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Personal tax

IR35 appeal - adviser's error (Lecture P1456 – 22.32 minutes)

Summary – The Limited Liability Partnership's application to make a late IR35 appeal was denied due to their agent's error.

Barry Cowan, a former professional tennis player, performed services as a tennis commentator for Sky UK Limited through his limited liability partnership, Cranham Sports LLP.

On 18 June 2021, HMRC issued an opinion based on communications with the partnership and Sky, concluding that under a notional contract between Barry Cowan and Sky, Barry Cowan would be regarded as employed by Sky. Under the IR35 legislation, HMRC sought to collect additional income tax and class 1 NICs that were due in respect of the 2013/14 to 2018/19. HMRC's opinion letter acknowledged they could have misunderstood/ misinterpreted information supplied and stated they would of readdress any consequent issues brought to their attention and advise accordingly.

On 8 July 2021, the LLP's agent replied by email setting out 23 disputed points. HMRC ignored these points and in a letter dated December 2021 and email to the taxpayer, the HMRC officer stated:

> 'If you disagree with HMRC's position, you have 30 days from the date of this letter within which to either accept my offer of an internal review by replying to this letter or notify the appeal to tribunal.
>
> If you neither accept the offer of a review nor notify the appeal to the tribunal, the appeal will be treated as settled by agreement under section 54(1) of the Taxes Management Act 1970 on the basis of my view of the matter as set out above.'

The agent replied promptly, accusing HMRC of failing to deal with any of the points previously raised, but did not respond to HMRC's 30-day deadline.

About two months later, the LLP appealed to the First Tier Tribunal, who, having considered the three-stage test in Martland v HMRC, did not accept the late appeal.

As a reminder, the three stages are:

1. Establish the length of the delay – The First Tier Tribunal confirmed that this was 60 days and considered this serious enough to move on to the second and third stages;

2. Consider the reason why the default occurred – The First Tier Tribunal stated that 'Acting prudently, a competent professional could have been expected to have protected the Applicant's position by formally asking for an internal review' rather than taking no action;

3. Evaluate "all the circumstances of the case" – The Tribunal stated that instead of 'seeking to remediate the position as soon as possible the representative continued

> to lock horns with what he considered to be the outrageous conduct of HMRC. He did not appeal but continued to make complaint to HMRC'.

The matter moved to the Upper Tribunal.

Decision

The Upper Tribunal found that there had been no errors of law made by the First Tier Tribunal.

The First Tier Tribunal had considered all of the relevant issues and was entitled to reach the decision that it had made.

Cranham Sports LLP v HMRC [2024] UKUT 00209 (TCC)

Rugby pundit caught by IR35 (Lecture P1456 – 22.32 minutes)

Summary – The Upper Tribunal overturned the First Tier Tribunal's decision, finding that the intermediaries legislation applied to a former rugby international, providing commentary and punditry services through his personal service company.

S & L Barnes Limited provided the services of Stuart Barnes to a number of media organisations, including *The Times, Sunday Times* as well as several broadcasters.

This case concerned two contracts covering the period 2013 to 2019 during which time S & L Barnes Limited supplied the services of Stuart Barnes to Sky TV, representing approximately 60% the company's overall income.

The First Tier Tribunal had applied the Ready Mixed Concrete three-stage test to the hypothetical contract between Stuart Barnes and Sky, ultimately finding in S & L Barnes Limited's favour. In reaching this decision, the First Tier Tribunal had identified twelve factors which pointed away from employment and concluded that IR35 did not apply.

HMRC appealed to the Upper Tribunal on two grounds:

> Ground 1: The First Tier Tribunal had erred in its construction of the hypothetical contract concerning Sky's right of first call over Stuart Barnes and purported variations to the contract.
>
> Ground 2: The First Tier Tribunal had erred in its interpretation and/or application of the third stage of the RMC test, including by taking into account irrelevant factors and failing to take into account relevant factors.

Decision

With both parties and the First Tier Tribunal having agreed that the intermediaries 'control' requirement was satisfied, the Upper Tribunal found that Ground 1 of this appeal was only relevant insofar as the First Tier Tribunal's findings influenced its decision regarding the third stage of the RMC test and/or its overall decision that IR35 did not apply. The extent of control in the hypothetical contract should be a relevant factor, at this time.

The Upper Tribunal were satisfied that this was taken into account by the First Tier Tribunal, as it was specifically identified as a relevant factor at that time.

The Upper Tribunal found that there was sufficient evidence available to enable the First Tier Tribunal to reach the decision which it did, including its acceptance of Stuart Barnes' evidence that he gave priority to his newspaper columns at certain times.

Moving the second ground of appeal where HMRC argued that the First Tier Tribunal had taken into account irrelevant factors and failed to consider material factors as required at the third stage.

The Upper Tribunal agreed with the First Tier Tribunal that certain factors were contrary to employment including the unrestricted use of his intellectual property by being allowed to recycle his Sky material in his newspaper columns, with Sky's full knowledge and the variation clause in the hypothetical contract that allowed him to make himself unavailable for match commentaries during various tournaments.

However, the Upper Tribunal found that the First Tier Tribunal had failed to take into account relevant factors pointing towards an employment contract which were significant and included:

- the long duration of the engagement, being a fixed term of four years extendable by two years;
- the lack of a right to provide a substitute;
- Sky's right of first call for 228 days a year;
- Sky's right of exclusivity;
- The 'very limited' financial risk undertaken by Stuart Barnes as he received a significant fixed monthly fee in advance that was not linked to actual work done. Further, Sky provided all studio equipment and related travel and accommodation bookings

Having found material errors of law which outweighed other the factors, the Upper Tribunal remade the decision, finding that the relationship under the hypothetical contract would have been one of employment. His work for Sky did not form part of his business on his own account

HMRC v S & L Barnes Limited [2024] UKUT 00262 (TCC)

Excessive CJRS claims (Lecture P1456 – 22.32 minutes)

Summary – The taxpayer had claimed excessive Coronavirus Job Retention Scheme payments, calculated based on salaries increased after the relevant cutoff date set out in the legislation.

Kingdom Travel Services Limited operates a travel business providing chauffeur services to passengers arriving and leaving Heathrow and Gatwick. The company owns some cars but does not employ drivers who are subcontracted.

Between March 2020 to March 2021 made 19 claims under the CJRS in respect of monthly salary payments of £2,000 said to have been made to three employees who were furloughed: Mr M Abdelbadia, Mrs Abdelbadia and Ms Al-Shemery.

Between September 2020 and December 2021 HMRC sought and were eventually provided with information relating to the business and the company's claims. HMRC established that in the PAYE return made on 29 February 2020 the employees were shown to have been paid their February salaries as follows

- Mr Abdelbadia £900.00 (gross);
- Mrs Abdelabdia £700.00 (gross); and
- Ms Al-Shemery £811.04 (gross).

The company claimed that on 22 February 2020, Mr Abdelbadia had notified each employee that they were to receive a salary increase payable from 1 March 2020 such that their salary increased to £2,000 per month.

With the reference salary for the purposes of the CJRS being determined by the pay reference period ended prior to 19 March 2020, HMRC determined that the company's entitlement to CJRS was limited to the lower salaries paid in February. In June 2022, HMRC issued assessments totalling just over £53,000 as well as penalties.

The company appealed to the First Tier Tribunal but no appeal was lodged in respect of the penalties, with any appeal now would be out of time.

Decision

The First Tier Tribunal found the company was entitled to receive CJRS payments for its three fixed rate employees calculated as:

- Mr Abdelbadia: 80% of £900.00;
- Mrs Abdelbadia: 80% of £700.00;
- Ms Al-Shemery: 80% of £811.40.

The Tribunal confirmed that the legislation did not make provision for salary increases either immediately before or during the operation of the scheme.

With the assessments raised by HMRC within 4 years of the earliest period to which they pertain, they were in time and therefore valid.

Mr Abdelbadia's argued that HMRC should not have allowed the company to continue to make the claims at £2,000. Had he known that his CJRS payments would be based on the lower salaries, he would not have paid the higher salaries.

He also claimed that if the CJRS payments were restricted then he should be entitled to reimbursement of the PAYE tax on the £2,000.

The Tribunal stated that:

- it was not for them to determine whether contractually the employees were entitled to £2000;

- if the £2,000 payments were contractually made, then the PAYE, NICs and pension contributions would have been calculated correctly irrespective of the company's entitlement to CJRS;

- it was not for them to determine whether HMRC should have stopped the CJRS payments as the Tribunal has no jurisdiction to consider HMRC's conduct generally

For these reasons the appeal was dismissed.

Kingdom Travel Services Limited v HMRC (TC09256)

UK business liable for employers' NICs **(Lecture P1456 – 22.32 minutes)**

Summary – The company was liable to account for employers' NICs under the 'host employer' provisions (SI 1978/1689, Sch 3 para 9).

Bilfinger Salamis UK Ltd supplied services to a North Sea oil platform operator, Marathon Oil UK Ltd, using its own employees. These employees were divided between a core team who were on permanent contracts and ad hoc employees on short term contracts.

At Marathon Oil UK Ltd's request, this arrangement was later modified to an offshore employment model, with the aim of avoiding employers' NICs. This involved the core team of Bilfinger Salamis UK Ltd employees being transferred to a Guernsey company, BIS Guernsey Limited, and then this Guernsey company then supplying the labour to Bilfinger Salamis UK Ltd. That core team worked on the oil platforms under Bilfinger Salamis UK Ltd's direction as part of fulfilling Bilfinger Salamis UK Ltd 's contract with the oil platform operator.

The issue to be decided by the First Tier Tribunal was whether Bilfinger Salamis UK Ltd was liable for Secondary Class 1 NICs in respect of their core team's earnings, despite them being employed by a Guernsey employer.

During the relevant period Para. 9 Sch. 3 of the Social Security (Categorisation of Earners) Regulations 1978 (SI 1978/1689) made an entity liable to secondary Class 1 NICs where it was a 'host employer' to whom 'the personal service' of a person employed by a foreign employer was 'made available', and where those services were 'rendered' to the host employer for the purpose of its business.

Decision

It was common ground that Bilfinger Salamis UK Ltd fell within the definition of 'host employer' and that, if the personal service of the relevant individuals was made available to Bilfinger Salamis UK Ltd, it was 'rendered' for the purpose of Bilfinger Salamis UK Ltd's business. The point in dispute was the interpretation and application of the requirement that 'the personal service' of Bilfinger Guernsey's employees was 'made available to' Bilfinger Salamis UK Ltd.

Bilfinger UK's argument was that para 9 only applied where there was an arrangement whereby the individual became in substance the employee of the host employer, with the host employer entitled to exercise such supervision, management and control over the individual as is normally conferred on an employer by an employment contract.

Taking a purposive approach to the legislation, the First Tier Tribunal found as follows:

1. The purpose of para 9 was to cover secondment-like arrangements (rather than ordinary subcontracting, or anti-avoidance).

2. 'Personal service' had the same meaning as in employment case law, namely the obligation that the employee work 'by one's own hands', not 'by another'.

3. For personal service to be 'made available' to the host employer, the host employer had to have some degree of direction over the relevant person, but this need not include a legal right to give such direction. The First Tier Tribunal noted here that if, as Bilfinger Salamis UK Ltd suggested, for para 9 to apply the foreign employer was required to alienate the legal right (vis-a-vis the employee) to direct the individual, then they would cease to be the foreign employer, thus rendering para 9 impotent.

4. The definite article, 'the', before 'personal service' in para 9 carried significance and required that the entirety (viewed realistically) of a given employee's personal service is made available and rendered. The obligation to the foreign employer persists, but at the choice and command of the foreign employer it is only rendered for the business of the host employer.

Applying its reasoning to the facts, the First Tier Tribunal found that viewed realistically the entirety of the 'personal service' of the core team of Bilfinger Guernsey employees was 'made available' and 'rendered' to Bilfinger Salamis UK Ltd for the purposes of Bilfinger Salamis UK Ltd's business. Accordingly, para 9 applied, meaning that Bilfinger Salamis UK Ltd was liable as the secondary contributor for Secondary Class 1 NICs during the relevant period. Bilfinger Salamis UK Ltd's appeal was therefore dismissed.

