were taxable employment income subject to PAYE under s62 ITEPA 2003.

With his employers based outside the UK, s710(20(b) ITEPA 2003 provided it was the UK end users who were liable for PAYE on the employment income. However, HMRC took the view it was not appropriate to hold those end users liable for the PAYE as they knew nothing of the arrangements that existed to avoid tax. Instead HMRC sought to collect the tax from Stephen Hoey, with no credit for PAYE. HMRC argued that the First Tier Tribunal had no jurisdiction to deal with the PAYE credit.

Stephen Hoey appealed to the Upper Tribunal, disputing the discretion HMRC exercised under s684(7A) ITEPA 2003. He argued that the employer's obligation to deduct PAYE was given by the PAYE regulations and that the First Tier Tribunal should have given him credit for PAYE deducted.

HMRC had also argued that the assessments and closure notice raised a charge under the Transfer of Assets Abroad regime. Given Stephen Hoey's concession on the employment charge, the First Tier Tribunal had not considered it strictly necessary to deal with this argument but nevertheless went on to analyse it. The Tribunal concluded that the income charged under regime was nil (once the amounts the offshore employers received were offset by the sums the employers paid out in remuneration). HMRC argued that the First Tier Tribunal had erred in law in reaching their decision.

Decision

The Upper Tribunal stated that it is only Self Assessment and assessment provisions that are relevant sources of the First Tier Tribunal's jurisdiction. Having considered the Self Assessment legislation contained within the Taxes Management Act 1970 and the PAYE regulations, the Upper Tribunal concluded that the PAYE credit did not alter the tax arising on the assessable income and was a matter of tax collection, not Self Assessment. Consequently, the First Tier Tribunal had no jurisdiction in this matter and Stephen Hoey was not entitled to a PAYE credit.

The Upper Tribunal found that the First Tier Tribunal had erred in finding that it did not need to deal with the Transfer of Assets Abroad issue. However, it was correct that the amount of income transferred offshore was nil, and that Stephen Hoey's motive was not tax avoidance

Stephen Hoey v HMRC [2021] UKUT 0082 (TCC)

Making the most of company pension contributions (Lecture P1256 – 21.38 mintes)

The low salary/ high dividend extraction route adopted by many owner-managed businesses results in their own personal pensions contributions being restricted to their earned income. This is normally no more than the personal allowance.

It should be remembered that company pension contributions are not restricted to the individuals earned income and this is often an efficient way of increasing pension input. When you factor in the corporation tax relief on the company contribution this is a very efficient way of extracting profit from an owner managed business.

Example

Consider a company with £300,000 of pre-tax profit that makes a corporate pension contribution of £10,000.

The company currently obtains £1,900 of corporation tax relief, but this will increase to £2,500 if paid on or after 1 April 2023.

But what is the effective rate of extraction?

Once eligible to withdraw money from their pension fund at 55, the individual can withdraw 25% tax free i.e. £2,500 if we assume the fund value remains the same. The balance of £7,500 can be drawn down in retirement when the client is a basic rate taxpayer resulting in income tax of £1,500 on the £7,500. Overall the taxpayer will suffer £1,500 tax on a £10,000 extraction from their pension fund. An extraction rate of 15% is attractive but when we factor in the corporation tax relief of 19% we have a negative tax rate on profit extraction.

Going forward company pension contributions will become even more attractive as corporation tax rates increase.

Deferring pension contributions?

Consider a company that consistently pays £40,000 pa into the directors' pension fund.

Corporation tax relief is given when the pension contributions are paid so we could consider accruing director pension contributions in the years to 31 March 2022 and 2023 (to maintain a smooth effect on distributable profit each year) with a view to paying the accrued contributions in April 2023. The corporation tax relief from 1 April 2023 would be 25% when profits exceed £250,000 or 26.5% when profits are between £50,000 and £250,000. The extra corporation tax relief could be between £4,800 and £6,000 on £80,000 of contribution.

Although the individual loses the growth on £40,000 per annum, the company gets a guaranteed saving. It should also be noted that the growth is by no means guaranteed as pension funds can go up or down during this time.

Delaying the payment could also help companies that are cash poor at present.

Accruing contributions in the accounts

To accrue £40,000 annual contributions in the accounts the company must follow the provisions of IFRS, FRS 102 or FRS 105.

These are all essentially the same and require:

- A legal or constructive obligation to make the contribution;
- That it must be probable that payment will be made, although timing can be variable; and
- A reliable measurement of the accrued amount can be made

It is the first condition that might cause problems. In practical terms, a specific clause in a contract of employment should suffice. For instance, the company would need to be obliged to pay a pre-agreed sum as a contribution, either as a fixed percentage of salary or fixed amount. The key is that it must not be in any way discretionary.

But most directors of family businesses do not have an employment contract. In these instances a pre year end board minute should suffice where the contribution is communicated to the director pre-year end.

Contributed by Dean Wootten

Enhanced protection late application **(Lecture P1256 – 21.38 mintes)**

Summary – Relying on advice given, the taxpayer had a reasonable excuse and was allowed to claim an enhanced lifetime allowance for his pension despite applying late.

In 2003, Maurice Gammell retired from his main role as managing director of Harry Ramsden, the fish-and-chip shop chain and seven years later he retired from all work.

In 2001, he had appointed financial advisors to advise on his pensions and investments but received no advice about enhanced protection in 2006 from those advisors or subsequently. When his named advisor changed in 2009 following illness, enhanced protection was still not brought to his attention. Further, he was not advised about the 2012 Fixed Protection Limit of £1.8m.

In August 2013, he was advised to apply for and received the 2014 Lifetime Allowance of £1.5m.

On 13 October 2015 a prospective new advisor alerted him to the failure to apply for:

- enhanced protection in 2009; and
- fixed protection in 2012.

Maurice Gammell took up the omissions with his existing advisors in December 2015, but by April 2016 he considered that there had been no progress in attempting to resolve the issue and so terminated their engagement.

Through his former advisor's complaints procedure, he was finally informed on 12 August 2016 that there was the possibility of applying for enhanced protection out of time. Maurice

Gammell sought additional information which was provided by specialist consultants. The application was submitted on 19 December 2016.

It was not until 11 December 2018 that HMRC notified their decision to refuse the late application. HMRC accepted that Maurice Gammell had a reasonable excuse for the delay until 2015, but not for the 14-month gap that followed, leading up to the late application.

Decision

Problems with his professional advisers, including following their complaints procedure, constituted a reasonable excuse for that period. Maurice Gammell had acted promptly and reasonably once he had cause to believe that he faced serious unexpected problems. It was reasonable for him to rely on his existing advisors and engage in their complaints process.

The First Tier Tribunal accepted the late application.

The appeal was allowed.

Mr Maurice Gammell v HMRC (TC08035)

High income for child benefit charge (Lecture P1256 – 21.38 mintes)

Summary – Although penalties were cancelled in respect of two tax years, they could not be cancelled for the third as by then the HMRC claim form was much clearer and the taxpayer had clearly breached the relevant limit.

Jonathan Hayden was a member of the sales team of his employer and earned a base salary and bonus depending on sales.

In 2012/13 when the High Income Child Benefit Charge (HICBC) was introduced his earnings were £44,403 so below the £50,000 threshold for the charge to kick in.

HMRC's electronic record of correspondence indicates that in August 2013 Jonathan Hayden was sent a letter informing him of the new charge but he had no recollection of receiving it. He explained that had he received it, he would likely have paid it next to no attention as he was earning less than £50,000 a year at the time and he had a lot on his plate as his first child had just been born.

His wife claimed the child benefit allowance. He stated that if his wife had asked him about his salary before she made the claim, he would have said he did not have a salary in excess of £50,000. His taxable income was only more than £50,000 when his bonuses and car benefit were included and pension contributions are disregarded.

His base salary for each of the years 2014/15 and 2015/16 was below £50,000 but rose above that level in 2016/17.

HMRC claimed that they sent two letters to Jonathan Hayden regarding the HICBC. Firstly, a generic letter concerning liability to pay HICBC and what must be done to avoid a liability to penalty in respect of the year 2016/17, and then a "final reminder" letter sent on 30 October 2018.

Neither of these letters was received as his father, a former HMRC officer acting as his agent, had had moved home but this change of address had not been notified to HMRC.

On 11 January 2019 HMRC wrote, advising Jonathan Hayden that he had a liability to pay HICBC in respect of the years 2014/15, 2015/16 and 2016/17.

Liability to pay the HICBC was accepted along with interest, but as Jonathan Hayden had no knowledge of the HICBC and HMRC had not been in touch with either him or his agent to raise an enquiry into any return, his father sought a reconsideration of any penalty and enclosed an article which had been published in a newspaper indicating that HMRC were undertaking a review of penalties imposed in 35,000 cases for failure to notify liability to HICBC where the taxpayers had received no prior notification of the charge.

The father could not understand why HMRC would write, as they say they did, in 2013 and not follow up within 30 days as they are required to do when making enquiries. To wait for more than four years to raise the issue of liability was extraordinary.

Decision

The First Tier Tribunal noted that the HICBC was a novel form of tax. It was not income tax. Its operation could involve a charge to tax or a disclaimer of a benefit. Further, there had been misleading headlines and articles in the press.

The First Tier Tribunal accepted that Jonathan Hayden had a reasonable excuse for the first two years, 2014/15 and 2015/16, and cancelled the related penalties. The Tribunal accepted that the original claim form, completed after the birth of their first child in 2013/14, was unclear. Further, HMRC recognised that the need to file a Self Assessment return due to HICBC was possible only when taxpayers were aware of their obligations. The Tribunal concluded that it was unrealistic to expect employees with no other sources of income, where their employers were administering their tax, to be monitoring HMRC's website to see if there was a new obligation to file a return.

The Tribunal concluded that Jonathan Hayden did not have a reasonable excuse for 2016/17 as by then the form was more clearly written. The 2016 claim form, completed after the birth of their second child, stated that the claimant or their spouse must file a Self Assessment tax return where income of one of them exceeds £50,000, whereas the 2013 form spoke of the possibility that income may need to be declared. The Tribunal did not accept ignorance after the birth of his second child as a reasonable excuse in the light of the very clear statement in the notes to the 2016 Child Benefit claim form and the fact that Jonathan Hayden had changed jobs and his new base salary was in excess of £50,000 in 2016/17.

The appeal was allowed in part.

Jonathan Hayden v HMRC (TC08037)

Property losses and personal allowances (Lecture P1256 – 21.38 mintes)

Summary – Property losses brought forward are set off against future property income prior to the deduction for a taxpayer's personal allowance.

Sarah Duncan had realised some £16,000 of property losses in 2007/08, 2008/09 and 2012/13.

She made property profits as follows:

2009/10	£5,037
2010/11	£969
2011/12	£3,001
2013/14	£7,056
2014/15	£4,992
2015/16	£2,277
2016/17	£2,132
	£25,464

She submitted her 2017/18 tax return and included a claim to use a property loss brought forward of £6,017 from previous years. In February 2019 HMRC gave notice of an enquiry into this return, indicating that they were looking into the use of the losses.

On 28 June 2019 HMRC sent a revised tax calculation showing additional tax payable of just over £1,800, stating that all of the property losses previously realised had already been offset against property income in earlier years (S23 ITA 2007). A closure notice to that effect was issued a month later.

Sarah Duncan appealed, arguing that the correct approach was to use reliefs and allowances in such a manner as to maximise the benefit to the taxpayer. Adopting her approach, her property losses had not been used in prior years as the property profits were covered by her personal allowances. Relieving the losses in earlier years would have wasted her personal allowances.

Decision

The First Tier Tribunal agreed with HMRC.

Under s23 ITA 2007, the steps to follow when claiming relief must be followed in the order laid out in the legislation. Consequently, at step 2, the brought forward property losses should be deducted prior to the taxpayer’s personal allowance, which is deductible at step 3.

The taxpayer's appeal was dismissed.

Sarah Duncan v HMRC (TC08066)

Capital taxes

'Just and reasonable' or not? (Lecture P1257 – 10.59 minutes)

In FA 2008, the previous taper relief regime for CGT was replaced by entrepreneurs' relief (now renamed business asset disposal relief). One of the key differences between the tax treatment for the two types of relief was where, over a period of ownership, property such as a shareholding was classified as both a qualifying and a non-qualifying asset.

Under taper, there were two categories of relief:

1. business asset taper relief (BATR); and
2. non-business asset taper relief (non-BATR),

with the former attracting a more generous deduction than the latter. If an asset was entitled to receive both BATR and non-BATR over its holding period, any gain on a disposal had to be split between the two components. One part of the gain was reduced by BATR, while the other part was reduced by the less advantageous non-BATR.

