CONTENTS

Budget 2010

Lecture P586 (18.59 Minutes)

Lecture B586 (17.07 Minutes)

PERSONAL TAXATION

Income Tax Rates, Rate Limits and Personal Allowances

The basic rate of income tax of 20% and the basic rate limit of £37,400 remain unchanged for 2010/11. The higher rate of income tax of 40% which applies to income in excess of £37,400 is also unchanged but an additional rate of income tax of 50% applies to taxable income over £150,000. The 10% starting rate limit for savings remains at £2,440.

Personal allowances remain unchanged except for taxpayers with adjusted net incomes in excess of £100,000, who for 2010/11 suffer a reduction of their personal allowance by £1 for every £2 of income over £100,000.

Special Guardianship Orders and Residence Orders

A new income tax exemption for special guardians and certain kinship carers is to be introduced from 6 April 2010 for payments received on or after that date. The exemption will apply to ‘qualifying payments’ made to ‘qualifying carers’. ‘Qualifying carers’ are individuals who care for one or more children placed with them under a special guardianship order or under a residence order (where the individual is not the child’s parent or step-parent). ‘Qualifying payments’ are payments made to the carer by the child’s parents or by (or on behalf of) a local authority, in relation to a special guardianship order or a residence order.

Kinship carers who are providing care to a child who has not been placed with them under a residence order will not be qualifying carers for the purposes of the above exemption. However, they will be entitled to claim the new income tax relief for shared lives carers that was announced in the Pre-Budget Report 2009 and which operates in a similar manner to the existing relief for foster carers. Broadly they can choose to pay tax only on their income (if any) from caring that falls above certain fixed limits or on their actual profits computed under the normal income tax rules for businesses.

Remittance Basis

Subject to detailed rules and conditions that were fundamentally revised in 2008, individuals who are resident but either not domiciled or not ordinarily resident in the UK may pay income tax and capital gains tax on the remittance basis. They will then be subject to UK tax on their foreign income and gains only when they are remitted to the UK, rather than on their total worldwide income and gains.

A minor amendment is proposed as below to the current rules. This will have effect for 2010/11 onwards.

The concept of relevant person was introduced in 2008 to ensure that an individual’s foreign income or gains which are remitted to the UK by way of a person closely connected to the individual (or for the benefit or enjoyment of such a person) are taxed on the individual. Such persons are known as ‘relevant persons’. They include, for example, the individual’s spouse (or civil partner) and their minor children and grandchildren. (A cohabiting couple are treated as husband and wife or, as the case may be, civil partners.)

‘Relevant persons’ also include any close companies (broadly companies under the control of five or fewer participators) and their subsidiaries in which such persons are participators. It is not currently explicit that references to a close company are intended to include subsidiaries of non-UK resident companies which would be close companies if they were resident in the UK. To remove any uncertainty, and to remove the potential for abuse, the legislation will be amended to make clear that a relevant person includes such companies.

EMPLOYMENT TAXATION

Employer-Funded Childcare

No liability to income tax arises on provision by an employer to his employees of qualifying childcare vouchers, except to the extent (if any) that the cash equivalent of the benefit exceeds £55 per week. One of the conditions for this exemption is that the vouchers are provided under a scheme that is open to all the employees or to all those at a particular location.

Where an employer's scheme provides the vouchers as part of a salary sacrifice arrangement, employees on the National Minimum Wage (NMW) (or just above it) have to be excluded because the salary sacrifice would take them below NMW levels. Legislation is to be introduced to ensure that the exemption can still apply even if these lower-paid employees are excluded. The legislation will be backdated to 2005/06 when the exemption was first introduced.

There is also an exemption from income tax where the employer provides childcare directly rather than through vouchers. Again, retrospective legislation will preserve the exemption in cases where the childcare is provided via salary sacrifice arrangements and lower-paid employees are excluded.