Bilfinger Salamis UK Limited v HMRC (TC09261)

Adapted from the case summary in Tax Journal (6 September 2024)

Expenses reimbursed by umbrella company (Lecture P1456 – 22.32 minutes)

Summary – An umbrella company's employees could not claim a deduction for reimbursed travel and subsistence expenses as each assignment was deemed to be a separate employment taking place at a permanent workplace.

Mainpay Limited was an umbrella company that engaged workers to undertake assignments for third party end users, such as hospitals and schools via an employment agency.

The company argued that:

- there was a 'single overarching contract of employment' covering gaps between assignments as well as the assignments themselves;

- each worker carried out assignments at multiple temporary workplaces;

- travel and subsistence expenses to and from the workplace were deductible from the workers' earnings for tax purposes.

HMRC disagreed stating that each assignment was treated as a 'separate employment' at a permanent workplace, and so denying relief for the travel and subsistence payments claimed. Determinations were raised accordingly against and the company appealed to the First Tier Tribunal who found in HMRC's favour and the case moved to the Upper Tribunal.

Decision

The Upper Tribunal agreed with the First Tier Tribunal that the contract between the umbrella company and each worker did not represent overarching contract of employment as they lacked mutuality of obligation. Despite Mainpay Limited having a contractual obligation to provide each employee with 336 hours of work each year, the workers had no obligation to accept work offered. However, Mainpay Limited was not obliged to pay the workers for the minimum number of hours of work, even if not worked.

The Upper Tribunal rejected the company's argument that even if there was no overarching contract of employment, the contract gave rise to a single employment relationship, meaning that the workplaces where workers carried out their assignments could not be "permanent workplaces" as they would not be workplaces for that single employment. The First Tier Tribunal was entitled to reach its conclusion that each contract was 'a framework agreement which provided the basis on which consecutive contracts of service for individual assignments could arise.'

Mainpay Limited sought to argue that just because a workplace was not considered temporary, that did not mean it automatically became a permanent workplace and that expenses could still be claimed as deductible provided that the employee did not regularly attend that workplace.

Even if a third category of workplace was permitted under legislation, the Upper Tribunal found that Mainpay Limited's argument relied on an employee not being in 'regularly attends in the performance of the duties of the employment'. The First Tier Tribunal was correct to construe the legislation as referring to attendance at a workplace 'every day during which the employment subsists', even if that was only for one day. The Tribunal accepted that for a one-day assignment, 'regular' was not the most obvious choice of word, but in that context, it simply means regular attendance during that day in the performance of the employment duties. The Upper Tribunal pointed out that Mainpay Limited's own evidence confirmed that the average assignment lasted eight weeks, and so there would be 'few instances' where the workplace would not have been regularly attended. As the employees were found to 'regularly attend' their workplace, the Upper Tribunal concluded that it was not necessary to determine the question of whether legislation contemplates that a third category of workplace, which is neither temporary nor permanent.

Although not necessary, the Upper Tribunal went on to consider whether, had the expenses been deductible, they could have been reimbursed using HMRC's system of benchmark scale rates. The Upper Tribunal stated that for such rates to be used, Mainpay Limited would have needed to have applied and obtained a dispensation to do so from HMRC. Such a dispensation allows HMRC to confirm that adequate procedures are in place to ensure that employees have actually incurred expenses and that any other relevant conditions (such as the workplace not being a permanent workplace) are complied with. With no such dispensation in place, the rates could not be used. The only amounts that could be deducted were the actual expenses incurred.

The final ground of appeal was that any loss of tax had not been brought about carelessly. However, although Mainpay Limited had obtained legal advice, it had not asked its advisers the right question.

The First Tier Tribunal accepted that advice had been sought regarding the deductible of reimbursed expenses but 'there was no detailed explanation as to what these expenses were and the basis on which they might be deductible or allowable for tax purposes.' As a result, the six-year time limit for making the assessments and determinations applied, meaning they were validly issued.

Mainpay Limited v HMRC [2024] UKUT 00233 (TCC)

Discretion not to apply PAYE obligations (Lecture P1456 – 22.32 minutes)

Summary - HMRC had misdirected themselves in law in its decision not to exercise its discretion to relieve the company of its PAYE obligations in respect of a former employee's income.

In 2002, as part of his remuneration package, Jonathan Wood and UBS AG entered into three gilt options, which were not exercised until 2012, after Jonathan Wood had left the company. The gilts were not received until 2016/17 due to certain valuation issues.

HMRC issued a determination under the Income Tax (Pay As You Earn) Regulations, SI 2003/2682, reg 80, requiring the company to account for PAYE.

The company challenged the determination, taking several different approaches, one of which was a request that HMRC should exercise its discretion under s 684(7A) ITEPA 2003 to remove obligation on employer to account for PAYE in respect of employee's tax liability on earnings in the form of gilts

HMRC stated that it was not appropriate for HMRC to make a decision on the use of the discretionary power at that time as the final liability had not been determined.

UBS AG sought judicial review of that decision arguing that:

- HMRC's refusal to exercise its discretion ran counter to the purpose of the statute;
- HMRC had misdirected itself in law and its decision was irrational.

The company sought an order requiring HMRC to exercise its discretion to relieve the company of liability.

HMRC argued that, because it had subsequently agreed to reconsider its discretion, the judicial review had been rendered academic and so should be dismissed.

Decision

The Upper Tribunal held that the issues were not academic because HMRC had only said that they would reconsider their decision and this did not give UBS AG what it sought, which was an order that HMRC be required to apply its discretion.

The Upper Tribunal found that HMRC had misdirected themselves on the law in two ways:

1. In considering that the exercise of the discretion was premature because the quantum of the liability had not been established. There was no reason in principle why the liability had to be established before considering the discretion.

2. HMRC had said that even if the discretion were exercised, UBS would still have to deal with HMRC in respect of NICs. The Upper Tribunal held that this did not detract from the efficiency savings claimed by UBS because its NIC liability would be determined by the amount taxed as employment income.

The Upper Tribunal therefore ordered that HMRC should remake its decision on whether to exercise its discretion, taking account of the mis-directions.

The King (on the application of) UBS AG [2024] UKUT 00242 (TCC)

Adapted from the case summary in Tax Journal (30 August 2024)

High Income Child Benefit Charge partial win (Lecture P1456 – 22.32 minutes)

Summary – The total amount assessed, penalties charged and interest payable were reduced when it was decided that the taxpayer had a reasonable excuse for last four years assessed by HMRC.

Sarah Manzi had been claiming child benefit from 2005 some 8 years before the 2013 introduction of the High-Income Child Benefit Charge (HICBC).

Between 2014/15 to 2019/20, tax was collected on her earnings through PAYE.

As her earnings were below £50,000, she did not pay attention to the 2012 media campaign. By 2014, her earnings were above £50,000 but she was unaware that this meant she should have notified her liability to the HICBC and filed a self-assessment return.

On 3 December 2019, Sarah Manzi received a letter from HMRC advising her to check her liability to the charge. A few days later, she called HMRC and was advised by an HMRC officer that the letter may have been sent in error but that she should deregister for child benefit and that no further action was required. She deregistered as advised.

In June 2021, HMRC informing her by letter that she owed £10,480 across the 2014/2015 to 2019/20 tax years for the unpaid HICBC.

HMRC paused work on all HICBC cases, pending the Upper Tribunal decision in the Jason Wilkes case. Following this decision, HMRC wrote, confirming the assessment had been reduced to reflect her only claiming child benefit for part of the 2019/20 tax year, the year when she was first made aware of the issue.

Finally, on 1 November 2022, HMRC formally issued assessments to collect the charge and penalties that were payable.

Sarah Manzi appealed claiming that she had a reasonable excuse which was 'ignorance of the law'.

Decision

The First Tier Tribunal considered the validity of the assessments raised by HMRC.

- Due to the delay by HMRC, only the assessments for 2018/19 and 2019/20 fell within the standard four-year time period.

- The earlier years could only be validly raised if Sarah Manzi had failed to take reasonable care or had no reasonable excuse in failing to notify her liability.

The First Tier Tribunal found that prior to December 2019, Sarah Manzi was an employee within the PAYE system and was unaware of the HICBC. This amounted to a reasonable excuse as the charge had not existed when she started claiming child benefit. Further, before this time, she had never been made aware of the requirement to notify her chargeability to the charge once when her income exceeded £50,000.

Although that excuse ended when she received HMRC's letter in December 2019, she had a further reasonable excuse based on the officer's advice that the letter could have been an error. She followed the officer's advice at the time by deregistering for child benefit and took no further action as instructed. Consequently, she had a reasonable excuse up until she received HMRC's letter in June 2021, by which time it was too late for her to notify by filing a Self Assessment return.

With HMRC failing to produce the call log to support their claim that the call in December 2019 never took place and that no officer would have given the advice claimed, the First Tier Tribunal found in Sarah Manzi's favour.

Sarah Manzi's appeal was allowed in part with only the assessments for the 2018/19 and 2019/20 being made within time and being valid. HMRC's assessments for 2014/15 to 2017/18 were out of time. The charge and penalty assessment were cancelled. The Tribunal noted that the total interest payable would need to be reduced accordingly.

Sarah Manzi v HMRC (TC09219)

Capital taxes

The problem of PETs (Lecture P1459 – 20.34 minutes)

As a result of speculation regarding the forthcoming budget on 30 October, a considerable number of clients are considering making transfers to their children or other relatives in case the inheritance rules (IHT) are tightened. This article shows some of the perils in doing this and the requirement for proper consideration before hasty and potentially irreversible action is taken.

Background

By way of background, the concept of potentially exempt transfers (PETs) has been around since the 1890s when Estate Duty was introduced. The principle then was that if an individual survived 5 years after making gifts, then those gifts would not be subject to Estate Duty. This rule applied until the introduction of Capital Transfer Tax in 1975 (CTT). CTT attempted to tax all transfers beyond an exempt band. CTT lasted until 1986 when tax on some lifetime transfers were lifted, and the tax was renamed Inheritance Tax.

The new regime of potentially exempt transfers extended the period under which transfers could be subject to IHT to 7 years before death. However, it did also introduce a taper arrangement whereby there was a progressively greater reduction in tax if the individual survived more than 3 years after the gift.

Also, a number of anti-avoidance rules that had been in Estate Duty but not required for CTT were reintroduced with IHT. These most notably included the gift with reservation clause, where broadly if one gives away an asset and continues to enjoy it, it remains within ones estate when one dies.

Potentially Exempt Transfers look like a relatively easy way of avoiding inheritance tax but there are a number of considerations which should give people pause for thought. First of all, there is the non-tax consideration that once the asset has been given away, they are no longer available for the individuals use. They may remain within the family but if the planning is to be effective, the individual can gain no benefit from them. This has a number of consequences, both tax and non-tax.

However, perhaps the non-tax consideration is the most important. Given that, life expectancy has been growing, particularly for the sort of people who have IHT issues, individuals should be aware that they may need considerably more money than they anticipated. This could be to fulfil whatever goals they have in retirement (the bucket list of travel places), but also the care fees which may become necessary. A quick review of care fee costs would show that one could get through a substantial amount of money very quickly indeed.

Family relationships are often fluid and therefore relying on family may not be wise even if the relationship may be good at the moment. Even if the relationship may remain good, one needs to take into account that the funds or property given to relatives may be beyond their ability to return even if circumstances change.

Moving on to the tax points, one needs to be aware that PETs could create unequal circumstances between those receiving funds. For example, if one had 3 children and one was to give Richard and James money but leave Alex to inherit when one died. Richard and James' gifts may be free of IHT under the current rules, but they would affect the amount of tax that Alex would suffer on his legacy as any PETs within 7 years of death would use up the nil-rate band. So, if Richard and James received £162.5k each, they would pay no IHT but if you then left Alex another £162.5k in your will and died within seven years of the earlier gifts, he would have IHT of £65k to pay.

You could therefore have been said to have dealt with the children equally, but some more equally than others!

Capital Gains Tax

You also need to consider that a taxpayer who gives away assets, standing at a gain, may have an immediate charge to Capital Gains Tax on the basis that they have made a disposal of an asset standing at a gain which is a chargeable asset. This could create a double-tax charge as if the taxpayer dies within 7 years there will be IHT on the failed PET, but no credit given for the CGT paid.

Some taxpayers may look to hedge their bets by giving amounts conditionally or with a revocation clause. This could well fall foul of any anti-forestalling measures announced at the budget. This is a common feature which may affect actions taken between the 30th of October and the end of the tax year when most measures are likely to come into place. It may also affect conditional arrangements which have not been finalised. Similar measures were introduced when Business Asset Disposal Relief replaced Entrepreneurs Relief with the allowance cut from £10m to £1m.