The legislation for business asset disposal relief has a completely different modus operandi. Provided that an asset qualifies over a requisite period (which nowadays represents the last two years of ownership), business asset disposal relief is available. This involves the application of a special 10% CGT rate to the gain. However, if the relevant requirements are not met, there is no relief and the normal rate of CGT is in point (which, in most cases, will be 20%).

It should be appreciated that the present system offers better tax planning possibilities. If an asset such as shares in an unlisted trading company does not currently attract business asset disposal relief (perhaps because the owner is not an officer or employee), it may be a relatively straightforward matter to put this right. If the requisite waiting period is then satisfied, full relief is available on an unrestricted basis when the shares are sold, despite the fact that they may have previously had non-qualifying status for several years. This contrasts with the taper relief rules described above.

The Upper Tribunal decision in Lee v HMRC (2020) had to consider the mechanism for splitting gains where both BATR and non-BATR applied. The taper relief provisions, which are of course no longer with us, were found in Sch A1 TCGA 1992. Of particular relevance were:

- Para 3 Sch A1 TCGA 1992; and
- Para 21 Sch A1 TCGA 1992.

Para 3 Sch A1 TCGA 1992 set out the basic approach to be adopted where BATR and non-BATR were applicable. The gain on the asset's disposal had notionally to be divided into a business asset gain and a non-business asset gain in proportion to the periods during which the asset was, and was not, a business asset. The appropriate taper relief percentages were then applied to the respective part gains as if those gains had arisen on separate assets held throughout the overall period of ownership. In other words, straight-line time-apportionment was the name of the game.

If Para 21 Sch A1 TCGA 1992 applied, the division had to be done on a 'just and reasonable' basis. However, this phrase was not defined in the legislation and HMRC's Capital Gains Manual provided no real guidance on how such an apportionment should be effected.

The question which the Lee case had to determine was: which of these two provisions took precedence?

In this dispute, the taxpayer (L) disposed of a shareholding on 12 March 2003 which was classed as a non-business asset from 6 April 1998 (when taper relief started) up to 5 April 2000 but as a business asset from 6 April 2000 up to 12 March 2003. L argued that most of his gain should be attributed to the second period which attracted a much more favourable deduction on the ground that there had been what the case report calls 'a dramatic increase in the value of the shares after April 2000'. L was invoking the 'just and reasonable' principle.

HMRC, on the other hand, contended that the statutory rule in Para 3 Sch A1 TCGA 1992 was essentially prescriptive. That is to say, a time-based formula had to apply.

The Upper Tribunal agreed with HMRC's reasoning. The judges said that the only circumstances in which Para 21 Sch A1 TCGA 1992 would be relevant were where there had to be an allocation because, for example, an asset used in a seasonal business would not, by definition, be used through the whole tax year. But these situations would be very limited. Effectively, therefore, Para 3 Sch A1 TCGA 1992 ruled the roost.

The judges also pointed out that any other interpretation would mean that Para 3 Sch A1 TCGA 1992 could almost always be overridden since it was very unlikely in practice that a gain would arise on an absolute straight-line basis over time.

L lost his case. Although taper relief was abolished as long ago as 2008 so that there are unlikely to be further cases coming before the Tribunals on this point, it should not be overlooked that there are other instances in the CGT code where there is a time-apportionment rule and so the Lee decision could still be significant.

Contributed by Robert Jamieson

Buy back was a distribution

Summary – When a company purchased its own shares, this was not treated as part of a wider arrangement and so the taxpayer was treated as receiving a deemed distribution that was liable to income tax of £600,000. It did not matter that the proceeds from the buyback were used to repay the loan taken out to purchase those shares from the original shareholders.

Bostan Khan had acted as management accountant of Computer Aided Design Ltd for many years.

The company's owners want to sell their company but failed to negotiate a sale. In order to extract the funds and wind up the company tax efficiently, they approached Bostan Khan for his help. They were aware that if they extracted funds as a pre-sale dividend or purchase of own shares there would be a large income tax liability.

Bostan Khan bought all 99 shares in the company from the shareholders for £1.95 million in cash using money that he had borrowed and then sold all but one share back to the company and repaid the loan.

HMRC raised a £600,000 income tax assessment on the £1.95 million treating the buy back as a distribution of the company's assets.

Bostan Khan had originally argued that:

1. it was a trading transaction with the aim being to wind up the company – he had owned the shares for less than an hour; it was effectively the company that had financed the deal; or

2. he should be taxed on the substance of the composite transaction, which was that he had received just one share and that the original shareholders had effectively received the proceeds.

Both First Tier and Upper Tribunals dismissed Bostan Khan's appeal, and case moved to the Court of Appeal on point 2. only.

Decision

The Court of Appeal agreed with HMRC and dismissed the appeal stating:

> "*This is a cautionary tale, which illustrates all too graphically the importance of seeking specialist tax advice before entering into commercial arrangements that might have adverse tax consequences, however remote that risk might appear.*
>
> *It is impossible not to feel some sympathy, for the appellant, Mr Khan, who was held liable to pay income tax of almost £600,000 on £1.95 million that was paid into his bank account and then paid out again almost immediately in respect of connected share sale and buy-back transactions. Yet he found himself in that situation because he relied upon an assumption that the consequence of his having to expend the £1.95m as soon as it was received, was that the persons to whom he paid it would be liable to pay tax on it instead of him.*"

The Court of Appeal agreed with the Upper Tribunal that under s385 ITTOIA 2005, the person liable to tax on the distribution was the person who received the distribution from the company. Mr Khan benefitted from the distribution as it enabled him to repay the loan.

The judge concluded:

'The vendor shareholders were entitled to a sum of £1.95m in respect of the sale of their shares to Mr Khan, not to the distribution in respect of the shares which the company bought from him.'

The taxpayer's appeal was dismissed.

Bostan Khan v HMRC [2021] EWCA Civ 624

BPR and surplus cash in the company (Lecture P1258 – 12.34 minutes)

BPR and company shares

Business property relief (BPR) applies to various form of 'relevant business property' for inheritance tax (IHT) purposes, including shares in an unquoted company.

The shares are not relevant business property if the company wholly or mainly carries on certain excluded activities, i.e. dealing in securities, stocks or shares, land or buildings or making or holding investments (IHTA 1984, s 105(3); all references are to IHTA 1984).

These exclusions are subject to certain exceptions (in s 105(4), (4A)), including where the company's business consists wholly or mainly in being a holding company of a group of companies whose business does not consist of excluded activities.

Is it 'excepted'?

If BPR applies, the value of relevant business property on which BPR is available is subject to a restriction in respect of the value of excepted assets.

The legislation in s 112 ('Exclusion of value of excepted assets') provides that an asset is an 'excepted asset' unless it satisfies at least one of two alternative tests (in s 112(2)):

> *"(2) An asset is an excepted asset in relation to any relevant business property if it was neither—*
>
> *(a) used wholly or mainly for the purposes of the business concerned throughout the whole or the last two years of the relevant period…, nor*
>
> *(b) required at the time of the transfer for future use for those purposes;"*

'Past use' test

The 'relevant period' in s 112(2)(a) above is either the two years immediately preceding the transfer of value in question, or the whole period of ownership if less than two years.

Thus (for example) a trading company may use surplus cash to acquire assets wholly or mainly for business purposes (e.g. plant and machinery), even if the acquisition takes place shortly before a transfer of shares in the company (on which BPR is claimed).

'Future use' test

If a trading company has (say) a large credit balance on its bank account, how much (if any) of that cash balance is 'surplus'? The 'future use' test in IHTA 1984, s 112(2)(b) can cause difficulties in practice.

For example, in *Barclays Bank Trust Co Ltd v IRC* [1998] STC (SCD) 125, the deceased held 50% of the shares in a company carrying on an old established trade of selling bathroom and kitchen fittings. It had a strong cash position. At the time of the deceased's death, the company held over £450,000 in cash. The Inland Revenue (as it was then) accepted that £150,000 was needed by the company at that time but maintained that the remaining £300,000 was an excepted asset.

The Special Commissioner upheld the Revenue's view, rejecting the argument that the cash was required for the future purposes of the businesses. The appeal was dismissed.

HMRC's view: Or is it?

If an asset is not 'caught' by one (or both) of the 'past use' and 'future use' tests, it is not an excepted asset, and BPR is not restricted on that basis. However, at the time of writing, HMRC guidance in its Inheritance Tax manual states (at IHTM25341):

'In broad terms IHTA84/S112 relates only to the assets used in the business and it makes them excepted assets… (i.e. it excludes them from relief) unless

- they were used wholly or mainly for the purposes of the business throughout the whole or the last two years of the relevant period, and

- they are required for future use for those purposes.'

The key word here is 'and'. It means that an asset would need to escape being caught by both the 'past use' and 'future use' tests to prevent being categorised as an excepted asset. The HMRC guidance does not appear to accord with the legislation. This point has been brought to HMRC's attention, but the guidance has not yet been changed.

Is it 'surplus'?

In practice, whether cash is 'surplus' will depend on the particular circumstances in each case. Factors to consider include the following:

1. Every trading company needs working capital. For example, in the *Barclays Bank Trust* case, the undisputed amount of cash needed by the company represented roughly 25% of its turnover.

2. Seasonal businesses will often hold substantial cash at certain times of the year.

3. Business owners may retain a higher proportion of funds during difficult trading conditions (not least due to the reluctance of banks to provide working capital in some cases).

4. To the extent that cash is surplus, the business may apply those funds in (for example) paying trade creditors or discharging other liabilities of the business.

5. The surplus cash could be used towards separate investment business activities. However, extreme care should be taken to ensure that the investment business activities do not predominate; otherwise, BPR may be lost entirely (IHTA 1984, s 105(3)).

6. If cash has been earmarked for future business use, clear evidence should be maintained of its intended use.

Contributed by Mark McLaughlin

Goodwill versus trade related property (Lecture P1256 – 21.38 mintes)

Summary - The valuation of property-based goodwill, where the profitability of two care homes was tied to the properties from which they were run, resulted in no SDLT being payable.

Dr Zyrieda Denning acquired the freehold interest in Manor Place Nursing Home together with the business operating therefrom in April 2000 for £499,000. In March 2001, she also acquired the business operating from Maple House Nursing Home and subsequently bought the freehold interest in the property in June 2006 for £1m.

The care homes were initially operated by Dr Denning acting as a sole trader. Having set up companies, in 2011, Dr Denning transferred one care home to each company with an agreement that the transfers were transfers as going concerns in consideration including goodwill.

Retaining the freehold interest in both Manor Place and Maple House, Dr Denning granted leases over the properties with no premium payable. The leases were for 5 years at an annual rent (without review) of £225,000 for Manor Place and £175,000 for Maple House. Under RICS guidance the leasehold interests were valued at a combined £1,200,000.

Deeds of assignment of the goodwill of the businesses from Dr Denning to the companies were for consideration of £1,125,000 and £675,000 respectively.

HMRC argued that the value goodwill was inherent in the property, making it inseparable from the value of the leases. HMRC raised SDLT discovery assessments against the companies in respect of the lease interest acquisitions.

Dr Denning and the companies appealed against tax return amendments and the SDLT discovery assessments. The taxpayers sought to show that the law recognises goodwill as a separate asset, distinct from the land asset. If that is so, then a valuation made on the basis that the goodwill is part of the land asset would be wrong in law.

Decision

The Upper Tribunal stated that the agreed market rent fully reflected the trading potential available to the tenant under the terms of the 5-year lease.

The Tribunal were satisfied that the trading potential of both the Manor Place and Maple House care homes was reflected in the agreed valuations and so those valuations represented transferable property-based goodwill. The Tribunal found that, using RICS guidance, the value of the leasehold interest represented goodwill only, with no additional premium on the lease that could be subject to SDLT.

Zyrieda Denning and others v HMRC ([2021] UKUT 76 (LC)

LBTT and LTT: the differences from SDLT (Lecture P1260 – 12.46 minutes)

Land and Buildings Transaction Tax

Land and Buildings Transaction Tax (LBTT) was introduced in Scotland in 2015.

The following is worth noting:

- The overall concept of LBTT shares much in common with SDLT. There are features in the LBTT regime that are different from SDLT, principally in respect of its administration and general anti-tax avoidance provisions, which are outlined below. However, there are some differences linked to the different wording of the LBTT legislation and a decision by Revenue Scotland (who administer LBTT) to accept a different analysis of the provisions.

- As regards partnerships, the LBTT regime adopts the same (and complex) structure as that of the SDLT. In so doing, the distinctive feature of a Scottish partnership as having a separate legal personality is therefore not reflected in the legislative design for LBTT.