Taxable Benefit Charges on Zero-Emission Vehicles and Low Emission Cars

From 6 April 2010 to 5 April 2015 there will be no benefit charge for employees provided with cars or vans which cannot produce any CO_2 emissions. In addition and with effect between the same dates, there will be a reduced benefit charge applying to cars with a CO_2 emissions figure of 75g per kilometre or less. To calculate the taxable benefit relating to such cars, the percentage applied to the car list price will be 5%.

CAPITAL GAINS

Increase in the Lifetime Limit for Entrepreneurs' Relief

The lifetime limit for entrepreneurs' relief is to be increased to £2m for disposals made from 6 April 2010. Disposals made before that date will be subject to the previous lifetime limit of £1m, with no additional relief available in excess of that limit. The increased limit will apply to individuals and trustees of settlements in which the beneficiary meets the entrepreneurs' relief conditions.

North Sea Fiscal Regime: Reinvestment Relief

A technical oversight is to be corrected in relation to chargeable gains reinvestment relief for oil and gas companies. This measure will ensure that the relief is available where a group company reinvests in new oil trade assets. The change has effect in relation to disposals on or after 24 March 2010 and it will be legislated in a Finance Bill to be introduced in the next Parliament.

SAVINGS AND INVESTMENTS

Venture Capital Schemes

Changes will be made to the rules on enterprise investment schemes (EIS) and venture capital trusts (VCT) to comply with a European Commission ruling on state aid.

In the next Parliament legislation will be introduced to:

- exclude any 'enterprise in difficulty' from qualifying for investment under the rules for EIS or VCT;
- remove the condition that the qualifying trade must be carried on wholly or mainly in the UK and instead the requirement will be that the company issuing the shares must have a permanent establishment in the UK.

The term 'enterprise in difficulty' takes its meaning from the European Commission's Rescue and Restructuring Guidelines.

Changes that will apply only to VCTs:

- the ordinary share capital of the VCT will be traded on any EU-regulated market (rather than only in the UK as at present);
- the definition of eligible shares will include shares which may carry certain preferential rights to dividends;
- 70% of the VCT's qualifying holdings must be in eligible shares (an increase from the 30% currently required).

These changes will take effect on the day the relevant legislation receives Royal Assent.

Enterprise Management Incentives

To ensure that the enterprise management incentive (EMI) share option scheme complies with EU state aid guidelines, legislation will be introduced in the next Parliament to remove the need for the company to operate wholly or mainly in the UK. Instead, the company granting the EMI options will only need to have a permanent establishment in the UK. In the case of a parent company, at least one company in the group that is carrying on a qualifying trade must have a permanent establishment in the UK.

A company has a permanent establishment in the UK if it has a fixed place of business in the UK through which the business of the company is wholly or partly carried on, or it has an agent in the UK who exercises authority to do business on behalf of the company.

This will have effect in respect of EMI share options granted on or after the date that the legislation receives Royal Assent.

Indexing of Individual Savings Account Limits

The increase in the annual subscription limits for individual savings accounts (ISAs) was previously announced in the 2009 Budget. From 2010/11, all savers can invest up to £10,200 per tax year in an ISA (of which £5,100 can be saved in cash). These subscription limits will rise further from April 2011, as legislation will be introduced via statutory instrument to increase the limits in line with the retail prices index (RPI). If RPI is negative, the limits will remain unchanged. HMRC are to announce the limits at least 4 months before the start of each tax year.

Pension Scheme Lifetime Allowance and Annual Allowance

The lifetime limit on the value of investments held by an individual in registered pension schemes is to be frozen at the 2010/11 level of £1.8m until 5 April 2016. The only exception is where an individual has pension scheme investments valued at more than the lifetime limit and has existing transitional protection in place. The annual allowance will remain at the 2010/11 level of £255,000 over the same period.