In choosing what gifts to give away, it is generally to choose items which either are not subject to CGT or where the chargeable gain is small, or indeed when one is crystallising a loss.

Foreign aspects

Inheritance Tax is a donor-based tax, as is Capital Gains Tax. One does however need to consider the residence and tax status of any donee as this may affect the overall effectiveness of protecting family wealth.

Family circumstances

One also needs to consider the potential impact of divorce on any family wealth. The general position has been a move towards clean break divorces. This means that if one gives away substantial amount to a child, it is quite possible that half of this would disappear if that child gets divorced. One way of protecting family assets would be to put the assets in trust for grandchildren and future descendants. This could protect the family assets.

One does need to bear in mind however that amounts that are put into trust above the nil-rate band will generally incur a 20% entrance charge. However, assets which are not subject to IHT or a full deduction at present such as AIM shares, unquoted UK trading shares etc. would not create an exit charge. The nil-rate band could be doubled by using the spouses unused band as well.

Conclusion

Although PET's sound deceptively simple, one should remember that the consequences are not just for Budget Day; they last a lot longer.

Contributed by Jeremy Mindell

Charitable donations and holiday lets (Lecture P1457 – 14.54 minutes)

Summary –Business Property Relief was not available on a let property and the 36% IHT rate did not apply.

Samuel Marks died in April 2014 leaving various pecuniary legacies with the residue of his estate to be held on trust for his wife, Hilda. The terms of the Will Trust stated that:

- Hilda was entitled to receive income from the trust during her lifetime;
- The trustees had the power to appoint funds out of the trust to specified relations, which they did, including a property to the grandchildren;
- On Hilda's death, the trust capital was to be divided 25:75 between a charity and specified relatives.

Hilda died in October 2015 and her executors submitted the IHT account IHT400 and supporting schedules, which included a charitable donation of £29,063 and a claim for Business Property Relief on a holiday let included within the free estate;

In November 2016 HMRC commenced a review, looking initially at the Business Property Relief claim and the valuation of the shares and properties included as part of the estate.

Following this review, the executors decided that the original Will Trust had been incorrectly interpreted and they submitted revised IHT Forms, including IHT Form 430, claiming the reduced rate of IHT as they believed that at least 10% of Hilda's net estate had been left to charity. On the IHT Form 430 the executors elected to merge the Free Estate and the Will Trust and to claim the reduced IHT rate on both components.

HMRC understood that the executors believed that:

- under the terms of the Will Trust the 25% of the estate payable to charity should be computed by reference to the value of the property in the Will Trust as at the time of creation of the Trust, and not by reference to the residue after the appointments out during Hilda's lifetime.
- As these appointments from the trust had left insufficient funds in the trust to be able to discharge the 25% charitable payment requirement in her husband's will, the shortfall should should be made from Hilda's Free Estate.
- The charitable contribution from the Trust should be recomputed by reference to the trust assets valued when created;

- As the recomputed charitable contribution would exceed 10% of both Free Estate and the Will Trust, the reduced rate of IHT should apply across both components in accordance with the election made in IHT Form 430.

HMRC disagreed and issued Determinations that effectively reinstated the original Form 400 position.

The Executor appealed challenging the entitlement to use the 36% tax rate and also the fact that HMRC denied the Business Property Relief claimed. On the latter, the executor sought to rely on two factors which he claims differentiated her property business, moving it into the non-investment category which were:

- Hilda’s personal involvement in the business; and
- the fact that it was a kosher holiday let, aimed at a specific type of holidaymaker.

Decision

The First Tribunal noted that, had the executor been right and the charitable donation be based on the value of the Will Trust on its creation, the contribution to charity would be in the region of £250,000 and would amount to at least 10% of the combined Will Trust and Free Estate. This would result in the lower rate of IHT applying to the entire estate.

By contrast, HMRC argued that the terms of the husband’s Will Trust provided for the charitable donation to be calculated as 25% of her husband’s residuary estate when Hilda died, and so after the appointments out during lifetime. This would have depleted the residuary estate such that the charitable contribution of 25% would be around £29,000. As this would not amount to 10% of the combined Will Trust and Free Estate, the lower rate of IHT would not be available across the entire estate.

Consequently, the First Tier Tribunal stated that it needed to determine:

- the correct interpretation of the late husband’s will as it applied to the charity donation;
- whether the appointments made to the grandchildren were advances in respect of their entitlement to the husband’s ultimate residuary estate or were they absolute appointments of trust property at the time. If advances, the payments would not deplete the residuary estate, and the sum to the charity would be calculated by reference to the intact residuary property.

On the Will interpretation issue, the First Tier Tribunal found in HMC’s favour. The Tribunal stated that on reading the terms of the Will, the late husband’s residuary estate was to be applied during Hilda’s lifetime by the Trustees as they saw fit and for the charitable donation to be determined by reference to what is left on her death. There was no requirement in her husband’s Will to maintain the quantum of the contribution to charity. Further, as noted by the Tribunal, the donation actually made was computed by reference to the remainder of the Residuary Estate after the appointments, resulting in only £29,063 being approved and paid over by the executors. Why had this happened if the executors had expected the sum to be around £250,000?

As for the ‘advances’ argument, this too was rejected, with the Tribunal stating that the Will Trust made specific reference to ‘appointments’; there was no mention of advances.

As a consequence, the First Tier Tribunal found that the lower 36% rate did not apply as the conditions had not been satisfied. The Tribunal accepted that the Trustees would not have taken the steps that they took had they understood the full IHT consequences of doing do, but this could have no impact on the outcome of their decision.

The Executor was no more successful in their claim for Business Property Relief. The Tribunal reminded us that:

- there is no statutory definition of what is meant by a business "wholly or mainly holding investments" for the purposes of Business Property Relief;
- each case is dependent on its own facts and an evaluative exercise must be carried out to determine the outcome.

Despite the claim that Hilda had been directly and personally involved in the running of the business, there was no ‘material direct evidence of the way in which the business was operated’ provided to the Tribunal, which included a lack of basic records that would typically be expected such as invoices and receipts or letting contracts and terms.

The Tribunal considered what activities had been undertaken by the deceased, but concluded there was nothing in this list that persuaded them that her business was anything other than one of mainly holding investments.

Some of the services provided were 'investment' related such as the steps taken to finding guests, letting them into the property, collecting the payments as well as expenditure on repairs and redecoration of the property.

The Tribunal commented that the provision of food could be a key non-investment service but no information as to how often guests would actually require it to be provided was supplied and the precise nature of the ‘catering’ service was also unclear.

The Tribunal reached the same conclusion on the Kosher related services. On the information available, the Kosher related services specified did not seem to be sufficient to alter what would otherwise be mainly a business of holding investments.

David Marks (Executor of Hilda Marks) V HMRC (TC09253)

IHT Deathbed scheme **(Lecture P1457 – 14.54 minutes)**

Summary – Although an IHT avoidance scheme was ineffective, HMRC could not recover the loss as a certificate of discharge had previously been issued.

On 16 May 2011, Jennifer Fleet established The Jennifer Fleet Trust with initial capital of £20,000 and her sons, Luis and Nicholas Carvajal as the beneficiaries. Bourse Trustee Company Limited was the trustee.

To assist funding the trust, Havelet Finance Limited offered a £1.4 million term loan facility which could be drawn in one amount up to a month from acceptance. The facility required Jennifer Fleet to provide a personal guarantee and indemnity. The loan was repayable on demand and was also repayable on whichever was the earlier of the death of Jennifer Fleet or five years following the date on which it was drawn down. The fee charged by the lender was £20,000.

On 17 May 2011, having satisfied the conditions, the loan was drawn down and credited to the trustee’s client deposit account, who immediately invested the money in Bonds, charging the bonds in favour of the lender and then seeking permission from the lender to distribute the Bonds to the trust beneficiaries. The lender gave permission, provided the beneficiaries "collateralised" the personal guarantee provided by their mother, which they did.

On 23 May 2011, having received guarantees and indemnities the trustees resolved to allocate the funds to the beneficiaries, which was reflected in the general ledger on that date showing the two capital distributions of £700,000 each. This left the trust with no assets.

Jennifer Fleet died the next day and the debt became repayable and in November 2011, Jennifer Fleet’s £1.4 million guarantee appeared on her Form 400 as a liability, reducing her death estate to below her available nil rate band

In March 2015, Havelet Finance Limited issued a demand, which was addressed to the beneficiaries, rather than as executors of Mrs Fleet's estate, referring to the absence of assets within the estate and requesting that the son’s settle the debt under the terms of their guarantees, which they duly did by paying £1,400,000 from the redemption of the Bonds. Havelet Finance Limited confirmed that the debt due by the trustee had been discharged in full.

The accountants for the estate applied for a certificate of discharge under s.239(2) IHTA 1984, which was issued by HMRC on 11 December 2018. In doing so, the executors did not populate section B of the IHT 30 form that related to IHT liabilities on lifetime transfers.

Later, having enquired into the case and unaware of the discharge certificate having been issued, HMRC stated that the scheme did not work and so raised determinations in June 2019 to collect the IHT due on the £1.4 million.

The executors appealed.

Decision

The First Tier Tribunal found that by implementing the tax planning, and providing the guarantee, Jennifer Fleet had not made a transfer of value. Consequently, the scheme was ineffective in reducing the value of her estate for IHT purposes.

However, with HMRC having issued the clearance certificate, which confirmed that no more IHT was due on her death, HMRC was prevented from clawing back the underpaid IHT.

HMRC argued that the execution of the guarantee had resulted in a chargeable lifetime transfer, which was not covered by the clearance certificate. However, the First Tier Tribunal rejected this. The scheme failed in its entirety as there was no lifetime transfer of value made by Jennifer Fleet on the execution of the guarantee.

The appeal was allowed.

Note: The Tribunal was clear that 'had the Respondents not issued the Clearance Certificate in error, and thereby debarred themselves from pursuing … the transfer of value on death … the Respondents would have succeeded in relation to the appeals.'

Luis and Nicholas Carvajal (Executors of Jennifer Elizabeth Fleet's Estate) v HMRC (TC09248)

IHT property valuations (Lecture P1458 – 13.44 minutes)

Background

Valuations of assets in general for tax purposes is a specialised area. HM Revenue and Customs (HMRC) recognises the specialised nature of valuation work. HMRC's officers don't normally engage in tax valuations of assets; instead, they enlist the help of specialists in other government departments, such as Shares and Assets Valuation for unquoted shares, and the Valuation Office Agency (VOA) for land and buildings. Useful information on the VOA's approach to its valuation work for IHT purposes is included in its Inheritance Tax Manual (www.gov.uk/guidance/inheritance-tax-manual).

IHTA 1984, Pt VI deals with valuation. Those provisions include the related property rules, which provide that the value of related property must be taken into account when valuing a person's estate if this results in a higher valuation. Property is 'related' for these purposes broadly if it is in the estate of the individual's spouse or civil partner, or alternatively if it is, or was within the preceding five years, the property of a charity or certain other bodies to which exempt transfers may be made as the result of an exempt transfer (after 15 April 1976) by the individual, spouse or civil partner (IHTA 1984, s 161(2)). Potential valuation discounts for jointly-owned property is another difficult and complex issue which isn't specifically dealt with in the IHT legislation, and is not considered here.

Little help

The general valuation rule as stated in the legislation is that market value is: "…the price the property might reasonably be expected to fetch if sold in the open market at that time; but that price shall not be assumed to be reduced on the ground that the whole property is to be placed on the market at one and the same time" (IHTA 1984, s 160).

For IHT purposes, taxpayers and personal representatives will generally prefer a lower property valuation to a higher one, to reduce exposure to IHT liabilities. HMRC therefore regards valuations as a 'high risk' area in terms of the potential loss of IHT where valuations are too low. If HMRC enquires into a property valuation and it transpires that the property was undervalued, HMRC may seek to establish whether the valuer was negligent for penalty purposes, or whether the taxpayer failed to instruct the valuer properly.

Professional valuations

There is no statutory requirement to obtain a professional valuation of land and buildings. However, simply guessing their value is not recommended. Aside from additional IHT and interest, as mentioned, the material undervaluation of a property may result in the imposition of penalties.

