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Personal Tax

Practical ramifications of HMRC6

On 6 April 2009, HMRC withdrew IR20 which set out their practice for determining an individual's residence status for UK tax purposes. It has been replaced with an ever expanding set of guidance notes and bulletins, but specifically the draft manual HMRC6.

The issue of whether under the old regime individuals were right to rely on IR20's guidance, and specifically the 90-day rule, is the subject of a judicial review brought by a Mr Gaines-Cooper, following the High Court's finding that he was UK resident for the relevant years of assessment (*Gaines-Cooper v HMRC* [2008] EWHC 2608). It is uncertain whether the substantive hearing will be heard by the end of the year.

Now that IR20 has been withdrawn and while there remains no statutory definition, determining residency issues will be even more challenging. For now, HMRC have provided a manual which is in draft and which 'has no legal force, nor does it seek to set out regulation or practice' (paragraph 1, HMRC6).

Day counting post-6 April 2009

HMRC state that the 90-day rule will still apply to those visiting the UK, either short term (paragraph 7.5, HMRC6) or long term (paragraph 7.7, HMRC6), and those leaving the UK (paragraph 8.2, HMRC6),

Following FA 2008, s 24 (and the introduction of ITA 2007, s 831(1A)) the issue of whether days of arrival and/or departure should be included when computing an individual's day count has fallen away. When looking at foreign income of individuals in the UK for temporary purposes only, the rule is simply that a day counts if the individual is in the UK at the end of the day (the new 'midnight' rule).

Other factors

HMRC consider that day counting is no longer the sole factor in ascertaining residence, except where the individual spends more than 182 days in the UK in a single tax year, in which case he becomes UK resident automatically (paragraph 2.2, HMRC6).

In practice it will be 'many different factors' (paragraph 2.2, HMRC6) which will determine whether someone is resident in the UK during a tax year.

These factors include:

- availability of accommodation in the UK;
- business ties in the UK (particularly if business is main source of income for the individual);
- social ties in the UK (memberships of private, social and sporting clubs and societies);
- family ties in the UK (immediate family remain in UK or children are educated here).

Case law

With the withdrawal of IR20 and the unsatisfactory nature of HMRC6, case law will play a bigger part in establishing an individual's residency status. In *Cooper v Cadwalader* 5 TC 101, a US lawyer who holidayed in Scotland annually for the grouse season (60 days or so) staying in the same shooting lodge, was found to be UK resident, despite no other ties with the UK.

Should alarm bells be ringing in the ears of those high net worth, internationally mobile individuals who have left the UK or who have never been resident here but who visit annually to escape the intense heat of their resident countries or to attend the UK's society events such as Royal Ascot, Henley and Wimbledon?

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Practicalities

If leaving the UK individuals should, in addition to counting days:

- File P45/P85 to obtain tax refund for year of departure + notify HMRC of intention to emigrate.
- Sever all ties with the UK (business, financial, family and social)
- Sell accommodation or, at the very least, let out retained property on a long lease and expect to justify the ownership of UK accommodation to HMRC because renting suggests a prospect of future return.
- Generate permanent ties in their new 'home' country: buy a house, open bank accounts, make a foreign will, take up foreign citizenship, join social clubs and associations and get on the electoral roll.
- Remain outside the UK (with no visits) for a full tax year or failing that at least ensure that no more than 90 days are spent in the UK over a four-year period.
- Be prepared to justify departure, evidenced by a written contract covering a whole tax year.

If coming to the UK individuals should, in addition to counting days:

- Retain foreign citizenship.
- Retain non-UK domicile if they have one.
- Ensure that they own a residence in home jurisdiction which is ostensibly their main home.
- Vote and take an active part in life in their home jurisdiction be it politically, culturally, religiously, charitably or getting involved with local/community issues.
- Retain/obtain a burial plot in their home jurisdiction.

Non-UK residency cannot be achieved by means of carefully structured holidays and business trips. HMRC look at the bigger picture and the settled pattern of one's way of life. They have caught out taxpayers by means of credit card statements, landing cards and even photos in the press (providing evidence of presence in the UK).

Coming out of the UK tax net

During the year of departure, by HMRC concession only (ESCs A11 and D2), the tax year may be split so that the individual only pays income or capital gains tax in relation to the period that they were living in the UK (and full reliefs/allowances should be available depending on whether they actively elect to be taxed on the remittance basis).

Where an individual has been non-resident in the UK for one complete tax year:

- income tax is avoided on income arising for this year;
- some forms of UK employment income, rental income and UK investment income will still be taxable but full reliefs/allowances are available to Commonwealth citizens and EEA nationals;
- for non-UK domiciliaries income tax is avoided on unremitted foreign income which arose during a period of residency if not resident in the UK for 4 out of the 7 tax years prior to departure;
- for non-UK domiciliaries income tax is avoided on remitted foreign income which arose during a period of residency if the 4/7 year rule does not apply;
- CGT is avoided on the sale of any assets if the 4/7 year rule does not apply.

Where an individual is non-resident for three complete tax years:

- the 4/7 year rule is still relevant;
- as above for UK source income;
- capital gains tax is also avoided on the sale of assets acquired after the individual has left the UK and sold while non-UK resident (even if the 4/7 year rule applies) as he is no longer ordinarily resident;
- if he never returns to the UK, he is able to shed UK domicile status from the start of the fourth year thereby limiting inheritance tax to assets situated in the UK.

Where an individual is non-resident for four complete tax years:

- the 4/7 year rule is still relevant;
- as above for UK source income;
- he can shed deemed domiciled status for IHT even if he returns to the UK subsequently, as an individual is deemed domiciled in the UK where UK resident for 17 out of the previous 20 tax years.

Where an individual is non-resident for five complete tax years:

- as above for UK source income;
- foreign income arising prior to departure can be remitted to the UK tax free;
- CGT is avoided on the sale of all assets during period of non-UK residency.

Changes in HMRC attitudes

HMRC have renewed their efforts to clamp down on undisclosed offshore accounts owned by UK residents.

A new disclosure opportunity is due in the autumn, to run from 1 September 2009 to 31 March 2010 for paper disclosures and 1 October 2009 to 31 January 2010 for online disclosures.

HMRC have made an application to the Tax Tribunal to obtain a 'blanket notice' against hundreds of banks to disclose customer details.

They have even set up a special unit to oversee the tax compliance of 5,000 of the UK's ultra high net worth individuals.

It is reasonable therefore to conclude that HMRC enquiries and tax investigations will increase.

From an article by Camilla Wallace TEP, Wedlake Bell

NIC and payments in kind

Several employers had taken advantage of schemes in the 1990s mitigating their liability to employers' National Insurance by saying that the payments were payments in kind.

HMRC determined that contributions were due the payments, and the employers appealed. The department's claims were subject to the Limitation Act 1980, s 9, limiting recovery to six years.

Realising that the six year limit was likely to expire before the case finished, HMRC devised a way of keeping the years in date. They asked the employers to pay £1 on account of the National Insurance claim to be accompanied by an express denial of liability.

Doubt was cast on the effectiveness of the plan, so HMRC relied on the written exchanges between themselves and the employers to prevent the latter from relying on s 9.

The substantive appeals were found in favour of HMRC, but the employers refused to pay the contributions.

The department therefore began county court proceedings. The employers defended the proceedings saying that s 9 applied. The case was referred to the Chancery Division.

Mr Justice Briggs said that with regard to the claims in respect of which the primary limitation period of six years under s 9 expired by 11 September 2001, the employers were estopped by convention from asserting that those claims are statute barred.

However, in relation to claims which became statute barred by the expiry of six years on any date after 11 September 2001, the defendants to such claims were not estopped from relying upon the Limitation Act 1980.

CRC v Benchdollar Ltd and others, Chancery Division, 11 June 2009

PA Holdings Ltd and another

PA Holdings was an employee-owned service company which paid its employees median salaries and bonuses from profits by individualised annual awards.

For the years up to 1999, the company paid a lot of its profits into an employee trust. In 1999, it introduced a restricted share plan whereby bonuses paid to employees were paid via a UK resident company.

In this way they were paid as dividends of a UK resident company and taxed as dividends.

HMRC issued regulation 80 determinations for income tax on the payments, claiming that they were emoluments for the purposes of TA 1988, s 19 (now ITEPA 2003, s6). In addition, they said that National Insurance contributions were payable. There was no allegation that the scheme was a sham.

The company appealed.

The First-tier Tribunal judges concluded that the payments made to eligible employees under the restricted share plan were emoluments from employment, but were also dividends payable.

While the payments did fall within s 19, they were also distributions subject to Schedule F. So they were subject both to Schedule E and F.

This could not happen as a matter of income tax law, and the answer was in s 20(2) (now ITTOIA 2005, s 366). Schedule F took precedence over Schedule E. Therefore the payments were to be treated as dividends.

The taxpayers' appeal against the regulation 80 determinations was allowed.

With regard to the National Insurance issue, while the payments remained both emoluments of earnings and distributions, there was no rule preventing them being within Social Security (Contributions and Benefits) Act 1992, ss 3 and 6. Payments either fell within class 1 or not. On the facts, the payments did fall within class 1.

The appeal against the Social Security (Transfer of Functions) Act 1999, s 8 decisions was dismissed.

The taxpayers' appeals were allowed in part.

Capital Gains Tax

Adams

In May 1999 an unquoted company in which the appellant was the majority shareholder was sold to C in exchange for cash and shares.

The appellant's tax advisers had earlier applied for capital gains tax clearance under TCGA 1992, s 182, disclosing the earn-out rights.

Clearance was granted but restricted to the question of whether the conditions of s 137(1) were satisfied.

The appellant's tax return for the year was submitted by a different tax adviser.

It included a computation of proceeds received of £1,661,716 cash, £553,907 in shares, and deferred consideration of £913,572. The capital gain was based on the cash element alone.

HMRC did not enquire into the return. However, an enquiry was made into the taxpayer's 2002/03 return, in which he had included the disposal of the shares received on the earn-out.

It was agreed that the return was made on the basis that an election under s 138A had been made.

HMRC assessed the taxpayer to capital gains tax in respect of the 1999/2000 transaction, on the basis of negligent conduct by the taxpayer for submitting an incorrect return in that it did not include all the consideration on the disposal of the shares.

The taxpayer appealed.

The tribunal judges said that a valid s 138A election had been made and any officer with sufficient knowledge of the law should have known that the appellant wished s 138A to apply, even if unaware of the clearance application.

The taxpayer's appeal was allowed.

Entrepreneurs' relief for furnished holiday letting properties debate

An interesting question and answer session arose on the Taxation Forum recently in respect of the abolition of the beneficial FHL tax rules from 6 April 2010.

Will the abolition mean that the business is treated as having ceased such that relief continues to be available if the property is sold within the following three-year period?

My client has a furnished holiday letting property which he has owned for several years and which is currently standing at a substantial gain. He has no intention of selling it in the near future, but is aware that the favourable capital gains tax treatment – the availability of entrepreneurs' relief (ER), giving an effective tax rate of 10% – is being taken away on 6 April 2010.

There is no time apportionment with ER; if you don't qualify for it at the point of sale, you don't qualify at all. My client might consider selling, but it's possible that there will be a tax-driven glut in the market for holiday properties at that time, because everyone will be thinking the same thing.

Presumably it is possible to transfer the property into a trust or a company in order to trigger the gain at the lower rate of tax, but both of those options create other legal and tax complications that the client would rather avoid.

It occurs to me that ER is available for the disposal of the assets of a trade within three years of the cessation of the trade.

By law, the renting of furnished holiday letting (FHL) property ceases to be a trade on 5 April 2010. Does this mean that ER is available on sales of the property up to 5 April 2013?

The rental business is likely to continue into the future (although it will no longer be necessary to count the days available and the days actually let), so the 'business' will not have ceased, but the 'trade' will.

This seems to be quite an important issue for the many people who own FHL property in the UK and, as we now know, elsewhere in the EEA. Does anyone know the answer?

Reply from Sparta

Weymouth is proposing that the repeal of the furnished holiday letting legislation will allow his client to defer a sale of his property until a date between 6 April 2010 and 5 April 2013 while still being entitled to claim entrepreneurs' relief on the ultimate disposal. It is a forlorn hope.

ITA 2007, s 127(3) serves to treat a holiday letting business as defined in ITTOIA 2005, Part 3, Ch 6 as if it were a trade. TCGA 1992, s 241 draws on the same definition in ITTOIA to achieve a comparable effect for capital gains tax purposes.

The material disposal of a business asset used in a sole trader's business at the time of its cessation is a qualifying disposal within s 169I(2)(b) and s 169I(4)(a) and (b) enables that disposal to take place up to three years after cessation while retaining the advantage of any available entrepreneurs' relief.

The problem Weymouth faces is that there will have been no cessation or sale of the business prior to 6 April 2010 if letting continues as we are advised.

After 5 April 2010 his client will still have a rental business, but one which will no longer be regarded as a trade following the repeal of TCGA 1992, s 241(3)(a).

There can be no qualifying disposal where an asset is sold without the sale or cessation of 'the business', the constantly recurring term in TCGA 1992, s 169I.

Rather, on 6 April 2010 the property will cease to constitute a relevant business asset, i.e. one which could attract entrepreneurs' relief, and will instead be an excluded asset within TCGA 1992, s 169L(4)(b) and any subsequent sale will therefore be unable to access the relief.

Prior to 6 April 2010, s 169L(4)(b) would have had no application.

If a third party sale in the current tax year is unpalatable to Weymouth's client, he could consider a sale within the wider family to crystallise entrepreneurs' relief at 10% and simultaneously uplift the capital gains tax base cost of the property in the hands of the purchaser.

The purchaser could dispose of the property at any time in the future and it might be that the consideration could be left outstanding until the ultimate sale, if the client's circumstances permit.

If Weymouth's client were more interested in longer term estate planning and had little need of the property's income stream, he could also consider a tax-free gift to family members using holdover relief under TCGA 1992, s 165.

From 6 April 2010, the only way to gift his property free of capital gains tax will be to transfer it to a relevant property trust – an immediately chargeable transfer for inheritance tax purposes subject to the available nil rate band. Gifts to individuals absolutely will be chargeable to capital gains tax, subject to the available annual exemption.

Reply from Southern Man

This looks like a good idea. The only problem is that we know what the current legislation is, but we don't know what the legislation will be once the furnished holiday letting (FHL) rules are repealed from April 2010.

Currently, TCGA 1992, s 169I and s 241(3) provide relief if a furnished holiday let property is sold within three years of the business ceasing. But will this relief still be available for three years after 5 April 2010?

Now there might be an argument that relief will not be due as the business does not cease; after all, the plan is that letting will continue. Ordinarily, I would agree that there would be a business throughout, both before and after April 2010; so no cessation and no entrepreneurs' relief.

However, this seems to ignore the fundamental point of TCGA 1992, s 169S(a) which states that 'for the purposes of this Chapter (my emphasis) "a business" means anything which is a trade, profession or vocation …'

So ‘business’ for entrepreneurs’ relief has a separate meaning. Ordinarily, one might be inclined to say that all trades are businesses, but not all businesses are trades; however, for entrepreneurs’ relief, I believe that the meanings are synonymous.

This brings us to the critical question of how the relief will actually be withdrawn. The simplest solution would be that s 241 is abolished with effect from 6 April 2010.

I think, in that case, a business would then ‘cease to be carried on’ in the same way as if, say a trade at a shop or factory ceased. If the let property, shop or factory were then sold within three years of the cessation, entrepreneurs’ relief would apply.

This would seem a fair solution, especially as the client has little or no choice but that his ‘business’ is brought to a premature end.

A closer look... furnished holiday lettings in the EEA

HMRC’s technical note *Furnished Holiday Lettings in the European Economic Area (April 2009)* has some information on the extension of the furnished holiday letting (FHL) rules to properties in the European Economic Area and the rules repeal from 2010/11.

Properties in the EEA that meet the FHL criteria can therefore now qualify for the special tax treatment rather than being treated as an ordinary overseas property business under ITTOIA 2005, Pt 3 (for income tax purposes) or as Schedule D, Case V income (for corporation tax).

Full details of the conditions are in HMRC’s *Property Income Manual* at PIM4112/4115.

If an overseas property is now to be treated as within the FHL rules for the first time, HMRC state that if within the normal time limits for amending a self assessment tax return, an amended return can be submitted.

This should include any FHL income, including income from qualifying holiday accommodation in the EEA, within the furnished holiday lettings section of the UK property pages of the tax return.

If it is too late to amend the return, the normal time limits for making a claim in respect of the particular aspect of FHL will apply and this can be made by writing to the taxpayer’s local HMRC office.

This may apply to claims for hold-over relief, roll-over relief, relief for losses carried forward, terminal loss relief and the landlords’ energy saving allowance, which must be claimed on or before five years after the 31 January following the end of the tax year in question (or within six years of the end of the accounting period for claims by companies).

Until 31 July 2009, HMRC will accept late amendments for the tax year ending 5 April 2007 (income tax and capital gains tax) and accounting periods ending on or after 31 December 2006 (for corporation tax).

To ensure that claims or requests are dealt with effectively, it should be clearly stated that it is being made under the extended time limits for EEA FHL as announced at Budget 2009.

Taxation 15 July 2009

Inheritance Tax and Trusts

Brander (PRs of the Fourth Earl of Balfour) v R&C Comrs

In 1968 the Earl of Balfour ("the deceased") acquired, on the death of his father, a liferent interest in a traditional Scottish landed trust estate, the core elements of which were farming, foresty, shooting, let properties and a private water supply which served about 40 houses. The deceased was involved in and took overall charge of the running of the estate; the trustees had very little involvement. For a number of years the deceased operated in hand farming at two of the farms on the estate, sometimes in partnership with another. He made no demarcation between the partnership and the estate. In 1999, the deceased's health began to decline and estate managers ("BA") were appointed to provide day to day management and they reported to the deceased on all matters. Between 1999 and 2002 there was no partnership. In November 2002 the House of Lords declared the deceased to be the fee simple proprietor of the heritable estate. On 16 February 2003 the deceased entered into a limited partnership, the W Farming Company ("W"), with his intended successor and nephew, MB. The effective date of the commencement of that partnership was backdated to 10 November 2002. The partnership agreement provided for the introduction of initial capital into the business on the basis that the heritable property comprising the whole of the estate belonging to the deceased was contributed and credited to the partnership capital account A, and belonged to the deceased; and that the capital of the operation previously known as W, one-half of which had been gifted to MB by the deceased, was contributed equally by the two and credited to partnership capital account B, and belonged to them equally. With effect from 10 November 2002 the capital value of the whole heritable estate was treated as a fixed asset of W in the partnership accounts, its initial stated value being £3m. The deceased died on 27 June 2003. In 2008 HMRC issued a notice of determination denying business property relief in respect of the deceased's interest in W for the purposes of IHTA 1984. MB, in his capacity as personal representative, appealed. The issue arose as to whether the deceased's interest in the partnership, which subsisted immediately before his death, replaced the previous business carried out by the deceased for the purposes of IHTA 1984 s 107, and if so, the nature of that business.

The tribunal judge found that IHTA 1984 s 107 applied. On the facts the activities which were carried on at the estate throughout the period between 1999 and 2002 were managed by the deceased as his single business. To that end the deceased used assets of the trust estate in the business activities being carried on at the estate. He took de facto responsibility for running all aspects of the estate and he either made the business decisions himself or made recommendations to the trustees which he expected them to approve, which they invariably did. The trustees rarely met and appeared entirely passive. In his capacity as liferenter (until November 2002) the deceased had to be treated as beneficially entitled to the property in which the liferent interest then subsisted. That was, essentially, the whole estate. The fact that the trust was a separate entity from the deceased did not mean that there had to be two separate businesses. The various activities on the estate were interlaced or dovetailed. Therefore from at least about 1999 until November 2002 the estate management and farming activities carried on at the estate were managed as a single composite business. Such business use as there was of the heritable property in the estate was exactly the same the day before the 2002 partnership began as it was the day after it had begun. The assets of the estate were used in that business. Therefore all the property replaced by the capital of the 2002 partnership was relevant business property immediately before (and for a period of more than two years before the deceased's death) it was so replaced, for the purposes of IHTA 1984 s 107. In those circumstances the deceased's interest in the W partnership was relevant business property within IHTA 1984 s 105(1)(a), subject to the provisions of s 105(3).

The tribunal judge considered that in determining whether a business consisted of mainly of holding or making investments for the purposes of IHTA 1984 s 105(3), it was necessary to establish what the preponderance of business activity was. That could be looked at from the point of view of a variety of relevant factors in an attempt to create an overall picture, to see whether that picture showed that the business activities on the estate consisted mainly of making or holding investments. Those factors included turnover, profit, expenditure and time spent by

everyone involved in the carrying on of the various business activities. Unless every hour of every employee, every item of income and expenditure was identified and analysed and overlapping activities taken into account, no precise quantitative assessment could be made. Such an assessment over any reasonable period was probably impossible to achieve and ultimately the matter had to be assessed on the basis of such evidence as the parties had been able to lead or point to. Where, as in the present case, there was incomplete evidence, it was a matter of more general assessment and impression as to where the preponderance of business activity lay. That meant looking at the activities being carried on at the estate in the round. The impression in the current case was that the management of a landed estate such as this estate even where a significant amount of the income was derived from letting income was, overall, mainly a trading activity. That was where the preponderance of activity and effort lay. BA were engaged as estate managers; most estates of the type under discussion were heavily based on farming and to some extent on forestry and woodland management and related shooting interests. The letting side was ancillary to the farming, forestry, woodland and sporting activities. The farming activities, albeit they included agricultural tenancies, occupied by far the greater area of the estate. Therefore the business activities carried on at the estate did not consist wholly or mainly of making or holding investments. Section 105(3) was not engaged. It followed that the appeal would be allowed.

Appeal allowed.