Changes to Pension Taxation

The following changes to the taxation of pension schemes are to be introduced in the next Parliament:

- the National Employment Savings Trust (NEST) will be allowed to register as a pension scheme with HMRC, allowing the members and their employers to benefit from tax relief on contributions and investment growth;
- under Pensions Act 2008 employers will have a duty to ensure all their employees are active members of a pension scheme, with automatic enrolment planned for 2012, and will be legally obliged to make contributions to a pension scheme on behalf of their employees and pay interest on any contributions paid late; currently any interest on late paid employer pension contributions is taxable on the employee, however this income tax charge is to be removed by the proposed legislation;
- rules on borrowing by registered pension schemes (currently there is a charge if this exceeds 50% of the fund value) will be relaxed to exclude any sums borrowed in order to establish and operate the scheme.

The proposed legislation will also include the facility for HMRC to correct via statutory instrument any unintended tax disadvantages arising from the introduction of NEST. These changes will be effective from the date the legislation receives Royal Assent.

Life Insurance Policies: Deficiency Relief

With effect from 6 April 2010, life insurance deficiency relief will be made available to reduce tax due on income subject to the additional rate and dividend additional rate of income tax. In addition, deficiency relief triggered by the surrender of a policy on or after 6 April 2010 may be restricted where the main purpose of an individual being a party to arrangements is to secure a tax reduction greater than the income tax due on earlier chargeable events that led to the relief. This provision will apply to arrangements made on or after 22 April 2009 that culminate in the surrender of the policy on or after 6 April 2010.

Financial Services Compensation Scheme

The Finance Bill will introduce legislation to provide the power to make regulations to ensure that, where the Financial Services Compensation Scheme intervenes to protect policyholders with insurance or annuity contracts, the tax treatment will broadly be the same as if it had not intervened. This will prevent an intervention under the scheme from having unintended consequences such as the loss of tax-advantaged status. This measure will take effect from the date of Royal Assent to the Finance Act.

Restriction of Tax Relief for Pension Contributions

As previously announced in last year's Budget and Pre-Budget Report, for 2011/12 onwards tax relief on pension contributions for individuals with income over £150,000 will be gradually tapered. Those individuals with income over £180,000 will receive only basic rate relief on their contributions. The restriction of tax relief will be achieved by means of an income tax charge via the self-assessment tax return. As well as affecting individuals whose total income (computed before deduction or relief for pension contributions and charitable donations) is £150,000 or over, the restriction will also affect those whose income (similarly computed) is £130,000 or over but whose income together with the value of any employer pension contributions is £150,000 or over.

For 2009/10 and 2010/11 anti-forestalling measures are in place to prevent individuals increasing their pension contributions before the new rules take effect.

INHERITANCE TAX

Inheritance Tax Nil Rate Band

As already announced in the 2009 Pre-Budget Report, the inheritance tax nil rate band will remain at the current level of £325,000 for the 2010/11 tax year. This freeze will now be extended so that the nil rate band will remain at £325,000 until the end of 2014/15.

TRUSTS

Tax Changes for Certain Trusts Compensating Asbestos Victims

A measure is announced which benefits trusts which were set up on or before 23 March 2010 for the benefit of victims of asbestos related conditions. The measure exempts trustees of such trusts from CGT, IHT and income tax. The changes apply from 6 April 2006 and the Government intends to legislate them in the next Parliament.

Tax Repayments on Settlor-Interested Trusts

New legislation to be introduced in the next Parliament will require settlors of settlor-interested trusts to pay any tax refunds they receive on the trust income to the trustees. These repayments will be disregarded for inheritance tax purposes. The new rules are expected to apply to repayments relating to income tax chargeable from 6 April 2010.

ADMINISTRATION OF TAX

Penalties for Late Filing of Returns and Late Payment of Indirect Taxes

Following three separate consultations, new penalties are to be introduced for late filing of returns relating to various indirect taxes and for late payment of such taxes. The taxes covered include VAT, insurance premium tax, aggregates levy, climate change levy, landfill tax and excise duties. The implementation of the penalties will be staged over a number of years.