HMRC's toolkit for tax agents or advisers when completing the IHT return form IHT400 for their clients (www.gov.uk/government/publications/hmrc-inheritance-tax-toolkit) states that for assets with a material value, taxpayers are 'strongly advised to instruct a qualified independent valuer, to make sure the valuation is made for the purposes of the relevant legislation, and for houses, land and buildings, it meets Royal Institution of Chartered Surveyors (RICS) or equivalent standards.'

HMRC also states that in the absence of proper instructions, the valuer will not understand the context or have all the necessary details to make a proper valuation. So, HMRC expects the person seeking the professional valuation to explain the context and draw attention to the definition of market value in *IHTA 1984, s 160*, and to provide the valuer with all the relevant details concerning the land and property, including copies of any agreements (such as leases), or full details where only an oral agreement exists. HMRC adds (in its Inheritance Tax Manual at IHTM36275):

> '...having first obtained a valuation or opinions of value, given entirely in good faith, they may subsequently become aware of further (marketing) information which casts doubt on whether the original valuations still properly reflect the open market value of the property at the date of death. If personal representatives are aware of such information we consider it is reasonable to expect them to ensure it is properly considered and reflected appropriately in the final valuation figure included in the account.'

Development value

A particular area of potential difficulty in property valuations is ascertaining a property's development value, which has been the subject of possible disagreement between valuers, and also an area of potential dispute with HMRC. When valuing a property, HMRC expects the valuer to consider whether there is any potential for development and, if so, to ensure that it is taken into account and reflected in the valuation. HMRC states (at IHTM36275) that it considers 'hope' value to be 'a component part of the open market value in appropriate cases, whether or not planning permission has been sought or granted'. The difficulty in establishing development value has resulted in several cases before the land tribunal.

For example, in *Prosser v IRC* (DET/1/2000 [2001] RVR 170, the garden of a house was large enough to potentially constitute a building plot. The district valuer suggested a figure as at the date of death assuming planning permission, and deducted an allowance of 20% to reflect that no planning permission had been given at the valuation date. However, the land tribunal held that there was a 50% chance of obtaining planning permission, and that a speculator purchaser in the absence of the planning permission wouldn't offer 80% of the development value, but would only offer 25%.

Subsequently, in *Palliser v Revenue and Customs* [2018] UKUT 71 (LC), a valuation of an individual's interest in a maisonette was obtained for probate purposes, which didn't reflect any hope value for future development or change of use. HMRC determined the value to be £1,829,880. The personal representative appealed, on the basis that the correct valuation was £1,113,840. The Upper Tribunal (Lands Chamber) considered that insofar as the property's potential for improvement hadn't been crystallised by planning permission, its value would be 'hope' rather than 'development' value, but either way, it could not be ignored. The tribunal determined the net valuation of the property with and without development. It then took 50% of the difference as representing the hope value. This was added to the market value of the property on death. The valuation in this case was complicated slightly in that the deceased's interest in the property wasn't 100%, but 88.4%. The value representing the deceased's 88.4% share was reduced by 10% to reflect the undivided share, giving a value of £1,603,930.

Major differences

Even if professional valuations have been obtained on behalf of both the taxpayer and HMRC, the approach taken by the professional valuers might differ, resulting in major differences in valuations for the tribunal to rule upon.

For example, in *Foster v Revenue and Customs* [2019] UKUT 251 (LC), a deceased individual's estate included 6.39 acres of an agricultural site. A dispute arose between the deceased's executor and HMRC about the open market value of the site for IHT purposes. The executor (on professional advice) valued it at £191,700; On the other hand, HMRC (on the VOA's advice) valued it at £850,000. The Upper Tribunal (Lands Chamber) (UT) considered that at the valuation date a hypothetical purchaser would have considered there to be a reasonable prospect of obtaining planning permission for the residential development of the site. However, there were problems to overcome (e.g., vehicle access to the site) which would be reflected in the price that the hypothetical purchaser would be prepared to pay. In addition, the valuation experts for the executor and HMRC took fundamentally different approaches to calculating the open market value of the site. The tribunal favoured HMRC's 'top down' approach (in other words, assessing the value of the site assuming it had residential planning permission at the valuation date and making deductions for access risk and planning risk and deferment) and applied a total risk adjustment factor of 80%. The tribunal determined the open market value of the site at the valuation date to be £590,000.

Forewarned is forearmed

The perceived high-risk nature of property valuations increases the possibility that valuations put forward on the taxpayer's behalf will be subject to enquiry by HMRC. If it transpires that there has been an undervaluation, HMRC will probably consider whether it was reasonable for the taxpayer to have relied on the valuation, or whether there something else known to them that would cast doubt on the value.

The types of questions HMRC might ask are listed in the Inheritance Tax Manual at IHTM36153 for undervaluations generally, and at IHTM36154 for undervaluations of land and buildings. The list at IHTM36154 asks:

- 'whether all relevant information available to the taxpayer concerning the property was passed to the valuer;
- that any professional valuation properly considered development potential and any 'hope' value was appropriately reflected in the overall valuation and not specifically excluded;
- whether the taxpayer questioned any valuation advice which obviously ignored relevant information or which did clearly not represent an open market valuation;
- whether any significant assumptions made by the valuer about the property which affected its open market value were checked by the taxpayer.'

In addition, if the property was for sale before the IHT return was submitted, HMRC may ask:

- 'were any offers received (if so, obtain details of any offers made, to include when they were made, by whom they were made and the amount offered).
- where applicable, were best and final sealed bids invited (if so, the same details as above should be sought).

- was a sale agreed or contracts exchanged before the account was delivered (if so, to whom, when and at what price)?'

Before submitting a valuation to HMRC, it may be helpful to consider what HMRC's approach might be if the valuation was subject to enquiry.

Contributed by Mark McLaughlin

Multiple dwellings relief claim (Lecture P1457 – 14.54 minutes)

Summary – Despite two dwellings having common utilities and internal doors, they were found to be suitable as separate dwellings and multiple dwellings relief was allowed.

James Winfield acquired Gilboa Barn for £1.8 million on 16 December 2021. On completion, the property comprised two "dwellings":

- Dwelling 1 had been unoccupied since completion, and consisted of a large bedroom, a snug/office, a bathroom, a large living/dining area, kitchen/utility room, downstairs toilet, office/storage room. It also had separate outside entrances.

- Dwelling 2, was where James Winfield's family currently lived; it had four bedrooms, two bathrooms, toilets, sitting room, dining room, kitchen/utility room, large hallway, and separate outside doors for access.

The electricity came into the back of Dwelling 1 but then split into two independent fuse boxes. Although there were two electricity meters, the electricity was billed to the property rather than the separate dwellings.

There was a single oil-fired boiler located at the same place as the fuse boxes which served both dwellings and provided hot water, and water for the central heating system for both dwellings. The boiler had a single timer and temperature setting for both dwellings. This too was billed to the property and not the dwellings separately.

Each dwelling had a separate water supply and stopcock, but the property had a single council tax account and postal address. Both dwellings are registered with the same title number with HM Land Registry and on purchase, the dwellings had been marketed as a single dwelling.

A letter from the previous owner indicated that at various times she had rented out one of the dwellings (and lived in the other), rented both dwellings out separately, and rented out the entire property.

James Winfield argued that property bought consisted of two separate dwellings, suitable for use as such and claimed multiple dwellings relief.

HMRC denied the claim, arguing that the property was a single dwelling, with a single council tax account and address, a lack of privacy and a lack of independent utilities.

James Winfield appealed.

Decision

The First Tier Tribunal adopted a multifactorial assessment, taking into account all of the facts and circumstances to consider whether the occupant's basic living needs were capable of being satisfied 'with a degree of privacy, self-sufficiency and security consistent with the concept of a single dwelling'.

On the privacy issue, the Tribunal commented that many rural developments involved barn conversions as well as other separate dwellings sited close together, often "around a single courtyard, where occupants of one dwelling can readily see into the rooms of another". Any perceived lack of privacy did not seem to matter to the buyers.

The First Tier Tribunal found that the internal doors provide adequate security between the properties as they were 'substantial, lockable, and … soundproof and fireproof'.

The First Tier Tribunal did not consider the utility access to be an issue. Freehold owners are often subject to common right-of-way. If dwelling 1 were let, access would be on the basis of a proper legal agreement.

Looking at the overall picture, the First Tier Tribunal concluded that multiple dwellings relief did apply. The Tribunal stated:

> "The physical configuration and attributes of each dwelling carries very considerable weight, and that is not, in our opinion, diminished by the common utilities or the state of the internal doors."

Multiple dwellings relief was allowed.

James Winfield v HMRC (TC09259)

Administration

Automated notices and assessments (Lecture P1457 – 14.54 minutes)

Summary – Automated notices and penalty assessments were validly issued. The effect of s.103 FA 2020 is that it is not necessary for HMRC to prove the involvement of an 'officer of HMRC' in the giving of a statutory notice or assessment.

Peter Marano was a US citizen who delayed reporting a very large capital gain, taxable on the remittance basis:

- In December 2012, his accountant had informed HMRC that he had remitted a chargeable gain, and that the CGT payable was estimated to be £5,744,219;
- On the same day, Peter Marano paid that tax so it could be claimed as a credit against his US tax liabilities;
- As this was part way through the 2012/13 tax year, HMRC had not yet issued any Self Assessment returns for that year.

On or after 6 April 2013, a notice to file a Self Assessment tax return for 2012/2013 was sent to Peter Marano at his last known residential address.

Having failed to file his return by 31 January 2014, HMRC issued a late filing penalty of £100, followed by a daily penalty and a six-month penalty.

In November 2014, HMRC issued a determination based on the amounts shown in Peter Marano's returns for earlier years and a late filing penalty based on that determination.

A second late filing penalty was issued on 3 March 2015.

In 2017, Mr Marano sought to file a tax return which was too late to be assessed but which enabled HMRC to calculate and issue a discovery assessment on 8 March 2017 for £5,744,219.

On 14 March 2017, HMRC also issued a late filing penalty for £574,422 made up of a six-month 5% tax-geared late filing penalty of £287,211 and a twelve-month late filing penalty of the same amount

Before the Court of Appeal, Mr Marano challenged the validity of the notice and the penalty assessments on the basis that their issuance had not involved an officer of HMRC.

S.103 FA 2020 provides that anything capable of being done by an officer of HMRC can be done by 'HMRC'.

- Mr Marano argued that s.103 FA 2020 required that statutory notices and penalty assessments required the involvement of an officer of HMRC and not the wider body or department of HMRC. These could not be automated.

- HMRC argued that the Peter Murano's interpretation of s.103 FA 2020 was too narrow and that the term 'HMRC' should be taken to mean the wider body or department of HMRC itself.

Decision

The Court of Appeal dismissed Peter Marano's appeal, holding that s.103 FA 2020 makes a distinction between an officer of HMRC and the body or department of HMRC itself. It allows decisions and acts of officers of HMRC to be undertaken by the body or department of HMRC.

This meant that s.103 FA 2020 does not require HMRC to prove that an individual officer, or an officer of a particular type or status, carried out the initial decision-making process involved in issuing the Notice and penalty assessments.

Automated notices and penalty assessments had been not validly issued

Peter Marano v HMRC [2024] EWCA Civ 876

Information notices – penalties (Lecture P1460 – 13.06.minutes)

This article will consider the general penalty provisions relating to information notices issued by HMRC under the provisions of Schedule 36, Finance Act 2008, and the associated assessment and appeal procedures for those penalties. Unless stated otherwise, all statutory references are to Schedule 36, Finance Act 2008.

Failure to comply with an information notice

A person fails to comply with an information notice if the information to be provided, or documents to be produced, have not been provided or produced within the time limit given in the notice. In such circumstances, the person may become liable to a penalty under Paragraph 39 for failure to comply with the notice.

If the person has provided some, but not all, of the information, or produced some, but not all, of the documents stated in the notice, HMRC's guidance instructs their officers to consider whether the information and documents provided are sufficient to enable the compliance check to be completed. If that is the case, officers are instructed not to take any further action to obtain the missing items. Otherwise, the officer may charge a penalty, £300, for the failure.

A penalty does not arise in relation to Paragraph 39 if the person complies with the notice within such further time, if any, that is granted by a HMRC officer.