Tribunal—J Gordon Reid QC, FCI Arb, ***14 May 2009***

Davies and anor v Revenue and Customs Comrs

On 19 December 2006 the deceased, a widower, died. Her estate, which was valued at just over £164,000 included a property and shares ("the assets") which she had inherited from her husband on his death in 1969. Under the terms of the husband's will, made in 1965, which mirrored that of the deceased's will made at the same time (save for the proviso that she left a legacy of £500 to each of their daughters), the deceased inherited his estate, including the assets which he had owned absolutely; had she failed to survive her husband by 28 days, the property would have passed to the daughters. Estate duty was paid on his death. After his death the deceased made a new will leaving the estate, including the assets, to her daughters. HMRC determined that the whole of the deceased's estate was chargeable to inheritance tax. The daughters appealed contending that part of the deceased's estate, comprising of the assets, should be left out of account for the purposes of IHTA 1984 s 4(1) on the following grounds: (i) the assets were derived from assets owned by the husband and inherited by the deceased from him and were either (a) the subject of a fully secret trust made in 1965, or (b) were subject to a trust as a result of mutual wills; (ii) the terms of the trust were that the first to die would leave his or her estate to the survivor on the understanding that after the death of the first spouse that estate would be left on the death of the second spouse to them; (iii) the existence of a trust meant that the property was settled property within the definition of FA 1894 s 22(1)(i) when the husband died; (iv) that it was subject to estate duty on the husband's death; and (v) that as a result of the terms of the trust the deceased was not competent to dispose of the property for the purposes of FA 1894 s 5(2), so that the provisions of IHTA 1984 Sch 6, para 2 were satisfied in respect of the assets. HMRC submitted that there was no evidence to support the existence of any trust and whilst the deceased's conduct in relation to assets derived from her late husband might be consistent with the existence of a secret trust, it was equally consistent with the existence of a non-binding moral obligation or a desire on her part to ensure that her children were not deprived of property which she considered to be their inheritance.

The tribunal judge found that although the deceased was determined to leave her assets to her two daughters and carried out her intention to leave all her assets to them, that was not sufficient for the exemption in IHTA 1984 Sch 6, para 2 to apply. The exemption only applied if there was settled property. In the instant case there was no written trust of any of the assets which passed from the deceased's husband to the deceased. His will provided for her to take an absolute interest. There was no evidence that her husband was the beneficiary of any written trust; the property owned by him and passed to the deceased was owned outright by him. Nor was there any evidence of a secret trust whereby the deceased's husband had imposed a legally enforceable duty on her to leave property derived from him to the children. Furthermore, there was no evidence that, on the balance of probabilities, there had been agreement between the two will makers in 1965 to dispose of their property in a similar way under mutual wills. It was not

sufficient to find mere simultaneity of wills and similarity of terms, although the fact that there were such wills was a relevant circumstance to take into account. The fact that the deceased made a new will in her daughters' favour shortly after the husband died was not an indication of a need to comply with any agreement; they would have inherited under the 1965 will since the husband had predeceased the deceased. Accordingly as there was no evidence to support the existence of a secret trust or of a trust arising from mutual wills, the exemption did not apply. The appeal would be dismissed.

Appeal dismissed.

Tribunal: Judge Judith Powell, ***9 June 2009***

IHT – Commorientes and the Transferable Nil Rate Band

The 'commorientes' rule is set out in the Law Property Act 1925, s 184. It provides as follows:

> "…where…two or more persons have died in circumstances rendering it uncertain which of them survived the other or others, such deaths shall… for all purposes affecting the title of property, be presumed to have occurred in order of seniority, and accordingly the younger shall be deemed to have survived the elder." (nb the above rule does not extend to Scotland).

For Inheritance Tax (IHT) purposes, the potential effect of the commorientes rule could be double (or multiple) IHT charges on such death, albeit subject to quick succession relief for chargeable transfers (IHTA 1984, s 141). The IHT legislation therefore includes the following relieving provision (IHTA 1984, s 4(2)):

> "…where it cannot be known which of two or more persons who have died survived the other or others they shall be assumed to have died at the same instant."

In addition, IHTA 1984, s 92 ('Survivorship clauses') addresses the potential problem of double (or multiple) IHT charges on successive deaths. It applies to deaths which are not (or are not treated as being) simultaneous but which follow within a short time period (i.e. six months). This rule broadly provides that if (under the terms of a will or otherwise) property is held for a person on condition that he survives another for a specified period of not more than six months, and another beneficiary becomes entitled to the property because the original beneficiary did not satisfy the survivorship condition, the IHT position is the same as if that other beneficiary had taken the property from the outset.

IHT Implications

Suppose that husband and wife (or civil partners) have wills leaving their estate to the surviving spouse on first death, and to the children on the second death. For these purposes, it is assumed that there is no survivorship clause in the wills (or that any survivorship clause is disapplied in commorientes circumstances). What is the IHT position if they both die simultaneously (e.g. in a car accident)?

For IHT purposes, as it cannot be known which of the two survived the other, they are assumed to have died at the same instant. Therefore the older spouse's estate does not increase the estate of the younger spouse (IHTA 1984, ss 4(2), 54(4)). The interaction of these provisions and the commorientes rule in LPA 1925, s 184 can result in the estate of the elder spouse or civil partner escaping IHT on both deaths. HMRC provide the following example in the *Inheritance Tax Manual* (at IHTM 12197):

Example

H by will leaves his estate to his younger wife, W. She by will leaves her estate if H does not survive her to their children. H and W are killed in an accident. The order of their deaths cannot be established so devolution is governed by S184 Law of Property Act. H being the elder is deemed to have died first. His assets therefore pass into W's estate. W's estate passes to their children.

The position for IHT is

- on H's death his estate is spouse or civil partner exempt because H's estate devolves on W and S4(2) does not prevent S18 applying
- on W's death S4(2) operates to exclude H's death estate from W's death estate for the purposes of the charge under S4(1) on her death. Since H and W are treated as having died at the same instant we tax only W's own estate in connection with her death.

The result is that H's estate escapes IHT on both deaths.

It therefore reaches the children, the beneficiaries under W's will without incurring a tax charge."

Different treatment applies to simultaneous deaths in Scotland and Northern Ireland (see IHTM12193, 12194).

Transferable nil rate band

The introduction of the facility to transfer unused nil rate bands between spouses or civil partners in Finance Act 2008 has potentially improved the IHT position further in commorientes circumstances. This is on the footing that the 'death at same instant' rule in IHTA 1984, s 4(2) only applies for the purposes of that section, and does not affect how the estate devolves. The potential transferability of any unused nil rate band is confirmed in HMRC guidance, which states the following (IHTM43040):

"In England & Wales, where spouses or civil partners die at the same time leaving Wills and it is not possible to establish who died first, there is a presumption that elder person died first. The couples' estates are treated for IHT on this basis and where the terms of the Will mean that there is unused nil rate band on the death of the first, it is available to be transferred to the estate of the surviving spouse or civil partner. IHTA84/S4(2) continues to operate on the death of the younger to exclude the assets received from the estate of the elder. **So in effect, the younger's estate could benefit from a double nil rate band and the assets accruing to their estate from the elder are excluded** (emphasis added)." The guidance adds:

"If the couple had died without Wills, the presumption does not apply, so each person's estate would pass on to their heirs under intestacy. In the event that one spouse or civil partner had any unused nil rate band, it is available to be transferred to the estate of the other, if required."

As mentioned, different provisions apply in Scotland and Northern Ireland regarding simultaneous deaths, i.e. both spouses (or civil partners) are treated as dying at the same moment, so neither can inherit from the other. Each spouse's estate passes whether by Will or under intestacy. If one spouse had any unused nil rate band, it is available to be transferred to the estate of the other.

Article by Mark McLaughlin

Lecture P549 (9.58 Minutes)

IHT recent issues

Penalties for incorrect IHT returns

A professional executor who submitted an IHT account (Form IHT200) on a deceased individual's death which contained a property valuation that later turned out to be too low successfully appealed against penalties sought by HMRC.

In *Cairns v Revenue & Customs* [2009] UKFTT 00008 (TC), HMRC imposed a penalty on Mr Cairns, a solicitor acting as a personal representative. The penalty sought by HMRC originally amounted to £33,560, and related to the valuation of the deceased's residence as returned on Form IHT200 (the summons served on Mr Cairns was actually dismissed because it did not specify the charge against Mr Cairns, but the Special Commissioner considered the case anyway).

Mr Cairns, a solicitor acting as the deceased's executor, submitted an IHT account (Form IHT200) to HMRC following the deceased's death in October 2004, which included a value of £400,000 for the deceased's residence. This was based on a valuation by chartered surveyors in January 2004, which

was stated to be an "…arbitary figure pending investigations as to costs involved in upgrading". The valuation was heavily qualified, due to the poor state of the property. Mr Cairns was uncertain of the property's value, but considered that the existing valuation was sufficient meantime. The District Valuer subsequently valued the property at £600,000 as at the date of death, which was also the amount for which the property was sold.

The Special Commissioner was asked to consider the following:

(i) Whether Mr Cairns submitted an incorrect IHT account; and

(ii) Whether Mr Cairns acted negligently (fraud was out of the question).

No negligence

HMRC argued that Mr Cairns should have obtained another professional valuation or "revisited" the valuation already obtained, and that there had been a "wilful default". However, it was considered that it must be established that the IHT account had been incorrectly and negligently delivered. The Special Commissioner held that "…the mere failure to obtain another valuation when it has not been established that a second valuation would have led to a different figure being inserted in the statutory form does not constitute negligent delivery of an incorrect account." He added:

"On the evidence before me, even if it were concluded that an incorrect account was delivered or furnished, it is simply not possible to conclude that it was negligently delivered or furnished except in one minor respect."

Careless, but technical

The minor matter referred to related to the fact that the valuation obtained had been heavily qualified, and was a provisional estimate. Mr Cairns had not disclosed this in the IHT account. The omission to do so was a careless error. However, the Commissioner added that "…it was minor, technical and of no consequence whatsoever."

The Commissioner concluded that there had been a "narrow, technical failure…" The account was incorrect. The sum of £400,000 should have been described as a provisional estimate. Whilst that failure was negligent, it was held to be a "failure of the merest technicality". Mr Cairns was held to have acted "perfectly sensibly and reasonably throughout".

The summons against Mr Cairns was dismissed. The Commissioner added that even if he had been wrong to dismiss it, he would have reduced the penalty to a nominal amount or recommended that it be so reduced.

The case offers some comfort to the personal representatives of a deceased person's estate on the circumstances in which penalties can be imposed for an incorrect IHT return. However, it also provides a warning as to the degree of disclosure required in respect of provisional valuations and estimates to avoid an accusation by HMRC of careless behaviour.

Investment accounts and 'settlements'

The transfer of a building society account into joint names has been held to constitute a settlement for IHT purposes.

In *Smith v HMRC* [2009] SpC 742, the deceased transferred a building society account into the joint names of herself and her son before she died on the basis that she would be solely entitled to the interest earned by that account, and he would become entitled to the capital when she died. However, due to a misunderstanding the value of the account was not included in the IHT return submitted by the executors. The building society account was subsequently reported to HMRC and Notices of Determination were issued. HMRC accepted that there was no fraud in the omission of the account from the IHT return, and that there was unlikely to have been negligence on the part of the executors, so no penalty was sought.

The Special Commissioner held that the money in the building society account was settled property and that the person liable for the IHT attributable to it was the deceased's son as trustee and as recipient of it. He was also liable as executor of the estate for any additional tax due and which was attributable to the assets returned in the original inheritance tax return. The appeals were allowed in part, and the Notices of Determination in respect of the deceased's son and other family members (in their capacities as executor and recipient of residue) were adjusted accordingly.

The deceased, Mrs Smith, inherited the Halifax account on her husband's death in January 2002. She transferred the funds in a Halifax account into joint names with her son Malcolm on 14 November 2002, and died on 15 March 2003. The arrangement had been that Mrs Smith was entitled to receive the income produced by the account, and Malcolm would receive the capital when she died. Interest earned on the account was always paid into an account in Mrs Smith's name. Capital withdrawals could have been made by either of them, but this did not happen. The arrangements were voluntary and informal. The capital balance inherited by Mrs Smith from her husband remained unchanged until she died, and although she might have drawn capital from the account she did not do so.

In determining the incidence and liability to IHT attributable to the value of the Halifax account, the Special Commissioner had to consider whether the property was settled property immediately before Mrs Smith's death. HMRC submitted that a 'resulting trust' can arise if a person puts property into joint names with another, in which case the property is held for the original sole owner. However, a resulting trust can be displaced if the original owner intended to benefit the joint owner (i.e. a presumption of advancement). HMRC stated that because it was a mother who made her son the holder of the account, there was a "rebuttable presumption" of advancement. If it had been rebutted, HMRC considered that there would have been a beneficial joint tenancy, but in any event the value of the account formed part of the deceased's estate for IHT purposes. HMRC's conclusion was that the property formed part of the deceased's estate under IHTA 1984, s 5 ('Meaning of estate').

IIP Settlement

The Special Commissioner pointed out that property put into joint names may be the subject of an express trust. Whilst there was no written evidence of the terms on which the joint account was held, the Commissioner considered that an express trust need not be made in writing in those circumstances. She concluded that there was an express trust of the property in the account. The property was held for Mrs Smith and then for Malcolm in a manner falling within the definition of "settlement" (in IHTA 1984, s 43(1)(a)). This includes "property held for persons in succession".

As Mrs Smith was entitled to the income from the property, she was beneficially entitled to an interest in possession (IIP) in settled property. Under the 'old' (pre-Finance Act 2006) rules on the IHT treatment of lifetime IIP settlements which applied in this case, Mrs Smith was beneficially entitled to the property itself, and it therefore formed part of her taxable estate when she died.

Setting aside documents and transactions

In certain circumstances, it can be possible to have transactions which result in adverse tax consequences set aside.

In *Bhatt v Bhatt* [2009] EWHC 734 (Ch) (reported in *Simon's Tax Intelligence*, 17 April 2009), the claimant, Mrs Bhatt, (who had a limited command of the English language) sought advice about how to deal with her late husband's estate. She was advised by a tax adviser that urgent steps were needed to avoid paying IHT. He advised Mrs Bhatt to let her late husband's share of the matrimonial home into trust for her children, and that she should make a new will. She accepted the advice in its entirety. Mrs Bhatt later became aware that her actions had potentially serious tax consequences. She therefore issued proceedings for equitable relief. This included rectification of the registered title to the property, and the rescission of a number of documents (a declaration of trust, deed of variation, notice of severance and a transfer of the property to her children).

Mrs Bhatt claimed that she had entered into the transaction under the following mistaken beliefs:

1. Steps were needed to mitigate the incidence of IHT on her late husband's death (although there was no need, due to the surviving spouse exemption);
2. IHT would be reduced or avoided on her death if the documents were executed (particularly the trust deed), and
3. She would continue to have an untrammelled right to occupy and to exercise control over the property during her lifetime, and to sell it if she wished at any time without having to obtain consent from anybody.

The court considered that if there had otherwise been an operative mistake, it had to be satisfied that if the claimant had known the true facts she would not have signed the documents. The facts were that there had been no need for a notice of severance (because one already existed), that the trust deed would unintentionally deprive her of substantive rights and confer other rights, and might have caused an incidental potentially exempt transfer for IHT purposes. The court considered that the

document did not accurately reflect the claimant's intentions or instructions. Her expectations were so seriously falsified that the documents could not stand, and the transaction had to be set aside. The transaction had divested her of control of the property during her lifetime, which (rather than saving IHT) had the potential to cause an IHT liability to arise. The court held that the documents and the transactions as a whole would be set aside, subject to HMRC being given a reasonable opportunity to contest the outcome.

In reaching its decision, the court followed the decision in another case involving IHT, *Ogden v Trustees of the RHS Griffiths 2003 Settlement and others [2008] EWHC 188 (Ch)*. In that case, Mr Griffiths made gifts in 2003, and a further gift in February 2004. In autumn 2004, he was diagnosed with lung cancer, and he died in April 2005. The executors argued that the transfers had been made under a mistake by the deceased as to the state of his health (ie that there was a real chance he would survive for seven years). The court refused to set aside the transactions in 2003, as they were made when the deceased had not had lung cancer, so he had made no mistake about the state of his health. However, the deceased had been suffering from lung cancer by the time of the third transaction in February 2004. Had he known that he was suffering from lung cancer, he would not have acted as he did. Accordingly, the court held that transaction to be voidable.

No mistake

However, applying to the court for rectification is not without its potential limits. In *Allnutt & Anor v Wilding & Ors* [2007] EWCA Civ 412, the taxpayer intended that a gift of £550,000 into settlement should be a PET. However, the gift was actually an immediately chargeable lifetime transfer. The Court of Appeal rejected an application for rectification, as the settlement correctly recorded the settlor's intention at the time. The fact that the taxpayer's fiscal purpose was not achieved was not considered to be material.

Article by Mark McLaughlin

Lecture P550 (9.18 Minutes)

Administration

Penalties for errors on returns

Section 97 and Schedule 24 to Finance Act 2007 set out the new penalty regime for errors on returns which has commenced. (Commencement details later). The new regime replaces all penalties for inaccuracies on returns under income and corporation tax, but also under PAYE and VAT. The new penalty regime charges an increasing penalty based on the tax lost, determined by the seriousness of the behaviour of the taxpayer. There are no penalties for mistakes made in good faith, and where adequate care has been taken.

Penalty triggers

A penalty will apply when a person gives a specified document to HMRC, and the document contains an inaccuracy which is careless or deliberate and which amounts to or leads to any of the following :

- An understatement of his liability to tax;
- A false or inflated statement of a loss he has incurred, or
- A false or inflated claim to repayment of tax.

The types of return covered by the legislation are listed in para 1 as follows:

Tax	**Document**
Income tax or capital gains tax	Returns under S8/8A of TMA (personal + trustee tax returns)
	Return, statement or declaration in connection with a claim for an allowance, deduction or relief
	Accounts in connection with ascertaining a tax liability
	Partnership return
	Statement or declaration in connection with partnership return
	Accounts in connection with a partnership return
Income tax	Return for the purposes of PAYE regulations
Construction industry deductions	Return for the purposes of regulations under Section 70(1)(a) of FA 2004 in connection with deductions on account of tax under the CIS. (monthly CIS return)
Corporation tax	Company tax return under para 3 of Sch 18 to FA 1998 (self assessment for CT)
	Return, statement or declaration in connection with a claim for an allowance, deduction or relief
	Accounts in connection with ascertaining a liability to tax
VAT	VAT return under regulations made under para 2 of Sch 11 to VATA 1994
	Return, statement or declaration in connection with a claim
Income tax, capital gains tax, corporation tax or VAT	Any document which is likely to be relied upon by HMRC to determine, without further enquiry, a question about : His liability to tax Payments by him by way of or in connection with tax Any other payment by him (including penalties), or Repayments, or any other kind of payment or credit to him.

Para 2 sets out a further trigger to penalty, based on an assessment to tax issued by HMRC. When an assessment is issued by HMRC to a person which understates his liability to tax and he has failed to take reasonable steps to notify HMRC within 30 days after that it is an under assessment, he is liable to a penalty. In determining what steps were reasonable to have taken, HMRC must consider whether the person knew or should have known about the under assessment, and what steps would have been reasonable to take to notify HMRC. The taxes affected by para 2 are income tax, capital gains tax, corporation tax and VAT.

Finance Act 2008 extended the new penalty regime to all other taxes and duties with the exception of tax credits. The commencement date for the new taxes is one year later than for the main taxes listed above – that is the regime will be active from 1 April 2010 in respect of behaviour on or after 1 April 2009.

The degrees of culpability which determine the rate of penalty are set out in para 3 to Sch 24. They are :

Careless – if the inaccuracy is due to failure by the person to take adequate care, or if an inaccuracy which was not careless or deliberate is discovered and the person did not take reasonable steps to notify HMRC.

Deliberate but not concealed – if the inaccuracy is deliberate, but the person does not make arrangements to conceal it, and

Deliberate and concealed – if the inaccuracy is deliberate, and the person makes arrangements to conceal it, for example by submitting false evidence in support of an inaccurate figure.

Amounts of penalty

The penalty rates rise according to the degree of culpability by the person. The rates of penalty are as follows :

Culpability	**Penalty rate**
Careless	30%
Deliberate but not concealed	70%
Deliberate and concealed	100%

The penalty rate for a penalty under para 2 (under assessment not notified) is 30%.

Potential lost revenue

The rates of penalty are applied to the “potential lost revenue”. This is defined by paras 5 to 8, with para 5 applying generally. The definition is logical and states that the potential lost revenue is the additional amount payable in tax and NIC as a result of the error being corrected. However, group relief and repayments of section 419 tax are ignored when calculating the potential lost revenue.

Where there are multiple errors, and the resulting additional tax would be different depending on the order in which the errors are corrected, the legislation provides clear guidance as to how this is achieved .

Para 7 deals with the calculation of potential lost revenue where losses have been overstated. In normal circumstances, when the loss has been set off and relief gained, the potential lost revenue can be calculated as normal. However, where part of the loss has not been wholly used as relief against tax due, the amount determined by para 5 is increased by 10% of the balance of the loss (the unused portion).

Where the inaccuracy overstates a loss in a group scenario, then group relief will be taken into account when calculating the potential lost revenue, as this would give relief to the loss. Finally, the potential lost revenue in respect of a loss is nil if there is no reasonable prospect of the loss being given relief and reducing the tax liability of any person.

Finally para 8 deals with the potential lost revenue where the tax has been delayed as a result of the inaccuracy. The potential lost revenue is 5% of the tax for each year, for each year of delay, with a pro rata adjustment for part years of delay. This does not apply where there are losses which have been overstated, as para 7 takes precedence.