Under the new rules there will be an escalating series of penalties depending on the number of failures within a set penalty period. Failure to file a quarterly return by the filing date will trigger a penalty period of one year and an immediate £100 penalty. Increased fixed penalties will then apply to subsequent failures within the period, and the period itself will be extended accordingly. Additional penalties of 5% of the tax on the return will be charged for continuing failure six and twelve months after the filing date. Penalties of up to 100% of the tax will be charged where the failure is intended deliberately to withhold information to prevent HMRC correctly assessing the tax.

Failure to pay tax due quarterly will also trigger a one-year penalty period although no immediate penalty will apply. A second failure in the period will attract a penalty of 2%, a third failure a 3% penalty and further failures a 4% penalty. Again, the penalty period is extended with each failure. Additional penalties of 5% of the tax will be charged for continuing failure six and twelve months after the due date.

Similar penalties will apply in relation to monthly returns and payments.

Offshore Tax Evasion

Legislation will be introduced in the Finance Bill to ensure larger penalties apply to those who fail to provide a full account of their offshore income tax or capital gains tax liabilities. These new penalties below will apply to tax periods commencing on or after 1 April 2011. Penalties for under-declaration of tax are determined by FA 2007, Sch 24 (penalties for inaccuracies in returns), FA 2008, Sch 41 (penalties for failure to notify) and FA 2009, Sch 55 (penalties for failure to make a return). Each Schedule provides for tax-geared penalties and such penalties are determined by the behaviour of the taxpayer and the quality of disclosure.

- Where the non-compliance occurs in a jurisdiction which has provision to exchange information on savings income automatically with the UK, the penalty percentages will be the same as those currently applicable in the Schedules that already exist for non-compliance arising in the UK.
- Where the non-compliance arises in a jurisdiction which has agreed to exchange information with the UK, but does not automatically share that information, the penalty percentages will be 1.5 times those set out in the existing Schedules.
- Where the non-compliance arises in a jurisdiction which has not agreed to exchange information with the UK, the penalty percentages will be double those set out in the existing Schedules.

Security for Payment of PAYE

The Finance Bill will introduce legislation to amend ITEPA 2003, s 684 so as to allow HMRC to issue notices requiring financial security from employers where payments of PAYE or NIC are seriously at risk. The amount of security will be set by HMRC in the light of the potential tax liability. The detailed arrangements for the security will be set out in regulations, which will provide a right of appeal against the imposition of the security and its amount. The draft regulations will be published on the HMRC website, and there will be a 12-week consultation period. Failure to provide security where required will be a criminal offence, which may lead to a fine of up to £5,000. It is intended that the operative date for this legislation will be 6 April 2011.

Excise Modernisation and Compliance Checks

The Government is to introduce legislation which will bring the compliance checking framework for excise duties into line with other duties and taxes. In particular:

- the high-level rules for record-keeping will be aligned. Detailed record-keeping rules will not be affected;
- information and inspection powers will be updated;
- the standard time limit for making claims will be increased from 3 years to 4 years.

The record-keeping and amendments to information and inspection powers will have effect from 1 April 2011. The changes to time limits require a transitional period and will not become fully effective until 1 April 2012.

BUSINESS TAX

Increase in the Amount of Annual Investment Allowance

The maximum amount of the annual investment allowance (AIA) will be increased from £50,000 to £100,000 for expenditure incurred on or after 6 April 2010 for businesses chargeable to income tax, and on or after 1 April 2010 for businesses chargeable to corporation tax. The maximum amount of the AIA will be pro-rated where a business has a chargeable period which spans the operative date of the increase. Anti-avoidance legislation will be introduced to disapply property loss relief against general income to the extent that the loss is attributable to the AIA for any losses arising as a result of tax avoidance arrangements entered into on or after 24 March 2010 where, broadly, the main purpose of the arrangements is obtaining a reduction in tax liability.

Capital Allowances for Expenditure on Cushion Gas

With effect from 1 April 2010 expenditure on cushion gas will be treated for capital allowances purposes as special rate expenditure, qualifying for writing-down allowances at 10%. All leases of cushion gas commencing broadly on or after 1 April 2010 will be treated as funding leases.