A Paragraph 39 penalty can also be imposed where a person conceals, destroys or otherwise disposes of, or arranges for the concealment, destruction or disposal of, a document in breach of Paragraphs 42 or 43. These paragraphs relate to the concealment, etc of documents following an information notice and informal notification respectively.

Daily default penalties

A daily default penalty can be charged, under Paragraph 40, if the failure to comply with an information notice continues after an initial penalty under Paragraph 39 has been imposed for that failure. The penalty can be up to £60 for each subsequent day on which the failure continues.

Advisers should note that there is a provision for increased daily default penalties in relation to a notice issued under Paragraph 5. Please refer to the session on those notices, which includes details of the relevant penalty.

Inaccurate information

Paragraph 40A provides that a penalty can be imposed for providing inaccurate information or documentation in complying with an information notice. The penalty, not exceeding £3,000, can be imposed where any of the following conditions are satisfied:

- the inaccuracy is careless or deliberate;
- the person knows of the inaccuracy at the time the information or document is provided but does not inform HMRC at that time;
- the person who provided the inaccurate information or document discovers the inaccuracy some time later and fails to take reasonable steps to inform HMRC.

The legislation provides that where the information or document contains more than one inaccuracy, a penalty is payable for each inaccuracy.

Tax-related penalty

The Upper Tribunal can impose a tax-related penalty in certain circumstances, in accordance with Paragraph 50. For the purposes of this session, the penalty can be imposed where a person fails to comply with an information notice, the failure continues after an initial penalty has been imposed, and HMRC have reason to believe that tax has been underpaid as a result of that failure. HMRC may apply to the Upper Tribunal in such circumstances, although they will only do so where the amount of tax is considered to be substantial.

HMRC must make their application to the Upper Tribunal within 12 months of the relevant date. The relevant date for this purpose is the date that the person becomes liable to the penalty under Paragraph 39. The date is extended if the associated information notice has been appealed, but there is no similar extension if the Paragraph 39 penalty has been appealed.

The Upper Tribunal decide the amount of the penalty, and, in doing so, must have regard to the amount of tax which has not been, or is not likely to be, paid by the person

A relatively recent tribunal case considered HMRC's ability to seek a penalty under this provision. In Baxendale-Walker v HMRC [2024] UKUT 154 (TCC), HMRC tried to impose a £14 million penalty on the taxpayer for continued non-compliance with a Schedule 36, Finance Act 2008 notice. HMRC had sought the approval of the tribunal before the notice was issued, and had allowed the taxpayer further time to comply. The Upper Tribunal's judgment addresses complex issues around whether HMRC has the authority to amend the time allowed for compliance after an information notice is issued, and the interaction between the penalty provisions. The outcome was that the tribunal allowed Mr Baxendale-Walker's strike-out application. The repercussions of the case are likely to impact on future recipients of information notices, with HMRC being less lenient in granting further time to comply with such notices.

Penalty assessment

HMRC have 12 months to assess, and notify, a penalty under the provisions of Paragraphs 39, 40 and 40A (Paragraph 46).

The penalty assessment under Para. 39 or 40 must be made within 12 months beginning with the date on which the person became liable to the penalty, subject to the following:

> "In a case involving an information notice against which a person may appeal, an assessment of a penalty under paragraph 39 or 40 must be made within the period of 12 months beginning with the latest of the following—
>
> (a) the date on which the person became liable to the penalty,
>
> (b) the end of the period in which notice of an appeal against the information notice could have been given, and
>
> (c)if notice of such an appeal is given, the date on which the appeal is determined or withdrawn" (Paragraph 46, (3))."

The assessment of a penalty under Paragraph 40A must be made within the period of 12 months beginning with the date on which the inaccuracy first came to the attention of and HMRC officer, and within the period of six years beginning with the date on which the person became liable to the penalty.

Appeals

A person may appeal against the imposition of a default or inaccuracy penalty (Paragraphs 39, 40 or 40A), or the amount of any such penalty (Paragraph 47). Any such appeal must be made to HMRC within 30 days of the penalty notice, and must be in writing.

Where HMRC, or the First-tier Tribunal, are satisfied that there is a reasonable excuse for failing to comply with an information notice, a penalty does not arise under Paragraphs 39 or 40 (Paragraph 45). There is not a statutory definition of 'reasonable excuse', and the position needs to be considered by reference to the circumstances of the case. The legislation states the following:

> "(2) For the purposes of this paragraph—
>
> (a) an insufficiency of funds is not a reasonable excuse unless attributable to events outside the person's control,
>
> (b) where the person relies on any other person to do anything, that is not a reasonable excuse unless the first person took reasonable care to avoid the failure …, and
>
> (c) where the person had a reasonable excuse for the failure … but the excuse has ceased, the person is to be treated as having continued to have the excuse if the failure is remedied, … without unreasonable delay after the excuse ceased".

The appeal against the penalty can be settled by agreement with HMRC, or notified to the tribunal. The adviser may consider using the statutory review process, or HMRC's Alternative

Dispute Resolution process to conclude the matter. The burden of proof in an appeal against a penalty for non-compliance is on HMRC.

Practical considerations

The adviser's primary aim should be that the client does not become subject to a penalty for a failure, or other offence, in relation to an information notice. The reality is that the objective should be that the client does not become subject to an information notice, at least not in relation to their own affairs.

However, where a penalty is assessed, the adviser needs to make sure that, firstly, any penalty charges have been correctly assessed by HMRC (as noted above), and that any appeal is submitted within the statutory 30 days. This sounds very basic advice, and it is, but I have seen numerous examples in the nearly 30 years that I have been helping professional advisers and their clients where the relevant deadline has been missed or overlooked. There is provision for a late appeal to be accepted, but failing to make the appeal on time adds an additional, and unnecessary, hurdle into the process.

Advisers need to be mindful of the wider implications where a penalty is imposed in relation to an information notice. Where additional tax liabilities are established, the HMRC officer is likely to reduce mitigation for any resulting penalty on those liabilities, if a formal information notice has had to be issued, and there has been a failure to comply with that notice, or other offence, such that penalties are charged. Such behaviour by the client is likely to be seen as a lack of co-operation, or otherwise helping with the enquiry. In addition, the imposition of penalties for failure to comply with an information notice may impact on the HMRC officer's view of the case and may result in a stricter approach to any future information requests.

This session focuses on civil penalties relating to information notices. Advisers need to be aware that criminal proceedings may be considered where a person conceals, destroys, or disposes of a document. HMRC's guidance notes, at CH27200, that "criminal proceedings may be appropriate where:

- the information notice was issued with the approval of the tribunal, or it was your intention to seek approval, and
- any document required by, or to be included in, the notice has been concealed, destroyed or otherwise disposed of".

Contributed by Phil Berwick, director at Berwick Tax Limited

Deadlines

1 October 2024

- Corporation tax for periods to 31 December 2023 for SMEs not paying by instalments

5 October 2024

- Advise HMRC of IT/ CGT for 2023/24 if no tax return or notice to file has been received

7 October 2024

- VAT return and payment for 31 August 2024 quarter (electronic)

14 October 2024

- Form CT61 and tax paid for quarter ended 30 September 2024
- Quarterly CT instalment for large companies depending on accounting year end
- File monthly paper EC sales list –businesses selling goods based in Northern Ireland

19 October 2024

- PAYE/CIS liabilities for month ended 5 October 2024 (cheque)
- File monthly CIS return
- PAYE settlement agreement tax /class 1B National Insurance (cheque)
- PAYE for q/quarter to 5 October 2024 if average monthly liability is less than £1,500

21 October 2024

- File online monthly EC sales list –businesses selling goods based in Northern Ireland

22 October 2024

- PAYE for q/e 5 October 2024 if average monthly liability is less than £1,500 (electronic)
- Settle electronic PAYE settlement agreement liabilities

31 October 2024

- 2023/24 paper SA tax returns
- Accounts to Companies House should have received accounts of
  - private companies with a 31 January 2024 year end

  - public limited companies with a 30 April 2024 year end

- CTSA returns for companies with accounting periods ended 31 October 2023

News

LLP salaried partners update (Lecture B1457 – 8.03 minutes)

The salaried members rules were introduced in FA 2014 to determine whether LLP members should be taxed as self-employed or employed.

The rules

The rules set out three conditions, and where all three conditions are met, the LLP member will be treated as an employee for tax purposes.

Condition A: Disguised salary

Condition A will be met if it is reasonable to expect that at least 80% of the total amount payable by the LLP in respect of the member's performance during the relevant period of services for the LLP will be 'disguised salary' (ITTOIA 2005 s863B), i.e. does not vary with the profits of the LLP as a whole.

Condition B: Significant influence

Condition B will be met if the member does not have significant influence over the affairs of the LLP under the mutual rights and duties of the members of the LLP, and of the LLP and its members (ITTOIA 2005 s863C).

Condition C: Capital contribution

Condition C will be met if the member's capital contribution to the LLP is less than 25% of their disguised salary from the LLP in the relevant tax year (ITTOIA 2005 s863D).

The TAAR

The salaried members rules include a targeted anti-avoidance rule (TAAR) which disregards arrangements with a main purpose of securing that one or more members are not deemed to be salaried members (ITTOIA 2005 s863G).

Existing practice

To ensure that members were treated as self-employed rather than employed, it has been common practice for LLP members to have a capital account of at least equal to 25% of any 'disguised salary'. Provided that this capital was genuinely at risk within the LLP, it was understood that it would not fall foul of the anti-avoidance provision.

HMRC's updated guidance

In February 2024, HMRC included a new example in its Partnership Manual at PM259200 regarding condition C and when the TAAR will apply which reads as follows:

> In 2018, upon joining the ABC LLP, member X contributed capital of £15,000 (this was not part of any arrangement with a main purpose of securing the salaried members rules do not apply and is a genuine contribution).
>
> In 2022 it is expected that X's remuneration for the next period will consist of £100,000 Disguised Salary, meaning that their contributed capital is below the 25% threshold, and they will meet Condition C.
>
> X contributes a further £10,000 as part of a separate arrangement with the LLP, where members increase their capital contribution periodically in response to their expected disguised salary, in order to avoid meeting Condition C.

HMRC state that this arrangement will trigger the TAAR and no regard can be given to the £10,000 when considering whether X meets Condition C. As such X will meet Condition C as their contributed capital remains at only £15,000.

The Chartered Institute of Tax's concern

The Chartered Institute of Tax (CIOT) disagree with HMRC and has written to them explaining their concerns about the new guidance. The CIOT believes it is contrary to the policy intent behind the TAAR which was designed 'to counter abusive arrangements' that 'have no other substantive effect'.

The CIOT stated that:

> 'We find it difficult to see how the making of a genuine capital contribution can be regarded as being abusive or has having no other substantive effect'.

HMRC's own guidance confirmed that no restriction was placed on the ability to make or increase capital contributions to comply with the Condition C requirement and fall outside of the salaried member rules.

The Institute believes that if 'sufficient capital is genuinely contributed by a member and gave rise to real risk, i.e. there were no artificial arrangements used to negate this risk, such as a non-recourse loan, then the TAAR would not apply and the member would not meet Condition C."

The CIOT also states this is a new stance being taken by HMRC who state:

> 'it is the experience of CIOT members that HMRC have historically agreed that LLPs and their members can achieve certainty in respect of the salaried members rules by complying with the requirements of Condition C and, in some cases, HMRC have even provided assurance that Condition C is not met so long as the requisite amount of capital has genuinely been contributed'.

The CIOT are aware that HMRC are seeking to assess liabilities going back up to six years based on the change of view.

CIOT summary

The CIOT consider HMRC's new approach goes against the legislation.

Further, it is unfair as it penalises LLPs and their members who have to date complied with the rules to the best of their knowledge, based on statements and guidance published by HMRC as well as direct discussions with HMRC officers.

The CIOT believe that HMRC should:

- remove the updates to the guidance made in February 2024;
- cease its compliance activity based on the revised practice.

https://assets-eu-01.kc-usercontent.com/220a4c02-94bf-019b-9bac-51cdc7bf0d99/e8ea19b1-b00c-4c74-825e-f1998661b295/240822%20Salaried%20members%20rules%20-%20CIOT%20letter_Redacted.pdf

ER Bulletins July and August (Lectures B1458/ 1459 – 20.43/12.46 minutes)

Tax calculation repayments for PAYE

Currently employees who receive a tax calculation letter and do not claim the repayment online automatically, receive a cheque after 21 days. In July, HMRC advised that from 31 May 2024, cheques would no longer be automatically issued. Customers will need to take action to receive their repayments.