Disclosure

The old scheme of mitigated penalties will no longer apply, but taxpayers can reduce the gross penalty by disclosure, for which a range of reductions have been specified. Para 9 first defines a disclosure of an inaccuracy as :

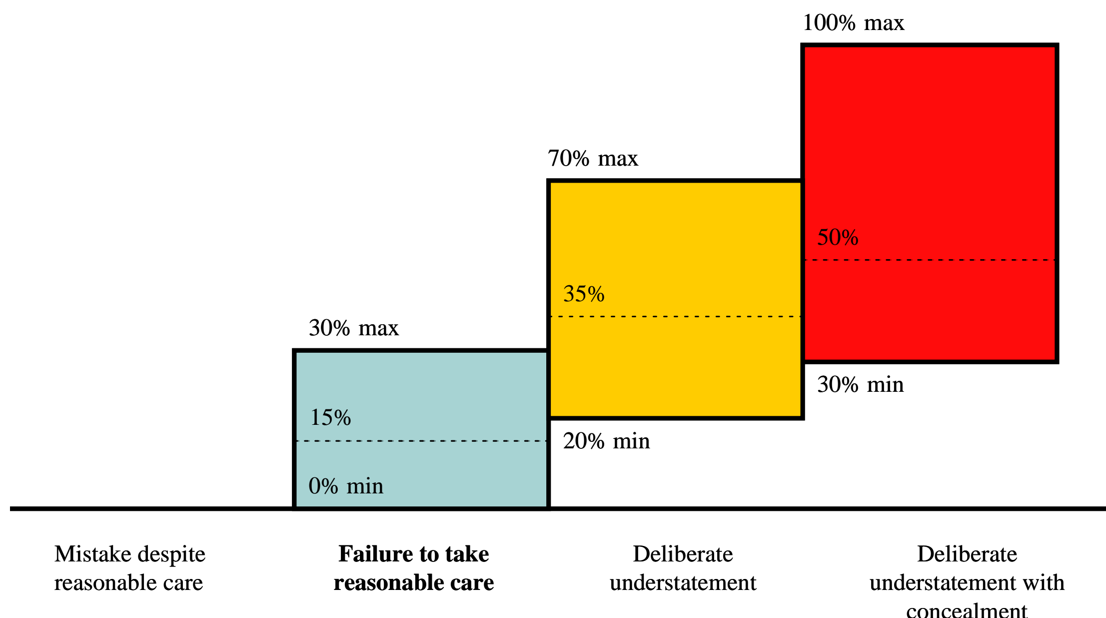
- Telling HMRC about the inaccuracy,
- Giving HMRC reasonable help in qualifying the inaccuracy or under assessment, and
- Allowing HMRC access to records for the purpose of ensuring that the inaccuracy or the under assessment is fully corrected.

It further goes on to list two types of disclosure and to refer to the "quality" of the disclosure. Disclosure is unprompted if made at a time when the person has no reason to believe that HMRC has discovered or are about to discover the inaccuracy or under assessment, and otherwise is "prompted". The quality of a disclosure is determined by the timing, nature and extent of the disclosure. The following rates of penalty will apply :

Culpability	Maximum penalty (no discount)	Unprompted minimum penalty	Prompted minimum penalty
Careless	30%	0%	15%
Deliberate	70%	20%	35%
Deliberate & concealed	100%	30%	50%

Finally, the penalty calculated can be reduced by HMRC in special circumstances, but these do not include inability to pay. HMRC also have power under para 11 to stay a penalty or to agree a compromise with regard to penalties. Penalties under paras 1 & 2 will be reduced by any other tax geared penalty which applies in relation to the same tax.

This can be represented by the following diagram :



Penalty reductions

Penalties may be reduced based on whether the disclosure is 'prompted' or 'unprompted', and based on the 'quality' of the disclosure.

The quality of the disclosure is determined by considering the following three factors:

1. telling (potential reduction of 30%)
2. helping (potential reduction of 40%)
3. access (potential reduction of 30%)

The resulting reduction is applied to the difference between the maximum and minimum penalties.

Example

Fred is a sole trader who did not keep his records up to date and has not kept any details of the amount of his drawings or of payments made in cash. HMRC opened an enquiry before any disclosure was made. He cooperated fully once enquiry commenced.

The likely offence is that of lack of reasonable care and the disclosure is prompted. The maximum and minimum penalties are 30% and 15%.

Fred can reduce the maximum penalty by the difference between the maximum and minimum penalty of 30% - 15% ie 15%.

The extra 15% reduction can be achieved by gaining the maximum reduction for telling (30%), helping (40%) and access (30%). However, for the purposes of demonstrating this example, say in this case he only achieved 80%. The additional 15% is therefore limited to 80% of 15% ie 12%. The maximum penalty of 30% can therefore be reduced by 12% and so the penalty is 18%.

Suspended penalties

Part 3 of the Schedule sets out the procedure for assessment, appeal and similar. This includes a further new development which is the power for HMRC to suspend a penalty for careless inaccuracy.

HMRC may notify a taxpayer that his penalty (all or part of it) has been suspended for a period of up to two years, and will set conditions of the suspension. However, the power to suspend a penalty will only be available if compliance with a condition of the suspension would help the taxpayer to avoid becoming liable for further penalties for careless inaccuracies.

At the end of the period of suspension, if HMRC are satisfied that the conditions of the suspension have been complied with then the suspended penalty will be cancelled; if the conditions have not been complied with, the suspended penalty will become payable. If during the period of suspension a further penalty becomes payable under para 1 (for an inaccuracy in a return) then the suspended penalty will also become immediately payable.

Errors when an agent is acting

Part 4 includes other miscellaneous provisions in relation to penalties. It extends the giving of a document to HMRC in para 1 to the authorisation of an agent to give the document on behalf of a taxpayer. The agency provision also applies to under assessments of tax, under which someone authorised to act on P’s behalf in relation to tax is deemed to act in the taxpayer’s stead in failure to promptly notify an under assessment.

The law states that a taxpayer is not liable to a penalty in relation to anything done or omitted by his agent if HMRC is satisfied that the taxpayer took reasonable care to avoid an inaccuracy. This would mean that the taxpayer would need some evidence that he took reasonable care over his tax affairs.

Officers of companies

Where a company is liable to pay a penalty for a deliberate inaccuracy which was attributable to an officer of the company, the officer as well as the company shall be liable to pay the penalty, and HMRC may seek recovery of such proportion of the penalty from the officer as they may specify. However, no more than 100% of the penalty assessed can be collected in this way, between the company and the officer. Officer in this context means director, shadow director and secretary.

Partnership returns

The person delivering the return in the case of a partnership return would be the firm. When an inaccuracy affects the amount of tax due by a partner, the partner is also liable for a penalty – this is termed the partner's penalty. The nominated partner would remain liable for the penalty on the firm. Potential lost revenue is calculated separately for the penalty on the firm and each partner's penalty, by reference to the proportions of any tax liability that would be borne by each partner.

Commencement dates

The new penalty provisions in Schedule 24 of FA 2007 were the subject of a commencement order in March 2008 (SI 2008 / No 568).

The overall commencement date for the new regime is 1 April 2008. However, there is a transitional rule, preventing the penalty form applying to documents which are required to be submitted before 1 April 2009.

This applies to relevant documents in respect of periods commencing on or after the date of 1 April 2008. This means that 2008-09 will be the first income tax returns affected by the new rules, as they are due for submission on 31 January 2010. For companies, returns for periods ending 31 March 2009 will be the first affected, which are due for submission by 31 March 2010. P35's relating to 2008-09 will be affected by the new penalty provisions with a due date of 19 May 2009.

The same date applies to relevant assessments for periods commencing on or after that date. This means that penalties cannot be due for VAT returns or assessments except in relation to the quarter ended 31 March 2009, which would be due for submission on 30 April 2009.

For eighth and thirteenth directive reclaims of VAT the dates are 1 January 2009 and 1 July 2008 for claims in relation to periods commencing on or after those dates.

1 April 2009 will be the commencement date for any other relevant reclaim of tax which is not related to a tax period.

Finally 1 April 2009 will be the commencement date in relation to any other document when the person's liability to pay the tax arises on or after that date.

Reasonable care

All of the penalty reform depends upon the definition of reasonable care adopted by HMRC. Guidance on this aspect was issued on 1 April 2008 as the first release of a new HMRC manual – the Compliance Handbook Manual. So far, only chapter CH80000 has been released, this being the chapter on the new penalty legislation. This includes significant guidance on "reasonable care".

Guidance on the meaning of reasonable care

This appears in CH81120. It sets out the principle that reasonable care will vary depending on the capabilities and circumstances of the individual acting, and in particular on the type of business or transaction he is dealing with. Thus :

- An unrepresented taxpayer will have a lower expectation of his capabilities than a represented taxpayer
- Where a complex or unusual transaction is to be undertaken, the taxpayer is expected to take extra care
- Reasonable care extends to the records that a taxpayer keeps to enable him to report his income and gains correctly
- Reasonable care can also extend to the systems in place to ensure that tax is dealt with properly in relation to business transactions.

Uncertainty and reasonable care

There is particular guidance for those undertaking a transaction about which the tax outcome is uncertain :

"In HMRC's view it is reasonable to expect a person who encounters a transaction or other event with which they are not familiar to take care to find out about the correct tax treatment or to seek appropriate advice.

If after that the person is still unsure they should draw attention to the entry and the uncertainty when they send the return or document to us. In these circumstances the person will have taken reasonable care to draw our attention to the point and if they are wrong they will not have been carelessly so."

Thus, disclosure, which is normally considered in the context of the issue of discovery, now will extend to the issue of penalties where it is found that a transaction or event has been incorrectly reported or taxed. The proper disclosure of the transaction and the uncertainty relating to it will achieve the "reasonable care" required in order for the taxpayer to avoid a penalty should the treatment prove incorrect. The guidance then provides some examples of when reasonable care has been applied and no penalty is due.

Examples of when a penalty would not be due include

- a reasonably arguable view of situations that is subsequently not upheld
- an arithmetical or transposition inaccuracy that is not so large either in absolute terms or relative to overall liability, as to produce an obviously odd result or be picked up by a quality check
- following advice from HMRC that later proves to be wrong provided that all the details and circumstances were given when the advice was sought
- acting on advice from a competent adviser which proves to be wrong despite the fact that the adviser was given a full set of accurate facts.

Reasonable care – agents acting

When an agent is acting on behalf of a client, the taxpayer must still exercise reasonable care, and must be able to evidence this to the officer concerned. This might involve providing access to correspondence between the agent and his client. The guidance states that reasonable care when an agent is acting includes :

- Appointing an agent competent to deal with his affairs,
- Giving the agent all of the relevant information, and
- Checking the return, as far as possible, before it is submitted.

Agents will want to review their process and procedures to establish how these aspects can be evidence and to provide clients with the support that they might need.

For example when sending a client the 2008/09 self assessment return it would be advisable to send them the summary sheet generated by the tax software system with an approval statement at the bottom for the client to sign. The client is far more likely to understand the summary sheet showing all forms of income, gains and deductions than they are the tax return. They are therefore more likely to review the summary sheet and spot obvious errors – for example no overseas rent included in their return because they did not tell you about their new source of income!

We need to counter clients signing returns without reviewing the return for obvious errors – the summary sheet may help.

Large businesses

The guidance on reasonable care by larger businesses was developed jointly between HMRC and the CBI, so that an agreement to an appropriate and balanced approach could be secured. The guidance states that a "person" (meaning in this context a business or corporate) has taken reasonable care if :

- arrangements or systems (such as comprehensive internal accounting systems and controls with specific reference to tax sensitive areas) exist that, if followed, could reasonably be expected to produce an accurate basis for the calculation of tax due by the internal tax department, or external agent, **and**
- despite the above, inaccuracies arise in processing or coding items through the person's accounting system which result in a mis-statement of tax liability, **and**
- the effect of the inaccuracies is not significant in relation to the person's overall tax liability for the relevant tax period."

Finally, it is worth considering the examples of situations in which the taxpayer failed to take reasonable care. They are at CH81142.

Example 1

Paul, a self employed plumber, does not pay much attention to his record-keeping responsibilities and has no structured system for making sure that his records are accurate.

When Paul completes his income tax return he cannot be certain that his figures are correct and is unable to check them. This attitude towards record keeping indicates a lack of reasonable care.

Example 2

Chandra, a shopkeeper decides to replace his old van with a new vehicle. He buys an estate car so that he can use it for business trips to his local cash and carry, and also uses the vehicle for personal use in the evenings and weekends.

Chandra is not sure about what input tax he can claim for his vehicle, but he doesn't contact his accountant or HMRC for advice, and wrongly claims all the input tax he paid on the car. This indicates at least a lack of reasonable care.

Example 3

A&B Ltd, a large company with a substantial advertising budget, does not have procedures to identify the entertaining element of advertising costs. So any expenditure on advertising is included in full in the advertising account, with no way of cross-checking how much of the expense relates to disallowable entertaining.

This would at least indicate failure to take reasonable care and could be shown to be deliberate. A&B Ltd's basic systems and procedures are inadequate to give appropriate levels of assurance.

Example 4

During an Employer Compliance review the compliance officer advises Able Ltd that reimbursement of private phone bills should be dealt with through the payroll and that PAYE and NICs must be deducted accordingly.

When Able Ltd sends you its next end of year return you carry out a review and discover that the company has not followed the advice given by the compliance officer and the end of year return is wrong as a result.

This indicates that Able Ltd has at least failed to take reasonable care because it has ignored the advice given by HMRC.

Example 5

On several consecutive VAT return periods Whizz Ltd tells you after the end of the return period that the return was wrong and gives you the correct figures.

Whizz Ltd's systems are not adequate enough to produce correct figures for the return by the end of the return period and this repeated inaccuracy may be seen as at least a lack of reasonable care.

Disclosure

The law (para 9 of Sch 24 to FA 2007) defines a disclosure as comprising three aspects :

1. ***telling*** HMRC about it,
2. ***giving*** HMRC reasonable ***help*** in quantifying the inaccuracy, (also referred to as ***helping***) and
3. ***allowing*** HMRC access to records for the purpose of ensuring that the inaccuracy or under-assessment is fully corrected.

Weighing all of this information, the adviser can come to the following conclusion, which is supported in the HMRC guidance on this at CH81141.

they will need to evaluate the circumstances which caused the inaccurate return to be made. If they conclude that this was an error made despite taking reasonable care, then they should ensure that as much evidence of that exercise of care as possible is on file. There is no penalty for errors made despite taking reasonable care, unless the trader fails to take reasonable steps to notify HMRC of the error, so the issue of disclosure is not relevant. The client can safely correct the inaccuracy on the next return if it meets the new limits, and HMRC have confirmed that this will be "taking reasonable steps" to notify them of the error.

If they conclude that there has been a failure to take reasonable care which has given rise to the error, they will need to advise the client to make a separate disclosure, irrespective of the size of the error. This means that some small errors will be disclosed to HMRC in spite of the fact that the tolerance for separate disclosure has been increased.

Guidance on making a disclosure

So how does one make a disclosure? More help is available in the Manual, which explains that the three elements of disclosure command a different amount of discount. This aspect will be considered in more detail in another article. But the manual considers each element in turn and provides the following help.

CH82440 explains what is mean by "telling". Telling includes :

- admitting the document was inaccurate or that there was an under-assessment
- disclosing the inaccuracy in full
- explaining how and why the inaccuracy arose.

The quality of the disclosure and the rate of discount therefore available for telling depends on the disclosure being given in full, essentially at the outset, subject to the complexity of the case.

CH82450 gives more guidance on "helping". Helping includes :

- giving reasonable help in quantifying the inaccuracy or under-assessment
- positive assistance as opposed to passive acceptance or obstruction
- actively engaging in the work to accurately quantify the inaccuracies
- volunteering any information relevant to the disclosure.

However, the judgement of the quality of "helping" will depend on the circumstances and capabilities of the individual concerned.

Finally, CH82460 explains "giving access". Giving access includes a person responding positively to requests for information and documents and allowing access to:

- their business and other records
- other relevant documents.

Access is needed to ensure that the inaccuracy or under-assessment is fully put right and is more than simply complying with requests for information.

Prompted and unprompted disclosure

The law states that disclosure is ***unprompted*** if made at a time when the person has no reason to believe that HMRC has discovered or are about to discover the inaccuracy or under assessment, and otherwise is ***prompted***.

The guidance (CH 82421) provides the following to an officer to determine whether a disclosure is prompted or unprompted : Whether a disclosure is prompted or unprompted is an objective test. It is not what the person believed but what the particular facts and circumstances gave him reason to believe.

A national campaign highlighting an area of the trading community on which HMRC will be concentrating would not stop a disclosure from being unprompted. However a disclosure would be prompted if a person made the disclosure after :

- we had contacted them to tell them we wished to make a compliance check of their return, or
- we had arranged to visit their premises to undertake a compliance check of their records.

It will be exceptional for a disclosure to be unprompted if a compliance check is in progress. It will be unprompted only if the disclosure is about something the compliance officer has not discovered or is not about to discover.

During a compliance check (e.g. VAT assurance, employer compliance) if a disclosure is related to the subject matter being reviewed then it will be considered to be a related disclosure and therefore prompted.

Some companies will be in continuous dialogue to share a Risk Profile with HMRC.

A disclosure can be unprompted if it relates to an

- an area identified by the company, or
- an area that has not been raised by us as a specific concern by us.

A person is only able to disclose something they know is wrong. They may be genuinely unaware that they have done anything wrong. However if the person has been careless, for example by not taking advice when they should have, then on challenge the disclosure cannot be unprompted. An unprompted disclosure can be made for both inaccuracies and under-assessments.

Example 1

Jemima returned a capital gain which is the subject of a compliance check. There is no intention to expand the scope of the compliance check during the review. She discloses that she has not declared her car benefit. This is an unprompted disclosure.

Example 2

During a VAT assurance visit considering the credibility of Alphonse’s sales records, he discloses that his sales have also been understated for income tax. This would be related to the subject under review and so is a prompted disclosure.

Example 3

During an Employer Compliance review the employer makes a disclosure that the basis of the transfer pricing calculation for Corporation Tax is wrong. This is unrelated to the subject under review and so there is an unprompted disclosure.

Article by Rebecca Benneyworth

Lecture P546 (9.20 Minutes)
Lecture P547 (13.30 Minutes)
Lecture P548 (10.44 Minutes)

Seeking advice and rulings from HMRC

A recent VAT case has underlined the importance of applying to HMRC for rulings and clearances in writing, by stating limitations on the reliance of advice given to taxpayers verbally.

Background

In *Corkteck Limited v HMRC* [2009] EWHC 785 (Admin), the company applied for judicial review to quash an amended VAT assessment for £315,504 plus interest and surcharge.

Corkteck is a wholesale supplier of beverages in the UK and EU. The company’s director, Mr Malde, alleged that he was given an oral assurance (or ruling or advice) over the telephone by an agent of HMRC’s telephone National Advice Service (“NAS”) as to the proper invoicing arrangements for VAT purposes in respect of shipments of drinks to a trader in Poland called Konto Spolka (“Konto”).

One of the suppliers to Corkteck was a company called Sintra SA ("Sintra"), which was based in Belize (i.e. outside the EU) and which had a European office in Poland. It was not a trader registered for VAT purposes in the EU.

Sintra approached Corkteck about selling cans of Red Bull soft drinks to Sintra (invoicing Sintra for them), but delivering them to Sintra's own customer in Poland, Konto. Konto was a trader registered for VAT purposes in the EU.

The VAT issue
Where a UK supplier registered for VAT in the UK sells goods to a supplier based in another EU country which is VAT registered in that country, but agrees to deliver the goods to the EU supplier's own customer who is a supplier also based in an EU country and registered for VAT in that country, the sale from the UK company to the first EU company is zero rated for VAT purposes. A simplified procedure ('triangulation') is available in these circumstances, which avoids the need for the first EU company to register for VAT in the Member State to which the goods are delivered. If this procedure is used, the UK supplier's supply is zero rated.

However, if the UK supplier (e.g. Corktech) sells goods to a supplier which is a non-EU company (e.g. Sintra) and is not registered for VAT purposes in the EU and that company requests delivery of the goods to its own customer which is a VAT registered supplier based in another EU country (e.g. Konto), the supply from the UK supplier to the non-EU company is not zero rated, so the UK supplier must charge VAT on the supply.

Telephone call to the NAS

Mr Malde called the National Advice Service (NAS). He claimed the advice given was that Corkteck could treat the supply to the non-EU company (Sintra) as zero rated if he used on the delivery note the address and VAT number where the goods were delivered (i.e. Konto). However, the NAS officer's computer notes made during or immediately after the conversation indicated that he advised that Corkteck could zero rate the supply if the conditions in section 3 of VAT Notice 725 were met. One of these conditions is "You obtain and show on your VAT sales invoice your customer's VAT registration number …".

Corkteck's customer was Sintra, which was not registered for VAT. Thus Corkteck would not be able to satisfy this condition. VAT Notice 725 carries the force of law.

Mr Malde was aware of the terms of Notice 725, and did not consider that there was a triangulation situation (triangulation only occurs when each of companies A, B and C are EU traders). However, he did not tell the NAS officer that he perceived that there was a problem. Nor did he explain the scale of the business (and therefore the potential VAT due in respect of the transactions). Mr Malde broadly understood the NAS officer to give him advice as to how to satisfy one of the conditions, to the effect that there would be sufficient compliance if the VAT registration details for the delivery address in the EU (i.e. Konto's VAT registration details) were included in the VAT invoice to be issued by Corkteck for its supply to Sintra. However, Mr Malde did not retain any notes of the conversation. A VAT inspection subsequently took place. HMRC disagreed with Corkteck's VAT treatment of its supplies of Red Bull to Sintra, and assessed Corkteck for VAT of £315,504, plus interest and a surcharge.

The Court did not accept Mr Malde's account of the conversation with the NAS officer (Mr Baker).

The Judge (Sales J) said:

"I think that Mr Baker's note of the conversation with Mr Malde is properly to be interpreted as indicating that he specifically called Mr Malde's attention to the requirements of section 3 in Notice 725 in providing guidance for Mr Malde. Since the conversation took place several years ago, I regard that contemporaneous note as the best evidence of what was actually said in the conversation."

He added that there had been a degree of 'wishful thinking' by Mr Malde in the way he interpreted what had been said to him on the telephone.

'Sheldon statement'

The court then considered whether the VAT liability could be remitted by HMRC under a concessionary practice known as the 'Sheldon statement', following a claim by Corkteck. This concession was described in the following terms:

"If a [HMRC] officer, with the full facts before him, has given a clear and unequivocal ruling on VAT in writing, or knowing the full facts has misled a registered person to his detriment, any assessment of VAT due will be based on the correct ruling from the date the error was brought to the registered person's attention."

Corkteck claimed that it had been given a clear and unequivocal assurance by HMRC as to the proper VAT treatment applicable to the proposed transactions, which it had relied upon to its detriment. However, this claim was rejected. The court did not consider that there was full disclosure by Corkteck (as required according to the principle established in R v Inland Revenue Commissioners, ex p. MFK Underwriting Agencies Ltd [1990] 1 WLR 1545), as Mr Malde "…did not put all his cards face upwards on the table".