- In respect of trusts, the basic principles of trusts in Scots law are derived from the Roman Law concept that a right *in personam* (a personal right) is distinct from a right *in rem* (a real right). Under Scots law, a trustee has the right *in rem* and a beneficiary has the right *in personam* against the trustee. In contrast, under English law, the distinction is drawn between legal ownership and equitable interests. A trustee has the legal ownership of the trust property at common law, and the beneficiary has the equitable interests in equity. This is the most significant theoretical difference for a trust constituted under Scots law from one constituted under English law. Though any differences emanating from this conceptual divergence are often smoothed out or removed in the drafting of modern trust deeds, they can still have practical implications on intestacy, on the interpretation of old deeds or home-drafted wills. For the purposes of LBTT however, trusts are to be treated as if they were constituted under English law, and a trustee is regarded as the legal owner of a land interest with a beneficiary holding the equitable interests in the land.

The rates of LBTT are as follows:

<u>Residential property</u>

Relevant consideration	Percentage rate of tax
Up to £145,000	0%
Next £105,000	2%
Next £75,000	5%
Next £425,000	10%

The remainder	12%

The LBTT supplement for second property (called the additional dwelling supplement (ADS)) is 4% and the time limit for the main residence relief for these purposes is 18 months rather than the 3 years which applies for SDLT purposes, although it was temporarily increased to 36 months for transactions between 24 September 2018 and 24 March 2020.

There is also no subsidiary dwelling exemption where more than one dwelling is bought in a single transaction. There was an increased nil rate band to £250,000 from 15 July 2020 to 31 March 2021. At the time of writing this had not been extended. First-time buyers' relief for LBTT purposes is only £175,000.

Non-residential property

Relevant consideration	Percentage rate of tax
Up to £150,000	0%
Next £100,000	1%
The remainder	5%

For non-residential leases, the nil rate band is £150,000 with 1% duty being paid up to £2m and 2% beyond this.

Land Law operates differently in Scotland. There are three key stages in the conveyance of property:

1. Conclusion of missives (which is equivalent to the exchange in English law) where the parties agree to be bound by the terms of the contract, but the seller remains the owner.

2. Settlement and delivery of disposition (which is equivalent to completion in English law) where the consideration is passed although the seller remains the owner. The purchaser would normally be able to take occupation from this date.

3. Registration of disposition (registration of title in English law) when the buyer assumes title and becomes the owner.

For LBTT purposes, the effective date of the transaction is the settlement date although it is still possible to have substantial performance as it is for SDLT purposes.

The three key stages in the tax administration for a land transaction are:

1. Filing of return

2. Payment of tax

3. Registration of title

For a purchaser, the registration of title is the ultimate goal of the transaction. Under SDLT, title registration is predicated on the issue of the SDLT5 certificate by HMRC, which in turn hinges on the submission of a satisfactorily completed SDLT return. As the registration of title is not dependent on payment of the requisite tax, it is possible in theory that a title could have been registered before the associated tax is paid.

Under LBTT, the three stages are tied up more closely, making title registration dependent on both return submission *and* payment of tax:

- The submission of the return and the payment of the tax are joined up as a one-stage process, and at the point of return submission, 'arrangements satisfactory' have to be in place for the payment of LBTT due.

- Registration of title is effected via automatic data-feed from the LBTT return system.

- There is no equivalent of SDLT5 certificate in the LBTT regime for the registration of title.

- *Arrangements satisfactory*' mean payment methods under the terms as directed by Revenue Scotland, and include Direct Debit, BACS or CHAPS for returns submitted online, or payment by cheque to accompany the submission of a paper return.

Leases and licences

It is in the areas of leases where the biggest differences exist between SDLT and LBTT. This is largely as result of the differences between Scots law and English law governing leases. In particular, variations of leases are not treated as the disposal and acquisition of a new lease. This means that there needs to be greater consideration given for anti-avoidance provisions to makes sure that value cannot be enhanced after the LBTT has been paid by varying the lease terms.

Under SDLT, the net present value (NPV) for the purposes of determining the chargeable rental for both residential and commercial leases is calculated on the basis that the rent for any year after the end of year 5 is at the highest annual rate payable over the first 5 years, regardless of whether the lease has in fact fixed the rent at a higher rate from year 6 onwards. There is effectively a capping of the NPV for SDLT purposes.

Under LBTT, the rates and bands are very similar to those for SDLT, but significant differences exist for residential and commercial leases, and not for the same reasons.

- **Residential leases** are largely exempted from LBTT. Only residential leases of more than 20 years' duration will be subject to LBTT. As a feature of Scots law, residential 'freehold' is the norm, and residential leases of over 20 years are extremely rare, since the *Land Tenure Reform (Scotland) Act* 1974 (ss.8–9) prohibits the grant of long leases of more than 20 years for private dwelling houses. (Any existing leases of more than 20 years' duration would have pre-dated the enactment of the 1974 Act.) Furthermore, the *Long Leases (Scotland) Act* 2012 deals with existing long leases by converting the tenant's interest under certain long leases to outright ownership on 28 November 2015. For these combined reasons, residential leases are by and large outwith the LBTT charging provisions.

- For **commercial leases**, the charging structure is similar to SDLT on rent, but tenants are required to submit LBTT returns every three years; there is no cut-off of assessment at the end of five years as with SDLT. LBTT is therefore effectively re-assessed at three-year intervals based on the actual rentals paid in the preceding three years; LBTT payable will then be adjusted accordingly. Any capital payment (i.e. premium) made for a lease will be assessed at the same rates as for a commercial purchase.

Licences to occupy are exempt under both SDLT and LBTT, but certain non-residential licences are likely to be brought within the ambit of LBTT.

Reliefs

Most reliefs under SDLT are replicated in LBTT with the additional of Crofting Community Right to Buy relief at 100%. The most notable difference between the regimes relates to sub-sale relief which is not replicated in LBTT. It is replaced with Sub-sale Development Relief (SDR).

SDR is available in the same type of cases as when the relief applies for SDLT purposes but with one additional condition. It only applies where there is significant development of the land or buildings. Development includes redevelopment but only where it is significant which is to be judged by the nature of extent of the work done in comparison to the pre-existing building. It is effectively targeted at genuine property development projects.

There are also some differences for Multiple Dwellings Relief purposes. The basic conditions are the same but there is a different minimum charge. For SDLT purposes, the rate of duty cannot fall below 1% of the chargeable consideration but for LBTT purposes, there is a 'minimum prescribed amount' which is 25% of the duty which would be paid without the relief being claimed.

There is also an interesting difference in interpretation of the rules where six or more dwellings are bought in one transaction. This would attract non-residential rates (as it does for SDLT purposes) but MDR is also available (using the non-residential rates) and no additional dwelling supplement is due. HMRC has confirmed that this interpretation does not apply for SDLT purposes.

Land Transactions Tax

Land Transactions Tax (LTT) was brought in for Welsh property transactions from 1 April 2018.

The rates of tax on residential-property transactions are (with an additional rate supplement of 4% being due on second homes):

Relevant consideration	**Rate of tax**
First £180,000	0%
Next £70,000	3.5%
Next £150,000	5%
Next £350,000	7.5%

Relevant consideration	**Rate of tax**
Next £750,000	10%
Balance over £1,500,000	12%

There was an extension of the nil rate band up to £250,000 applying for transactions from 27 July 2020 and this has been extended so it applies up to 30 June 2021. This does not apply to transactions where the higher rate for supplementary dwellings applies. The subsidiary dwellings exemption does apply for LTT purposes, with the same conditions as for SDLT purposes. There is no first-time buyers' relief.

The non-residential rates (which also apply for mixed use property too) are as follows:

Relevant consideration	*Percentage rate of tax*
First £150,000	0
Next £100,000	1
Next £750,000	5
Balance over £1,000,000	6

There are differences for leases. LTT is only payable on the premium element of residential lease transaction, with the rent not being taken into account.

For non-residential leases, there is a nil rate band up to £225,000 with 1% being paid above this up to £2m and 2% above £2m. The 0% band which would apply to premiums is increased to 1% where the rent exceeds £13,500 (from 4 February 2021, with the previous figure being £9,000).

Contributed by Ros Martin

Administration

Tax avoidance schemes – Joint campaign (Lecture P1259 – 15.22 minutes)

On 26 November 2020, HMRC and the Advertising Standards Authority launched a major campaign to put a stop to misleading marketing by promoters of tax avoidance schemes.

The newly announced joint enforcement notice aims to disrupt the activity of promoters and to protect people being presented with deceptive advertisements which might otherwise tempt them into tax avoidance. In particular, it requires promoters to be clear about the potential consequences of tax avoidance in any online marketing. Immediate sanctions include having promoters' paid advertising removed from search engines, along with follow-up compliance action such as referral to Trading Standards.

This course of action came into being alongside the introduction of HMRC's 'Tax avoidance: don't get caught out' awareness drive, warning and educating contractors about:

- how they can identify that they are being offered a tax avoidance scheme; and
- the pitfalls of using such schemes.

The main message from Government is that, if any arrangement involving tax looks too good to be true, it almost certainly is.

Simultaneously, HMRC published on their website a very interesting report entitled 'Use of marketed tax avoidance schemes in the UK' which, for 2018/19 (the latest tax year for which data is available), discusses:

- the main types of scheme used; and
- the characteristics of taxpayers taking advantage of schemes.

With regard to the size of the problem, HMRC state:

> 'Tax avoidance is not as widespread as people might think. In 2018/19, we estimate that 95.3% of all the tax that was legally due in the UK was paid. That is £627.9 billion in revenues in 2018/19. Of the revenues HMRC brought in, £34.1 billion was additional tax from tackling avoidance, evasion and other non-compliance.
>
> In the same year, HMRC estimate that around £1.7 billion was lost to tax avoidance. Around half of this gap (£0.9 billion) is attributed to corporation tax. The £0.6 billion element relating to avoidance schemes marketed to individuals is made up of unpaid income tax, NICs and CGT. Other direct taxes and VAT account for the smallest share of avoidance (each at £0.1 billion).'

The report goes on to tell us that the reasons why tax goes unpaid involve several other areas where the relevant amounts are significantly greater.

One of HMRC's charts shows the following:

Reasons why tax goes unpaid	Tax lost
Failure to take reasonable care	£5.5 billion
Legal interpretation	£4.9 billion
Evasion	£4.6 billion
Criminal attacks	£4.5 billion
Non-payment	£4.1 billion
Error	£3.1 billion
Hidden economy	£2.6 billion
Tax avoidance	£1.7 billion

As you can see, tax avoidance comes a long way down the list.

HMRC's analysis reveals that the overall amount lost through tax avoidance schemes targeted at individuals has more than halved since 2013/14. This reduction is mainly the result of policy and operational reforms such as the introduction of the GAAR in FA 2013 and the development of follower and accelerated payment notices in FA 2014 which, in the words of HMRC, 'fundamentally changed the economics of avoidance (for example, by requiring any disputed tax to be paid in full up front while any dispute was resolved or went through the Courts)'.

In 2013/14, the main tax avoidance schemes for individuals involved:

(i) disguised remuneration arrangements; and

(ii) sideways loss relief.

With reference to (ii) above, many of these schemes were marketed as representing investment opportunities for high-income investors. For example, the 'Ingenious' scheme used losses arising from investments in a range of blockbuster films such as 'Avatar' and 'Die Hard 4'. The 'Icebreaker' scheme, to take another example, created losses from investments in LLPs. HMRC summed up the effect of participating in such arrangements as follows:

> 'In both schemes, the individuals using them tried to claim more in tax relief than they had invested. These schemes did not work and individuals faced big bills for interest and legal fees on top of the unpaid tax.'

Another of HMRC's charts illustrates the change in the proportion of scheme types between 2013/14 and 2018/19:

Scheme type	2013/14	2018/19
Disguised remuneration/contractor loan	60%	98%
Sideways loss relief	36%	1%
Other	4%	1%

Nowadays the investment schemes utilising sideways loss relief have largely disappeared and the market has been dominated by disguised remuneration arrangements (and their variants). However, it is anticipated that, as a result of the loan charge legislation in F(No2)A 2017 (which was significantly amended by FA 2020), they too will dry up.

An interesting statistic about individuals involved in tax avoidance schemes in 2018/19 is that their use was most prevalent among the 41 – 60 age group. And many of these individuals were involved in more than one scheme. Turning to the individuals' incomes, HMRC's 2018/19 data shows that the percentages involved in tax avoidance at different income levels were as follows:

Reported income	Individuals in this category
Up to £25,000	87%
£25,001 – £50,000	8%
£50,001 – £75,000	2%
£75,001 – £100,000	1%
Over £100,000	2%

On reflection, it is perhaps not wholly surprising that 95% of those who used tax avoidance schemes reported having an income of no greater than £50,000, given that taxpayers involved in disguised remuneration schemes would originally not have returned their full income for tax purposes.