Customers can claim their repayments at tax overpayments and underpayments (https://www.gov.uk/tax-overpayments-and-underpayments). They can also request a cheque if preferred.

Instructions on how to claim will be available when they receive their tax calculation letter.

PAYE Settlement Agreements (PSA) – 2023/24

Where an employer or their agent has agreed a PSA with HMRC for 2023/24, any tax and national insurance payable must be paid by 22 October 2024 if paying electronically and by 19 October 2024 if paying by post.

A calculation of the liability must be submitted for HMRC so they can agree what the payment is for and that the amount is correct.

The easiest way to do this is online at “Tell HMRC the value of items in your PAYE Settlement Agreement” https://www.gov.uk/government/publications/paye-paye-settlement-agreement-psa1

This is a service for employers to submit their yearly calculations online and it determines the amount of tax and Class1B national insurance is due to tax year 2023/2024. To submit the calculation the employer needs:

- E’er reference
- Tax year of PSA calculation – must send in calculation even if it is a NIL return
- Type of expenses and benefits included in PSA
- Number of employees receiving each expense or benefit
- The correct rate of tax for each employee

Once calculation processed HMRC with automatically issue a payslip confirming amount due and payment reference number

RTI for off payroll workers (IR35)

Off-payroll working rules have been in place for several years. They were introduced to ensure individuals working through an intermediary – like a personal service company – pay similar income tax and NIC to other employees working in a similar way.

The responsibility for determining whether the rules apply moved to public sector bodies from April 2017 and medium and large sized organisations from April 2021.

If the rules apply, the individual is classed as a "deemed" employee and is added to the deemed employer's payroll as a new starter.

A record must be kept of all payments made as well as income tax and national insurance contributions which must be reported under RTI using the FPS.

The RTI flag – "the off-payroll worker marker" – should be set to show the individual is an off-payroll worker. This is to ensure the worker is treated correctly for tax and for status determination

Deemed employers must not take deductions for student or postgraduate loans from deemed Employees. The deemed worker will make these on their Self Assessment tax return.

The deemed worked has NO employment rights with deemed employer.

Reporting advances of salary

HMRC has been mentioning this issue since February 2023.

Strictly, advances of salary are just pay received in advance of pay day. This should be reported to HMRC via an RTI return on or before midnight on the pay day. However, employers had been not reporting the advances through the pay month, just catching up when the monthly pay was run. HMRC realised reporting twice in a month was a pain, but employers are required to comply with the law.

HMRC now confirm it will only expect one RTI report for each pay period where certain conditions are met:

- the salary is ordinarily paid at regularly intervals of between one week and one month and employer pays part of salary in advance;
- the salary advance reasonably represents work undertaken or obligations performed by the employee under their contract with the employer and no other relevant payment has been made for this work;
- employer makes a regular relevant payment to the employee at the regular payday after the advance payment is made , they should reduce the regular relevant payment by the amount of the salary advances.

P11D and P11D(b) for tax year 2023/24

2023/24 P11Ds should have been filed online by 6 July 2024, otherwise a penalty will be due

The form needs to be completed correctly first time, although corrections can be made using the online P11D amendment form.

A P11D is required for each employee in receipt of benefits or non-exempt expenses unless they were taxed through the payroll.

If there is nothing to declare, you only make declaration if HMRC asks for P11D(b).

Common errors

- Putting in tax year start and end date in when the car is available all year;
- Submitting P11D forms over several days; they must all be submitted together with P11D(b)

When reporting a fully electric car ensure, you must include the approved CO_2 emission, and when reporting a hybrid car with an approved CO_2 emissions figure between 1 and 50g/km make sure you include the approved zero emissions mileage.

Finally, only send one P11D(b) for each scheme showing the total amount due. Do not do separate returns for employees and directors as each separate P11D(b) received is treated as an amendment to any previous one submitted.

Paying Class1A National Insurance contributions

Electronic payments for Class 1A NIC declared on the P11D(b) must be cleared funds with HMRC by 22 July 2024.

The right payment reference for the payment must be used which is the 13-character accounts office reference followed by 2413 with no gaps. Adding 2413 tells HMRC the payment is for tax year 24 and 13 indicates it is for Class 1A

Student and postgraduate loans

Where a student loan or postgraduate loan start notice is received – SL1/PGL1 or both from HMRC for an employee, the employer must:

- check and use the correct information;
- include the loan or plan type and the start date shown on the start notice;

If employee earnings are below the threshold, update the employee’s payroll record to show the loan and file start notice. Do not return it to HMRC.

If employee earnings are above the threshold and deductions have not been taken, HMRC will send a generic notification service prompt as a reminder; if deduction is still not started, HMRC may contact employer.

Deductions should continue until HMRC say STOP.

If no start notice is received but the student says they have a loan, ask which plan or loan type. If they are unsure, they can log into their student online account

Pensions for seasonal staff

This was a reminder about taking on seasonal staff as Christmas and New Year approach.

Failure to comply with workplace pension duties may result in a warning notice with a deadline to comply. Failure to comply can result in a fine

Do not forget that you must check all new employees to see if they are eligible for automatic enrolment for workplace pensions.

Seasonal or temporary employees must also be assessed each time you pay them.

Where staff will work for less than three months, the employer can use postponement which delays the assessment. At the end of the postponement, the assessment would need to be complete if they were still on the payroll.

Getting your new employee on the right pay

Once an employer has registered with HMRC it can take up to 30 working days for them to receive their Employer PAYE Reference number - a key piece of data for RTI reporting. Do not call HMRC unless more than 30 days has elapsed – it does take time!

Here are a few HMRC tips to avoid making errors during the “onboarding” process:

- Gather the correct personal information from your new employee - the right name, correct date of birth and NI number and enter in the correct format;
- Double check against official documents e.g. passports to check data correct;
- Find the correct starter declaration code and tax code;
- If the starter does not have form P45, use the online starter checklist to find appropriate codes.

When the starter code checklist determines the employee should be on starter declaration code C, use tax code BR.

If you are unable to complete the checklist and your employee has no form P45 use tax code OT with starter declaration code C

Statutory Neonatal Care Pay and Leave

Under Neonatal Care (Leave and Pay) Act that was passed last year, a neonatal baby is a baby that is aged 28 days or less and had been in hospital for 7 days or more. From day one, employees have the right to receive up to 12 weeks paid leave where in addition to all of their other statutory leave and pay.

Agents Update 123 - issued September 2024 states that from April 2025 there will be a new statutory allowance introduced:

- NEW Statutory neonatal care leave;
- NEW Statutory neonatal care pay.

Rates broadly expected to follow other existing statutory payments such as statutory parental bereavement pay and leave.

Article created from the two online sessions by Alexandra Durrant

Business taxes

SEISS, CJRS or nothing? (Lecture B1456 – 24.34 minutes)

Summary – As a director who performed work during the pandemic, the taxpayer was not entitled to COVID related payments of any kind.

Until 5 February 2019, Sofia Lorenzo operated as a self-employed, semi-permanent, makeup and beauty therapist. From that date the business was incorporated, with her becoming an employee, sole director and shareholder.

During COVID she applied for and received coronavirus support payments under the Self-Employed Income Support Scheme (SEISS).

HMRC raised assessments to reclaim the payments made because, as an employee, she had no entitlement under the SEISS as she was not self-employed.

Despite later accepting that she was not eligible for the sums received, she appealed HMRC's assessment on the basis that:

- she had received payments under SEISS because of an innocent mistake; and
- as an employee, she should have been entitled to receive payments funded through the Coronavirus Job Retention Scheme (CJRS);
- her CJRS payments would have been greater than the amounts paid under SEISS.

She sought to have her SEIS payments treated as if they had been valid payments under CJRS. However, the witness statement and skeletons identified that it was not clear that the company would have been entitled to make CJRS claims and so there was a factual and legal dispute which needed to be determined.

Decision

The First Tier Tribunal found that, had a claim been made under the CJRS, for a number of reasons it would have been invalid. The reasons included that during the pandemic:

- the company did not pay her a salary;
- she had performed some duties during the furlough period, beyond the directors' duties permitted under the CJRS rules.

The appeal was dismissed.

Sofia Lorenzo v HMRC (TC09227)

Entitlement to SEISS and bounce back loan (Lecture B1456 – 24.34 minutes)

Summary – As the taxpayer was no longer trading on a self-employed basis, he was not entitled to claim under the Self Employment Income Support Scheme.

Ali Sadiq Jaafar traded as a self-employed minicab driver for a number of years before ceasing on 30 September 2019, a date confirmed in his Self Assessment return as well as separately by his agent in writing.

On 12 September 2018 he became the sole director and shareholder of a newly incorporated company, Fly Services Limited, which filed dormant accounts for the year to 30 September 2019 and micro company accounts for subsequent periods.

Ali Sadiq Jaafar applied for and received three payments under the Self Employment Income Support Scheme (SEISS) in June, September and December 2020. He argued that he had in fact continued to trade on a self-employed basis in the 2020/21 tax year.

HMRC accepted that being a company director did not prevent him resuming self-employment but stated that no evidence was provided supporting his claim that he did so in 2019/20 or later years. His 2020/21 return only showed the support payments and expenses and nothing was reported in 2021/22.

Consequently, HMRC contended that Ali Sadiq Jaafar was not entitled to claim under the SEISS as he did not meet the requirements which were that he must have:

- carried on a trade, the business of which had been adversely affected by Coronavirus; and

- intended to continue to carry on a trade in the tax year 2020/21.

Consequently, HMRC raised assessments to recover the three payments previously made.

Ali Sadiq Jaafar appealed.

Decision

The First Tier Tribunal acknowledged that Ali Sadiq Jaafar had provided copies of his TfL private hire driver's licences with expiry dates 8 December 2020 and 17 January 2024, and the V5C and MOT certificates for a Mercedes Benz car in his name as well as copies of his car insurance. However, the Tribunal did not accept that these were sufficient to show that he was self-employed in the period in question:

- he would have needed the same licences to be able to drive as an employee;

- the fact that he had owned the car in his own name, rather than transferring it to the company, did not mean that he must have been self-employed; and

- his car insurance showed that he was insured to drive the car for social, domestic and pleasure purposes only;

- his company, Fly Services Limited, had applied for and been granted a bounce back loan, the terms of which required that the company had to be trading as a limited

> company. This was not consistent with his claim that he had continued in self-employment and had not traded through the company.

While his bank statements did show 'some small payments from Ontime Chauffeurs', the First Tier Tribunal found that there was no documentation to indicate in what capacity these had been received.

In conclusion, the First Tier Tribunal found that Ali Sadiq Jaafar had ceased self-employment on 30 September 2019 and had no intention to 'continue to carry on' as self-employed in 2020/21. Consequently, he was not entitled to support payments.

The appeal was dismissed

Ali Sadiq Jaafar v HMRC (TC09279)

CIS determinations challenged **(Lecture B1456 – 24.34 minutes)**

Summary – The First Tier Tribunal dismissed the company's appeal against determinations relating to its failure to make deduction at source under the CIS legislation. The appeal against late filing penalties were also dismissed.

The Oaks (Gatley) Limited was set up to carry out a one-off residential development project. As part of that project the company paid various construction service providers, failing to make deductions at source as required by the CIS rules.

Despite accepting that it had failed to make the deductions, the company appealed against HMRC's determinations issued to recover the tax relating to one sub-contractor, Dreamspace, arguing that HMRC had not followed its own Regulations when raising the determinations.

Regulation 9 states that an HMRC officer may direct that a contractor is not liable to pay any shortfall between the amounts it should have deducted under CIS and the amounts actually deducted if the sub-contractor brings into account the payments made to it. On appeal, the company included a letter from Dreamspace confirming that it had brought all amounts received from Oaks (Gatley) Limited into account in calculating its corporation tax liabilities. Consequently, there was no net loss of tax to HMRC.

Decision

The First Tier Tribunal found that it had jurisdiction to consider whether CIS deductions were due as well as the quantum of such deductions.

The Tribunal acknowledged that HMRC's Compliance Operational Guidance manual does indicate that officers should consider the overall tax/regulation 9 position before moving forward with a regulation 13 determination.

COG909400 makes it clear that:

> "you must always consider all the information you hold in respect of possible claims [for relief under regulation 9] prior to the issue of regulation 13(2) determinations".