"General advice"

Perhaps more significantly, the Court held that even if Mr Malde's account of the conversation with the NAS officer had been accepted, it could not reasonably be relied upon. Sales J said:

"The NAS was only held out as a source of "general advice"…rather than as a source of binding rulings on the proper tax treatment of specific transactions. Moreover, Mr Malde's approach to the Defendant was not in writing, involved only a telephone conversation of about six or seven minutes duration (with no prior notice to Mr Baker even of the broad nature of problem on which his view was to be sought) and did not involve full disclosure of the transaction and the perceived problem which Mr Malde wished to have addressed."

The Judge concluded that Mr Malde "…could not reasonably have thought that what Mr Baker said (according to Mr Malde's witness statement), in a short telephone conversation, was capable of overriding the specific guidance as to the proper approach to VAT given in the Notice." Corkteck's appeal was dismissed.
Achieving certainty
There are various means of obtaining clearances and rulings from HMRC on transactions, including:
HMRC Code of Practice 10 ('Information and Advice');
Statutory Clearances (see http://www.hmrc.gov.uk/cap/statutory-clearances.pdf);
VAT Notice 700/6 ('VAT rulings');
An informal clearance service for businesses (http://www.hmrc.gov.uk/cap/links-dec07.htm); and
An Inheritance Tax clearance service for business owners (http://www.hmrc.gov.uk/cap/links-dec07.htm).
However, it is necessary to note the specific circumstances in which HMRC will (and will not) be bound by a particular ruling or clearance application). It is also important to follow the above guidance closely when drafting an application for clearance or a ruling. If an application is incomplete or incorrect, a clearance or ruling given by HMRC on the basis of that application cannot generally be relied upon.

Article by Mark McLaughlin

Lecture B548 (8.19 Minutes)

Revenue and Customs Brief 43

Practitioner psychologists are to be regulated by the Health Professionals Council with effect from 1 July 2009.

HMRC have published *Revenue and Customs Brief 43* explaining that, as a result, any supplies of medical care they make became exempt from VAT from that date.

Practitioner psychologists come under seven domains: clinical, counselling, educational, forensic, health, occupational, and sport/exercise.

Psychologists who work purely in academic research and experimental psychology and who do not offer services to the general public are excluded from regulation, meaning that there will be no change in the VAT treatment of their services.

HMRC say that 'medical care' means any service relating to the protection, maintenance or restoration of the health of the person concerned, including mental health.

It includes services such as counselling, working with children with emotional problems, dealing with criminals' behavioural problems or running stress management courses.

However, as is the case for all health professionals, the VAT exemption excludes services that are not primarily for the benefit of the patient, for example, assessing a patient's mental condition for legal reasons at the behest of a third party.

This is because the primary purpose of such services is to enable a court to take a decision on whether the patient is fit to stand trial rather than any immediate concern about the patient's mental health.

Business Tax

Golden hello to a partner

A 'golden hello' payment is made to a partner on his joining a partnership. Is this subject to tax and, if so, is it as an income or capital payment? It seems unlikely that goodwill is being introduced and it seems more likely that this may be a payment of a higher profit share for the first year as a partner.

I am familiar with the idea that a golden hello paid to a new employee is taxable as an inducement. What about a golden hello to a partner?

The individual concerned has left an employment in which he would have been entitled to share awards had he stayed, and because he has foregone those awards his new partners have made a lump sum payment to him on joining the partnership.

My immediate reaction is that this is probably taxable; but on the other hand a payment by him to join the partnership would be regarded as capital and would not be deductible from his profit shares for income tax purposes, so why should the other partners' payment to him be added to his profit share?

I cannot immediately find any precedent cases. I do not think that the payment is 'linked with the termination of his employment' in the sense required for the golden handshake rules to apply – it is linked with the loss of his option rights, which I believe has been held in past cases to be a different thing.

Does anyone have any strong views that this receipt should, or should not, be taxable as income?

Reply from The Snark

I think that the 'golden hello' is chargeable to income tax.

To deal with the ancillary issue first, it is common for an incoming partner to be asked to make a contribution to the capital on joining the partnership.

There is insufficient information in the question to know whether that is the case here.

However, it is not exclusively the case that such a payment actually purchases anything for the new partner. Indeed, in many modern partnership agreements, incoming partners expressly do not acquire anything in return for their subscription.

Rather, the payment has the character of a loan.

If we turn this around the other way, by making a payment to the incoming partner, what could the firm be purchasing?

Presumably there are no capital assets which the individual is introducing.

One might tentatively introduce the concept of goodwill. But what is goodwill?

In simplistic terms it is an intangible appendage to a business; it cannot exist in isolation. It is what might make an independent purchaser pay more for a business than its value as a mere collection of assets.

Without a business goodwill cannot exist. The new partner was an employee elsewhere, so he has no business to transfer to the new partnership. Therefore he cannot bring in goodwill.

There might be anticipation that the partnership can win new work from the incoming partner's contacts, but that cannot amount to goodwill.

I rather think that the payment made by the partnership has a character of income.

That is not to say that I think it is an allowable deduction in arriving at the profits. Rather, it is an appropriation of those profits.

It seems to me incontrovertible that the corollary is that it should be that it is income in the hands of the newcomer, in recognition and anticipation of services in the future.

That may not be the end of the story. Why is the payment being made?

The individual has left his employment voluntarily and forfeited his rights to some 'share awards'.

We do not know how those awards would have been taxed. Except in the case of certain schemes, such as the enterprise management incentive, share-related remuneration is usually charged to income tax.

It seems to me that the payment is compensating for what would have been income.

Does that give it the character of income? I rather suspect so.

The nearest parallel I can find in case law is *Shilton v Wilmshurst* [1991] STC 88, although that did concern a footballer moving from one employment to another.

The House of Lords had little difficulty in deciding that a third-party inducement payment to join the new employer was earnings under what is now ITEPA 2003, s 62. ITTOIA 2005, s 5 similarly charges income tax on the profits of a trade, profession or vocation.

I have little doubt that a court would find that this payment is part of those profits.

Reply from Hodgy

The exact tax outcome will depend on the particular agreement between the client of Terminator and the partners of the partnership which he has joined. I will consider what I feel are the two most likely possibilities.

The first option is that the payment is an extra fixed profit share for one year only.

As such, the extra amount paid to the client will be additional profit and subject to income tax and Class 4 National Insurance contributions.

As a profit share, this would not be deductible in the partnership tax computation, but this is not a problem.

The partnership taxable profit is a finite sum and so if an additional portion is allocated to Terminator's client, the profit shares for the other partners will be reduced by the same amount. It follows that their tax liabilities will also reduce.

The other possibility is that the client may be introducing additional profit earning potential into the partnership.

The fact that the existing partners are willing to make this payment, particularly in the current economic climate, leads to the conclusion that they must have high hopes as to the abilities of Terminator's client.

If this is the case, it could be possible to argue that the payment is a payment for goodwill.

On that basis, the amount received would be taxed as a capital gain.

We are not given any details to be able to make a definitive statement, but it seems likely that any such goodwill will have a cost figure of nil.

Depending on any other disposals made by the client, there may be an annual exemption to set against the sum received and any excess will be taxed at 18%.

If any goodwill held by the client is personal to him, he cannot transfer that goodwill to the partnership in the same way that you cannot place a value on personal goodwill when incorporating a business.

This would bring us back to the idea that the payment is an extra one-off profit share.

Terminator needs to review any documentation relating to the payment, but two possible treatments are that the payment is a one-off profit share or possibly a payment for goodwill.

Taxation 28 July 2009

UITF40: are we there yet?

In the beginning

The standard, although not primarily concerned with revenue recognition, requires short-term work in progress to be stated at the lower of either cost or net realisable value. This rule does not apply to long-term contracts where SSAP9 requires the value of work done to be recorded as sales, with work in progress treated as a debtor.

When published in November 2003, the implications of Application Note G from FRS 5 were widely debated because they were seen as modifying UK GAAP.

In March 2005 UITF 40 was published applying to accounting periods ending on or after 22 June 2005. Its aim was to clarify GAAP.

Contractual arrangements

UITF40 requires that where the substance of an engagement is that the seller's contractual obligations are performed gradually over time, revenue should be taken to the profit and loss account as contract activity progresses, to reflect the seller's partial performance.

Where the substance of a contract is that a right to consideration does not arise until the occurrence of a critical event, revenue is not recognised until that event occurs.

With regard to contingent fees generally, provided the future event is outside the control of the service provider, then the provider has no right to bill until the contingency is resolved. If there is no right to bill, the net book value of any work in progress is nil.

Fair value

UITF40 requires revenue to be recognised at fair value. In the case of part-completed work, this will require the application of judgment to areas of uncertainty including the overall amount of the fee, overruns, unforeseen problems, etc. If no reliable estimate can be made, no revenue should be recognised.

Judgment will therefore be required in arriving at an estimate of the accrued revenue to date. It might also be appropriate to apply discounts for extended settlement periods.

The adjustment

The difference between the SSAP9 method and the UITF40 calculation may give rise to an accounting adjustment. This is acheived by revisiting the figures on the first day of the straddling year of account.

For the year ended 31 March 2006, the adjustment will be evaluated by reference to the figures at the commencement of business on 1 April 2005. For entities complying with UK GAAP in their financial statements:

- The opening figures for the straddling period will be restated on the new basis. This is the 'tax adjustment' figure.
- Comparative figures will have to be computed for the year prior to the change.
- The financial statements will be prepared using the revised UITF40 basis, with the result that the accounts will disclose the opening restatement of capital and reserves, and movement in the year calculated under the new accounting basis.

Work in progress might be reduced or eliminated and replaced by 'accrued income'.

However, where contracts do not give a right to income, work in progress should be evaluated in the normal way. This generates its own uncertainties, to which we return below.

Spreading for tax

FA 2006, Sch 15 allowed firms to spread the UITF40 tax adjustment over a period of between three and six years, with the length of the period depending on the size of the adjustment in relation to the firm's normal taxable income each year.

Contingent contracts

Despite the publication of UITF40, the treatment of contingent contracts and the recognition of income where a contingent event occurred between the balance sheet date and the signing of the accounts generated continuing uncertainty.

Two distinct views began to emerge within the accounting profession.

1. UITF40 made it clear that, if completion of the contract was contingent on a specific event, the performance of which was outside the seller's control, no income or profits should be recognised until that event had occurred. As the key date for assessing contract performance was the accounting date, post-balance sheet events should be ignored.
2. If the contingent event occurred between the accounts date and the date of signing, it was possible that the asset could have a value and this should be reflected in accordance with FRS21.

ASB comments

In July 2008, the ASB published a statement clarifying the treatment of contingent fee arrangements which straddled the accounting year end. The statement confirmed that the resolution of a contingent event in the post-balance sheet period is a condition that arises after the balance sheet date.

As a result, the position taken at the balance sheet date should not be amended following the post-balance sheet resolution of the event.

The ASB did not provide guidance on the acceptability of two approaches to accounting for the cost of work performed under contingent fee contracts:

- expensing the cost as incurred; or
- recognising the costs as work in progress at the period end.

In a letter to the ICAEW dated 5 May 2009, the ASB agreed that either approach is permissible under UK GAAP. We understand that either approach is therefore acceptable to HMRC.

What happens now?

Conversations with fellow tax professionals suggest that, following the publication of the ASB letter, HMRC have instructed offices to conclude enquiries in line with the acceptable diversity of positions outlined in that letter.

The IASB has published a discussion document 'preliminary views on revenue recognition in contracts with customers' with the stated aim of developing a single model for revenue recognition across all industries.

It proposes that revenue from services should be recognised when the customer receives the service.

This means, for example, that revenue from performing an audit will not be recognised until the audit report is issued and fees for a conveyance will not be recognised until the transaction has completed.

Currently, in both cases, revenue would be recognised based on the activity performed at the reporting date, even if the customer will not receive the benefit of the service for some time.

The new rules might sound like a return to pre-UITF40 days, but the logic behind them is actually very different.

Depending on how IAS evolves, that suggests a possibility that the accounts and tax computations of professional firms may be subject to further upheaval.

From an article by George Bull and Peter Cass, Baker Tilly writing in Taxation, 1 July 2009

Lecture B546 (8.46 Minutes)

Corporation Tax

Loan of surplus funds to director investing money on behalf of company

A client close company has substantial cash balances earning interest now at a derisory rate. Individual savings seem to attract a higher interest rate than corporate deposits.

The managing director (MD) and controlling shareholder has suggested that an account be opened in his name as undisclosed agent for the company.

The intention would be that he declares himself bare trustee for the company and a suitable document evidencing this be drawn up, and signed and sealed on behalf of him and the company so that there is no doubt about the arrangement.

The company would then pay money under such an arrangement to the MD which he would immediately deposit in a separate account.

All the interest would accrue to the company and there would be no intermingling of personal and company funds; the balance in the account would belong wholly to the company. Interest credited would be included in the company accounts and corporation tax paid thereon.

The matter concerning me is whether, irrespective of the arrangements proposed, HMRC might successfully argue that the company had made the MD a loan such that TA 1988, s 419 applied and that the MD would be taxed under the beneficial interest provisions.

The contrary argument would be that the MD has received no loan: he is merely a bare trustee and undisclosed agent for the company.

The higher interest rate that the funds could earn for the company in the MD's name as undisclosed agent would be negated if the beneficial loan deemed interest provisions and s 419 were to apply.

What do readers think? Have I missed any other relevant points?

Query 17,437 – Country Bumpkin.

Reply from Exile

I have seen this suggestion more than once. Provided the interest is shown in the company's accounts and taxed accordingly, HMRC tend to accept the position, the position being that the individual has received the interest as bare trustee for the company.

However, the mere fact that HMRC are complicit in an illegal act does not make the act legal.

What is the aspect that is illegal?

The aspect is that the individual has breached the terms of the account. I do not know what account is being opened.

However, the opening of the account will involve certain assertions being made about the status of the account holder, etc.

Will MD declare himself as a bare trustee when opening the account?

I will not even wait for the answer. The reason that this declaration will not be made is because MD is opening the account using a fraudulent representation.

I do not know how the banks and building society accounts can justify different rates between the corporate and individual investor, but they are allowed to do this even though this approach does not seem equitable. Nevertheless, the perceived inequity does not allow the investor to use illegal means to rectify the position.

If HMRC had anything about them they should argue that the use of an account as described in the enquiry is illegal and, therefore, they should tax the income on the MD as a benefit in kind and also look at an overdrawn account to a participator.

They will not. They will look for the path of least resistance, not which one is correct.

Reply from Sparta

If the director acts as bare trustee or nominee for his company, it is almost inevitable that he will end up with an overdrawn account with the company.

It is well established that where a director receives company funds into a private bank account, the transaction represents a loan from the company such that tax is payable under TA 1988, s 419.

Although the s 419 tax will be repaid when the funds are returned to the company, there nevertheless remains the considerable cash flow downside which will outweigh any advantage of a higher interest rate.

A benefit in kind under ITEPA 2003, s 175 will also arise on the director if the sum exceeds £5,000 at any time over the course of the tax year which it invariably will if a substantial sum is involved.

The best possible chance of rebutting these tax implications is to render the nature of the transaction beyond doubt from the outset.

A formal trust deed between the company and the MD should be drawn up to give the company a legal right to the funds in the account and enable it to include the asset on its balance sheet.

Board minutes should refer to the creation and use of the bank account, the intentions underlying it as well as the amount, date and terms on which the funds are released to the MD.

The account should be maintained as a business account with private transactions strictly precluded both in principle and in practice. It would be useful if there were evidence that the company is free to draw on the funds when required, subject to the terms of the account, and that the funds are ultimately applied for company purposes.

The history of any previous or existing loan accounts with the director or an absence of them may be seen as relevant by HMRC.

The real difficulty with the proposal is that this robust defence sits uncomfortably with the savings protocol the relevant institution will probably adopt.

As Country Bumpkin is aware, account providers often take a different view when accepting savings from individuals and companies and are likely to be particularly vigilant in the current economic circumstances.

The terms and conditions of the account may require or at least imply that the identity of the beneficial owner should be disclosed where not identical to that of the legal owner.

If the beneficial owner is deliberately concealed from the institution then the application will have been completed dishonestly and perhaps fraudulently. Country Bumpkin must also consider the money laundering implications for all parties concerned.

For instance, the Money Laundering Regulations SI 2007 No 2157 require that the institution establishes the company's identity (Regs 5(b) and 6) and this requirement is reflected in industry guidance such as that of the Joint Money Laundering Steering Group.

The prudent advice is to properly disclose the arrangement to the institution and live with their decision as to whether they then wish to proceed with opening the account in the name of the MD. If they proceed, the disclosure will substantiate the desired tax treatment.

If they do not proceed, the MD may wish to reflect on the possibility that placing funds under false pretences could easily encourage HMRC to maintain that the bare trust is void or at least voidable and thus invite the very tax treatment he seeks to avoid.

At the time of writing, it is possible to obtain rates of interest in excess of 3% on substantial business deposits and the MD should devote serious consideration to whether this presumed improvement on current arrangements represents an acceptable fall back position for the company funds should the relevant institution decline to proceed on the above basis.

Taxation 28 July 2009

Cash extraction for owner-managed companies under the super tax regime

The amount available to be paid out as 'proprietorial reward' is determined by:

- Personal spending and saving requirements, and their personal tax position
- Amount required for future retention to satisfy future working capital or capital investment purposes
- Level of the company's distributable reserves and 'free' cash flow
- Provisions or restrictions laid down in shareholder agreements or the company's articles
- Desire to 'de-risk' part of any surplus cash generated by the business by taking it out of the company
- Possible IR35 considerations in fixing the level of 'remuneration' to be paid out

But how should this be paid out?

Salary and bonus

Typically, the owner-manager should pay a salary to use up their personal allowance since no 10% tax credit is available to the extent to which dividends are covered by personal allowances.

From the individual's view point, bonuses are currently taxed at either 20% or 40% with employees' NIC due on top at 11% (falling to 1% for earnings exceeding £43,875).

For the company, in addition to paying the salary and bonus, 12.8% employers NIC is due, all of which is fully deductible for corporation tax purposes for the period in which it is charged in the accounts (provided it is actually paid within nine months following the end of the accounting period, CTA 2009, s 1288).

Dividends

For many years, higher rate taxpayers have been subject to a special tax rate of 32.5% on their dividend income which after taking account of the 10% tax credit, gives an effective tax rate of 25%.

If a company pays tax at the small companies' rate, it is particularly beneficial to extract 'surplus' profits by means of a dividend where national insurance is not an issue and the higher rate of income tax do not apply.

As a general rule, dividends will often be preferred to bonuses particularly when the timing of the tax payments are taken into account.

Looking beyond 5 April 2010

The 2009 budget imposes a new super tax rate of 50% from 6 April 2010 where an individual's taxable income exceeds £150,000.

For those owner-managers who earn substantial salaries/bonuses, this tax hike will mean that the combined marginal tax/NIC costs for employment income (above £150,000) would be 51% for the individual and 12.8% for the employing company – all quite painful.

From 6 April 2010, dividends also become subject to their own super tax rate of 42.5%. This corresponds to an effective rate of 36.11% of the cash dividend received, which will apply to dividend income falling within the '£150,000 plus' taxable income.

Where substantial dividends are being paid (falling within the £150,000 plus income band), this represents an increase of nearly 45% on the pre-6 April 2010 effective dividend tax rate of 25%.

Dividend income below the £150,000 super tax threshold will remain subject to the effective rate of 25%.

Going forward, owner-managers should therefore exercise more care with the timing of their dividend payments to lessen the impact of the new top effective rate of 36.11%.

Pre-6 April 2010 dividend planning

Many owner-managers are likely to accelerate the payment of planned future dividend payments before the super dividend tax rate 'kicks-in' on 6 April 2010.

Some may feel that their company's cash-flow may not be able to support large dividend payments, but this should not be the case. The owner-manager can pay the dividend (before April 2010) – remembering that the 'tax point' for interim dividends is the date they are paid (see *Potel v IRC* [1970] 46 TC 658). All or most of the dividend monies can then be lent back to the company by crediting the shareholder's loan account. The 25% effective income tax liability on the dividend would need to be found by 31 January 2011.

HMRC's *Company Tax Manual* (at CT20095) treats interim dividends as being paid when an 'unreserved right' to draw a dividend exists, such as when they are credited to the owner-manager's account in the company's books.

HMRC go on to say that if 'as may happen with a small company, such entries are not made until the annual audit, and this takes place after the end of the accounting period in which the directors resolved that an interim dividend be paid, then the 'due and payable' date is in the later rather than the earlier accounting period'.

This can be a murky area and therefore it will be important to ensure that everything is done to ensure that the required dividend is legally valid and paid before 6 April 2010.

I generally prefer an exchange of cheques (for the dividend and the loan-back) to 'stamp' the timing of the dividend payment beyond doubt.

Income splitting still rocks

Following HMRC's defeat in *Jones v Garnett* 2007 STC 1536 (often referred to as the *Arctic Systems* case), a large number of owner-managed companies continue to take advantage of providing tax efficient dividend payments to the owner-manager's spouse.

HMRC's attempts to introduce anti-avoidance legislation were quickly derailed in the face of a massive 'thumbs-down' by the professional bodies and industry groups. The draft legislation was shown to be completely unworkable and it was difficult to see how it would be policed by HMRC and how they would collect the anticipated tax revenues.

Mr Darling seems to have shifted 'income splitting' onto the back-burner – at least for the time being – following statements issued in both the pre-Budget report 2008 and the Budget 2009. Income splitting (provided it is implemented correctly) is therefore very much alive and kicking.

Hitherto, the splitting of dividends between married couples has largely been designed to make full use of the spouse's 10% basic rate band for dividends. After 6 April 2010, it may be given a further twist as owner-managers seek to mitigate the effect of the 36.11% effective rate for dividends.

Loans to shareholders

Under the post-6 April 2010 regime, some might consider making use of loans rather than dividends. Based on current understanding, there are no plans to increase the rate of the TA 1988, s 419 tax – which is 25% of the amount of the loan/overdrawn current account.