Capital Allowances on Environmentally Beneficial Technology

Permanent magnet synchronous motors and biomass-fired warm air heaters will be added to the list of technologies, expenditure on which qualifies for 100% first-year allowances. Compact heat exchangers and liquid pressure amplification will be removed from the list. The criteria for taps and showers qualifying for the allowances will also be tightened. The changes will have effect on or after a date to be appointed by Treasury Order.

100% First-Year Allowances on Zero-Emission Goods Vehicles

A 100% first-year allowance is announced for goods vehicles which produce no CO_2 emissions. The allowance is available on expenditure incurred on or after 1 April 2010 and before 1 April 2015 for corporation tax or on or after 6 April 2010 and before 6 April 2015 for income tax.

As a result of state aid rules there are a number of restrictions to the availability of the allowance and a cap on the amount of expenditure which may qualify.

Sale of Lessor Companies: Option to Elect

CTA 2010, ss 382–431 (deriving from FA 2006, Sch 10) are intended to prevent a loss of tax when a lessor company changes hands, by calculating a charge and matching relief designed to recoup the tax timing benefit enjoyed by the selling group and returning it to the buying group. The Finance Bill will include legislation to offer companies the opportunity to opt for an alternative treatment that is intended to recoup the tax timing benefit by isolating the profits of the business following the sale of the company as an alternative to an immediate charge. The legislation will differ from the draft legislation which was published at the time of the Pre-Budget Report, in order to:

- preserve entitlement to capital allowances on expenditure in some circumstances;
- ensure that the legislation will operate fairly where the lessor company is a controlled foreign company or leases ships into tonnage tax; and
- address a flaw in the draft that would have allowed a lessor company owned by a consortium to contrive to end the period during which profits are isolated without the tax timing benefit being recouped in full.

Changes that benefit the taxpayer will take effect from 9 December 2009, while other changes will take effect from 24 March 2010.

Corporation Tax Relief Removed for Release of Loans to Participators

Finance Bill 2010 will amend the corporation tax rules relating to the write-off or release of loans to 'participators' made by 'close companies'. Corporation tax relief will be denied for a debit in the accounts arising from the write-off or release of such a loan on or after 24 March 2010.

The person to whom the loan is made will continue to be treated as if they had received a distribution.

Bank Payroll Tax

The Government has confirmed that the bank payroll tax announced in the Pre-Budget Report will be enacted in the 2010 Finance Bill. The tax will be chargeable on banks and building societies, on awards of bonuses over £25,000 made to, or in respect of, certain employees in the period 9 December 2009 to 5 April 2010. It will be charged at 50% on the aggregate of the excess of each bonus over £25,000 awarded in the above period.

A number of changes to the previously published draft legislation are to be made to clarify the scope of the tax and to provide machinery for assessment and collection.

Worldwide Debt Cap

A number of changes have already been pre-announced in relation to the worldwide debt cap regime following consultation with business. (A summary of these can be found in the Pre-Budget Report (PBR Note 4).) These changes aim to ensure that the provisions operate as originally intended. In addition, it has been announced that further provisions will be enacted in relation to securitisation companies which will:

- ensure that the results of any securitisation companies are not included in group consolidated accounts when calculating the financing costs of the group as a whole;
- include a regulation-making power to enable companies involved in capital market arrangements to transfer any additional corporation tax liability incurred as a result of the debt cap regime to another group company.

Risk Transfer Schemes

The legislation relating to risk transfer schemes was announced in the 2009 Pre-Budget Report and applies broadly from 1 April 2010. It has effect in relation to financial instruments that are treated for tax purposes as loan relationships or derivative contracts. In order to counter any avoidance that might be undertaken by affected companies, a regulation-making power will be introduced, subject to the negative resolution power, to extend the scope of the original provisions, as necessary, to cover other instruments held on trading account by financial traders.