HMRC have commented further:

> 'It is unclear what proportion of the people who reported income of £0 – £25,000 were genuinely on incomes of this level. However, anecdotal evidence in the wake of the loan charge and the fact that promoters of avoidance schemes targeted nurses and other NHS workers indicates an increased level of interest from promoters in individuals on middle incomes.
>
> As would be expected, given the density of the population in these areas, tax avoidance in the UK is concentrated in London and the south-east of England. However, we are seeing a significant shift away from the London postcodes more usually associated with those on higher incomes, including the City of London and Knightsbridge, towards the outer boroughs and commuter belt. There are noticeable concentrations in Barking, Dagenham, Thurrock, Greenwich and Croydon.'

If you have clients who live in these areas, you will need to be on the alert!

Contributed by Robert Jamieson

Computer generated notice to file

Summary – Appeals against closure notices were struck out as there was no reasonable prospect of success that the closure notices were invalid as a result of the relevant notices to file being invalid because they were issued by computer.

Asher Sternlicht and others appealed against 2011/12 closure notices that disallowed their claims for share loss relief. Having withdrawn their initial grounds of appeal, the taxpayers applied to make a late appeal arguing that the Closure Notices were invalid arguing that:

- For the Closure Notices to be valid, there must be a valid notice of enquiry into each relevant tax return;
- For there to be a valid notice of enquiry there must be a return being enquired into;
- For there to be a valid return, there must have been a valid notice requiring a return under s8 TMA;
- For the notice to be valid, it should have been issued by an officer and not by computer.

It was accepted that under s87 FA 2019, a return did not have to be in response to a notice and that this was retrospective. However, the taxpayers said the 'retrospective legitimisation of the tax return does not and cannot also have the effect of retrospectively legitimising any purported enquiry'.

HMRC opposed the application.

Decision

Referring to the Upper Tribunal decisions in CRC v Rogers and Shaw (2020) STC, the First-tier Tribunal decided the appeal had no reasonable prospect of success.

1. It seemed 'fanciful' to suppose the taxpayers would doubt that HMRC approved the issuance of notices of file using the 'parameters and machinery in existence' at the time.
2. It seemed unlikely that the taxpayers would challenge that the notices had been issued on the instructions of HMRC staff.
3. The judge said:

   'In the present case, the returns were received by HMRC on 28 January 2013. The legislation was treated as in force on that date (s 87(3)). On the assumption that the appellants are correct that no valid s 8 notice had been given, s 12D applied (s 12D(1)); the return is treated as having been delivered pursuant to a s 8 notice given on that date (s 12D(2)). Therefore, on 28 January 2013 and all subsequent dates, there was a return given in response to a valid s 8 notice. The necessary consequence of this is that when the s 9A notice of enquiry was subsequently given, that was a notice of enquiry into a return that was treated as having been made under s 8. The s 9A notice was therefore valid, so were the enquiry and the closure notice.'

In essence, s 12D provided a 'complete answer' to the ground of appeal which stood no chance of success. HMRC's application for the appeal to be struck out succeeded.

Asher Sternlicht and others v HMRC (TC08044)

Adapted from the case summary in Taxation (22 April 2021)

Stale discovery **(Lecture P1256 – 21.38 mintes)**

Summary – Discovery assessments issued four years after the start of an investigation and some three years after the taxpayer had admitted the inaccuracies were held to be stale.

Kashif Mehrban owned and operated a small retail store selling newspapers and magazines, alcohol, tobacco products and other general household goods. He also operated a “Paypoint” and “Payzone” terminal (which allowed customers to make bill payments in store) and a national lottery terminal.

On 21 March 2013, HMRC made an unannounced visit to his shop to check the credibility of his VAT and income tax returns. In 2014, an investigation was initiated under COP 9 and Kashif Mehrban was informed that HMRC suspected that he had committed tax fraud and invited him to enter into a Contractual Disclosure Facility to avoid criminal prosecution by making a complete and accurate disclosure of all tax irregularities. He made a statement in November 2014 that he had understated taxable profits.

It then took until 2017 for HMRC to issue discovery assessments for 2002/03 to 2015/16.
The total amount assessed was £176,513.39 plus penalties.

Decision

The First Tier Tribunal found that HMRC had discovered that there had been an insufficiency in the tax charged at the very latest on or around 25 March 2014. By that time HMRC had:

- concluded that the gross daily takings were not being recorded on a daily basis, and that the numbers declared were not credible;
- conducted a cash-up exercise and carried out test purchases which revealed that sales appeared to be understated by about 70%; and
- concluded that purchases had been suppressed by around £18,811.64 over a three-month period.

It was at this time that HMRC had referred the case for investigation for fraud under the COP9 procedure.

The Tribunal then turned to the question of whether the discovery had become stale by the time that the assessments were made on 21 April 2017, over three years later.

The Tribunal asked the question what happens if HMRC makes an assessment which is wrong, leading to an underassessment of tax? The Tribunal concluded that delaying issuing their discovery assessment to ensure that they have the full information was missing the point. Where additional information later comes to light, HMRC would have discovered something new, so making a fresh discovery, enabling HMRC to make a further discovery assessment where objectively reasonable for them to do so.

Consequently, the Tribunal held that the significant delay of over 3 years between the discovery and the assessment had caused the discovery to become stale and the assessments were therefore invalid.

Kashif Mehrban v HMRC (TC08039)

No deliberate inaccuracy and no concept of staleness (Lecture P1256 – 21.38 minutes)

Summary – There was no deliberate inaccuracy in the taxpayer's return as he had made it clear what he had done and the tax position that he wanted to take.

Mr Tooth entered into an arrangement known as "Romangate" in an attempt to obtain an employment loss. He had submitted his tax return, claiming the loss as a partnership loss, rather than an employment loss, before retrospective legislation was enacted that nullified the event.

He had informed HMRC in the "white space" to the return that the loss he claimed was an employment related loss but as his approved software did not allow to him to enter the loss as an employment loss, he had included the amount on his partnership pages.

HMRC issued a discovery assessment on Mr Tooth (after the enactment of the legislation which nullified the arrangement) on the basis that:

1. HMRC had discovered an insufficiency in Mr Tooth's return;

2. Mr Tooth's return contained an inaccuracy (in that the loss was entered on the partnership pages of the return and Mr Tooth's explanation as to why he had done this did not alter the nature of what HMRC consider to be an inaccuracy); and

3. This inaccuracy was deliberate.

The First Tier Tribunal found that although HMRC had made a discovery, there was no deliberate inaccuracy.

The Upper Tribunal agreed that there was no deliberate inaccuracy but found that the discovery had gone stale between 2009 when they said it was originally found and 2014 when the assessment was raised.

The Court of Appeal found that there had been a deliberate inaccuracy but that there was no qualifying discovery.

HMRC appealed to the Supreme Court.

Decision

The Supreme Court held that there had been a valid discovery by HMRC but that the inaccuracy was not deliberate.

The Supreme Court concluded that for there to be a deliberate inaccuracy within s118(7) TMA, there must be 'an intention to mislead' HMRC. Mr Tooth had "done his best" given the inadequacy of the software that he was presented with and, when reading the return in its entirety, he had made it clear as to what he was claiming and why.

Although not necessary, the Supreme Court went on to consider the arguments relating to whether a valid discovery had been made. Both the Upper Tribunal and the Court of Appeal had found that the original discovery was made in 2009 and so by 2014 that discovery had become stale. Interestingly, the Supreme Court disagreed finding that different HMRC officers are able to make the same discovery but at different times, with each entitled to issue a discovery assessment. Further, there is no concept of staleness. Two points from the Press release relating to the Supreme Court's decision are reproduced below:

> "First, there is no principle of 'collective knowledge': section 29(1) focuses on the state of mind of the individual officer of the Revenue who makes the assessment; if an officer had already made a discovery, that must not be regarded as a discovery 'once and for all' by the Revenue such that other officers cannot make the same discovery in future [64-65]. This is because of the language and structure of section 29(1) [68], the similar language in section 29(5) [68], the history of section 29 [69], and the ordinary principle of the exercise of powers in public law [70].
>
> Second, there is no concept of 'staleness': any idea that a discovery might lose its quality over time is contrary to the ordinary use of language, the leading authorities, and the statutory scheme [73-77]. The question is whether the officer of the Board who is deciding whether to make a discovery assessment has subjectively made a discovery that there has been an under-assessment of tax. It is perfectly possible for someone to make a discovery even if it is something already known to others [78-82]."

HMRC v Tooth [2021] UKSC 17

Deadlines

1 June 2021

- SME corporation tax for periods to 31 August 2020 where not paying by instalments
- Check for revised HMRC advisory fuel rates

7 June 2021

- Electronic filing of VAT for quarter ended 30 April 2021

14 June 2021

- Quarterly corporation tax instalment for large companies depending on year end)

19 June 2021

- PAYE/NIC/CIS/student loans payment for month to 5 June 2020 (non electronic)
- File monthly CIS scheme return

21 June 2021

- File online monthly EC sales list (businesses based in Northern Ireland selling goods)
- Submit supplementary intrastat declarations for May 2021
  - arrivals only for a GB business
  - arrivals and despatch for a business in Northern Ireland

22 June 2021

- Electronic payment of PAYE/NI/CIS for month ended 5 June 2021

30 June 2021

- Accounts to Companies House for:
  - private companies with 30 September 2020 year end
  - public limited companies with 31 December 2020 year end
- CTSA returns filed for companies with accounting periods ended 30 June 2020

News

Freeports and secondary Class 1 NIC

The NIC Bill 2021 contains more details on the NIC exemption for employees of a Freeport employer.

From April 2022, where employees spend 60% or more of their time in a Freeport tax site, employers will be eligible for relief on secondary Class 1 NICs for 36 months.

The relief will be available to new employees but only on earnings up to £25,000 per annum.

In a policy paper, HMRC has stated that the scheme may be extended to 2031, subject to a review scheduled for 2026.

https://www.gov.uk/government/publications/zero-rate-of-secondary-national-insurance-contributions-for-freeport-employees/zero-rate-of-secondary-nics-for-freeport-employees

Migration to the IT system and new direct debits

In preparation for HMRC's VAT mainframe being decommissioned in 2022, HMRC will be moving all remaining taxpayer accounts to their new system between July and September 2021. The taxpayers affected are VAT businesses not signed up to making tax digital (MTD) who pay by direct debit.

UK Banking Regulations require HMRC to inform customers paying by direct debit of the amount and date their direct debit will be taken. Due to the very short timeframe between submission of the VAT return and payment of the tax, HMRC will be unable to send postal notifications and so will be using taxpayers' email addresses to inform them.

Where HMRC do not hold email addresses, direct debits will need to be cancelled prior to moving them to the new system. HMRC sent letters to those concerned in May. The letter asks taxpayers to regularly log in to their Business Tax Account between July 2021 and September 2021. Once an account has been moved, the customer's Business Tax Account will automatically prompt them to set up a new direct debit and provide a contact email address when they next login.

There is a similar issue for agents as HMRC are unable to advise agents exactly when their clients' accounts will be migrated to the new system. HMRC advise that when submitting returns on behalf of their clients, agents will sign into the 'old' agent portal as normal. If the obligation to file their VAT return is there, the return can be submitted. If the obligation is not there, the client's VAT record has been migrated and the agent should login to their Agent Services Account (ASA) and submit the VAT return using the non-MTD filing service within ASA.

https://www.gov.uk/government/publications/agent-update-issue-83

Self-isolation support payments

Individuals who self-isolate due to COVID-19 may be entitled to a £500 support payment under one of the government support schemes:

- Test and Trace Support Payment Scheme (England);
- Self-Isolation Support Scheme (Wales);
- Self-Isolation Support Grant (Scotland).

These payments are taxable. HMRC has published guidance on how to report these payments, stating that where individuals are required to file a Self Assessment return, these payments must be accounted for as income.

Employees

For employees the amount must be included in the 'Other benefits (including interest-free and low interest loans)' box of the 'Benefits from your employment' section in the employment supplementary pages (SA102). Individuals should also report the payments this way if they are both employed and self-employed, or employed and a partner in a trading partnership.