Even when the income tax (and NIC) under the beneficial loan rules (ITEPA 2003, s 175) is added on, loans to owner-managers may still prove to be a more attractive option than an outright dividend payment suffering the relevant super tax rate of 36.11%.

It is important to ensure that the loan is properly documented. Although it may seem tempting to draw regular loans/advances, these payments may look like 'PAYE-able' earnings to a vigilant tax inspector.

From an article by Peter Rayney FCA CTA (Fellow) TEP, BDO Stoy Hayward's

Lecture B547 (20.12 Minutes)

Dawsongroup Ltd v Revenue and Customs Comrs

The appellant company, a private company, was the parent company of a group of companies in the UK and Ireland, and to a lesser extent in Europe. In 1988 the company became a public company and 25 per cent of its shares were floated on the London Stock Exchange. In the build up to that flotation the appellant devolved its trading activities to its subsidiaries. Under the group structure the subsidiaries and, in some cases, their own subsidiaries, variously owned the properties from which the group carried on its business, and undertook the core activities of leasing vehicles and equipment. In addition to holding the shares in the subsidiaries, the appellant provided various facilities for them—"head office" functions such as financial, banking and treasury, information technology; legal and company secretarial services—and it charged the subsidiaries, on an arm's length basis, for its services. Unfortunately the floatation was not a success and in 2000 the company decided that the shares should be delisted, and in respect of which expenditure of £433,574 was incurred. The appellant sought to deduct that expenditure in computing its profits for the purposes of corporation tax on the basis that, as it was an "investment company" within the meaning of TA 1988 s 130, the expenditure was deductible as an expense of management. HMRC disallowed the deduction on the basis that the company was a trading company. The appellant appealed. At the hearing the parties agreed that the company was a trading company but the appellant contended: (i) it was, nevertheless and in addition, an investment company since its principal activity was the holding of assets—ie the shares of its subsidiaries; (ii) it had held shares in its subsidiaries since at least 1988 and therefore some 12 years or so before the relevant expenditure was incurred and in that period new subsidiaries had come into the group, some by acquisition, others being created for the purpose of carrying on new trading activities or existing activities in other countries. It was undoubtedly "in business" and any of its activities beyond the provision to its subsidiaries of the various head office services had to, by process of elimination, be investment activities; and (iii) once it was established that a company was in business, the nature of that business had to be identified, if necessary by the process of elimination and a company did not have to be a very active investor in order to be considered an investment company. HMRC submitted that: (i) although it was possible for a company to be both engaged in trade and an investment company, the appellant's principal activity, determinative of its status, was the control of and provision of services to its subsidiaries, which was to be regarded as a trading activity rather than a function of investment; and (ii) the reality was that the appellant's business was the provision to its subsidiaries of head office functions and strategic management. The holding of the subsidiaries' shares was no more than an adjunct to the appellant's principal activity of controlling a trading group.

The tribunal judge considered that in determining the business of a company for the purposes of TA 1988 s 130, the critical question was whether the holding of assets to produce a profitable return was merely incidental to the carrying on of some other business, or was the very business carried on by the taxpayer. What had to be looked at was the nature of the operations or functions of the company. The search was not for a company making investments but for a company whose main business was the making of investments. Whilst it was possible to be simultaneously a trading company and an investment company, on the facts the appellant was a trading company which carried out its business by means of the subsidiaries which it controlled, that it held the shares in its subsidiaries as a necessary incidental to its chosen means of carrying on that activity, and that the holding of the shares was not an end in itself, a business activity in its own right. An investment company was one which dealt in, or merely held assets, such as shares, land or bonds, in order to profit, by dividends, rents or interest, from its investments but not, as in the instant case, as the means by which it was able to control the assets. Standing back from the matter, the appellant was in reality engaged in trade. Therefore it was not an investment company within the meaning of TA 1988 s 130. Accordingly the appeal would be dismissed.

Appeal dismissed.

Tribunal: Judge Colin Bishopp, 9 June 2009

Claims at inception of swap agreements

The taxpayer company, Prudential, made two foreign exchange hedging transactions, one with the Royal Bank of Scotland and the other with Goldman Sachs. Prudential claimed amounts paid at the inception of the swap agreements in its corporation tax self assessment return.

HMRC denied the claim saying that the payments were not qualifying payments within FA 1994, s 153.

They were no more than prepayments of part of the final exchange of principal under the hedging agreements.
The Special Commissioners and High Court agreed with HMRC, so the taxpayer appealed.

The main issue before the Court of Appeal was whether the two front-end payments were made in consideration of RBS and Goldman Sachs entering into their currency contracts.

The Court of Appeal said that the prepayments did not come within FA 1994, s 151(1)(b).

Section 151(1)(b) drew a distinction between payments made to secure a contract and the principal payments exchanged on maturity.

Payments which were part of the final principal did not change nature just because it was agreed that they should be made in advance.

Nor did such payments acquire the quality, i.e. inducement, which payments within s 151(1)(b) would have to display.

Payments within that section were ones which the counter-party required as a consideration for agreeing to enter into a foreign exchange transaction. They were distinct from the sums paid to buy or sell the currency.

The taxpayer's appeal was dismissed.

Prudential plc v CRC, Court of Appeal, 25 June 2009

Paycheck Services 3 Ltd and other cos.; R&C Comrs v Holland and another

The respondents were directors of PS Ltd, which they operated as their trading company. They each held 50% of the issued share capital. PS Ltd itself held 100% of the issued share capital of P (DS) Ltd (PD) and P (SS) Ltd (PS). All those companies were together known as the "composite companies". PD and PS were incorporated to act as sole corporate director and company secretary respectively of each of the composite companies, and the respondents were each appointed as directors of PD and PS. The issued share capital in the composite companies comprised one voting "A" share, and approximately 50 non-voting shares, each of a separate class. The A share was held by PST Ltd (PST), a company of which the respondents were each directors and in which they each held 50% of the issued share capital. There was only an advantage in being a non-voting shareholder/employee of the composite companies so long as the relevant composite company paid lower rate corporation tax for which there was threshold under s 13 of the Income and Corporation Taxes Act 1988, limited to profits of £300,000 pa in respect of an "associated company". Section 13(4) of the 1988 Act provided that for the purposes of that section, a company was to be treated as an "associated company" of another at a given time if at that time one of the two had control of the other or both were under the control of the same person or persons. Section 416 of the 1988 Act provided that a person would be taken to have control of a company if he possessed the greater part of that company's voting power. Section 417(3) of the 1988 Act provided that "associate" meant, inter alia, the trustee or trustees of any settlement in relation to which the participator was a settlor. It was accepted that as a matter of the strict application of ss 13 and 416 of the 1988 Act, that the composite companies were associated through the fact that PST controlled each of them, and because the collective turnover exceeded the £300,000 threshold, they were each liable for corporation tax. However, the respondents relied on Extra Statutory Concession C9 (ESC C9) for maintaining that the composite companies should not be treated as "associated". ESC C9 provided that the Revenue should not treat one company as being associated with another because they were controlled by the same trustee by virtue of the rights and/or powers held in trust by that trustee, provided that there was no past or present connection between the companies other than those rights and/or

powers. In April 2001, the Revenue wrote to the respondents, expressing the view that the composite companies might not be entitled to rely on ESC C9. The respondents acted on professional advice, but none of those advisors suggested that the composite companies should stop paying dividends. On 9 August 2004, the respondents received advice from counsel to the effect that the composite companies were liable to pay corporation tax on the basis that ESC C9 did not apply to them. On 18 August 2004, the respondents had a consultation with leading counsel, who confirmed the advice received on 9 August 2004. The Revenue took the view that by continuing to pay dividends after April 2001, each composite company had been left with insufficient reserves with which to meet any further liability for the higher rate of corporation tax that the Revenue had determined had to be paid. It was the Revenue's case that even after receiving counsels' advice in August 2004, the respondents had caused the composite companies to continue to trade and pay dividends while knowing that such companies were thereby rendered insolvent with no reasonable prospect of avoiding insolvent liquidation, with the effect that the respondents had failed to act in the best interests of the composite companies and were in breach of their duties to those companies. The Revenue commenced proceedings under s 212 of the Insolvency Act 1986 against the respondents, seeking to make the respondents liable for payment of the corporation tax in question. The judge held that the first respondent was a de facto director of each company and so was answerable to the Revenue's claim. The first respondent appealed.

He submitted, inter alia, that the only director of the composite companies was PD. Whilst he conceded he had been, along with the second respondent, a director of PD and they were the human agents behind all that PD had done in its capacity as a director of each of the composite companies, those facts had not entitled the judge to find that he was also a de facto director of those companies.

On the established authority, the crucial issue in relation to whether a director of a corporate director could or would act so act as to cause himself to be regarded as a de facto director of the subject company was whether the individual in question had assumed the status and function of a company director so as to make himself responsible under the Company Director Disqualification Act 1986 as if he were a de jure director (see [64] of the judgment).

It mattered not what the individual was called but what he had done (see [65] of the judgment).

In the instant case, the judge had erred in finding that the first respondent was a de facto director of the composite companies. On the facts, there was nothing that required the first respondent to be regarded as a de facto director of the composite companies (see [63], [74], [76] of the judgment).

Kaytech International plc, Re, Secretary of State for Trade and Industry v Kaczer [1999] 2 BCLC 351 applied; *Hydrodam (Corby) Ltd, Re* [1994] BCC 161 considered; *Secretary of State for Trade and Industry v Hall* [2006] All ER (D) 432 (Jul) considered.

Per curiam—nothing said in the instant case is intended to suggest that there can never be circumstances in which a director of a corporate director can or will act so act as to cause himself to be regarded as a de facto director of the subject company. But something more will be required than the mere performance by him of his duties as a de jure director of the corporate director (see [74] of the judgment).

Decision of Mark Cawson QC [2008] All ER (D) 319 (Jun)—reversed.

The appeal would be allowed.

Court of Appeal, Civil Division Ward, Rimer and Elias LJJ 2 July 2009

Value Added Tax

Deposits relating to sales of land on which dwellings are to be constructed

This Brief clarifies HMRC's view on how deposits paid in relation to sales of land, and in particular sales by developers to registered social landlords, should be treated.

This Revenue & Customs Brief clarifies HM Revenue and Customs' (HMRC) view on how deposits paid in relation to sales of land, and in particular sales by developers to registered social landlords (RSLs), should be treated.

Background

Where development land is sold to RSLs, it is normal for a deposit to be paid at the time of exchange of contracts when construction has not commenced and the land is bare land. In many cases this deposit will be held by a stakeholder and will not create a tax point for VAT purposes until it is released to the vendor (or vendor's agent), normally at the time of completion. Completion of the sale will in most cases occur at a time when construction of the dwellings has commenced and progressed beyond what is commonly known as the "golden brick", that is, beyond foundation level. This means the supply can normally be zero-rated.

It has, however, become increasingly common for the deposit to be made available to the vendor at the time of exchange when the land is still bare land. This has raised questions about the VAT treatment of the deposit, and in particular, whether it can be treated as part payment for the future zero-rated supply.

HMRC's interpretation of the correct VAT treatment

HMRC takes the view that where the deposit is released to the vendor and it is clear from the contract or agreement that what will be supplied at completion, or the time of the grant, will be partly completed dwellings (beyond "golden brick"), the deposit is part payment for the grant/supply that will occur at that time. It follows that the VAT liability of the deposit is determined by the anticipated nature of the supply and that zero-rating will be appropriate if it is intended that the conditions for zero-rating will be satisfied at the time of completion. For example, there must be a clear intention that the vendor will have commenced construction of the dwellings at that time and acquired "person constructing" status.

It is possible that the state of the land at completion will differ from that which was anticipated and where this is the case it will be necessary to revisit the VAT treatment of the deposit. It is not possible to give more detailed guidance as the position will depend upon the facts and contractual terms applicable in the particular case. Where taxpayers are uncertain about the correct treatment they should refer to the National Advice Service by phoning 0845 010 9000.

HMRC Brief 36/2009 8 July 2009

Rank (mechanised cash bingo and gaming machines)

The High Court issued its decision in this case on 8 June 2009—the judgment being in Rank's favour [see *Revenue and Customs Comrs v The Rank Group* [2009] All ER (D) 65 (Jun)]. It confirmed that there had been a breach of fiscal neutrality in the tax treatment of the supply of mechanised cash bingo (MCB). This means that participation fees for playing MCB should have been exempt from VAT and businesses can now submit claims to HM Revenue & Customs (HMRC) for repayment of any output tax wrongly accounted for, subject to the guidelines below.

In relation to gaming machines, the High Court judgment relates to an appeal against an interim ruling of the VAT Tribunal. As the Tribunal has not yet ruled in respect of Rank's full appeal, HMRC will not at this time consider any claims relating to this issue.

Background

Rank, which operates Mecca bingo halls, claimed there had been inconsistencies in the way VAT had been applied to the participation fees customers paid to play MCB and to the takings of gaming machines.

Last year the VAT Tribunal ruled there had been a breach of fiscal neutrality in the case of MCB as some participation fees were taxed while others were exempt. (Fiscal neutrality means that similar supplies must be treated the same for tax purposes to avoid any distortion of competition). The High Court has agreed with the Tribunal's decision that all participation fees for MCB should have been exempt from VAT.

The VAT Tribunal also issued an interim decision regarding the way HMRC taxed gaming machines, stating there had been a breach of fiscal neutrality in some cases and over a short period of time before the law was changed in December 2005.

Implications of this judgment

HMRC will now consider claims for output tax wrongly accounted for by bingo operators on MCB participation fees.

As bingo duty is charged on the VAT-exclusive value of participation fees, this judgment will have an effect on bingo duty declarations although HMRC is still considering the precise implications. However, HMRC will now enforce those bingo duty assessments already made. Further assessments to bingo duty may be made as appropriate.

As the gaming machine case is continuing, with a VAT Tribunal hearing later this year, HMRC will not credit any claims on this issue.

Making claims or adjustments

Where a business wishes to make a claim to HMRC for output tax wrongly accounted for in respect of MCB participation fees, they may do so, although evidence must be produced that output tax was accounted for, to substantiate the amount claimed.

All claims will be subject to the four-year time limit in section 80(4) of the VAT Act 1994 (as amended) and no claim for periods ending on or prior to 31 March 2006 will be considered.

Correcting the error on your VAT return

Overdeclarations of output tax can also be corrected by adjusting the current VAT return if the net amount of all errors in the accounting periods being corrected is:

– £10,000 or less; or

– less than £50,000 and less than 1% of the box 6 figure on the VAT return in which the adjustment is being effected

These de minimis levels apply to the entire “claim”. Thus if your “claim” is for ten accounting periods, it is the net overdeclaration for all ten periods that must be within these levels.

Under regulation 34(1A) of the VAT Regulations 1995 (as amended), all adjustments must be made within four years after the end of the accounting period in which the overdeclaration was made but no accounting period can be adjusted if it ended on or before 31 March 2006.

Further information

Details of where to send your claim can be obtained from update 2 to VAT Notice 700/45 - How to correct VAT errors and make adjustments or claims from the HM Revenue & Customs National Advice Service on 0845 010 9000.

HMRC may reject all or part of a claim if repayment would unjustly enrich the claimant. More details on “unjust enrichment” can be found at part 14 of VAT Notice 700/45 How to correct VAT errors and make adjustments or claims.

There may be direct tax implications where amounts of overdeclared output tax are repaid to businesses and your attention is drawn to R&C Brief 14/2009 issued previously.

HMRC Brief 40/2009 14 July 2009

Zero-rating new buildings used for a relevant charitable or residential use - change

This HMRC Brief announces a change in the HMRC interpretation of the of the legal provisions that apply the zero rate to new buildings used for a relevant charitable purpose, and the withdrawal of Extra Statutory Concession (ESC) 3.29 and two related concessions.

This Brief announces a change in HM Revenue & Customs (HMRC) interpretation of the of the legal provisions that apply the zero rate to new buildings used for a relevant charitable purpose, and the withdrawal of Extra Statutory Concession (ESC) 3.29 and two related concessions. VAT Information Sheet 08/09 provides further detail.

Background

A building intended to be used solely for a relevant charitable purpose (non-business use) can be zero-rated if the charity provides their developer with an appropriate certificate before the first supply is made.

If, however, the building is put to a business use within ten years of the building's completion, VAT must be paid to HMRC (a change in use charge) to reflect that the building has ceased to be eligible to benefit from the zero-rate.

Under Extra Statutory Concession 3.29, HMRC has permitted zero-rating where a building was used 90% or more for a relevant charitable use. No change of use charge arises in a case where a building ceases to be eligible if it was zero rated only as a result of the application of this concession.

The two related concessions, the “switching areas” concession (where the overall use of the building was unchanged) and the “look through” concession, (where the occupiers' use of the building was for a relevant charitable purpose) enabled some business use of a building to be disregarded.

Outcome of review

Having fully considered the application of the provision and considered appropriate decisions of the higher courts, HMRC now recognise that the term “solely”, as used in the phrase “solely for a relevant residential or relevant charitable purpose”, can incorporate an appropriate de minimis margin. And in order to avoid unnecessary disputes in marginal cases, HMRC will accept that this statutory condition is satisfied if the relevant use of the building by the charity is 95% or more.

In the light of this change of view, the ESC is no longer considered to be necessary or appropriate. It will therefore be withdrawn, subject to a 12 month transitional period, as described below.

Way Forward

A person can now rely on this revised interpretation of “solely” that is, 95% or more, to determine whether a building will be eligible for the zero rate or not.

For this purpose, use for a relevant charitable purpose does not have to be calculated using one of the three methods described in ESC 3.29. Any method may be used to calculate the qualifying use of the building, so long as it is fair and reasonable. Prior approval from HMRC for any method of calculation is not required.

If a building is zero rated as a result of applying this new interpretation, there will be a change of use charge if it ceases to be eligible within ten years of the buildings completion.

ESC 3.29 and the two connected concessions will now be withdrawn, subject to a 12 month transitional period starting on 1 July 2009. During this transitional period, charities will be able to continue to apply ESC 3.29, or choose to apply the revised interpretation of the statutory provision described above.

Further details are in VAT Information Sheet 08/09.

The meaning of the term "solely" will depend on the legal context in which it occurs and on the nature of the underlying transactions to which any particular piece of legislation is directed. The revised interpretation described above applies only to the construction of the phrase "solely for a relevant residential or relevant charitable purpose" as used in the context of Groups 5 and 6 of Schedule 8, Group 1 of Schedule 9 and Part 2 of Schedule 10 to the VAT Act 1994.

Further information

If you have any enquiries about this brief, please contact the National Advice Service on Tel. 0845 010 9000 or, if a charity, the Charity Helpline on 0845 302 0203.

Revenue & Customs Brief 39/2009 VAT

Three-year cap for VAT claims - decision in Scottish Equitable

The Court of Session has held that the VAT and Duties Tribunal was wrong to decide, in its 2006 decision in the Scottish Equitable case, that the absence of a transitional period for VAT claims meant the three-year time limit provisions were void. The court instead followed other authorities in holding that claims for accounting periods ending after the enactment of the new time limit in 1996 were properly capped.

Three-year cap for VAT claims – *CRC v Scottish Equitable Plc (unreported)* – Order of the Inner House of the Court of Session

The judgment of the Inner House

In an Order handed down on 2 July, the court overturned the 2006 decision of the VAT and Duties Tribunal that the introduction of the three-year time limit without a transitional period in 1996 meant that it had never been lawfully enacted.

The Inner House held that the Tribunal was wrong to decide that the absence of transitional provisions, that enabled claims to be made under the old time limits before the new time limit took effect, meant that the provisions were void. The court stressed that it was well recognised that national legislation which breaches Community law is not void and noted that the Tribunal had failed to recognise the difference between rights to claim that accrued before the enactment of the three-year cap and those that accrued afterwards.

The Inner House followed the judgment of the House of Lords in CRC -v- Fleming (t/a Bodycraft) [2008] STC 324 in which the Law Lords held that the three-year time limit should be disapplied in relation to rights to claims that had accrued before its enactment and that that disapplication should continue until the expiry of an adequate, prospective transitional period.

There will be no application for leave to appeal to the House of Lords.

Current case law on time limits

There are a number of judgments of the European Court of Justice (including *Marks & Spencer Plc -v- CCE* [2002] STC 1036) confirming that the imposition of reasonable time limits does not breach principles of Community law and that they are necessary to provide legal certainty for both the citizen and the state.

The judgment of the House of Lords in Fleming (referred to above) led to the enactment of section 121, Finance Act 2008. This provided businesses with a prospective transitional period of twelve months, ending on 31 March 2009, in which claims could be made for accounting periods ending before the introduction of the new time limits.

The Inner House in Scottish Equitable has taken the same view as the High Court in *Local Authorities Mutual Investment Trust -v- CCE* [2004] STC 246, which held that VAT claims for accounting periods ending after the enactment of the new time limit were properly capped.

Status of VAT time limits

All VAT claims are now capped at four years, or back to 1 April 2006, whichever is the shorter – see section 80(4) of the VAT Act 1994 as amended by Articles 2 and 6 of the Finance Act 2008, Schedule 39 (Appointed Day, Savings and Transitional Provisions) Order 2009, SI 2009/403

(output tax claims) and regulation 29(1A) of the VAT Regulations 1995 as amended by regulation 3 of the VAT (Amendment) Regulations 2009, SI 2009/586.

Appeals on-hold behind this litigation

A significant number of appeals to the First Tier Tribunal (Tax Chamber) are on-hold, pending the outcome of this litigation. Appellants will need to consider, in the light of the recent order, whether they wish to withdraw their appeal or proceed to a full hearing. HM Revenue & Customs are now taking steps to have these appeals restored to the Tribunal list so that, where necessary, a hearing date can be fixed.

Issued 17 July 2009

VAT package 1- Place and Time of Supply of International Services

This article reviews part of the "VAT package" measures which will be implemented on 1 January 2010. This is an EU development that will be implemented in all the member states. It has been a long time coming, and is the culmination of many years of discussion. The main elements of the VAT package are:

- changes to the place and time of supply of services (this lecture);
- changes to reporting of international goods and services on European Sales Lists;
- changes to the system for claiming refunds of VAT incurred in other member states under the 8th Directive.