UK Real Estate Investment Trusts and Stock Dividends

Legislation is planned for the next Parliament to relax the rules on distributions by UK real estate investment trusts (REITs). Currently, in order to meet the conditions to qualify as a REIT, the company (or group of companies) must distribute at least 90% of the profits from its rental business to its shareholders by way of a cash dividend. From the date of Royal Assent, any stock dividends issued by the REIT to its shareholders will also be included to determine if 90% of the profits have been distributed.

Furnished holiday lets

The abolition of the special rules for furnished holiday lettings are to be dropped from FB 2010.

This means that the existing rules under which certain holiday lettings are deemed to be a trade will continue. We understand that this will include holiday lets in the EEA as well as in the UK but further clarification of the detail is expected. If a labour government is re-elected this measure may be reintroduced, although whether it will apply for the current year remains to be seen. The conservatives are clear that they will retain the special treatment if they are elected.

CORPORATION TAX

Corporation Tax Main Rates

There is to be no change in the main rates of corporation tax. The main rate of 28% for financial year 2010, commencing on 1 April 2010, was fixed in FA 2009. The Finance Bill will set the main rate for financial year 2011 at 28%. The main rate for ring-fenced oil industry profits was fixed at 30% for financial year 2010 and will remain at 30% for financial year 2011.

Corporation Tax Small Profits Rate

There is no change in the small profits rate of corporation tax. The Finance Bill will set the rate for financial year 2010 at 21% and the fraction used in calculating marginal relief will be unchanged at 7/400. The December 2009 Pre-Budget Report announced that an increase in the small profits rate to 22%, originally planned to take effect from 1 April 2009, would be deferred until 1 April 2011.

The small profits rate for ring-fenced oil industry profits will be unchanged at 19% for financial year 2010, and the marginal relief fraction for such profits will remain at 11/400.

Capital Distributions

Legislation will be introduced to put beyond doubt the treatment of certain distributions received by UK companies. Essentially the provisions will confirm HMRC's existing practice of treating all UK distributions as being of an income nature unless they are specifically excluded. The legislation will have retrospective effect (although companies can elect for the legislation not to apply retrospectively).

Changes in Accounting Standards

Following a period of consultation and draft legislation issued on 12 February 2010, regulation-making powers contained in the rules on loan relationships and derivatives will be extended. The purpose of this is to enable the tax rules to be changed where necessary in line with changes in accounting standards implemented by the International Accounting Standards Board (IASB) and UK Accounting Standards Board (ASB). This legislation will have effect from the date that the Finance Act 2010 receives Royal Assent, but regulations allowed as a result may have retrospective effect.

Interest Harmonisation: Corporation Tax and Petroleum Revenue Tax

Corporation tax and petroleum revenue tax will be brought within the harmonised interest regime introduced in the Finance Act 2009. The new harmonised interest provisions will replace the current range of differing regimes with a single legislative framework for interest chargeable on late payments and payable on repayments and this will apply to all taxes and duties administered by HMRC. Interest will be charged from the date the tax or duty was due to be paid to HMRC until the date it is paid. HMRC will pay interest on repayments from the date the tax or duty was due to be paid or, if later, the date the payment was actually received, to the date the repayment is made. The statutory description of interest for each of these taxes will be 'late payment interest' and 'repayment interest'. These changes will take effect from a date to be specified by Treasury Order. The rules for quarterly instalment payments remain unchanged and do not form part of the harmonised rules that will apply to corporation tax.

Life Insurance Companies: Apportionment of Income and Gains

The apportionment rules relating to life insurance companies will be modified in an attempt to ensure that deferred profits are taxed on an appropriate basis, and to prevent attempts to avoid the application of these rules by transferring non-profit business from one fund to another. This change will take effect from 24 March 2010.

CHARITIES

UK Charity Tax Reliefs for Certain European Organisations

Legislation will be introduced to extend UK charity tax reliefs to certain organisations equivalent to UK charities and Community Amateur Sports Clubs (CASCs) in the EU, Norway and Iceland. Other changes will also be made.