Self-employed individuals (or partners in a trading partnership)

Taxpayers must include the amount in the calculation of profits for the tax year. As the payments are exempt from Class 2 and Class 4 National Insurance Contributions, adjustments must be made in box 102 on the self-employment supplementary pages (SA103F). If a taxpayer has already submitted a return for 2020/21 without the required adjustments, they should correct the return. Where a paper return was submitted, they should write to HMRC asking for the return to be amended.

https://www.gov.uk/guidance/how-to-reportself-isolation-support-payments

Mini umbrella company fraud

BBC Radio 4 has reported that more than 48,000 companies have been created in the past five years to exploit the government's £4,000 Employment Allowance.

Mini umbrella companies have been used to exploit the allowance by employing temporary workers. Some staff at COVID test centres run by G4S have been employed through such schemes. G4S has stated that, when this came to its attention, HMRC was notified.

https://www.bbc.co.uk/news/uk-57021128

HMRC has published new guidance explaining what mini umbrella company fraud is and the checks that businesses can carry out to protect their labour supply chain.

Mini umbrella company fraud usually involves the creation of multiple limited companies to enable fraud with only a small number of temporary workers employed by each company. These workers usually do not know who their employer is and can be moved regularly between mini umbrella companies to help maximise profits from the fraud.

HMRC say that the fraud is primarily based around the abuse of two government incentives aimed at small businesses (the VAT Flat Rate Scheme and the Employment Allowance) but can also result in the non-payment of other taxes such as PAYE, National Insurance and VAT.

Warning signs

HMRC has highlighted some signs to watch out for:

- Unusual company names - Multiple companies are often set up around the same time and given a similar or unusual name. The registered address may not seem suitable for their types of business activities.

- Unrelated business activity - The business activities listed on Companies House entries will often not relate to the services provided by the workers.

- Foreign national directors - Foreign nationals who have no previous experience in the UK labour supply industry, are often listed as directors. They can replace a temporary UK resident director after a short period of time.

- Movement of workers - Employees may be moved frequently between different mini umbrella companies.

- Short-lived or transient businesses - These individual mini umbrella companies have a relatively short lifespan (often less than 18 months) before being allowed to be dissolved by Companies House as they do not meet filing obligations. New mini umbrella companies will then be created, often requiring new key information documents to be completed by workers on a regular basis.

Checks to carry out

Businesses that use or provide temporary labour must:

- undertake necessary and proportionate due diligence checks;

- be clear who pays their workers and how they are paid;

- check the credibility of the supply chain

Businesses can contact HMRC if they have concerns about a supplier, hirer of labour or associated activities and report potential fraud or tax evasion.

https://www.gov.uk/guidance/mini-umbrella-company-fraud

Business Taxation

Partnership and IR35 (Lecture B1256 – 16.27 minutes)

Gary Lineker and his former wife Danielle Bux formed Gary Lineker Media, a partnership through which Gary Lineker provided his presenting services to the BBC (Match of the Day) and BT Sport (UEFA Champions League).

HMRC believe that these arrangements fall within the intermediaries legislation and issued Determinations in respect of income tax deductible via PAYE as well as Notices in respect of Class 1 National Insurance Contributions totalling around £5 million.

HMRC's statement of case describes the main issue in the appeal as

> "… whether each of the hypothetical contracts between Mr Lineker and the BBC/BT would have been contracts of service …or contracts for services…."

HMRC has requested the Tribunal give a decision in principle only on the above issue and that a further hearing should be listed, if required, to resolve any outstanding issues regarding the quantum of any taxes due.

GLM disputes that IR35 applies, arguing that Gary Lineker would not have been regarded as an employee of the BBC and/or BT Sport.

In March 2020, Gary Lineker Media sought permission to amend its Grounds of Appeal so that the hearing, when it happens, considers both quantum and liability. This has been delayed for over a year due to administrative delays, exacerbated by coronavirus restrictions. However, on 14th April 2021, the First Tier Tribunal announced its decision, stating that as in most cases, the Tribunal should determine the quantum and liability issues at the same hearing.

It will be interesting to read the arguments and the Tribunal's decision when this appeal eventually comes to court. How will the use of a partnership rather than personal service company affect the technical arguments that are usually made in IR35 cases?

Gary Lineker & Danielle Bux t/a Gary Lineker Media v HMRC (TC08084)

Capital allowances on satellite leases

Summary - The Upper Tribunal upheld the First tier Tribunal's decision that the company was not entitled to capital allowances in respect of expenditure incurred by its predecessor on launching satellites into space.

Inmarsat Global Ltd was the successor to the business of International Maritime Satellite Organisation (IMSO), an international organisation established by a convention to operate satellites for maritime communications.

Six satellites were leased to IMSO by financial lessors and IMSO paid the costs of launching them into space. IMSO was exempt from corporation tax and so did not claim capital allowances in respect of the launch costs.

Several years later, Inmarsat Global Ltd acquired the business and assets of IMSO's trade in return for the issue of shares and claimed capital allowances in respect of IMSO's launch costs.

It argued that by paying the launch costs, IMSO had incurred capital expenditure on the provision of the satellites, which it was required to incur under the terms of the leases so that, under s61(4) CAA 1990 (now s70 CAA 2001), the satellites were deemed to belong (in part) to IMSO. When Inmarsat Global Ltd succeeded to IMSO's trade, IMSO's assets, including its interest in the satellites, were treated as sold to Inmarsat Global Ltd at market value under s78 CAA 1990 (now s266 CAA 2001). The company contended that, as a result, that interest was deemed to belong to it, and it was entitled to capital allowances on a proportion of the satellites' market value.

Decision

The Upper Tribunal considered that the company would need to succeed on each of three issues for its claim to succeed.

The first issue was whether s78 CAA 1990 deemed the satellites to belong to Inmarsat Global Ltd. The Upper Tribunal held that the section was primarily concerned with the tax position of the predecessor and had no application to a successor unless it became the actual owner of the asset in question. It therefore did not deem Inmarsat Global Ltd to own the satellites, so that the company did not meet the ownership requirement for a claim to allowances and its claim failed.

Although not strictly necessary, the Upper Tribunal also considered the other two issues, and here it found for the company. The second issue was whether IMSO had incurred the launch costs 'on the provision' of plant for the purposes of s 61(4). The Upper Tribunal held that it had, despite acknowledging the presence of anomalies in the legislation. The third issue was whether the other requirements of s 61(4) were met by IMSO. In particular, the Upper Tribunal decided that the company had been 'required' to incur the launch costs under the leases.

Inmarsat Global Ltd v HMRC [2021] UKUT 59 (TCC)

Adapted from the case summary in Tax Journal (8 April 2021)

IBAs in period of disuse

Summary – An LLP was entitled to industrial buildings allowances (IBAs) in respect of buildings which remained unused throughout its period of ownership.

In 2004, the LLP purchased several buildings which had been used by the previous owner in its manufacturing trade, but which had fallen into disuse for the last 13 months. The LLP instructed agents to market the site to attract potential tenants and extensive active marketing took place. Those efforts were unsuccessful, and the LLP sold some of the buildings in 2005 and the remainder in 2006. It claimed IBAs on the basis that there was a period of 'temporary disuse' of the buildings beginning when the previous owner stopped using them and ending on the disposals by the LLP so that under s285 CAA, the buildings continued to be treated as industrial buildings during that period.

HMRC argued that temporary disuse required a period of actual use at both ends of the disuse. Further, there was no 'bridge' which enabled a period of temporary disuse begun under the ownership of one taxpayer to continue following a balancing event arising on a sale to another taxpayer.

Decision

The Upper Tribunal rejected both of HMRC arguments.

A period of temporary disuse could be followed by permanent disuse. This was consistent both with the ordinary meaning of the word 'temporary' and with the purposes of the legislation.

There was also nothing in the legislation suggesting that a balancing event should interrupt a period of temporary disuse; the focus of the legislation was on the building itself and the use to which it was being put rather than on the circumstances of the taxpayer. Here, there was a period of temporary disuse which began when the previous owner stopped using the buildings and ended when the LLP ceased its marketing efforts. At the latter time the period of temporary disuse ceased because the LLP no longer wanted the buildings to be used as industrial buildings.

Mark Shaw v HMRC [2021] UKUT 100 (TCC)

Adapted from the case summary in Tax Journal (7 May 2021)

Compensation for lost profits (Lecture B1256 – 16.27 minutes)

Summary - Money received under a legal settlement against a former accountant and auditor was revenue in nature, representing compensation for lost profits.

Charlton Chauffeur Driver Limited provided international ground transportation services and ceased trading on 31 December 2015.

In early 2013, the directors became suspicious about the activities of the company’s then Finance Manager, who had been employed since 2003 as a bookkeeper. Following investigation, it was established that she had been embezzling money between 2004 and 2012. She was prosecuted and sentenced to prison for four and a half years. Both the accounts and corporation tax returns were amended showing the embezzled funds as deductible business expenditure wholly and exclusively incurred for the purposes of the trade.

Following forensic investigation by KPMG, legal action was taken against both the negligent consultant accountant and auditor. This was settled out of court in August 2016, with Charlton Chauffeur Driver Limited receiving £566,000 that it treated as a capital receipt.

On 27 September 2018, HMRC opened an enquiry into the company’s corporation tax return for that period, later concluding by Closure Notice that the company should bring the settlement into account as a trading receipt.

The company appealed.

Decision

The First Tier Tribunal found that the compensation received was not a payment for giving up the right to pursue the claims.

The Tribunal concluded that was clear that the settlement was a "decision commercially taken as being the best way to achieve optimal recovery of the losses incurred with the least cost and risk". The was compensation was for loss of profit, not loss of cash.

The embezzled funds had never been taxed but had been deducted for corporation tax purposes. The compensation was a revenue trading receipt.

The appeal was dismissed.

Charlton Chauffeur Drive Limited v HMRC (TC08042)

Loss claims denied

Summary – A loss relief claim created from capital allowances was dismissed as the conclusions in HMRC's closure notices were not inconsistent with the losses being reduced to zero.

The taxpayers were limited liability partnerships that acquired 25-year licences for equities trading software, funded by bank loans. They acquired the licences as part of a marketed tax scheme which included a warranty agreement under which partnerships were compensated if projected profits were not achieved. They claimed first-year allowances on the licences which resulted in significant tax losses.

After an enquiry, HMRC issued closure notices which stated:

> 'I conclude, of the losses claimed, only a currently unquantifiable part may be allowable.'

It amended the loss figures on the taxpayers' returns to nil.

The First Tier Tribunal dismissed the taxpayers' appeal.

Decision

The main issue in the subsequent appeal to the Upper Tribunal concerned the closure notices.

The taxpayers said the wording of the closure notices either expressly or by implication accepted that some of the losses were allowable. The First Tier Tribunal was therefore not entitled to use the prior history relating to the scope of the enquiry to widen an otherwise narrowly drawn closure notice. The Tribunal had erred in law by disallowing all of the losses.

The Upper Tribunal said the lower tribunal had erred in law in its approach to construing the closure notices. It should have considered the precise conclusions stated in the notices and whether those conclusions were too narrow to support the amendments made to the tax returns.

The judges said the closure notices should be construed as a whole. They said the notices in this case could be described as 'unspecific' and 'uninformative' and could have been 'better framed'. However, the issue was whether 'the reasonable recipient' knowing the scope of the enquiry, would have considered on reading the notices that HMRC was allowing some of the losses.

The tribunal said this was not tenable. If this had been the case, the amendments to the returns would not have been so explicit to reduce the losses to nil. Instead, they would have set out how 'the unquantifiable losses could be quantified'.

The taxpayers' appeal was dismissed on this point. As a result, the First Tier Tribunal's decision to disallow the losses stood.

Daarasp LLP & Betex LLP v CRC, Upper Tribunal (Tax and Chancery Chamber) [2021] UKUT 0087 (TCC)

Adapted from the case summary in Taxation (22 April 2021)

Loan relationships - Convertible bonds (Lecture B1257 – 25.20 minutes)

Convertible debt poses multiple issues for the issuer:

1. Initial recognition in the accounts – liability or split between liability and equity?

2. Deductibility of interest expense;

3. Tax implications of conversion to shares or redemption for cash.

CTA 2009 (Part 5 Loan Relationships and Part 7 Derivatives), CTA 2010 (s1015 – special securities) and TCGA 1992 (especially on redemption) are potentially relevant.

The rules are perhaps best explained by using a numerical example and then flexing it for alternative scenarios.

Example

A company has £50 million 5% convertible bonds in issue, issued on 2 January 2019 at par. The issue costs were £1.2 million.

Interest is payable semi-annually on 30 June and 31 December and the bonds are redeemable at par on 31 December 2023 or are convertible into a fixed number of ordinary shares in the company at that date at the option of the holder.

The market rate of interest for a similar but non-convertible 5-year bond would have been 7% per annum on 2 January 2019.