The second and third points will be covered in the next article.

The notes that follow:

- give an overview of what is changing;
- reproduce the latest HMRC guidance on this part of the VAT package;
- reproduce the HMRC summary of consultation responses, which highlight some of the problems that people anticipate arising from the new rules.

Articles

There is a two-part article about the VAT package in Tax Adviser, April and May 2009, as well as numerous articles in other publications.

Summary of changes

The April Budget included more details of the VAT package changes, covering place of supply, time of supply and the filing of ESLs. The proposals have been covered in past updates, but here is a summary of the Budget announcement.

Place of supply

From 1 January 2010, the "basic rule" for international business-to-business supplies changes from "where the supplier belongs" to "where the customer belongs", and the reverse charge will be extended accordingly to more supplies. Supplies to non-business customers will still be taxed where the supplier belongs.

From 1 January 2010, valuation and work on goods will move to "where the customer belongs" if the customer is in business; most B2B cultural, artistic, sporting etc. services will also move to the reverse charge from 1 January 2011, although admission charges will still be taxed where the event takes place.

Land-related services remain where the land is. There is currently some doubt about where the services of booking hotel rooms should be: some member states are suggesting that it should move to where the land is, which would be inconvenient for travel agents established in other states. This is subject to discussion with the Commission.

From 1 January 2010, short-term hire of means of transport (30 days for most means, 90 days for vessels) moves to where the transport is put at the customer's disposal. Long-term hire will fall

under the new general rule (where the customer belongs for B2B, where the supplier belongs for B2C). From 1 January 2013, long-term hire to non-business customers will also move to where the customer is established.

From 1 January 2010, restaurant and catering services will be charged where they are physically performed. Where this is on an intra-EU journey, the place of supply will be the place of departure.

From 1 January 2010, supplies of intermediaries, transport of goods and ancillary transport services will move to the general rule. Transport and ancillary services for non-business customers will remain under the old rules (where physically performed, or point of departure for intra-EU transport of goods).

The place of supply of “schedule 5 services”, passenger transport, supplies subject to the “use and enjoyment provisions” and electronically supplied services for non-business customers will remain unchanged.

BN74

The change to the time of supply rule for reverse charges will take effect on 1 January 2010. Instead of the tax point being triggered only by payment, it will be the earlier of the completion of the service and the date on which it is paid for. Continuous supplies will be supplied at the end of each billing or payment period, or the date of payment if earlier. For continuous supplies that are not subject to billing or payment periods, the supply will be the end of the calendar year or the date of payment if earlier.

BN75

In May 2009 HMRC published detailed guidance on the new rules. The following section reproduces the main part of that guidance from the HMRC website.

www.hmrc.gov.uk/vat/cross-border-changes-2010.htm

Part 2

Place of Supply of Services and Time of Supply Changes

Overview

2.1 Place of supply

From 1 January 2010, the new basic rule (the ‘general rule’) for the place of supply of services will tax B2B supplies of services at the place where the customer is established and no longer at the place where the supplier is established, as is currently the case.

For B2C supplies of services, the general rule for the place of supply will continue to be the place where the supplier is established. However, from 1 January 2015, the place of supply of intra-EU B2C supplies of telecoms, electronically supplied services and broadcasting will be where the customer is established or usually resides. The Commission will report on the feasibility of the new B2C rules before entry into force.

As now, there will be exceptions to the general rule for certain services, with a view to achieving taxation in the place of consumption. In the main these will be implemented on 1 January 2010, with further changes to the ‘where performed’ rule from 1 January 2011 and for long-term hire of means of transport from 1 January 2013.

In the majority of cases, business customers will account for VAT using the reverse charge procedure (and recover tax subject to the normal rules) as is currently the case.

More detail on the changes, which takes account of frequently asked questions during consultation, is at section 3.

2.2 Time of supply

From 1 January 2010 the time of supply (or tax point) for reverse charge services will be based on when a service is performed. For single supplies, this means that the tax point will occur when the service is completed or when it is paid for, whichever is the earlier.

In the case of continuous supplies, the tax point will be the end of each periodic billing or payment period. For example, if leasing charges are billed monthly or the customer is required to pay a monthly amount, the tax point will be the end of the month to which the bill or payment relates.

Again, if a payment is made before the end of the period to which it relates or before the end of the billing period then that payment date, rather than the end of the period, will be treated as the tax point.

Continuous supplies that are not subject to billing or payment periods will have a tax point on 31 December each year unless a payment has been made beforehand. In that case the payment will create a tax point.

Further information about the impact of the time of supply changes can be found in Part 4. Draft legislation to implement the changes can be found at Part 5. Any comments on these parts should be sent to vat.package@hmrc.gsi.gov.uk.

Part 3

Place of Supply of Services – changes post 1 January 2010

3.1 GENERAL RULE

3.1.1 How is the basic rule changing?

The current basic rule for the place of supply of services is that VAT is due where the supplier belongs. Under the new basic rule (or 'general rule' as it will be known):

The place of supply of services to a relevant business person will be where the customer belongs.

The place of supply of general rule services to a person who is not a relevant business person will be where the supplier belongs. This is the same as under the existing basic rule. The supplier will be required to charge UK VAT, as required, even if their customer belongs in another Member State.

As now, there will be exceptions to the general rule.

3.1.2 What is a 'relevant business person'?

In the majority of cases, the revised legislation uses the term relevant business person to determine how the rules apply. A relevant business person is a person to whom one of the following applies:

- is a taxable person within the scope of Article 9 of the Principal VAT Directive
- is registered for VAT in the UK
- is registered for VAT in another Member State
- is registered for VAT in the Isle of Man

For the purposes of this guidance we will refer to business to business (B2B) supplies for supplies to a relevant business person and business to consumer supplies (B2C) for all other supplies.

3.1.3 How will UK businesses know if their customer is in business?

In most circumstances business customers in other Member States will be able to supply a valid VAT number issued by their tax authorities. This, together with reasonable checks, will normally be sufficient evidence of business status. If the customer is not VAT-registered then alternative evidence may be used. This could be in the form of letters from their tax authority or Chambers of Commerce.

If you have regular customers but do not yet have their VAT number, you might want to start collecting them now in advance of the changes.

3.1.4 What if customers don't provide evidence that they are in business?

If your customer cannot provide sufficient evidence to show that they are in business, or if you have concerns about whether the evidence relates to your customer, you should treat them as a non-business customer. If the evidence is subsequently provided then an adjustment should be made.

3.1.5 What if my customer is involved in both business and non-business activities?

From 1 January 2010, if your customer is engaged in both business and non-business activities (for example, a charity or government department) general rule supplies to that customer will be treated as a B2B supply for the purposes of the place of supply rules. This means, for example, that general rule supplies by UK businesses to overseas charities will be outside of the scope of UK VAT, even if the services relate to the charity's non-business activities, providing that the charity has some

business activities. Similarly, where a UK charity which is engaged in both business and non-business activities receives general rule services, it will always be required to account for reverse charge VAT on those supplies, even if they relate solely to its non-business activities.

3.1.6 What if supplies are received wholly for a private purpose?

If a supply of services is made to a business customer who will use it wholly for their own private use or the private use of their staff, then the supply will be treated as a B2C supply.

For example, a VAT-registered builder may send a domestic appliance - that is not used in his business - away for repair. This would be regarded as wholly for a private purpose.

A company, charity, or government body cannot act in a private capacity.

3.1.7 How are the establishment rules changing?

There are no changes to the approach for determining where a company is established or whether there is a fixed establishment. This is covered in section 3, Notice 741 Place of supply of services.

3.1.8 How should I determine which establishment is receiving a service?

The test to determine which establishment of a business receives a supply mirrors that for determining from which establishment the supply is made. This takes into account whether the establishment has sufficient human and technical resources to make/receive the supply, although the level of human and technical resources required for receiving a service may be different to that required to make a supply - see section 3, Notice 741 Place of supply of services.

3.1.9 How should global contracts be treated?

In order to determine the place of supply of a 'global contract', it is important to first of all distinguish between a global contract that forms a single supply for VAT purposes and a global framework agreement, often between the business head office and a supplier, that sets the terms for a number of individual supplies.

For example, a business could enter into a contract for a single supply of consultancy services. The consultancy services analyse the global set-up and business practices at the head office and overseas branches. HMRC would regard this as a global contract with a clear direct benefit to the business as a whole, including a number of establishments. In this scenario the services would be supplied to the main business establishment.

Where a framework agreement exists it is important to look at the individual transactions which, as separate supplies, will have separate treatments for VAT purposes. For example, a head office of a business could enter into a framework agreement with a global firm of consultants. The agreement specifies the fees, terms and conditions. Individual branches then draw up and purchase work from the local branches of the consultant under the terms of the framework. These services will be viewed as supplied to the branches even if the head office dictates the terms and receives an indirect benefit.

3.1.10 What is the VAT treatment of supplies of service from/to a virtual office?

Our understanding of a virtual office is the situation where a business has no central office and all functions are carried out by remote workers. In this case, the business establishment is usually where the key decisions of the business are made, where the central policy is determined, and where business administration is carried out. If a business has no such place then it will be considered to be established where it normally resides. This is normally where the company is incorporated. This guidance may be reviewed or enhanced once we have further details of how virtual offices operate in practice.

3.***2 LAND RELATED***

3.2.1 How are services related to land changing?

The place of supply of land related services will remain unchanged, and will continue to be where the land is situated. Hotel and holiday accommodation will be explicitly included but this is for clarification only as these supplies have always been treated as land related services.

3.2.2 Travel agents and hotel booking - land related service or general rule?

There is currently some uncertainty as to whether the services provided by travel and hotel booking agents should be treated as land related or intermediary services covered by the general rule. We are

aware of the burdens likely to be caused by treating these as land related supplies and have raised the issue at EU level for discussion with other Member States and the European Commission. We will provide further guidance in due course.

3.3 PASSENGER TRANSPORT

3.3.1 How are passenger transport services changing?

The place of supply of passenger transport services will remain unaffected by these changes - see section 3, Notice 744A Passenger transport.

3.4 HIRE OF MEANS OF TRANSPORT

3.4.1 What is the place of supply of the hire of a means of transport?

The place of supply of the hire of a means of transport depends upon whether it is a short-term or long-term hire. A short-term hire is where there is continuous possession of the vehicle for up to 30 days, or 90 days in the case of vessels.

The place of supply of a short-time hire will be the place where the vehicle is put at the disposal of the customer.

The long-term hire of a means of transport will fall under the general rule (i.e. supplier location for B2C supplies, customer location for B2B supplies). However, from 1 January 2013 for B2C supplies on long-term hire, the place of supply will be where the customer is established, except for pleasure boats where the place of supply will be where the vessel is put at the disposal of customer if the supplier has an establishment there.

3.4.2 What is meant by 'put at disposal of'?

HMRC's view is that the term 'put at the disposal of' means the place where the vehicle is located at the time it is physically made available to the customer. This is an issue being discussed with other Member States and the European Commission with a view to achieving consistency of treatment.

3.4.3 What is meant by 'continuous possession'?

The definition of 'continuous possession' is being discussed with other Member States and the European Commission with a view to achieving consistency of treatment across the EU. Following those discussions HMRC will discuss application with the relevant trade bodies in advance of providing comprehensive guidance on this issue.

3.4.4 What are the reasonable checks of a hirer to determine the place where a non-business customer belongs?

Evidence to prove that a hirer has made reasonable checks of where a customer belongs include a driving license, utility bill or credit card billing address.

3.5 CULTURAL, ARTISTIC, SPORTING, SCIENTIFIC, EDUCATIONAL, ENTERTAINMENT AND SIMILAR SERVICES

3.5.1 How are the rules for cultural, artistic, sporting, scientific, educational, entertainment and similar services changing?

From 1 January 2010 the place of supply of cultural, artistic, sporting, scientific, educational, entertainment and similar services will be where the activity takes place. This is essentially the same as under the existing rules, i.e. taxed where performed.

However, from 1 January 2011 supplies of cultural, artistic, sporting, scientific, educational, entertainment and similar services will fall under the general rule. Only supplies of admissions to an event and services ancillary to admissions will be taxed where the event takes place. Supplies to consumers will remain unchanged.

3.5.2 What is meant by admission to an event?

In its strictest sense, admission means right of entry. However, there are clearly some borderline issues, in particular between whether a supply is admission to an event or an educational activity, for example in-house training seminars where costs are shared between different businesses within a group. This is an issue under discussion with other Member States and the European Commission with a view to achieving consistency of treatment across the EU. We are aware of business views on this and will issue comprehensive guidance as soon as agreement has been reached.

3.5.3 When is a supply ancillary to admission to an event?

A service is ancillary to admission to an event when it is necessary for the event to take place. In most circumstances it will also be performed at the same place, for example washroom and cloakroom services (if they form a separate supply). This is an issue being discussed with other Member States and the European Commission with a view to achieving consistency of treatment across the EU.

3.5.4 Are ticket agents to be treated as ancillary to an admission or as intermediaries?

HMRC's view is that the services of ticket agents will be treated as an intermediary service and will fall under the new general rule when supplied to business customers, but for non-business customers the place of supply will be where the event takes place. This is an issue being discussed with other Member States and the European Commission with a view to achieving consistency of treatment across the EU.

3.5.5 How should organisers' services be treated?

The services of organisers are supplied where the person carries out their role. This is not necessarily in the same place as where the event is held. This treatment will remain unchanged on 1 January 2010. From 1 January 2011 B2B supplies of organisers' services will fall under the general rule.

3.5.6 What are similar services?

A supply is similar to cultural, artistic, sporting, scientific, educational, or entertainment services if it is in connection with a meeting or event and the supplier is required to attend in order to carry out their obligations.

3.6 RESTAURANT AND CATERING SERVICES

3.6.1 What is the place of supply of restaurant and catering services?

Restaurant and catering services will treated as made in the country in which they are physically carried out. There will be separate rules for restaurant and catering services carried out on board ships, planes and trains during EU journeys.

3.7 RESTAURANT AND CATERING SERVICES ON BOARD SHIPS, PLANES AND TRAINS

3.7.1 What is the place of supply of restaurant and catering services on board ships, planes and trains as during part of transport in the EU?

The place of supply of restaurant and catering services during part of a transport within the EU will be the place of departure. This will mirror the rules for supplies of goods for consumption on board. There will be no change to the existing treatment in the UK for these supplies.

3.8 USE AND ENJOYMENT

3.8.1 How are the use and enjoyment provisions changing?

The use and enjoyment provisions, as applied by the UK, remain unchanged after 1 January 2010. They will still apply to the hire of goods, telecommunications, television and radio broadcasting and electronically supplied services to business customers.

3.8.2 At what stage does use and enjoyment apply?

The use and enjoyment takes place where a service is consumed. Whilst this will normally be at the final stage of supply (in particular for telecoms, broadcasting, and e-services), it can occur at earlier stages in the supply chain.

3.8.3 How should use and enjoyment be measured?

Determining the level of use and enjoyment will depend very much upon the exact circumstances surrounding the particular supplies. It is important to identify where the customer is physically using the service and where the benefit is felt.

3.8.4 How do other Member States apply the use and enjoyment provisions?

From 1 January 2010 Member States may, if they choose, apply use and enjoyment provisions to general rule services, hire of means of transport, EU to non-EU services other than electronically supplied services to non-business customers.

We are aware that there is concern amongst UK business about the inconsistency of application, both in terms of scope and interpretation.

3.9 INTERMEDIARIES

3.9.1 How is the place of supply of intermediary services changing?

The services of an intermediary, ie where a person arranges or facilitates a supply between two parties, will fall under the general rule from 1 January 2010 when it is performed for a business customer. The place of supply of B2C intermediary services will remain unchanged, ie in the same place as the underlying supply that is being arranged.

3.10 TRANSPORT OF GOODS

3.10.1 How is the place of supply of the transport of goods changing?

The place of supply of the transport of goods, including intra-community transport of goods, made to business customers will fall under the general rule from 1 January 2010.

For B2C supplies, the place of supply will remain where the transport takes place, in proportion to the distances covered within each country. However, the place of supply B2C supplies of intra-community transport will be the place of departure.

3.10.2 How is 'in proportion to the distances covered' to be calculated?

To determine the extent that a supply takes place in another Member State an apportionment is usually made by dividing the distance travelled with that country by the total distance covered.

3.11 ANCILLARY TRANSPORT, VALUATION AND WORK ON GOODS

3.11.1 How is the place of supply of ancillary transport, valuation and work on goods changing?

From 1 January 2010 supplies of ancillary transport services, valuation and work on goods to business customers will fall under the general rule. B2C supplies of these services will remain taxable where performed.

3.12 SUPPLIES OF SERVICES TO NON-TAXABLE PERSONS OUTSIDE THE EU

3.12.1 What services are supplied to non-taxable persons and what is the place of supply?

From 1 January 2010, the place of supply of B2C supplies of certain specified services will be where the recipient belongs when supplied to customers outside the EU. The services covered are those currently covered by Schedule 5 of the VAT Act 1994, with the exception of intermediaries arranging such a service (see Notice 741 Place of supply of services).

3.13 REVERSE CHARGE

3.13.1 How is the reverse charge changing?

The reverse charge is a simplification measure designed to avoid overseas businesses needing to register in a Member State when it is possible for the customer to account for the VAT on a supply. The mechanism itself is not changing, however there are a few consequential changes.

The reverse charge currently only applies insofar as the customer receives the supply for a business purpose. From 1 January 2010, an organisation that is involved in both business and non-business activities will have to account for VAT on a supply via the reverse charge even if the service is received in connection with its non-business activity. However, supplies received wholly for private purposes will be treated as B2C supplies.

In addition to the mandatory reverse charge for general rule supplies to business, the UK will continue to apply an extension to the reverse charge. This is where an overseas supplier provides non-general rule services to a UK VAT-registered customer and the place of supply of those services is the UK.

Details of how the reverse charge currently operates can be found in section 16, Notice 741 Place of supply of services.

3.13.2 Does the reverse charge apply even if the overseas supplier has a UK VAT registration?

The reverse charge is mandatory in relation to B2B general rule services made cross-border. However, if the overseas supplier is making the supply from a fixed establishment in the UK, they will need to charge UK VAT on the supply.

3.14 FORCE OF ATTRACTION

3.14.1 What is meant by force of attraction?

The force of attraction is a principle adopted by some countries whereby VAT is due from a business established in the same territory as their customer even though that business establishment does not play an active role in supplying the services concerned.

The EC legislation will include a new Article [192a] from 1 January 2010 stating that a VAT is not due from a fixed establishment within the territory of a Member State unless that establishment intervenes in the supply.

3.14.2 What is meant by the term intervenes in a supply?

HMRC's view is that a fixed establishment of a business can only intervene in the making of a supply when there is a substantive involvement. This is an issue being discussed with other Member States and the European Commission with a view to achieving consistency of treatment across the EU. We are aware of business concerns that an inconsistent approach will lead to double taxation.

3.14.3 Why has Article 192a not been enacted in UK VAT legislation?

The statement that a fixed establishment is not making a supply unless it intervenes in the services has been included in European law to address concerns over the 'force of attraction' principle. The UK has never adopted this principle. Although not explicitly covered in legislation, we believe that the overall UK legislation together with interpretation achieves the right result.

3.15 DISPUTES

3.15.1 How will disputes between Member States be dealt with?

Article 398 of the EC VAT Directive (2006/112/EC) provides for an advisory 'VAT Committee' which comprises delegates from each Member State chaired by a European Commission official. The VAT Committee can consider any questions concerning how EC VAT legislative provisions should be interpreted and applied, as well as any differences in the approach taken by Member State.

3.16 TRANSITIONAL ARRANGEMENTS

3.16.1 What are the transitional arrangements for these changes?

In cases where:

- VAT is correctly charged on a supply in another Member State under the existing rules in force and
- VAT becomes due in the UK on or after 1 January 2010/2011/2013 under the new rules

HMRC will not seek to collect the UK VAT, if evidence is available to demonstrate that VAT has been charged and paid for in another Member State. This will avoid double taxation.

Part 4

Time of Supply for Reverse Charge Services

4.1 Why are the time of supply rules changing?

The changes are intended to harmonise the time of supply rules for reverse charge services throughout the EU. At present Member States are permitted to set their own rules. If this were to continue after 1 January 2010 it could lead to mistiming in the reporting of supplies by the supplier (on their EC Sales List) and customer (on their VAT return) in their respective Member States.

4.2 What supplies are affected?

The new rules apply to cross-border supplies of services received in the UK by businesses that are required to account for the VAT on those supplies as a reverse charge.

4.3 Why do the new rules cover all supplies subject to the reverse charge arrangements in the UK?

The UK is required to adopt the harmonised time of supply rules for all supplies subject to a reverse charge under the new general rule for place of supply of services. We have opted to also apply them to supplies covered by the UK extension to the reverse charge arrangements, as this will provide consistency for businesses both in applying the rules and maintaining their accounting systems.

4.4 When do the changes come into effect?

The new rules will be implemented by secondary legislation, to come into effect at the same time as other VAT Package changes on 1 January 2010.

4.5 How will I treat supplies that span 1 January 2010?

The legislation will include measures that take into account supplies that are in progress on 1 January 2010. This will ensure that they not only remain properly liable to VAT, but also that they are not taxed twice. Further information about this will be available in due course.

4.6 What impact will these rules have on completion of UK EC Sales Lists?

Supplies reported on UK EC Sales Lists will be governed by the rules as they apply in the customer's Member State. So, for example, the time at which a supply is to be included will be based on the corresponding time of supply rules in that Member State, please see the ESL guidance.

4.7 How will the new rules apply to a single supply of services?

The tax point will be completion of the service, with an earlier tax point to the extent that they are paid for beforehand.

4.8 How will the new rules apply to continuous supplies of services?

For continuous supplies there will be a tax point at the end of each periodic billing or payment period (or on payment where this is earlier), with a compulsory tax point on 31 December each year in cases where such periods (or payments) do not arise.