A new definition of an organisation eligible for charity tax reliefs and exemptions will be introduced. Broadly, the organisation must be set up for charitable purposes only, be located in an EU member state or other specified territory (currently Norway and Iceland), be regulated in their home country and be supervised by 'managers' who are 'fit and proper' persons. CASCs will also be required to meet the 'location' and 'managers' conditions.

Further changes will ensure that:

- organisations apply donations received under payroll giving for charitable purposes in order to obtain tax exemption;
- UK charities making payments outside the UK take more steps to ensure monies are used for charitable purposes;
- certain rules relating to Gift Aid apply equally to UK resident and non-UK resident donors; and
- new procedures for making tax repayments to charities under Gift Aid will apply.

Most of the new rules will have effect later in 2010/11, although restrictions on payments of charity funds overseas and payroll giving will apply with effect from 24 March 2010 and the new definitions and Gift Aid provisions will apply to donations made on or after 6 April 2010. Claims to tax relief in respect of certain donations made to non-UK charities between 28 January 2009 and 31 March 2010 inclusive will be considered.

ANTI-AVOIDANCE

Share Incentive Plans

Currently companies can obtain a corporation tax (CT) deduction where they make payments to the trustees of an employee Share Incentive Plan (SIP) to purchase shares from non-corporate shareholders for use in the SIP. There is no provision for the deduction to be denied in cases where the company makes the payment without any intention that shares will genuinely be passed to employees under the SIP. This has led to avoidance schemes. The company carries out transactions that alter the share capital or the rights attaching to the shares, so that employees in the SIP receive few if any shares carrying real value. The transactions effectively strip away the value of shares held in the SIP.

In relation to payments made and alterations to share capital or rights attached to shares taking place on or after 24 March 2010, CT deductions will not be allowed where a payment to a SIP trust is made as part of a tax avoidance scheme, where the main purpose or one of the main purposes of the company in making the payment is to obtain a CT deduction. The proposed legislation will also close a potential loophole in the rules allowing HMRC to withdraw approval of a SIP where alterations to share capital or changes in rights attaching to shares materially affect the value of participants' plan shares.

Company Share Option Plans

Under an approved Company Share Option Plan (CSOP), a director or employee can be awarded options over shares with a market value of up to £30,000 at the time of the grant. Provided the requirements of the scheme are met, there is no charge to income tax or national insurance contributions on the exercise of the option.

HMRC have discovered that arrangements are being used which fall under the general description of 'geared growth' and which can be used to deliver additional reward to employees beyond that intended under the schemes. This avoidance involves share options granted over shares in companies that are under the control of a listed company. To counter this avoidance, with effect in relation to options granted on or after 24 March 2010, CSOP share options can no longer be granted over shares in a company which is under the control of a listed company.

Companies will be allowed a transitional period of six months to amend their scheme rules, if necessary, to bring them into line with this change.

Transactions in Securities

Legislation is to be introduced to replace the existing 'transactions in securities' anti-avoidance legislation with 'clearer legislation targeted more effectively at arrangements involving tax avoidance'. The effect of the legislation will continue to be to counteract the income tax advantage obtained from the transaction. The measure will generally have effect for transactions where the tax advantage is obtained on or after 24 March 2010.

The new legislation will make it clear how the tax advantage is to be quantified but will continue to counteract it in the same way. A wider range of companies will be covered but the new income tax advantage test and a new exemption covering fundamental changes in ownership of close companies (broadly companies under the control of five or fewer participators) should mean that fewer people need to consider whether the legislation applies to them.

Double Tax Relief Avoidance

Provisions will be introduced to counter certain avoidance in relation to double tax relief (DTR).

In particular, legislation will be introduced to confirm that a person may only deduct foreign tax from any foreign income if that person has included the foreign tax in his taxable income. Furthermore, in relation to manufactured overseas dividends (MODs), regulations have been laid to ensure that where certain financial traders have used the MOD rules to offset foreign tax against a liability to pay tax on a MOD it pays, they cannot also claim relief under the DTR rules.