Although the company asserted that there was no tax loss, the Tribunal stated that there was no material evidence supplied to support that assertion.

The Tribunal stated:

> “Saying that HMRC could work out the sub-contractors' UTRs for themselves and find the required information is not sufficient.”

The Tribunal went on to say:

> “In the circumstances, if public law arguments could have been introduced, we would have held, on the basis of the evidence before us, that HMRC did not depart from the process they outlined in the Manual or, if they did, they did not do so in a way which is conspicuously unfair to (the company).”

The appeals were dismissed.

The Oaks (Gatley) Limited v HMRC (TC09233)

Mis-selling of interest rate hedging products (Lecture B1456 – 24.34 minutes)

Summary – The redress payments put the taxpayers back in the position they would have been in but for the mis-selling in relation to their property rental business. These payments were revenue in nature and taxable as part of the property rental business.

Simon and Edward Hackett were brothers who ran a property business.

In 2006, they bought interest rate hedging products from HSBC and RBS to help manage fluctuations in interest rates on loans.

It was later agreed that some of these products had been mis-sold and the Financial Conduct Authority set up a compensation scheme to put customers back in the position they would have been in had the mis-sale not taken place.

Simon and Edward Hackett received compensation but did not include these sums in their Self Assessment tax returns as trading receipts.

Following an enquiry, HMRC issued closure notices assessing them to tax on the payments.

The Hackett brothers appealed, arguing that the payments were for the cost of lost opportunities of being able to enter into different hedging products and, as a result were not part of the profits of the property business. This meant that, under s.271 ITTOIA 2005, the payments were not liable to income tax and the interest was not chargeable under s.369.

Decision

The First Tier Tribunal did not agree, finding that the compensation was for business expenditure on the mis-sold interest rate hedging products. The brothers were not put in a better position but were put back in the position they would have been had it not been for the mis-sold products. Both the compensation and interest were liable to tax. The appeal was dismissed

Simon and Edward Hackett v HMRC (TC09267)

Adapted from the case summary in Taxation (8 August 2024)

R&D claim for sub-contractor costs (Lecture B1456 – 24.34 minutes)

Summary – Although creation of a director's loan constituted payment, there was a lack of evidence to support the claim that this was qualifying R&D.

Tills Plus Limited developed technology for the hospitality industry and in this case, a virtual hospitality manager using Artificial Intelligence and Big Data.

The company wanted to develop a new product or suite of products, the funding for which was to come from the sole director's father-in-law, who was resident in Iran.

Due to international sanctions, it was extremely difficult to move money out of Iran. Consequently, the company looked for a partner in Iran to carry out the necessary development work, choosing a company called iWond as they had the necessary expertise and had the best English language capabilities.

The agreement between iWond and Tills Plus Limited did not set out any specific fees for the work but simply provided that Tills Plus Limited would be invoiced every three months.

Due to the difficulties in moving money in and out of Iran, it was agreed that iWond's invoices would be paid direct by the father-in-law from his bank account in Iran, who would make a loan to the UK director who would in turn make a loan, recorded on a director's loan account, to Tills Plus Limited. The loans were interest free and repayable on demand but was only put in writing once HMRC's enquiries had begun.

Tills Plus Limited submitted claims for research and development expenditure, including subcontractor costs, for the years 2018 and 2019.

- For 2018, a tax credit payment of just over £390,000 was claimed and paid by HMRC;
- For 2019, a tax credit payment of a little over £275,000 was claimed but HMRC did not pay this

Following an enquiry, HMRC concluded that both claims should be disallowed and sought to recover the £390,000 already paid. S.1133(1) CTA 2009 defined a "sub-contractor payment" as "a payment made by a company to another person (the 'sub-contractor') in respect of research and development contracted out by the company to that person". HMRC argued that the sums claimed had not been paid as to be eligible, the invoices needed to be paid from the company's bank account to the subcontractor company in Iran.

Tills Plus Limited appealed.

Decision

The First Tier Tribunal considered whether the expenditure:

- had actually been 'paid';
- was qualifying R&D expenditure.

On the payment issue:

- The company argued that it would be very odd if a payment did not satisfy the requirements of the legislation simply on the basis that there was no physical payment by the company to the sub-contractor;

- HMRC argued that there was a difference between payment by credit card and a payment using borrowing where the actual payment to the sub-contractor was made by the lender rather than the borrowing company.

The Tribunal concluded that it could not have been Parliament's intention that the availability of relief should depend on fine distinctions as to the way in which a payment was made to a sub-contractor. The First Tier Tribunal agreed with the taxpayer, who could see no avoidance or abuse taking place where the debt was settled by the loan arrangement. The Tribunal concluded that what was required was that an obligation to the sub-contractor was discharged at the cost or expense of the company, which is what happened here:

- iWond's invoices were addressed to Tills Plus Limited and were therefore an obligation of Tills Plus;

- The invoices were physically paid by the father-in-law but this was treated by agreement as a loan from him to the director and then a loan by the director to Tills Plus Limited.

This meant the obligation to iWond represented by the invoice was discharged and was replaced by an obligation for Tills Plus Limited to repay the resulting loan, so at the cost or expense of Tills Plus Limited.

It did not matter that it was not a commercial loan, with no interest and no fixed date for repayment. The Tribunal did not consider that the reasons why payment was made in a particular way was relevant to the issue of statutory interpretation.

Unfortunately for the company, the First Tier Tribunal went on to conclude that there was insufficient evidence to show the company had carried out qualifying R&D. One report being relied on was found to contain an expert's opinion/ assertion but he was unavailable to give evidence to support the claims or be cross-examined. The Tribunal stated that it was possible that the work could constitute qualifying R&D but evidence was lacking and 'without further evidence, we cannot say that what was being done would be acknowledged by a competent professional working in the field as a genuine and non-trivial improvement'. With the company failing to provide a satisfactory explanation of the advance in technology being sought, the claim failed.

Tills Plus Limited v HMRC (TC09235)

Reallocation of Special Capital (Lecture B1456 – 24.34 minutes)

Summary - Allocations by a corporate member of a mixed member partnership to individual members constituted miscellaneous income.

An investment management business, GSA, transferred its high-frequency foreign currency trading team to the HFFX LLP, a mixed partnership LLP whose members where:

- Individual members of the trading team who became self-employed LLP partners;
- GSA Member Ltd, a company that was independent of the individual members.

HFFX LLP's business was to second members of the team to GSA Capital Partners LLP, GSA's primary trading entity.

Individual LLP member received payouts from the profits they earned for GSA, but a substantial proportion was deferred via a "Capital Allocation Plan".

Under this plan:

- 50% of the pay-out that the team would otherwise have received was allocated to GSA Member Ltd, who invested these sums in funds managed by GSA;
- On the first, second and third anniversaries of the allocation, the corporate member sold a third of the investments, contributing the net proceeds back to HFFX LLP as "Special Capital";
- The corporate member then decided to reallocate the Special Capital to individual members, who were able to withdraw it.

The scheme was designed with the intention that:

- the corporate member would be taxed at corporation tax rates on the amounts allocated to it (rather than the higher income tax rates to which individual members would be subject if the profits were allocated to them);
- the subsequent reallocation of Special Capital would not give rise to tax for the individual members.

HMRC disagreed, stating that the reallocated special capital was taxable as miscellaneous income under s.687 ITTOIA 2005.

The First Tier Tribunal and Upper Tribunal found in favour of HMRC.

The individual members appealed. It was not disputed that the amounts were income in the hands of the individual members. The central issue was whether that income had a source. The members argued that the corporate member's discretion to reallocate Special Capital was purely voluntary, which meant that it did not constitute a source of taxable income.

Decision

The Court of Appeal agreed with HMRC that the case was 'materially indistinguishable' from BlueCrest Capital Management LP and others v CRC [2024] STC 92, in which the court decided the miscellaneous income issue in HMRC's favour.

The deciding factor was that the individual members had legal *'rights under the Partnership Deed'* for the corporate member to reallocate Special Capital to the individual members.

This was enough to make such receipts taxable as miscellaneous income under s.687. The receipts were not a 'pure gift'.

The taxpayers' appeal was dismissed.

HMRC v HFFX LLP [2024] EWCA Civ 813

Apple State Aid case **(Lecture B1456 – 24.34 minutes)**

Summary - The Court of Justice of the European Union (CJEU) has overturned the General Court's 2020 ruling in the Apple State Aid case. The decision reinstates the European Commission's 2016 ruling that Ireland provided illegal State Aid to Apple and therefore confirms that the company should repay €13bn in taxes to Ireland.

Explaining the background to the judgment, Heather Self, tax consultant at Blick Rothenberg, said: 'Ten years ago, in June 2014, the EU Commission announced an investigation into rulings issued by Irish tax authorities on the calculation of the taxable profits allocated to the Irish branches of two companies, Apple Sales International (ASI) and Apple Operations Europe (AOE). ASI and AOE were incorporated, but not tax resident, in Ireland. In both cases, the Irish branches declared low profits, claiming that the profits relating to intellectual property were attributable to the head office and not taxable in Ireland. However, due to the interaction of Irish and US tax rules at the time, the profits were not taxed anywhere.

'In a decision in 2016, the Commission said that the rulings allowed profits from 1991 to 2014 to be calculated in a way "that did not correspond to economic reality" and said that this was State Aid. They ordered Ireland to recover €13bn from Apple. Both Ireland and Apple appealed, and in 2020 the General Court annulled the Commission's decision, holding that the Commission had not sufficiently established that ASI and AOE enjoyed a selective advantage. The Commission appealed to the Court of Justice (ECJ).

Self said: 'On 10 September 2024, the CJEU has now issued its final ruling. The decision of the General Court has been overturned, and the Commission's original decision has been upheld. In particular, the CJEU held that the Commission was correct to compare the activities of the Irish branches with the head offices of ASI and AOE, and not to take into account the activities of other group companies such as Apple Inc.

'This is an important decision, even though it deals with events from some years ago and the Irish rules on tax residence have now been updated. In particular, the US warned in 2016 that the EU risked damaging international agreements on tax reform if it continued to act as a "supra-national tax authority". The CJEU's decision that Europe should collect tax of this magnitude from Apple may push the US towards finally implementing the OECD's proposed reforms – or could have the opposite effect of causing Pillar One to collapse altogether,' Self added.

Reproduced from Tax Journal (13 September 2024)

VAT and other indirect taxes

Hair loss treatment (Lecture B1460 – 23.28 minutes)

Summary - The supply of the taxpayer's Kinsey System did not qualify for zero-rating under Group 12 Schedule 8 VATA 1994 as 'significant hair loss or baldness in women is not, in itself, a disability'.

Mark Sharp worked as a hair extension technician and created the Kinsey System for hair loss, named after his friend, Glenn Kinsey.

The pair co-founded Mark Glenn Ltd, trading from premises in London and was registered for VAT from 12 July 2001.

The Kinsey System involves fitting a custom-made wig over the hair loss area together with an additional wig mesh with natural hair drawn through the mesh, thus appearing alongside the wig hair. The hair is then styled and cut, with customers returning for hair maintenance roughly every six weeks.

Based on advice received from their VAT advisors, the company treated the hair loss treatment as zero rated under Schedule 8, Group 12 (Drugs, medicines, aids for the [disabled,] etc) VATA 1994. This covers the supply to a disabled person for domestic or his personal use of certain goods. Subsection 3 extends this to the supply to a disabled person of services of adapting goods to suit their condition and subsection 5 allows the repair or maintenance of such goods. Note 4 confirms that wigs were specifically deemed to be included as a medical appliance.

In 2020, HMRC opened a compliance check and in August 2020, sought information as to whether or not any of the staff were medical practitioners.

The company replied, confirming that none of the staff were medical practitioners but that referrals were received from medical practitioners, with the NHS sometimes paying for the service provided by the company.

In September 2021, HMRC wrote, advising that the company's treatment did not fall to be included as zero-rated under VAT Group 12, which was upheld on review.

The company appealed.

Decision

The First Tier Tribunal found, and both parties agreed, that the supply of the Kinsey System was a supply of services, so the issue was whether item 3 of Group 12 applied – 'The supply to a disabled person of services of adapting goods to suit his condition'

Note 3 states that this section only applies to a 'person who is chronically sick or disabled' which, according to VAT Notice 701/7 means a person with a physical or mental impairment which has a long-term and substantial adverse effect on their ability to carry out everyday activities.