4.9 What is the difference between a single and continuous supply?

The definition of a continuous supply will follow existing time of supply rules for domestic supplies. So, something like the leasing of equipment or provision of telephone services which are already treated as a continuous supply for time of supply purposes, will be treated as continuous supplies under these new rules. As a general rules supplies of services normally fall within one of the following categories:

- Single supply of services - for example the repair of a lorry for a transport business. The vehicle is left with a garage who will normally undertake the work the same day or within a couple of days. The services are completed when the required repair work has been performed.
- Series of separate supplies - for example, where the transport firm above takes its vehicles to the same garage for repair and servicing as required. This could mean that the garage is undertaking work on a regular basis. Nevertheless, in the normal course of events, each repair, etc, will amount to a separate discreet supply.
- Single supply of services over an extended period - for example, a consultant preparing a report. The process may take some time given the need to research the issues, followed by the drafting of the report. During that period the client is receiving little in the way of a tangible service. What the client requires is the final outcome ie delivery of the written report. Again this is when the service is performed.

Continuous supply of services - for example something like the provision of telephone services. Here, instead of an outcome, what the customer receives might be described as a recurring stream of supplies, each portion of which carries equal weight in terms of the customer being able to use and consume them. In this case the supplies are never 'completed' in the same way as the other categories are. The supply might be terminated but this is more a case of the supply ceasing rather than something finally being accomplished.

4.10 My existing accounting system does not recognise completion of a service, so can I use the date of the invoice as being roughly the equivalent?

The tax point in each case will depend on the nature of the supply and the underlying commercial arrangements. This prevents our providing general markers as to what might represent, for example,

when a supply might be treated as having been completed. Nevertheless, events such as receipt of an invoice, entry of a transaction into the accounts or payment might, depending on individual circumstances, be appropriate indicators of when that point is reached. As a general principle though, you may adopt any methodology that reasonably identifies completion, with the benchmark for that being that it results in VAT being accounted for in the correct period.

PART 5

DRAFT TIME OF SUPPLY LEGISLATION

Regulation 82 VAT Regulations 1995

Services from outside the United Kingdom

(1) This paragraph applies to services which are treated as being made by taxable persons under section 8(1) of the Act which are not services to which paragraph (3) applies.

(2) Subject to paragraph (5) the services to which paragraph (1) applies shall be treated as being supplied when they are performed.

(3) This paragraph applies to services which are treated as being made by taxable persons under section 8(1) of the Act which are supplied for a period for a consideration the whole or part of which is determined or payable periodically or from time to time.

(4) Subject to paragraphs (5) and (6) services to which subparagraph (3) applies shall be treated as separately and successively supplied at the end of the periods in respect of which payments are made or invoices issued and to the extent covered by the payment or invoice.

(5) If, before the time applicable under paragraph (2) a payment is made in respect of a supply, or in the case of paragraph (4) a payment is made at a time that is earlier than the end of the period to which it relates, the supply shall be treated as being supplied at the time the payment is made.

(6) if the services to which paragraph (3) applies

(a) are commenced before 1st of January and continue after 31st December of any year; and

(b) during that year no invoice is issued that has effect for the purposes of paragraph (4) and no payment made in respect of that supply

the services supplied during that year shall be treated as being supplied on the 31st December of that year to the extent that the recipient has received the benefit of them.

Comments on place of supply

HMRC have also published a summary of responses to the consultation on the implementation of the VAT package. Responses were received from businesses, professional associations and firms of accountants and lawyers. The following section is reproduced from the HMRC website: it is useful to see what the respondents were concerned about in thinking about how they would apply the new rules.

http://customs.hmrc.gov.uk/channelsPortalWebApp/channelsPortalWebApp.portal?_nfpb=true&_pageLabel=pageImport_ShowContent&propertyType=document&columns=1&id=HMCE_PROD1_029449

3.1 General rule

a) Use of the term 'taxable person'

From 1 January 2010 the new general (or basic) rule for the place of supply of services to business customers will be the place where the customer is established. The general rule for the place of supply of services to non-business customers will remain as it is now; where the supplier is established.

The draft legislation referred to 'supplies to taxable persons'. Seventeen written responses to the consultation questioned whether this properly implements the EC Directive. Of these fifteen highlighted difficulties with the use of the term "taxable person" as this is defined elsewhere in UK VAT legislation by reference to UK VAT registration and has a different meaning to the EC definition. These comments have been taken into account when making changes to the draft legislation.

b) Supplies made to business customers for private use

From 1 January 2010, EC legislation makes clear that for place of supply purposes a business customer will be treated as such even in relation to purchases it makes in relation to its non-business activities. However, this treatment will not extend to purchases for the private use of the customer or their staff. A further point raised on taxable person status was whether private purchases were caught by the reverse charge under draft legislation. One response considered that they were caught but should not be. Two responses suggested that private purchases were not caught but should be in light of the European Court's decision in Kollektivavtalsstiftelsen TRR Trygghetsrådet [C-291/07]. These comments have been taken into account when making changes to the draft legislation and comprehensive guidance will be provided on this issue.

c) Determining status of customer

The most frequently raised point on interpretation centred on the use and definition of the term 'taxable person' when the business was not registered for VAT. Fourteen responses concerned the need to understand what alternative evidence of business status of their customer would be required in the absence of a VAT number. Going forward, given the EC Sales List requirement for services, obtaining a VAT number should be the normal evidence of business status – this has not been the case to date. However, if the customer is not registered for VAT, HMRC's Public Notice 741 already gives examples of alternative evidence such as certificates from fiscal authorities, business documents and letterheads, and letters from local chambers of commerce. We intend to expand our guidance on this area.

In determining the status of their customer, suppliers are required to check the validity of VAT registration numbers supplied to them by their customers. This is done via Europa [see section 4.4(c)]. One respondent asked whether HMRC could provide a qualified checking service that would allow businesses to not only check the validity of the number but also the name of the registered entity. HMRC is currently working with other Member States on developing a system that will provide enhanced information (such as partial address and validity) for checking VAT numbers provided by EC customers.

d) Global contracts

When determining the place of supply it is necessary to decide whether the supply is made to the business establishment or other fixed establishment of the customer. Fourteen written responses raised the issue of how to treat global contracts, in particular how to determine the hierarchy of establishments for the receipt of services. This is an existing issue under the current rules. HMRC has highlighted the need for greater clarity at EC level and will consider if we can provide clearer guidance in the meantime.

e) Dispute Resolution Service

Two respondents highlighted the need for procedures to address differences in Member States' application of the place of supply rules. Such a procedure already exists. Article 398 of the EC VAT Directive (2006/112/EC) provides for an advisory 'VAT Committee' which comprises delegates from each Member State chaired by a European Commission official. The VAT Committee can consider any questions concerning how EC VAT legislative provisions should be interpreted and applied, as well as any differences in the approach taken by Member States.

f) Other issues

A number of other specific questions on interpretation were raised. Further information addressing the issues raised during the consultation, and the HMRC position in respect of each will be available through a Revenue and Customs Brief on 1 May 2009.

3.2 Services connected with immovable property

a) Scope

The only change to the rules, at EC level, for services connected with immovable property (land related services) is that hotel and holiday accommodation is now explicitly covered.

Three respondents highlighted that land related services in the draft legislation are defined in terms of UK land law and pointed out that this restricts the scope of services falling into this category. It was questioned whether the UK legislation should go into the level of detail that it does. This is the same approach as is applied under existing legislation. A further question was raised as to whether

the phrase "involved in matters relating to land" (UK legislation) has the same meaning as "connected with immovable property" (in the EC legislation).

Despite these comments, as the approach adopted going forward largely reflects what is covered by existing legislation, HMRC is not aware of any difficulty in its approach to the place of supply of land related services. If there are specific areas of concern we would welcome further examples or explanation of the difficulties likely to be encountered. A number of respondents asked for the guidance on the type of services seen as land related to be expanded. There are already a number of examples in existing guidance but we will consider if more detailed guidance is required.

b) Travel agents

The main area of concern regarding land related services concerns travel agents and whether an agent's services when arranging hotel bookings are land related or fall within the general rule. HMRC has sought clarification at EC level on this issue, and will confirm the outcome as soon as possible.

3.3 Passenger transport

Passenger transport is treated as supplied where the transport takes place. This rule is not subject to change and no comments were made on it in the consultation.

3.4 Hire of means of transport

The place of supply changes will see new rules for the hire of means of transport e.g. motor vehicles. The EC law introduces a number of new terms (such as 'put at the disposal of' and 'continuous possession') that might be open to differing interpretations across the EC, as might the distinction between long-term hire and short-term hire. A number of concerns about consistency were raised during the consultation process. These came from the car hire sector, large accountancy firms, and representative tax bodies. They also highlighted potential difficulties where contracts are changed mid-term and where hires span the implementation date.

This is an issue which is being discussed with the European Commission and other Member States with a view to achieving consistent interpretation. Once agreement has been reached, HMRC will provide detailed guidance.

3.5 Cultural, artistic, sporting, scientific, educational, entertainment and similar services

The place of supply rules relating to cultural, artistic, sporting, scientific, educational, entertainment or similar activities will remain essentially the same from 1 January 2010.

Although the new rule will refer to where the activity takes place HMRC does not see any change in practice from the application of the existing 'where performed' rule. With effect from 1 January 2011 the scope of this rule for supplies to business customers will be limited to admissions to an event and ancillary services related to admissions.

Supplies to business customers of other services (not admissions) within this category will become subject to the general rule. The place of supply of cultural, artistic, sporting, scientific, education entertainment and similar services to non-business customers will remain subject to the specific rule – i.e. supplied where the activity takes place. The definition of admission was the second most widely raised interpretation issue. This point was raised by ten respondents. The main difficulty highlighted was how to treat educational events or classes which participants pay to attend. This could be classified as either admission to an event or a supply of educational services. These options could result in different places of supply.

This is an issue that is being discussed with the European Commission and other Member States with a view to achieving a consistent approach on interpretation. Comprehensive guidance will be provided on what constitutes admission to an event once agreement has been reached.

3.6 Restaurant and catering services

The place of supply of restaurant and catering services is not currently specifically identified in UK VAT law. From 1 January 2010 the place of supply rule will be that these services are taxable where performed. No comments were received in relation to these services.

3.7 Restaurant and catering on board ships, planes and trains

There is a new place of supply rule for restaurant and catering services supplied on board ships, planes and trains. This mirrors the place of supply rules for goods consumed on board ships, planes and trains in the same circumstances.

Two respondents felt that there was some inconsistency between the draft law the EC directive and HMRC's interpretation, and that this represented a change from the rules for goods on board ships. HMRC has looked again at this but remains of the view that the VAT treatment of these supplies will remain the same post 1 January 2010 as now.

3.8 Use and enjoyment

Member States will be permitted to apply use and enjoyment provisions set out in Article 59a of the EC Directive to services covered by the general rule, hire of means of transport and EC to non-EC services (which includes electronically supplied services, radio and TV broadcasting services and telecommunication services). However Member States will not be able to apply use and enjoyment to EC to non-EC electronically supplied services for non-business customers.

Eight respondents commented on the difficulty in applying the use and enjoyment provisions in the UK. There were also concerns raised about the different scope and application of the use and enjoyment provisions across Member States and the need for clarity. This is an issue that is being discussed with the European Commission and other Member States to see what scope there is for providing greater clarity for business. In the meantime HMRC will consider if guidance can be clarified in this area.

3.9 Intermediaries

Under current law intermediary services are generally taxed in the same place as the underlying transaction. However, from 1 January 2010 this rule will only apply to supplies to non-business customers. Supplies of intermediary services to business customers will fall under the general rule.

One respondent questioned whether the UK draft legislation goes wider than the EC law that it implements. This is because it includes 'or other activity intended to facilitate the supply'. HMRC has considered this point but believes that the draft legislation is consistent with EC Law.

3.10 Transport of goods

The place of supply of services rules for the intra-community transport of goods from business to consumers will remain the place of departure of the goods from 1 January 2010. The place of supply of the intra-community transport of goods for business customers will fall under the new general rule. One respondent felt that Article 52 of the Directive, which allows Member States to not tax part of intra-Community transport taking place outside the EC, should be implemented into domestic legislation by the draft law. HMRC has looked at this and believe this is implicit in the draft legislation.

It was also asked how the place of supply will be determined "in proportion to the distances covered". HMRC considers that this will normally involve an apportionment to be carried out based upon the mileage in each Member State.

3.11 Ancillary transport services and valuation of work on goods

From 1 January 2010 ancillary transport services, valuation of and work on goods supplied to business customers will fall under the general rule. Supplies to consumers will continue to be supplied where performed.

No responses were received on this change.

3.12 Electronically supplied services

The place of supply of electronically supplied services to consumers will remain unchanged from 1 January 2010. The only question on this rule concerned the scope of electronically supplied services. This is covered in existing guidance but HMRC will consider if further clarification is required.

3.13 Supplies to non-taxable persons outside the EC

The place of supply of services covered by this provision made by a supplier established in the EC to a non-business customer residing outside the EC will be the non-EC customer's country. These are

services currently identified in Schedule 5 of the VAT Act 1994, with the exception of Schedule 5 intermediaries which are now covered by 3.9 above. No comments were received on this rule.

3.14 Reverse charge

Two respondents asked whether the draft legislation had the effect of making unregistered businesses more likely to have to register as a result of buying services from overseas suppliers. Currently services falling within the reverse charge as a result of paragraph 9, Schedule 5 of the Act (i.e. where the EC Directive does not provide for a mandatory reverse charge), only apply the charge where the customer is registered for VAT in the UK. The overseas supplier is potentially liable to register for VAT in the UK when the services are supplied to non-registered businesses. The receipt of these services by a VAT: Place of Supply of Services 12 non-registered business does not count towards the customer's total taxable supplies made for the purposes of the VAT registration threshold.

As the general rule from 1 January 2010 is wider in scope than it is under the current rules, more services will be covered by the mandatory reverse charge, the receipt of which will count towards the registration threshold and could result in more customers being required to register for VAT as a result of receiving these services.

Another respondent asked whether the new legislation would be compatible with a recent European Court decision in Kollektivavtalsstiftelsen TRR Trygghetsrådet [C-291/07].

HMRC has taken these views into account in finalising the legislation.

One respondent stated an objection to the widening of the reverse charge and increasing irrecoverable input tax for businesses without the right to recovery.

3.15 Force of attraction

The force of attraction is a principle adopted by some countries whereby VAT is due from a business established in the same territory as their customer even though that business establishment does not play an active role in supplying the services concerned.

Article 192a of the Directive seeks to ensure that the 'force of attraction' principle does not feature in determining the place of taxation and the business customer remains liable for VAT due on general rule services if the establishment of the supplier in his country does not "intervene" in the supply. This point drew a number of comments, mainly on interpretation and business facilitation measures.

Seven respondents sought a common EC definition of the meaning of intervening for the purposes of choosing between fixed and business establishments when making supplies. This is an issue which is being discussed with the European Commission and other Member State with a view to agreeing a consistent approach across Member States. Comprehensive guidance will be provided once agreement has been reached.

Some respondents questioned whether the UK draft law should incorporate Article 192a of the Directive. HMRC believes that the force of attraction principle has never been a feature of UK law or HMRC policy and so there is no benefit in adding this provision into the legislation. We are of the view that the legislation and interpretation of it are sufficient.

3.16 Time of supply and the reverse charge

Fourteen written responses commented on the time of supply changes that were adopted by the EC after the consultation document was prepared. The new rules will come into effect on 1 January 2010 and provide that the time at which a recipient of a taxable general rule service is required to account for a reverse charge will be the earlier of completion of the services or the date of payment. For continuous supplies, it will be the end of each billing or payment period (or on payment where this is earlier), with a compulsory tax point of 31 December each year in cases where such periods (or payments) do not arise.

The UK law provisions will determine the time when UK VAT registered persons account for a reverse charge on cross-border supplies. In addition the changes at EC level also impact on when the supplier of a taxable general rule service should complete their EC Sales List entry (see Section 4).

A large proportion of responses highlighted the difficulties in determining the performance date using existing systems. Whilst most respondents felt that they should be able to rely on the invoice date, others also requested that business should continue to apply the date of payment.

HMRC recognises the need to minimise burdens on businesses whilst at the same time meeting the requirements of the Directive. We are aware of the difficulties, for example, in determining when a service has been completed. In some cases events such as entry of a transaction into the accounts, receipt of an invoice or date of payment might, be appropriate indicators of when that point is reached. But this will inevitably depend on the precise nature of the supplies and existing commercial procedures. We will be discussing this issue further with business representatives, to try to identify a way forward that will not be too costly or burdensome.

3.17 Other issues

Although not part of the changes, respondents also highlighted existing differing treatments by Member States of certain supplies of goods and services, what supplies are included in Tour Operators Margin Scheme (TOMS), vouchers, tripartite contracts, and third party considerations and how these might be compounded by the changes in the place of supply rules. HMRC is aware of existing difficulties in these areas which are already being reviewed and in some cases part of ongoing European reviews (such as with vouchers). Comments made in response to this consultation will be taken forward as part of that work.

Article by Mike Thexton

Lecture B549 (24.54 Minutes)

VAT package 2: ESLs and 8th Directive Claims

This article reviews part of the "VAT package" measures which will be implemented on 1 January 2010. This is an EU development that will be implemented in all the member states. It has been a long time coming, and is the culmination of many years of discussion. The main elements of the VAT package are:

- changes to the place and time of supply of services (last month's lecture);
- changes to reporting of international goods and services on European Sales Lists;
- changes to the system for claiming refunds of VAT incurred in other member states under the 8th Directive.

The second and third points will be covered in this article.

The notes that follow:

- give an overview of what is changing;
- reproduce the latest HMRC guidance on this part of the VAT package;
- reproduce the HMRC summary of consultation responses, which highlight some of the problems that people anticipate arising from the new rules.

Articles

There is a two-part article about the VAT package in Tax Adviser, April and May 2009, as well as numerous articles in other publications.

The new 8th Directive rules are reviewed by Neil Warren in Taxation, 7 May 2009 p.443.

Budget announcement/summary of changes

Up to the end of 2009, European Sales Lists are required to be submitted quarterly by businesses which despatch goods to business customers in other member states. They record the sales values and the foreign VAT registration numbers (VRNs) of the customers, and support box 8 of the VAT return (although ESLs are always for calendar quarters, and the returns may be to different dates or monthly).

ESLs will be required from 1 January 2010 to report supplies of services to business customers who will be required to account for a reverse charge. The returns will be filed for each calendar quarter and will have to show the VAT registration number of the customers and the total value of the supplies to each customer.

ESLs for goods will also move from quarterly to monthly in many cases (details below).

The time limit for submission will be 14 days for paper and 21 days for electronic submission.

BN76

HMRC summarised the coming changes to ESLs as follows:

The main changes relate to the submission of ESLs. In principle, the new Directive provides that these should normally be submitted monthly, but it allows Member States to offer their businesses certain options. The United Kingdom intends to implement these as follows:

- ESLs relating to services may be submitted quarterly, relating to calendar quarters.
- From 1 January 2010, ESLs relating to goods may be submitted quarterly, relating to calendar quarters, provided that the value (excluding VAT) of supplies of goods to other Member States has not exceeded £70,000 in any of the previous 4 quarters.
- A business entitled to submit quarterly ESLs for goods can continue to do so unless the value of supplies of goods to other Member States exceeds £70,000 (excluding VAT) per quarter from 1 January 2010 to 31 December 2011 or £35,000 (excluding VAT) per quarter from 1 January 2012 onwards.
- If a business exceeds the quarterly goods threshold by the end of the first or second month in a quarter, an ESL must be submitted at the end of that month, covering the month or months in that quarter. Lists must be submitted monthly from then.
- Once a business is on a monthly cycle, because it has exceeded the threshold in any quarter, it must continue to submit monthly ESLs for goods until the value of its intra-Community trade in goods has been below the threshold for five consecutive quarters – it may then revert to quarterly submission if its trade remains below the threshold.
- A business required to submit monthly ESLs relating to goods may still submit ESLs relating to services quarterly.
- Any business may submit ESLs for goods and/or services monthly, if it wishes.

The other change to ESLs is that the time, within which both UK businesses and then HM Revenue & Customs (HMRC) must carry out their respective ESL obligations, has been reduced from three months to one. We intend to discuss this issue with business to explore how implementation can balance the needs of business and HMRC. Our current thinking is that businesses that submit paper ESLs would have 14 days from the end of the (last) month to do so. This period would be extended to 21 days for electronic submission of ESLs.

The VAT update in Accountancy magazine, April 2009, points out that it will not be straightforward to identify the services which are to be recorded on the ESL. For example, it will be those that are subject to a reverse charge in the other country: that may cause difficulties where there is a difference between the VAT rules of the UK and the customer's country, because the UK supplier may think of the supply as something that is not VATable.

Guidance notes

On 1 May 2009 HMRC published further details of the new rules. A guidance statement on ESLs includes FAQs which confirm that the existing ESL penalty regime will continue for the time being (daily penalties of £5, £10 and £15 for non-submission, £100 for material inaccuracies). The document also notes that the threshold for quarterly submission of goods ESLs will fall from £70,000 to £35,000 on 1 January 2012.

www.hmrc.gov.uk/vat/ec-sales-lists.pdf

PART 2

VAT Package - Extension of ESLs to include services

When ESLs are required

ESLs are currently only required for B2B intra-EC supplies of goods. From 1 January 2010 ESLs will also be required for intra-EC supplies of services (covered by Article 196 of Council Directive 2006/112/EC) to which a reverse charge applies in the customer's Member State.

They will not be required for:

- supplies which are exempt from VAT according to the rules in the customer's Member State; or
- supplies covered by Article 194 of Council Directive 2006/112/EC
- B2B supplies where the recipient is not VAT registered; or
- B2C supplies.

Information required on ESLs

The ESL form that is currently used for reporting intra-EC supplies of goods (VAT 101) will also be used for services. The following information must be entered on the form:

- customer's country code
- customer's VAT Registration Number
- total value of supplies in sterling; and
- code 3 in the Indicator Code Box if it is a supply of services; no Indicator Code is required for supplies of goods unless it is a triangular supply of goods when Code 2 must be entered.

ESL reporting periods

The ESL reporting period for taxable supplies of services will be a calendar quarter, although businesses may instead choose a reporting period of a calendar month.

Methods of submission

It will be possible to submit ESLs to HMRC either electronically through the 'ECSL Service', or by using the paper ESL Form VAT 101.