1. How is the bond accounted for under IFRS and FRS 102 up to the point just before it is redeemed or converted?

2. How would the accounting differ if the bond was convertible into a variable number of shares in the company?

Analysis

Split the gross proceeds and issue costs between a debt and equity component. The debt component of the gross proceeds is the present value of the interest and redemption price to be paid, discounted at a market rate of interest.

The equity element is the balance of the gross proceeds.

Issue costs are split between the debt and equity components in the same ratio as the gross proceeds.

Debt element: PV of interest and redemption amount

		discount rate 7% per annum , or		3.441%	per half year	
Half year	**Cash flow**	**PV factor**	**PV**			
1	1,250,000	0.9667	1,208,421			
2	1,250,000	0.9346	1,168,224			
3	1,250,000	0.9035	1,129,365			
4	1,250,000	0.8734	1,091,798			
5	1,250,000	0.8444	1,055,481			
6	1,250,000	0.8163	1,020,372			
7	1,250,000	0.7891	986,431			
8	1,250,000	0.7629	953,619			
9	1,250,000	0.7375	921,898			
10	51,250,000	0.7130	36,540,542			
			46,076,152			

Analysis of net proceeds:	**Gross**	**Issue costs**	**Net**
Debt element	46,076,152	-1,105,828	44,970,325
Equity element (balance)	3,923,848	-94,172	3,829,675
	50,000,000	-1,200,000	48,800,000

Accounting under IFRS (FRS 101) and FRS 102

IRR of debt element:			Amortised cost of debt		
Half year	**Cash flow**	**B/fwd.**	**Int exp**	**Cash flow**	**C/fwd.**
0	44,970,325		3.7232%		
1	-1,250,000	44,970,325	1,674,333	-1,250,000	45,394,658
2	-1,250,000	45,394,658	1,690,132	-1,250,000	45,834,790
3	-1,250,000	45,834,790	1,706,519	-1,250,000	46,291,309
4	-1,250,000	46,291,309	1,723,516	-1,250,000	46,764,825
5	-1,250,000	46,764,825	1,741,146	-1,250,000	47,255,972
6	-1,250,000	47,255,972	1,759,432	-1,250,000	47,765,404
7	-1,250,000	47,765,404	1,778,400	-1,250,000	48,293,804
8	-1,250,000	48,293,804	1,798,073	-1,250,000	48,841,877
9	-1,250,000	48,841,877	1,818,479	-1,250,000	49,410,356
10	-51,250,000	49,410,356	1,839,644	-51,250,000	-
			17,529,675		
IRR	3.7232%				

Tax implications:

The initial credit of £3,829,675 to shareholders funds has no immediate tax implications. It is not treated as a derivative because it is not accounted for as such (s579 CTA 2009) even though it is a 'relevant contract' under s585.

The interest expense figures on the previous slide will be the allowable loan relationship debits for the 5-year life of the bond.

If holders decide to convert the bonds for shares, the accounting entry is:

- Dr Bond liability £5 million

- Cr Share capital / share premium £5 million

There is no effect on profit so no tax implications under the loan relationship rules.

Bond convertible into a variable number of shares in the issuing company

The accounting treatment will differ, depending on whether the company is using FRS 102 or IFRS/FRS 101. The numerical examples use the same data as above.

FRS 102

The bond would be booked entirely as a liability (FRS 102, Section 22, para 3b(i)), either at fair value (expensing the initial costs), or net proceeds (see below). Because the bonds contain an option for the holder to convert them to shares, their treatment falls within FRS 102, s.12.

Generally, this means booking the bond each period end at fair value through P&L and the initial costs must be expensed immediately. But if the issuer is a small company under UK company law, then FRS 102 requires it to use amortised cost to account for the liability (initial recognition is at net proceeds of £48.8 million). Do not assume the accounts are correct – check the basis on which they have been prepared.

Small company treatment

There is no splitting of the bond into a liability and equity component, so the bond liability is initially recorded at the net proceeds (£50m minus £1.2m issue costs), i.e. £48.8 million.

			Amortised cost of debt		
Half year	**Cash flow**	**B/fwd.**	**Int exp**	**Cash flow**	**C/fwd.**
0	48,800,000		**2.7782%**		
1	-1,250,000	48,800,000	1,355,751	-1,250,000	48,905,751
2	-1,250,000	48,905,751	1,358,689	-1,250,000	49,014,439
3	-1,250,000	49,014,439	1,361,708	-1,250,000	49,126,147
4	-1,250,000	49,126,147	1,364,812	-1,250,000	49,240,959
5	-1,250,000	49,240,959	1,368,001	-1,250,000	49,358,960
6	-1,250,000	49,358,960	1,371,279	-1,250,000	49,480,239
7	-1,250,000	49,480,239	1,374,649	-1,250,000	49,604,888
8	-1,250,000	49,604,888	1,378,112	-1,250,000	49,733,000
9	-1,250,000	49,733,000	1,381,671	-1,250,000	49,864,671

10	-51,250,000	49,864,671	1,385,329	-51,250,000	-
			13,700,000		
IRR	**2.7782%**				

Tax implications

Interest expense each period in the table above will be allowable, subject to any restrictions in CTA2009 or s1000 CTA2010 'special securities' (see later).

If the bonds are redeemed for £5 million at the end there is no tax implication as no profit or loss is recognised

If the bonds are converted to (a variable number of) shares, then again, no profit or loss is recognised, just a derecognition of the bonds replaced by equivalent value of share capital and share premium.

Non-small companies

The bonds should be fair valued at each period end. The change in the fair value should be shown in P&L and will be a taxable LR credit (for gains) or deductible LR debit (for losses) under Part 5 CTA 2009 (unless held by a financial entity as part of its trade when the gains and losses form part of trading profit).

If the bonds are later redeemed, any profit or loss on redemption is also a taxable credit or allowable loss under the LR rules.

If the bonds are converted to (a variable number of) shares in the company, the fair value of the bonds will be replaced by the same value of share capital and share premium, so no impact on P&L and therefore no tax effect.

IFRS treatment

IAS 32, Para 11, financial liability definition (b)(i) initially at fair value, with no equity component.

The conversion option is an 'embedded derivative', and must be split out from the bond

- The bond is accounted for at amortised cost
- The embedded derivative is fair valued with changes taken to P&L

Issue costs must be split between

- The bond – deducted from the initial value and recognised as part of interest expense as seen before
- The embedded derivative – must be recognised immediately in P&L

Do not assume the accounts are correct – check the basis on which they have been prepared as this is not a well understood area in practice.

Ask how the embedded derivative has been valued and how the initial costs have been treated.

Tax implications

The host instrument (the bond) and the embedded derivative must be considered separately (s585).

Interest expense on the loan charged to P&L will be allowable as LR debits, subject to any specific restrictions in CTA 2009 (such as CIR). This will include the effects of the issue costs allocated.

Issue costs relating to the embedded derivative are not specifically addressed by CTA 2009 so will presumable be allowable when expensed (i.e. immediately).

The movement in the fair value of the embedded option must be booked in P&L, but s651 disapplies the normal taxation rules for derivatives for issuers of securities with embedded derivatives where the 5 conditions in s652 are met.

This is very likely for this type of convertible bond unless issuer is a banking business, securities house, authorised unit trust, investment trust, OEIC or VCT).

Tax will only arise on conversion, exchange, cash settlement or redemption of the bonds (ss653 – 655).

Options exercised and shares issued/transferred in exchange for the bonds

S144(2) TCGA 1992 applies. The deemed consideration for grant of the option = the tax-adjusted carrying value of bond <u>when issued</u>.

But the grant and exercise are considered as a single transaction. If the grantor will settle by issuing shares, there is no disposal for TCGA purposes, so no tax will arise.

If settlement is made in cash or shares in another entity, a gain or loss can arise. This is calculated as the amount paid to settle minus fair value of host contract (bond) minus tax-adjusted carrying value of option when bond was issued.

If the issuer ceases to be a party to the convertible bond where the option is not exercised, a gain or loss arises. For example, where the option lapses or the bondholder required the bond to be redeemed for cash.

The issuer is treated as making a deemed disposal:

- Gain or loss = CV – X
- CV = tax adjusted carrying value of the option when the bond
- X = amount paid to redeem the bond minus fair value of host loan (X cannot be less than zero)

Possible disallowance of interest

A convertible bond is a 'special security' (s1015 CTA 2010) if

- Not listed on a recognised stock exchange (RSE), or
- Not issued on terms reasonably comparable with similar securities listed on an RSE

S1000 treats interest paid in respect of special securities as a distribution and as such they would be disallowed. But where the interest does not exceed a reasonable commercial return and is paid to another UK company within the scope of CT, it will be allowable (s1032 CTA 2010), as long as the interest received by the other UK company is not exempt from tax.

Contributed by Malcolm Greenbaum

Repayment of participator loan (Lecture B1259 – 12.56 minutes)

On 16 December 2020, the GAAR Advisory Panel gave a unanimous opinion in connection with an arrangement involving the repayment of a close company participator loan. They were asked to determine whether the entering into and carrying out of the transactions in question represented a reasonable course of action in relation to the relevant tax provisions, having regard to all the circumstances.

HMRC had referred the case to the Panel in a letter dated 31 July 2020. At the same time, they wrote to the company and their advisers, informing them of the referral to the Panel and inviting them to make representations within the 21-day timescale allowed. In the event, no representations were made.

Before dealing with the Panel's decision, it will be helpful to set out the background to the case:

- A property dealing company (P) was incorporated in 2008. Initially, the single issued share was held by an individual (Mr X).
- On 3 June 2011, P issued a further 500,000 shares which were held as follows:
  - 375,000 by Mr X; and
  - 125,000 by two other companies.
- On 12 August 2015, one of those companies transferred its 100,000 shares to Mr X so that he held just over 95% of P's share capital.
- P's corporation tax return for the year ended 31 December 2014 showed that Mr X had an overdrawn loan account balance of nearly £1,600,000. It was stated that this amount had been repaid to P before 1 October 2015 so that no liability to tax arose under S455 CTA 2010.
- The dispute with HMRC revolved around the repayment of this loan balance and whether the repayment was effective for the purposes of ensuring that there was no charge under S455 CTA 2010 (as supplemented by Ss464A – 464D CTA 2010).

The scheme was designed to prevent a participator loan charge arising on a balance owed to a close company by a shareholder.

Mr X who owed the debt to P incorporated a second company in Guernsey (Newco) with an initial share capital of 1,000 shares of £1 each. These shares were fully paid up.

Newco then arranged a further issue of 1,999,000 shares of £1 each but did not make a call on these shares. However, Mr X personally guaranteed that he would meet that call when it was made.

To begin with, Newco's shares were held by two nominee companies on behalf of Mr X, but, on 25 September 2015, the shares were transferred to P in satisfaction of the outstanding loan. P accepted the transfer as a repayment of the loan balance. Thus, the participator loan was technically repaid before a S455 CTA 2010 charge could arise. The result was that Mr X had a positive balance on his account with P.

This planning ploy was not approved by the Panel. They said:

> 'We start by noting that there is nothing contrived or abnormal *per se* about paying back an outstanding loan before the nine-month deadline in order to avoid the need to pay over the S455 CTA 2010 charge. The legislation clearly contemplates that repayments may be made in time and so avoid the need to pay over the potential tax.
>
> What needs to be considered is the way in which the repayment was effected. In our view, the arrangements as a whole are contrived and abnormal and appear to us to serve no purpose other than to seek to avoid the S455 CTA 2010 tax charge,
>
> There are, in particular, a number of features of the arrangements which strike us as particularly contrived or abnormal:
>
> 1. The use of a separate company needs to be considered. Involving another company does not, in our view, necessarily make the step contrived or abnormal. But causing a new company to be incorporated does appear contrived in the context we see here. The new company we are concerned with in these arrangements has no commercial purpose or substance.
>
> 2. A key part of the arrangement is the way the share capital of Newco was set up. To issue an additional near £2,000,000 share capital and leave it uncalled does seem to us abnormal. The lack of any economic substance in terms of funding is an indicator of contrived arrangements,
>
> 3. The retained obligation, namely the agreement for (Mr X) to remain liable to pay a call on the new shares, does seem to be a contrived step, given the amounts involved and that this relates to a new company (which) as yet has no trading record. The way that value is generated in Newco seems to us to be contrived.
>
> 4. The paying back of the loan by way of transfer of the shares needs to be considered. We do not see anything objectionable in a

> taxpayer transferring assets to a company to satisfy a debt: that is contemplated by the legislation. But here the asset being transferred has been specifically created for the purpose of enabling the transfer to be made and the debt satisfied. Instead of a debt due on loan account, (Mr X) is left with a potential liability for the uncalled share capital. The net result for (P) is that it is still (through its inactive subsidiary) owed the money from (Mr X). This seems to us to be effected by contrived steps.