The First Tier Tribunal rejected the argument that significant hair loss in women should be considered a disability. The company failed to produce any evidence that 'baldness in women is considered as a chronic sickness by the medical profession'. Significant hair loss or baldness 'does not necessarily have a long-term and substantial adverse effect upon the ability of an individual to carry out everyday activities.'

The Tribunal found that the Kinsey System was not designed solely for the relief of a severe impairment or severe injury, nor was it the supply of services adapting goods to suit a disabled person’s condition. Rather, the Kinsey System was the labour-intensive supply of the fitting of a wig, which allowed for a semi-permanent transformation, with regular maintenance required. It was not the adaptation of a wig.

The Tribunal stated that:

> ‘We find that to consider the Kinsey System as one of services of adapting goods to suit his condition would be to dissect artificially what the Kinsey System does.
>
> We find that the Kinsey System is a single supply of services and that it does not, therefore, fall within Item 3 of Schedule 8 of Group 12 VATA94.’

This was not the service of adapting goods for a disabled person but rather the supply of a single service followed by a regular maintenance programme. The sums charged were therefore standard rated.

Mark Glenn Ltd v HMRC (TC09255)

Overstated zero rated sales (Lecture B1460 – 23.28 minutes)

Summary – The ‘rough and ready’ approach to calculating the split of sales between zero and non- zero-rated supplies was not accepted by the Tribunal who upheld HMRC’s 2% best judgement assessment.

Mr. Babar Saddiq was the sole director and shareholder of B J Shere Khan Star City Limited, a company that operated a restaurant trading as Shere Khan at a leisure and entertainment complex in Birmingham.

In this case, HMRC sought to collect VAT and related penalties in relation to understated sales and overstated zero-rated sales from Shere Khan as well as omitted sales from a second restaurant, called Oodles.

Mr Saddiq stated that Oodles had been closed for refurbishment, with the intention that the modernised premises would operate a Pan-Asian restaurant as a division of B J Shere Khan Star City Limited. The company had been paying £160,000 rent per annum on an empty site that he had personally guaranteed. In order to avoid the rental payments, he had granted a two-year licence to Zahoor Malik and Zeeshan Hamid to run Oodles as an ethnic led concept. They paid the rent and overheads and completed the refurbishment. Mr Saddiq stated that Oodles then traded through two companies, Star City Noodle Bar Limited and Recoverage Limited, with which he was not involved.

On whether there had been suppression of takings at Shere Khan, HMRC argued that a review of bank statements and annual accounts suggested there was such a suppression.

Finally on the zero-rated sales, the Tribunal was told that the restaurant tills did not distinguish between zero rated and standard rated goods. This split was determined at the end of each day by staff members who went through the till receipts to calculate the split, which was claimed to be consistently 12%. Following the calculation, the receipts were destroyed. Mr Saddiq supported the 12% used by stating that:

> "The majority of the time, our zero-rated sales came very close to 15%
> but in order to be careful we used 12% of our total sales as zero rated."

Decision

On whether sales had been omitted sales from Oodles, the First Tier Tribunal found against HMRC. While the Tribunal appreciated that HMRC could have thought that this was the case, based on the evidence supplied, this was no more than a suspicion. The Tribunal found Mr Saddiq’s explanation to be credible and plausible.

The First Tier Tribunal did not accept HMRC’s assertion of understated sales at Shere Khan. Periods where bank deposits were greater than gross sales declared was not evidence of suppressed sales. These differences were shown to be miscalculations by HMRC and the fact that money was not always regularly banked. HMRC did not challenge this evidence.

The First Tier Tribunal found it unlikely that staff members would calculate by hand the zero-rated supplies each day or twice weekly when the bookkeeper came in, as was alternatively suggested. The Tribunal found that the calculation was “most likely based on a rough and ready method of sampling: hence why the amounts were rounded down to avoid overclaiming.”

The Tribunal stated that it was for the appellant to show that the supplies were zero rated, which they had failed to do. Consequently, the Tribunal accepted HMRC’s best judgment assessment of 2%, stating that:

> “Whilst this figure is quite likely too low, we find the appellant has not discharged the burden of proof, which is on it, to show that a higher figure is appropriate.”

Moving to the penalties, the First Tier Tribunal reached the view that the behaviour was careless, rather than deliberate. Further, given the detailed correspondence and calculations provided to HMRC the Tribunal considered the reduction for helping as too little and increased the percentage from 10% to 20%.

Having found that the inaccuracy was not deliberate, the appeal against the Personal Liability Notice was allowed.

B J Shere Khan Star City Limited and Mr. Babar Saddiq v HMRC (TC09244)

Property purchase input tax recovery **(Lecture B1460 – 23.28 minutes)**

Summary – With no indication that the converted flats would be sold, but rather they would be let out on exempt short-term leases, HMRC had been correct to deny the input VAT claim.

In February 2014, Abdul Ghafar bought the Kenthouse Tavern, a pub with residential accommodation upstairs. He paid £645,000 plus VAT, and was VAT registered at the time of the purchase.

In October 2015, he obtained planning permission to create six one-bedroom flats on the first and second floor of the property.

Two months later, Kenthouse Properties Limited was incorporated, with Abdul Ghafar as its sole director and the following occurred:

- March 2016, the property was transferred to the company, for £915,000 but no VAT was charged on the transfer as Abdul Ghafar thought it was a transfer of a going concern (TOGC) as he had opted to tax the building;

- May 2016, the company registered for VAT but this meant that the TOGC conditions had not been met – as the buyer need to be registered for VAT when the transfer took place;

- October 2018, the company opted to tax the property, more than two years after the transfer had taken place.

HMRC collected output tax on the sole trader’s business, which Kenthouse Properties Limited reclaimed as input tax on its September 2018 return.

HMRC disallowed the claim, on the basis that the company made wholly exempt supplies of short-term rentals and not zero-rated supplies of the sale of freehold or long leasehold dwellings in a building that has not been used for residential purposes in the previous ten years (Group 5 Schedule 8 VATA 1994). Both its application to register for VAT and form VAT5L confirmed there was no intention to sell the properties but that the flats were to be let out on short leases.

The company claimed that the intention had always been to sell the flats which were taxable supplies, keeping just the ground floor commercial element. With the option to tax in place, these rents would have been standard rated. He claimed that market conditions meant that with no buyers, he was forced to change his plans.

Decision

At the hearing, the First Tier Tribunal commented the company was making submissions on the basis that the property transfer was a TOGC. As the appeal notice made no reference to this, the Tribunal could only consider the input tax reclaim issue actually referenced. The Tribunal commented that if the company considered that the transaction was a TOGC, it would not have made a VAT return claiming input VAT as no input VAT would have arisen.

From the evidence contained within the VAT application and Form VAT5L, the First Tier Tribunal found that the company had intended to make and had only made exempt short term lets. There was no evidence that the company had made 'any attempt to sell the flats' which would then have been zero-rated taxable supplies. The tribunal agreed with HMRC that the input tax claim was linked to exempt rather than taxable supplies and so the input VAT was not recoverable.

The appeal was dismissed.

Kenthouse Properties Limited v HMRC (TC09250)

Sightseeing packages (Lecture B1460 – 23.28 minutes)

Summary – Visitor passes, combining transport with entry to London attractions, were multi-purpose vouchers rather than tickets, meaning they were outside the scope of VAT.

Go City Limited (formerly the Leisure Pass Group Limited) sold two types of passes, both of which entitled the buyer to enter various attractions at discounted prices and to use certain forms of transport in London without further payment.

The company had a history of appeals with HMRC to decide whether its pass was the supply of an outside the scope voucher at the time the voucher was bought, or a standard rated ticket. Following the implementation of the VAT Voucher Directive (effective from 1 January 2019), and wanting to avoid the disruption of further litigation, the company restructured its passes to ensure they continued to qualify as multi-purpose vouchers and were out of the scope for VAT. Under the restructuring the company believed that they were supplying credits, to be regarded as a preliminary transaction, which was not an aim in itself for customers, with the credits working as follows:

- the company sold a credits package to customers:
- when used for entry, the attraction supplied the company with a right of entry at a fixed rate, with the company making an onward supply of that right to the customer;
- the customer could use a set number of credits based on the standard gate price of the attraction;
- each customer could use a maximum number of credits, which protected the company against heavy users;
- The use of credits was the point at which VAT needed to be considered based on whether the credits had been used on standard-rated, zero-rated or exempt supplies.

HMRC challenged the treatment, raising four assessments in 2021 covering the VAT quarters 3/19 to 12/20 totalling some £9 million.

The company appealed and the parties agreed there were four issues in dispute:

1. Whether the First and Second Assessments were out of time because, when they were issued, it did not appear to HMRC that the VAT returns were incorrect;
2. Whether the supply of passes was outside the scope of VAT because they were Multi-Purpose Vouchers, or whether they failed as they were "instruments functioning as tickets";
3. Whether the supply of the passes was outside the scope of VAT as a result of the company's new contractual arrangements;

4. Where a pass expired without having been used up, whether the entirety of the money received by the company from customers should have been allocated as consideration for its supplies.

Decision

The first two assessments were found to be out of time. Based on the evidence provided, the assessments were issued to protect HMRC's position under the two-year time limit rule, rather than because HMRC had formed a view that the relevant VAT returns were incorrect before the assessments were issued. The assessments were invalid.

Under the rules applying from 2019, the credits were multi-purpose vouchers, outside the scope of VAT when initially supplied. The Tribunal found that the passes were not "instruments functioning as tickets". This was supported by the post Brexit decision in *DSAB* (Case C-637/20), where city passes were found to be multi-purpose vouchers. It would be wrong to class the credits as tickets rather than vouchers as they did not relate to a specific event. The use of the passes depended solely on the decisions taken by the customer.

On the third issue relating to the company's restructuring, the passes were also found to be outside the scope. VAT was not due until the credits were used to enter an attraction.

Finally, HMRC's claim that all of the consideration paid for the passes should be allocated as consideration for supplies, was inconsistent with the legislation and the case law. Where a customer did not use all of their credits, the unallocated part of the payment was not a consideration for supply.

The company's appeal was allowed.

Go City Limited (formerly the Leisure Pass Group Limited) v HMRC (TC09263)

Static caravan DIY builder (Lecture B1460 – 23.28 minutes)

Summary – The Tribunal had no powers to consider whether HMRC's decision to refuse a VAT refund could be successfully challenged. Having relied on advice received from HMRC's helpline, the correct approach was through judicial review.

Gregory Sewell lived in the New Forest. Wanting to live close to his son to whom he had essentially given his main property, he decided that it would be easier to get planning consent if he constructed a substantial static caravan.

He contacted HMRC's helpline and was very clear on what he told HMRC over the phone:

- He wanted to build a static caravan on a concrete base;
- He understood the rate of VAT on constructing a building was 0% but on the construction of the caravan, it was 5%.

Having sought advice from a more senior colleague, he was told by the HMRC operator that this was a new build for VAT purposes and hence was zero rated. He was told that even though it was a caravan, it was a permanent structure "so as far as we're concerned that's classed as a new build... Under the VAT Notice 708, section 3 that is dealt with a (sic) new build so it's zero rated".

Following the call, Gregory Sewell made a claim for just over £16,000 under the DIY housebuilders scheme to recover the input tax that he had incurred.

However, there was no doubt that the advice given was wrong and so HMRC refused the claim as caravans were not within the scheme.

Gregory Sewell appealed arguing that HMRC should be required to stand by its advice.

Decision

The Tribunal stated that it was well-established that the correct way for him to challenge misleading advice by HMRC was through the judicial review process.

Despite sympathising with Gregory Sewell, the appeal was dismissed as the First Tier Tribunal had no jurisdiction to deal with this matter. In the Upper Tribunal decision in HMRC v Hok Ltd, the Upper Tribunal made it clear that the First Tier Tribunal "does not have a jurisdiction to enforce any common law duty of a public body to act fairly in administering its statutory powers."

The case was struck out.

NOTE: The Tribunal stated that the taxpayer might consider pursuing a claim for legitimate expectation that HMRC would honour their advice. However, it was clear that Gregory Sewell did not rely on HMRC's advice to his detriment; he would have constructed the caravan whatever the VAT position.

Gregory Sewell v HMRC (TC09269)