Electronic methods of submission are:

- The on-line form.
- Bulk upload of data using a Comma Separated Variable (CSV) or Extensible Mark up Language (XML) file. The 'Bulk Upload' options will be of particular use to businesses that regularly submit in excess of 20 lines.
- XML channel; or
- Using UN-EDIFACT format.

PART 3

Anti-Tax Fraud Strategy - Reduced timeframes

Current reporting period for ESLs

The current ESL reporting period for intra-EC supplies of goods is normally a calendar quarter.

New ESL reporting period for goods

From 1 January 2010 the ESL reporting period for goods will be a calendar month for supplies over a specified threshold (see paragraph 12 below). Where a business makes supplies of goods below the specified threshold, they may use a reporting period of a calendar quarter.

Thresholds for quarterly reporting periods for goods

During the period 1 January 2010 to 31 December 2011 quarterly ESLs can still be submitted if the total quarterly value of supplies of intra-EC goods, (excluding VAT), does not exceed £70,000 in the current quarter, or any of the previous four quarters.

And from 1 January 2012 onwards, if the total quarterly value of supplies of intra-EC goods, (excluding VAT), does not exceed £35,000 in the current quarter, or any of the previous four quarters.

However, the option to submit quarterly ESLs for goods will cease at the end of any month during which the total value, excluding VAT, of the taxable supplies of intra-EC goods exceeds the relevant quarterly thresholds i.e. £70,000 or £35,000.

Businesses will be required to submit monthly ESLs from the first day of the month following the month in which they exceed the threshold. For example where a business submitting quarterly ESLs exceeds the quarterly threshold during the month of February, they will be required to submit a final 'quarterly' ESL covering just two months (January and February) and commence submitting monthly ESLs from 1 March.

Businesses should notify HMRC as soon as the total quarterly value of supplies of intra-EC goods exceeds the relevant threshold figure. Arrangements will then be made to change to 'monthly' the businesses recorded declaration period.

Current timeframe for submitting ESLs to HMRC

Businesses currently have 42 days from the end of the reporting period to submit their ESLs to HMRC.

New timeframes for submitting ESLs to HMRC

With effect from 1 January 2010 the new timeframes for submitting ESLs to HMRC will be:

- for paper ESLs, 14 days from the end of the reporting period; and
- for electronic submissions, 21 days from the end of the reporting period.

PART 4

Questions & Answers

ESLs

1. What is an ESL?

An ESL (EC Sales List) is a declaration that lists supplies of goods and/or services made by a UK VAT registered trader to a VAT registered customer in another EU Member State. These declarations are called 'Recapitulative Statements' in EC VAT legislation.

2. Why do I need to submit an ESL?

Within the EU Single Market there are no frontiers, or borders, between different Member States, even though they are separate fiscal territories. Prior to 1993 goods had to be declared as they moved from one Member State to another. ESLs provide the tax authorities in the different Member States with a post-event declaration, or notification, to alert them to the cross-border supply of goods and services from 1 January 2010. These declarations enable the tax authorities to monitor taxpayer compliance and to fight VAT fraud.

3. After 1 January 2010 I expect to be making intra-EC supplies of services (covered by Article 196 of Council Directive 2006/112/EC), that are taxable in my customer's Member State. What should I do?

You must notify HMRC about such supplies by completing and submitting to HMRC an ESL form (VAT 101) in accordance with the requirements set out in this guidance. To obtain a VAT 101 form, businesses should contact the HMRC National Advice Service on 0845 010 9000.

4. What methods can I use to submit an ESL to HMRC?

ESLs can be submitted to HMRC either electronically through the 'ECSL Service' (via the 'Online Services' option at www.hmrc.gov.uk), or by using a paper ESL Form VAT 101.

5. Can I use an agent to send in my ESL?

You may use an agent to act on your behalf, but remember the legal responsibility for the accurate and timely completion and submission of an ESL remains with you.

6. How long will I have to submit an ESL?

From 1 January 2010, the deadlines for submitting an ESL to HMRC will be:

- for paper ESLs, within 14 days of the end of the reporting period

- for electronic (on-line) ESLs, within 21 days of the end of the reporting period.

7. Is there going to be a new ESL form for services?

No. We will be using the existing form VAT 101. On the appropriate line on the ESL declaration you should enter a Code 3 in the Indicator Box to identify the supply of services.

8. Will there be any changes to the VAT 101?

There will be no significant changes to the form but it will be necessary to introduce a minor change to the box on the form currently named 'Calendar Quarter', to allow for monthly submissions.

For all ESLs covering a period from 1 January 2010 onwards, this box will be renamed Period Reference and will consist of a four digit reference ie MM/YY instead of the existing YY/Q format.

If you submit your ESLs quarterly it will show the last month of the calendar quarter ie 03/10, 06/10, 09/10 and 12/10.

9. I supply goods to other Member States to the value of £200,000 per annum; can I still submit quarterly ESLs?

Not necessarily. This will depend on the value of your supplies of goods in any particular quarter; see paragraphs 12 to 15 of this guidance note for details of the thresholds for quarterly reporting of goods.

10. How will HMRC determine if I am required to submit monthly ESLs for goods, with effect from 1 January 2010?

The EU legislation states that Member States may allow taxable persons to submit quarterly ESLs, providing the total quarterly amount (excluding VAT) of the supplies of goods does not exceed the threshold, in the current or any of the previous four quarters.

In line with this, we will be checking which businesses have exceeded the quarterly threshold (£70,000), by reference to the ESLs submitted for each of the calendar quarters in 2009. Businesses that have exceeded the threshold in any one of these quarters will be advised of their requirement to submit monthly lists from 1 January 2010.

A similar exercise will be carried out in 2011, in readiness for the threshold being reduced to £35,000 on 1 January 2012.

11. I haven't made any supplies this month (quarter) do I still have to submit an ESL?

No. It is not necessary to submit 'nil' returns.

12. When can I move back to quarterly ESLs for goods?

As soon as the value of goods (excluding VAT) in the current quarter and the previous four quarters falls below the specified thresholds (see paragraphs 12 to 15 of this guidance note).

13. I only supply services, when do I have to submit an ESL?

ESLs for services are required on a calendar quarterly basis. However businesses may opt to submit them monthly.

14. I supply both goods and services. Can I put them all on the same ESL?

Yes. However you must use Indicator Code 3 to separate supplies of services from supplies of goods for each of your customers.

15. What is the frequency for submitting ESLs if I supply goods and services?

If a business supplies both goods and services and they are above the quarterly reporting threshold for goods, they are obliged to submit monthly ESL reports for goods. Businesses may either:

report only goods in month 1, report only goods in month 2 and report goods in month 3 AND services for the whole quarter; or

report both goods AND services in each month.

If a business supplies both goods and services and they are below the quarterly reporting threshold for goods, all the supplies may be reported to HMRC on a quarterly basis.

16. Is it possible and acceptable for a business to submit both an electronic and a paper ESL declaration for the same reporting period?

Although HMRC would prefer a business to submit their ESL by the same method each period, HMRC systems can and will accept a mixture of electronic and paper ESLs, provided the different submission deadlines are respected.

17. If I want to check the validity of my customer's VAT registration number how do I do it?

The Europa website provides an electronic number registration number checking facility of all Member States VAT registration numbers. The HMRC National Advice Service (NAS) (contact number 0845 010 9000) can validate VAT numbers and verify that names and address belong to that number.

http://ec.europa.eu/taxation_customs/vies/vieshome.do?selectedLanguage=EN

18. In respect of supplies of services, how do I determine the liability of the supply in the customer's Member State?

The law requires that businesses report supplies that are taxable in the customer's Member State and the onus is on businesses to comply with the law. If reasonable attempts, which may include discussing with the customer, or the customer's tax authority, have failed to ascertain what the VAT treatment is in the other Member State(s), businesses may wish to assume that the UK VAT treatment will apply to those supplies, on the basis that this should be consistent with the EC VAT Directive and therefore with the law in other Member States.

19. Does a UK business need to consider whether their customer in another Member State may have exercised an 'option to tax'?

No.

20. How will UK suppliers know if their customer is in business?

In most cases business customers in other Member States will be able to supply to supply a valid VAT number issued by their tax authorities. This, together with reasonable checks, will normally be sufficient evidence of business status.

21. Do I need to submit an Intrastat declaration for supplies of services?

No. Intrastat declarations are for goods only.

Errors

22. How do I make a correction to an error?

The Internet service includes front end validation of data, so errors will be identified on screen. If you submit a paper based ESL HMRC will notify you of any errors that they identify using the form VAT 104 (ESL Error Report). The computer-generated form is sent to you with a copy of our 'Helpful Hints' document. The form will show the error lines and the reasons for the errors. Please correct the errors in the spaces provided and return the form to the address shown. Alternatively, businesses can voluntarily submit a VAT 101(B) at anytime notifying HMRC of errors they have made on their ESL.

Penalties

23 How will the HMRC penalties regime impact on the new ESL requirements?

ESLs are not covered by the new HMRC penalties regime. ESL penalties are issued in accordance with separate provisions in the UK VAT Act Sections 65 (Inaccuracies) and 66 (failure to submit). At least for the time being, these provisions will continue to apply.

In terms of their application, HMRC will adopt a proportionate approach particularly while the new ESL arrangements bed in across the EU. HMRC will expect businesses to take reasonable and appropriate steps to ensure the completeness and accuracy of their ESL declarations. However, HMRC appreciates that in the early months of the new arrangements some businesses, for valid operational reasons, may face some difficulties. Provided a business can demonstrate that they have taken 'reasonable care' to comply, HMRC will not seek to apply a penalty.

24. Will I be penalised if I fail to submit my ESL, send it in late, or make mistakes?

If you fail to submit your ESL by the due date (see question 6) you may be liable to a penalty of £5, £10 or £15 per day that you are late. The actual rate applicable will depend on the number of times you have been late.

It is recognised that some businesses may not be ready to submit ESLs by 1 January 2010. However, as long as businesses can demonstrate that steps are being taken to comply with the new legislation at the earliest opportunity, HMRC will not levy penalties.

If you submit an ESL that contains a material inaccuracy and you fail to tell us, you may be liable to a penalty of £100. Material inaccuracies fall into three main categories:

- Data missing from the EC Sales List.
- Lines on the EC Sales List are factually incorrect.
- An invalid Vat number is used.

You will not be liable to a penalty if you can satisfy us that you have a reasonable excuse.

25. What is meant by a 'reasonable excuse'?

There is no legal definition of a reasonable excuse but we will look closely at the circumstances of each case. If you can show that your conduct was that of a conscientious business person who accepted the need to comply with VAT requirements, then there may be a reasonable excuse. Genuine mistakes, honesty and acting in good faith are not accepted as reasonable excuses for penalty purposes. The law provides specifically that you do not have a reasonable excuse if you relied on some other person to perform any task for you. In addition, the fact that you have:

- quoted a VAT number for your customer that does not conform to the published format for your customer's EC Member State; or
- used a VAT number which HMRC has informed you is invalid;
- will not be accepted as a reasonable excuse for the material inaccuracy.

Legislation

26. When will the UK's ESL legislation be published?

We are including the changes to primary legislation in the 2009 Budget Statement. Changes to UK secondary legislation (VAT Regulations) will follow in the summer of 2009.

27. Must a business record on the ESL declaration supplies to a 'taxable person' in another Member State if they do not have a VRN?

You should only record on an ESL supplies to businesses in other Member States that are VAT registered and can provide a valid VRN. The amended Article 264 of the VAT Directive makes it clear that the customer's VRN must be included on the ESL. If you make a supply to a business which is not registered for VAT in their Member State because it is below the registration threshold, but which has provided you with evidence that it is in business (for place of supply purposes), you should not include these supplies on your ESL because the absence of a VAT registration number would cause it to be rejected. However, in some cases receipt of the supply will result in the business being required to register in their Member State. If this is the case and a VRN is subsequently given to you, an amendment should be made the EC Sales List at that time.

Reverse Charge

28. What is a reverse charge?

Normally, the supplier of a service is the person who must account, to the tax authorities, for any VAT due on that supply. With effect from 1 January 2010, it is the customer who must account for VAT due on intra-EC taxable supplies. Although called reverse charge, the procedure may also be referred to as tax shift. Reverse charge is not a complicated accounting procedure. Where it applies to services which you receive, you, the customer must act as if you are both the supplier and the recipient of the services.

29. How do I account for reverse charge services on my VAT return?

You should credit your VAT account with an amount of output tax, calculated on the full value of intra–EC taxable supplies of services received from other Member States and at the same time debit

your VAT account with the input tax to which you are entitled, in accordance with the normal rules. The partial exemption implications for reverse charge services are explained in Notice 706 'Partial exemption'.

You should then include in the following boxes of your VAT return:

- the amount of output tax in box 1 VAT due on sales
- the amount of input tax in box 4 VAT reclaimed on purchases
- the full value of the supply in box 6 total value of sales; and
- the full value of the supply in box 7 total value of purchases.

ESL consultation responses

HMRC have also published a summary of responses to the consultation on the implementation of the VAT package. Responses were received from businesses, professional associations and firms of accountants and lawyers. The following section is reproduced from the HMRC website: it is useful to see what the respondents were concerned about in thinking about how they would apply the new rules.

http://customs.hmrc.gov.uk/channelsPortalWebApp/channelsPortalWebApp.portal?_nfpb=true&_pageLabel=pageImport_ShowContent&propertyType=document&columns=1&id=HMCE_PROD1_029449

4.1 Introduction

From 1 January 2010, EC Law requires that EC Sales Lists (ESLs) must be completed for taxable services which are subject to a reverse charge in the Member State of their customer. Respondents to the Consultation Document had three main concerns about the proposed new ESL arrangements for reverse charge services. First of all, businesses were not being allowed enough time to prepare their IT systems to implement the new reporting requirements. Many respondents reported that most major IT changes have a 24 month design, develop, build, install and test cycle. However, in this case most businesses would only have about 12 months. Secondly, for many intra-EC supplies of services, particularly those in the financial services sector, it would often be very difficult to identify whether a supply was liable to a reverse charge in the customer's Member State.

Finally, many businesses thought it would sometimes be difficult to obtain their customer's VAT Registration Number (VRN), or to check its validity.

4.2 Legal Interpretation

When the Consultation Document was issued, it included only the adopted EC legislation for ESLs, as the draft UK legislation was not available. Although comments were specifically invited about the clarity of the EC legislation, none were received. Consequently HMRC has now prepared the draft UK legislation on the understanding that there are no substantive issues surrounding how the law should be interpreted and applied. The draft UK legislation has now been circulated to selected business associations for comment and will be published on the HMRC website shortly.

4.3 Format of ESL Declaration (VAT 101)

There were several enquiries as to whether there would be any changes to the ESL Declaration (Form VAT 101) to include intra-EC supplies of services. HMRC can confirm that the form will not be changed, as to identify intra-EC supplies of services, businesses will simply be asked to enter Code 3 in the Indicator Box; currently the only code that is used is Code 2 for triangular supplies of goods. HMRC does intend to slightly modify the format of the paper version of the Form VAT 101 so that the declarations can be more easily scanned, but the basic format will not be changed.

Businesses requested early confirmation of changes to the CSV/XML formats for the ESL declarations and also wanted to know if a testing facility will be made available through SDST. Meetings are being held with software developers and the delivery of a test service is expected by early July.

4.4 Determining when ESLs are required

a) Determining taxable and exempt transactions

ESLs will only be required for taxable services subject to a reverse charge. Fifteen respondents expressed concern at having to determine whether a supply of services is taxable or exempt in the Member State of consumption. This is a particular problem in the financial services sector where the liability position differs from one Member State to another. There are ongoing discussions in EC Council meetings on the Financial Services Review to seek clarification and agreement as to which supplies are taxable and which exempt, but this may take some time to resolve. HMRC is fully aware of the importance of this issue to businesses and is actively discussing possible ways forward with business representatives in a joint Business/Government ESL Working Group. HMRC will therefore seek to publish agreed guidance at an early date.

b) Business customers who do not provide a VRN

This was another area of concern, with eleven respondents requesting guidance on how they will deal with business customers who do not provide them with a VAT number.

HMRC's view is that only supplies to businesses in other Member States that are VAT registered and can provide a valid VRN should be recorded on the ESL. HMRC said the following in its Place of Supply of Services Consultation Document:

"Supplies to non-registered business customers - if you make a supply to a business which is not registered for VAT in their Member State because it is below the registration threshold, but which has provided you with evidence that it is in business (for place of supply purposes), you should not include these supplies on your ESL because the absence of a VAT registration number would cause it to be rejected."

HMRC stands by this statement, as the amended Article 264 of the VAT Directive makes it clear that the customer's VRN must be included on the ESL. However customers may register between transactions so it should not be assumed that the treatment of later supplies will be the same as the treatment of earlier ones.

c) Checking the validity of a customer's VRN

A number of businesses said they were unsure about whether and how often they should check the validity of their customer's VRN.

The Europa website provides an electronic number registration checking facility of all Member States VAT registration numbers. The HMRC National Advice Service (NAS) (contact number 0845 010 9000) can validate VAT numbers and verify that names and address belong to that number.

http://ec.europa.eu/taxation_customs/vies/vieshome.do?selectedLanguage=EN

It is the responsibility of the business making the supply to be satisfied that their customer is VAT registered and that the services will be used for business purposes. As the nature and extent of relationships between businesses can vary extensively, HMRC cannot provide specific advice as to whether, or how frequently, a supplier should validate their customer's VRN.

d) Businesses supplying both goods and services

Some respondents questioned whether goods and services could be declared on the same ESL form. As indicated above, on the ESL declaration (Form VAT 101), businesses will be able to identify supplies of services by entering Code 3 in the Indicator Box on the relevant lines of the declaration.

4.5 Determining the Time of Supply for ESL purposes

Fourteen responses commented on the new time of supply (tax point) rules for intra-EC supplies of services. These define the tax point as being the earlier of either the date of performance, or date of payment. These new tax point rules have been introduced to ensure that the supplier of the service declares the supply on their ESL at the same time as the customer records receipt of the service on their VAT return.

As noted at 3.16, HMRC is aware of the difficulties these rules pose for businesses, and is in active discussions with business representatives to try to identify a way forward that will not be too burdensome or costly.

4.6 Reduced timeframes for submission

Several businesses said they were unclear about the proposed reduced timeframes (i.e. 14 days for paper and 21 days for electronic) for submitting their ESLs to HMRC after the end of the monthly or quarterly reporting period.

These deadlines are necessary because the time allowed for Member States to collect, process and exchange ESL data with other Member States is reduced to one month in total. HMRC is seeking to give businesses as much of the limited available time as possible so that is why we have decided to allow businesses that submit electronic ESLs 21 days after the end of the reporting period. However, we can only allow businesses 14 days to submit their paper ESLs as we will require additional time to either key-in or scan the documents onto the HMRC VAT Information Exchange System (VIES) database ready for transmission to other Member State tax authorities by the month end.

4.7 HMRC Penalty Regime

There was a request for clear guidance on the penalty process for the new ESL regime, particularly during the transitional phase.

ESLs are not covered by the new HMRC penalties regime. ESL penalties are issued in accordance with separate provisions in the UK VAT Act Sections 65 (Inaccuracies) and 66 (Failure to submit). At least for the time being, these provisions will continue to apply.

Under the current ESL penalty regime arrangements, if a business fails to submit an ESL by the due date it may be liable to a penalty of £5, £10 or £15 for each day that the ESL is late. The actual rate applicable will depend on the number of times the business has submitted ESLs late in the past. If a business submits an ESL that contains a material inaccuracy and it fails to tell HMRC, it may be liable to a penalty of £100. But in both cases it will not be liable to a penalty if it can satisfy HMRC that it had a reasonable excuse.

When applying the penalty regime, HMRC will adopt a proportionate approach while the new ESL arrangements bed in across the EC. HMRC will expect businesses to take reasonable and appropriate steps to ensure the completeness and accuracy of their ESL declarations. However, HMRC appreciates that in the early months of the new arrangements some businesses, for valid operational reasons, may face some difficulties.

Provided a business can demonstrate that it has taken “reasonable care” to comply, HMRC will not seek to apply a penalty.

4.8 Timeframe for implementing the above ESL system changes

HMRC fully understands the concerns of UK businesses and recognises that the time allowed to implement these changes to the ESL regime is challenging, particularly in the current business environment. It will therefore do all it can to implement the requirements in a way that keeps administrative burdens and business costs to a minimum.

Electronic refund system

The Budget included details of a new electronic refund procedure for VAT incurred in other member states. From 1 January 2010 claimants will submit claims electronically to HM Revenue & Customs in the UK, rather than directly to the authorities in the other member state. It appears that this will apply to claims made after 1 January 2010 for the calendar year 2009, even if interim claims for 2009 have already been made during the year.

Businesses will be able to submit claims up to 9 months from the end of the calendar year in which the VAT was incurred, rather than 6 months as at present. Tax authorities will have 4 months, rather than 6 months, to make repayments, unless further information is requested in which case the deadline is extended to 8 months. The refunding member state will pay interest where the business has met all its obligations but the authorities fail to meet their deadlines.

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Further guidance on the new system was published by HMRC on 1 May 2009. The document is split into three parts:

1. Background and the main differences between the new system and the current, paper-based system.
2. Summary of the changes for UK businesses making claims to the tax administrations in other Member States. It also describes the process from the user's point of view and in Q&A format.
3. Draft UK secondary legislation. The draft primary legislation is primarily an enabling provision and will be included in the Finance Bill.

Detailed guidance on the new system is currently being prepared and this will be published towards the end of the summer.

Interesting points at this stage include the requirement only to scan and send invoices above a set limit. It will no longer be necessary to send in every invoice with the claim, even in electronic form.

Another practical point is that the portal will only recognise claims from the representative member of a VAT group. This could be important as it will also only accept five claims a year from each registered trader in respect of any individual country (intended to be four quarterly claims plus a "sweep-up" at the end of the year, although claims do not have to be made like that). This means that VAT groups will need to consolidate their claims before submitting them.

www.hmrc.gov.uk/vat/refund-procedure.pdf

Article by Mike Thexton

Lecture B550 (11.56 Minutes)