We also have to note that the transactions were proposed as a set of steps in a letter from (Mr X's) advisers on 16 September 2015 and were completed by the taxpayers on 25 September 2015, as planned in the 16 September 2015 proposal. We are bound to conclude that the arrangements, by being put in place in such a short timescale yet apparently creating value of £2,000,000, were contrived.

We also note that Newco's substance seems to depend on its providing consultancy services to its sole shareholder (Mr X) in return for the individual granting Newco an option to acquire an annuity. We do not have any evidence of any services or this option being exercised (and HMRC say in correspondence that Newco has never traded), but, in any event, it seems to us that the arrangements are also contrived. There is no evidence of the £2,000,000 capital being required for the services (or being called).'

It would appear that the arrangements were seeking to take advantage of the decision in *RKW Ltd v HMRC (2014)*. This was a First-Tier Tribunal case which held that uncalled share capital does not constitute a debt. Unfortunately for the taxpayers in this instance, they were ineffective. The Panel concluded that the overall scheme was not a reasonable course of action to take.

Contributed by Robert Jamieson

Substantial shareholding exemption case **(Lecture B1258 – 10.48 minutes)**

SSE requirements

The substantial shareholdings exemption (SSE) legislation (TCGA 1992, Sch 7AC) broadly provides that a gain on the disposal by a company of shares (or an interest in shares, or certain assets related to shares) will not normally be a chargeable gain, provided two conditions are met:

1. The company making the disposal (the 'investing company') must have held a 'substantial shareholding' in the company whose shares are being disposed of ('the company invested in' but commonly known as the 'investee company');

2. Certain requirements must be met in relation to the investee company, which largely involve the company being a trading company or the holding company of a trading group or a trading subgroup for a specified 12-month period prior to the disposal (and in some cases immediately after the disposal as well).

There is an exception from the second condition for qualifying institutional investors. There are also circumstances where the SSE does not apply, such as where arrangements were made with a sole or main benefit of ensuring that a gain on disposal is covered by the SSE (Sch 7AC, para 5). In addition, there are exclusions from SSE such as for no gain, no loss disposals (Sch 7AC, para 6).

Substantial shareholding requirement

The ‘substantial shareholding requirement’ is that the investing company must have held a substantial shareholding in the investee company throughout a 12-month period beginning not more than six years before the day of the disposal (NB this six-year period was increased from two years in Finance (No. 2) Act 2017).

A ‘substantial shareholding’ broadly means that the investing company must hold at least 10% of the investee company’s ordinary share capital and be entitled to at least 10% of the profits and assets available for distribution to equity holders by the investee company (NB there is an exception to this requirement for disposals of shares by companies who are themselves owned by qualifying institutional investors where certain conditions are met).

Intra-group transfers

There is an important relaxation in this 12-month ownership rule (in TCGA 1992, Sch 7AC, para 15A) in group situations. If certain conditions are met, the minimum 12-month substantial shareholding requirement is treated as having been met for the period that assets were used for a trade conducted by another group company before being transferred to the investee company.

There are four general conditions for this treatment to apply (in TCGA 1992, Sch 7AC, para 15A(2)). These are paraphrased below:

1. Immediately before the disposal, the investing company holds a substantial shareholding in the investee company;

2. At the time of the disposal the asset was being used for the purposes of a trade carried on by the investee company;

3. At the time of the transfer of the asset to the investee company by the investing company (or any other company), they were all members of the same group;

4. The asset must previously have been used by a member of the group (other than the investee company) for the purposes of a trade carried on by that member when it was a member of the group.

If the conditions are met, the effect of the investing company being treated as having held the substantial shareholding at any time during the final 12-month period ending with the time of disposal is that it can include a period before the company invested in existed.

SSE not available

In *M Group Holdings Ltd v Revenue and Customs* [2021] UKFTT 69 (TC), the appellant company (‘MGH’) traded as a standalone company prior to 29 June 2015. In 2015, the company’s owner started to receive interest from potential buyers of the business and sought professional advice.

Subsequently, on 29 June 2015 MGH incorporated a company (‘MCS’) as its wholly-owned subsidiary. On 30 July 2015, MGH acquired the entire issued share capital of another company (‘M5A’). On 30 September 2015, MGH hived down its trade and assets to MCS. On 28 October 2015, M5A commenced trading. On 27 May 2016, MGH sold the entire issued share capital of MCS to a third-party purchaser. The events all took place in 10 months and 28 days.

HMRC disallowed MGH’s SSE claim in respect of the chargeable gain arising on the share disposal, and MGH appealed. The issue for the First-tier Tribunal (FTT) to decide was whether SSE was available despite MGH having owned the shares in MCS for less than 12 months and where there had not been a group of companies in existence for the 12 months prior to the share sale. This turned on the correct construction of TCGA Sch 7AC, para 15A(3), which treats an investing company as having held a substantial shareholding at any time during the final 12-month period when the asset was used by another group member for the purposes of its trade.

The FTT considered relevant case law principles of statutory construction, and how TCGA 1992, Sch 7AC, para 15A(3) should be construed. The FTT also reviewed extra-statutory and other materials. However, the FTT was unable to determine from the wording of the legislation anything which pointed either way on the issue in the appeal of whether the purpose of the legislation included providing relief for standalone trading companies acquiring and selling subsidiaries within 12 months.

The FTT found that HMRC’s interpretation of TCGA 1992, Sch 7AC, para 15A(3) did not amount to a wholly unreasonable result sufficient to justify a “strained interpretation”. The FTT concluded that paragraph 15A only extended the period of ownership for the purposes of paragraph 7 during such time as the relevant asset was used by another company (i.e. MGH in this case) whilst it was a member of the same group. MGH’s appeal was dismissed.

Where are we now?

Subject to any appeal, the position according to the FTT is that the SSE provision in Sch 7AC para 15A cannot apply where the transferee company is a newly-acquired subsidiary of what was previously a standalone trading company.

On that basis, it would be prudent to ensure that where a standalone trading company is likely to dispose of a trade at some point in the future, consideration should be given to creating a subsidiary at least 12 months in advance to enable a hive-down in advance of a disposal of the subsidiary’s shares, if possible.

Contributed by Mark McLaughlin

New residential property developer tax (Lecture B1256 – 16.27 minutes)

In February 2021, the Government set out a five-point plan to bring an end to unsafe cladding, provide reassurance to homeowners and support confidence in the housing market.

To ensure that developers play their part and make a fair contribution, the plan included introducing an industry levy and a new tax on residential developers.

The government has now announced that it plans to introduce:

- A new Gateway 2 levy, which will be applied when developers seek permission to develop certain high-rise buildings in England;
- A new tax on the residential property development sector.

In an attempt to raise at least £2 billion over a ten-year period, the government plans to introduce a time-limited new tax, the Residential Property Developer Tax ("RPDT") targeted at large developers.

A consultation explains that the new tax is planned to be effective for profits recognised in accounting periods ending on or after 1 April 2022 and will apply to the profits of companies undertaking residential property development, but only if they exceed an annual £25m allowance. The rate of tax has yet to be decided.

What is residential property?

The consultation refers to a number of definitions of 'residential property' with legislation and states that they intend the tax to apply to:

> "a house or flat that is considered as a single residence, generally together with the grounds and garden or any other land intended for the benefit of the dwelling"

As for SDLT, the tax will include:

- any building that is suitable for use as a dwelling, where it is not so used at the relevant time;
- any existing building that is being adapted, restored to, or marketed for, domestic use;
- undeveloped land where a residential building is being or would be constructed on it.

These rules will be extended to include any undeveloped land or land undergoing a change in use, for which planning permission to construct residential property has been obtained.

It is suggested that the tax will apply to companies developing affordable housing and communal dwellings.

However, the government is seeking views on excluding the development of purpose-built student accommodation in certain situations. So, for example, individual self-contained units with their own kitchen, bathroom and toilet could fall within the charge, while student accommodation with shared facilities could be excluded.

The government has suggested that specialist communal dwellings should be excluded from the definition of residential property.

This could include:

- Hotels;
- Residential homes for children or the elderly;
- Hospitals and hospices;
- Purpose-designed supported housing with communal facilities providing accommodation with care and/or support for homeless, rough sleepers, people with a disability, drug or alcohol dependency, poor mental health, people with a learning disability and/or autism and older people;
- Residential accommodation for members of any of the armed forces;
- Boarding schools;
- Monastery, nunnery or similar establishment;
- Prisons.

Models being considered

The consultation considers two possible models are being considered:

<u>Model 1 — a company-based approach</u>

Under this model, the tax would apply to all of a company's profits where activities included more than an “insignificant” amount of residential property development.

<u>Model 2 — an activity-based approach</u>

Here the new tax would apply to any company undertaking any UK residential property development, but the tax would only be applied to profits from the residential property development activities.

The consultation seeks views on how the relevant profits will be calculated, if and how old and new losses will be relievable by the company and how interest and other funding costs should be treated.

Other areas covered by the consultation include registration and reporting through the existing CT system as well as payment of the tax due through the quarterly instalments system for large companies.

The consultation closes on 22 July 2021.

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/982206/20210427_RPDT_consultation_FINAL__002_.pdf

VAT and indirect taxes

Historical bad debt relief claim

Summary – A claim for historical bad debt relief by the VAT group representative could not be made as there was lack of evidence to prove that relief had not already been claimed.

Saint-Gobain Building Distribution Limited had brought a number of companies into its VAT Group. In 2014, arguing that the acquired companies had failed to reclaim VAT on bad debts relating to building material supplies due to retention of title clauses, the company claimed historical bad debt relief on their behalf for the period 1 April 1989 to 18 March 1997.

HMRC rejected the £9.9 million claim arguing that bad debt relief claims could already have been made by the previous companies, prior to joining the group.

The First Tier Tribunal dismissed the claim on the basis that there was no evidence to show that previous claims for the periods had not been made as the VAT records had been destroyed as it was so long ago.

Saint-Gobain Building Distribution Limited appealed to the Upper Tribunal arguing that Notice 700/18 had been misconstrued by the First Tier Tribunal. The company argued that for the periods concerned, the guidance stated that bad debt relief was not available where retention of title clauses were present in contracts. With the building supplies sold subject to such retention of title clause, a bad debt relief claim could not have been made in the past.

HMRC argued that when the building supplies were incorporated into the customers' building projects, those goods passed to the customer and so bad debt relief claims could have been made.

Decision

The Upper Tribunal concluded that retention of title clauses are not always effective where legal title is transferred on to customers. The Tribunal stated that bad debt relief claims could have been made as the building supplies had passed on to a third-party following incorporation into the properties that were sold.

Without adequate evidence to support the bad debt relief claim, the First tier Tribunal had been right to conclude that Saint-Gobain Building Distribution Limited had failed to prove on the balance of probabilities that bad debt relief had not already been claimed.

The appeal was dismissed.

Saint-Gobain Building Distribution Limited v HMRC [2021] UKUT 0075 (TCC)

Car parking services or right to occupy land for car washing (Lecture B1256 – 16.27 minutes)

Summary – The grant of a car wash facility within a car park was the taxable supply of a car park and not the exempt supply of a licence to occupy land.

RK Fuels Limited rented out the car park at its premises to a tenant who ran a car wash business, treating the income as an exempt supply of land. The company argued that it was supplying a licence to occupy the land and not a parking facility. The use to which the tenant put the land was not relevant. It was up to them how they used the land – as a car park, to run a car wash business or for some other purpose.

Following a visit, HMRC raised an assessment to collect output tax on the basis that the supply was standard rated. HMRC stated that the fact that RK Fuels Limited had permitted an alternative use of the car park to run a car wash did not cause the area to cease to be a car park, nor did it mean that it could not be used as a car park. There was a need for cars to be parked on the land whilst waiting to be washed, dried and cleaned. Without the ability to park a car on the land, the permitted use could not occur.

RK Fuels Limited appealed to the First Tier Tribunal relying on the section of the lease agreement that stated:

> "The car park will be used for only the following permitted use (the Permitted use): as a car wash business. Neither the car park nor any part of the premises will be used at any time during the terms of this lease by the tenant for any purpose other than the permitted use.'

Decision

The First Tier Tribunal concluded that the supply was standard rated. Having considered the lease agreement in its entirety, the Tribunal found that there was considerable force in HMRC's submission that the words "Car Park" featured frequently throughout the lease agreement. The area being leased was a car park, albeit under the terms of the lease agreement that car park enabled a car wash facility to operate.

The Tribunal was satisfied that a site for parking is any place where a car may be parked. The agreement was 'simply a means of allowing the supply; namely the right to operate a car wash'. HMRC's assessment was upheld.

RK Fuels Limited v HMRC (TC08053)

Hospital parking

Summary – The supply of car parking services was an 'economic activity' but not an activity closely related to exempt hospital and medical care. Consequently, the supplies were chargeable to VAT at the standard rate.

Northumbria Healthcare NHS Foundation Trust provides NHS and private medical services. At some of its sites, it provides pay-and-display car parking for staff, patients and visitors. The Trust provides car parking free-of-charge to a range of hospital users, including cancer patients and those visiting patients that are in hospital for an extended period. Staff pay reduced rates for parking depending on their level.

The Trust had originally accounted for VAT at the standard rate on the fees that it charged for parking but in 2017, it submitted a claim for repayment of VAT for in VAT periods 05/13 to 03/16. The Trust argued that, as an exempt supply, the supply of parking was not an economic activity and further, the supply was closely related to hospital and medical care and so exempt as part of those activities.

Arguing that the supply of car parking was standard rated, HMRC refused to repay the £267,000 of VAT being claimed.

Northumbria Healthcare NHS Foundation Trust appealed to the First tier Tribunal.

Decision

The First Tier Tribunal found that car parking charges were set so as to make a profit and support the work of the hospital, making its supply an economic activity.

The Tribunal concluded that the supply of car parking was not closely related or essential to the supply of hospital and medical care. The Tribunal stated:

> “For the supply to be exempt, the car parking supply needed to be “an indispensable stage in the supply of hospital and medical services for the purposes of achieving the therapeutic objectives, namely diagnosis, treatment and, in so far as possible, cure of diseases or health disorders. It is not sufficient that services improve the comfort and well-being of the patients.”

The car parking was too remote from the medical treatment to qualify for the VAT exemption. The supply was standard rated and the appeal dismissed.

Northumbria Healthcare NHS Foundation Trust v HMRC (TC08056)

The Prudential Assurance Company Ltd v HMRC

Summary – No VAT was due on intra-group services where invoices were issued after the supplier left the group. The continuous supply of services rules was not in point.

The Prudential Assurance Company Limited was the representative member of a VAT group. Silverfleet Capital Ltd was a member of that group and provided fund management services to The Prudential Assurance Company Limited in return for a management fee and performance fees where sub-funds exceeded a set benchmark rate of return.

It was the performance fees that were the subject of this case. Given the time required to create value from the investments, performance fees became payable more than 10 years after the fund investments were originally made.

In November 2007, following a management buy-out, Silverfleet Capital Ltd left the Prudential VAT group and the role of investment manager was taken over by M&G Investment. From this point, Silverfleet Capital Ltd was no longer entitled to receive management fees but would continue to be entitled to performance fees in respect of existing investment funds.

During 2014 and 2015 the hurdle rate set under an investment management agreement was met and Silverfleet Capital Ltd invoiced The Prudential Assurance Company Limited for performance fees payable totalling some £9, million plus VAT at 20 per cent.

In March 2019, Silverfleet Capital Ltd made a claim under S80 VATA 1994 to recover the VAT on the performance fees on the basis that the performance fees were consideration for services performed entirely during the period when Silverfleet Capital Ltd and The Prudential Assurance Company Limited were members of the same VAT group.

On 30 May 2019, HMC rejected Silverfleet Capital Ltd's claim arguing that Silverfleet Capital Ltd's services qualified as a continuous supply. The tax point, or time of supply, for such services is when an invoice is issued or when the consideration is received by the supplier. On that basis, VAT was payable on the performance fee when it was invoiced and paid as at that stage the company was no longer part of the group. Further, they argued that at the time that the supplies were made, they were deemed to be made by the principal member of the VAT group rather than Silverfleet Capital Ltd.

The Prudential Assurance Company Limited appealed arguing that the services were only supplied when the two companies were part of the same VAT group and so the fees were outside the scope of VAT.

Decision

The First Tier Tribunal concluded that, applying the time of supply rules in Regulation 90 of the General VAT regulations (SI 1995/2518), Silverfleet Capital Ltd's actual supply of investment management services should be treated as supplied when they were invoiced, at a time when the companies were not part of a VAT group.

However, in reaching their final decision, the Tribunal turned to the Court of Appeal decision in *B J Rice & Associates* [1996] STC 581. Here, the taxpayer had supplied tax consultancy services and had invoiced the payment due for those services when not registered for VAT.

The client failed to pay and the amount was written off as a bad debt. Several years later, when the taxpayer was registered for VAT, the client sought further tax advice but was told that they must first pay off his bad debt, which they did. Relying on the then equivalent of Regulation 90, HMRC said that VAT should be accounted for on the payment because the taxpayer was a taxable person, and the supply was fully taxable.

They argued that the original invoice was not a tax invoice as it was issued before the taxpayer was registered or liable to be registered. The services should therefore be treated as supplied on the receipt of payment.

The case went to the Court of Appeal where the majority disagreed. Agreeing with the taxpayer, the court concluded that all four elements of the charge referred to in s.4(1) VATA must be met before the time of supply rules in s.6 VATA are engaged. The four elements being that there must be:

1. a UK supply;
2. which is taxable;
3. by a taxable person;
4. in the course or further of their business.

In *B J Rice*, element 3. was not met as the original supply was made at a time when the taxpayer was not VAT registered.

The Tribunal went on to say that Silverfleet Capital Ltd was a member of the The Prudential Assurance Company Limited's VAT group throughout the time when it actually supplied the investment management services. S.43(1) VATA clearly states that throughout that time any business carried on by a member of the group is to be treated as carried on by the representative member.

The Tribunal stated that this would seem to place Silverfleet Capital Ltd in a similar position to that of the taxpayer in the *B J Rice* case, as element 4, was not satisfied by Silverfleet Capital Ltd.

The appeal was allowed but the Tribunal did go on to say that:

> "If there is a point of distinction - and I have not been convinced by HMRC's arguments in this appeal that there is one - I think it must be for a higher Tribunal or Court to find it."

The Prudential Assurance Company Limited v HMRC (TC08036)

R&C Brief 5 (2021) (Lecture B1256 – 16.27 minutes)

This brief explains HMRC's amended policy concerning the VAT treatment of installation of manual blinds and shutters. The policy change is effective from 5 October 2020.

The construction of a dwelling and building materials provided by the persons supplying the construction services are zero-rated for VAT purposes. Building materials covers materials ordinarily incorporated by builders in a building and includes bricks, timber, kitchen units, sinks and toilets.

Prior to the First Tier Tribunal's decision in Wickford Development Co Ltd, roller blinds could not be zero-rated. However, HMRC now accepts that the installation of manual blinds and shutters are building materials for VAT purposes and can be zero-rated when installed in a qualifying build.

HMRC confirms that the new treatment does not extend to window blinds that are motorised, that are considered 'electrical appliances' and so subject to the input tax blocking order (Value Added Tax (Input Tax) Order, SI 1992/3222).

The brief also states that DIY housebuilders can use a refund scheme to claim VAT charged on manual blinds.

https://www.gov.uk/government/publications/revenue-and-customs-brief-5-2021-vat-liability-of-installation-of-blinds-first-tier-tribunal-decision

VAT on e-commerce goods (Lecture B1260 – 20.53 minutes)

From 1 July 2021, the EU e-commerce directive comes into force and the VAT rules on cross-border business-to-consumer (B2C) e-commerce trading within the EU changes. This article will provide a useful reminder of the position both before and after that date.

Consignments up until 30 June 2021

Where consignments of goods valued up to €22 are sold to a customer in an EU country, the UK supplier will treat that as a zero rated export. As the goods are classed as a low value consignment, there is no import VAT payable in France. No Duty is payable provided the goods fall below the €150 threshold or the goods are of UK origin.

Up until the end of June 2021, where consignments are valued at greater than €22, there is still no UK VAT but import VAT is now payable in the destination country. This is normally accounted for via the French postal import system.

Under the postal import system, the customer is responsible for the VAT in the destination state. The tax authorities will collect the import VAT that is due before releasing the goods to the customer.

On their website, the UK supplier will be selling the goods net of VAT, with a note that the customer is responsible for settling the import VAT in their country. However, some e-commerce suppliers are giving their customers the option of paying gross, meaning that the local VAT is added to the sales price at check-out. This VAT is paid to the transport company so that the goods can be cleared at the border.

Consignments from 1 July 2021

From 1 July 2021 the EU e-commerce directive comes into force and the import VAT exemption for small consignments of a value up to €22 will be removed. This means all goods imported in the EU will now be subject to VAT but the way that it is collected is changing.

Where goods are imported with a value of up to €150, the seller will have to charge the destination country's VAT rate at the point of sale. This means that the seller should be advertising the goods net of VAT and then adding the correct country's VAT at the point of sale.

This declaration and payment of tax will be facilitated through the EU's new scheme for distance sales of low value goods, known as the Import One Stop Shop.

Where the supplier sells via an online marketplace (OMP), then the OMP will charge and account for the VAT that is due.

Import One Stop Shop (IOSS)

The UK supplier will need to register for IOSS in an EU member state of their choice by 1 July 2021. Having registered, the supplier will receive an IOSS registration number that must be communicated to the transport companies responsible for delivery of any goods sold. This should ensure that goods pass through Customs with minimal interruption. The IOSS number should be evidence that VAT has been accounted for at point of sale and there is no duty for consignments up to €150.

To facilitate this, the UK supplier will need to appoint a local representative to prepare their monthly IOSS returns. Monthly payments will be due via the registration portal of the member state chosen to register in. The returns will only include EU output VAT for each country where the supplier has traded, on a line by line basis.

Consignments over €150

These goods are not accounted for in the same way. Where such goods are sold to an EU customer, the UK supplier will continue to have a zero rated export but the EU VAT due will be payable through the relevant country's postal import system.

Where the goods are of 'UK origin', no duty will be payable. However, in cases where the origin rules are not satisfied, duty will also be payable.

Storing the goods in the EU

Where a UK supplier stores goods in an EU country prior to sale to EU customers, the UK Supplier will need to register for VAT in the country where the goods are stored.

So for example, if a UK supplier stores goods in Belgium for onward sale to customers in France, the UK supplier must:

- Register for VAT in Belgium;
- Charge Belgium VAT on the sale to the French customer.

Up until 30 June 2021, if the distance selling thresholds are breached in France, the supplier would need to register in that member state as well. From 1 July 2021, distance selling becomes a thing of the past. The point of sale system becomes effective and French VAT would need to be charged at point of sale.

Third party storage facility

What if the goods were being stored in an Amazon fulfilment house in Belgium?

Provided that Amazon are acting as the supplier's own-name agent, there is effectively a deemed sale to Amazon and then Amazon are deemed to sell the goods on. This would be a zero rated export for the UK supplier and Amazon would be responsible for the EU output VAT.

From 1 July 2021, the EU are also introducing an online marketplace rule whereby the online marketplace would be responsible for the local VAT, irrespective of own name agent status.

E-commerce into the UK from 1 January 2021

The UK introduced a similar system to the EU for consignments up to £135 but six months earlier.

Where a non-UK company sells goods valued up to £135 to a UK customer, no duty will be payable. However, UK supply VAT is due at the point of sale, meaning that the overseas supplier must charge UK VAT at the point of sale and must register for VAT in the UK.

If that supplier was selling through an online marketplace, the online marketplace must be registered for UK VAT and account for the point of sale UK VAT.

Selling to a business

Most e-commerce transactions are B2C supplies. However, where a non UK company sells goods to a UK business for an amount up to £135, provided that the overseas company obtains the UK company's VAT number, the UK company must reverse charge the supply. The same will apply where a UK company sells to an EU business.

Goods stored in the UK by overseas supplier

If goods valued at up to £135 are in the UK at point of sale, then the overseas supplier will already be UK registered as the goods have been imported into the UK.

If the goods are then sold to unregistered customers via an online marketplace the:

- overseas supplier has a zero rated supply to the online marketplace;
- point of sale VAT is accounted for by the online marketplace.

If the goods are sold to a VAT registered customer, the supplier must charge VAT, with the online marketplace simply providing the supplier with the sales information.

Consignments into the UK greater than £135

These will be treated as a zero rate export in the country of dispatch but import VAT, rather than supply VAT, will be due in the UK. There will be an import declaration at time of arrival.

If the supplier is the importer of record, the supplier will register in the UK and use the UK postal import system

Remember, from 1 July 2021, the EU introduces the same rules for goods over *€150.*

Created from the seminar recorded by Dean Wootten