The amendments made by primary legislation will have effect for foreign tax paid on or after 1 April 2010 (for corporation tax purposes) or 6 April 2010 (for income and capital gains tax purposes). The amendments made to secondary legislation have effect in relation to MODs paid 21 days after 24 March 2010.

Disclosure of Tax Avoidance Schemes (DOTAS)

Amendments will be made which are intended to toughen the DOTAS regime.

The new provisions include the following:

- a new trigger point for disclosure which will be the date when the scheme promoter first communicates a fully designed scheme to a third party;
- a requirement that a person introducing a client to the scheme must provide HMRC with the client's name and address and details of the scheme promoter;
- increased penalties for non-disclosure; and
- a requirement that promoters must provide details of clients implementing notifiable schemes.

Regulations will be introduced which extend the definition of 'hallmarks' for disclosable schemes.

NICs regulations will be introduced to mirror DOTAS legislation as it applies to income tax.

It is expected that these measures will have effect from a date in autumn 2010.

VALUE ADDED TAX

Registration and Deregistration

With effect from 1 April 2010, the VAT registration threshold will be increased from £68,000 to £70,000. The deregistration threshold will be increased from £66,000 to £68,000. The registration and deregistration thresholds for acquisitions from other EU member states will also be increased from £68,000 to £70,000.

Change to Zero-Rating of Qualifying Aircraft

The definition of aircraft which may be supplied at the zero rate will be amended with effect in relation to supplies made on or after 1 September 2010. From that date, zero-rating will apply to supplies of aircraft 'used by airlines operating for reward chiefly on international routes'. (The current definition refers to aircraft weighing not less than 8,000kg, and neither designed nor adapted for recreation or pleasure.)

This change is to bring UK legislation into line with EU legislation.

Gas, Heat and Cooling: Changes to VAT Treatment

With effect from 1 January 2011, the application of the reverse charge to certain supplies of gas and electricity will be extended to supplies in all categories of natural gas pipeline, where the pipeline is situated in the EU or is linked to such a pipeline. The reverse charge will also apply to heat and cooling supplied through networks.

In addition, the import VAT relief (in the form of zero-rating) will apply to all natural gas, heating and cooling imported via a network (including liquefied natural gas by tanker).

Postal Services

With effect from 31 January 2011, the exemption for supplies of postal services by Royal Mail will be restricted to those services which are made under a licence duty, i.e. public postal services and incidental goods. Other services (such as those made by Parcelforce) will become standard rated.

Reverse Charge for Emissions Allowances

With effect from 1 November 2010, a purchaser of emissions allowances will be required to account for the VAT due under the reverse charge procedure. This is an anti-fraud measure and will replace the zero-rating of such supplies which was brought in as an interim measure on 31 July 2009. There will be no additional reporting requirements.

Changes to Lennartz Accounting

The Lennartz procedure, under which a business may initially recover VAT in full on the purchase of an asset even where there is an element of non-business use, is to be changed. Amendments to VATA 1994 will:

- distinguish between business input tax and non-business VAT;
- ensure that VAT is not recoverable on the private use of a 'relevant asset';
- ensure that VAT is not recoverable on the private or non-business use of specified assets.

The capital goods scheme will be amended to take into account changes in the business/private use of an asset.

As a revenue protection measure taxpayers who choose not to 'unravel' existing arrangements will be required to continue to account for output tax under the Lennartz mechanism.

The changes will also remove the need for the legislation concerning the recovery of VAT on directors' accommodation.

The changes will, for the most part, apply from 1 January 2011, with the proviso that the revenue protection measure will be deemed always to have had effect.

STAMP TAXES

Stamp Duty Land Tax: Rates and Thresholds

The Finance Bill will introduce a higher rate of stamp duty land tax of 5% for purchases of residential property where the consideration exceeds £1m. This rate will apply to residential purchases where the effective date (normally the date of completion) is on or after 6 April 2011.

Stamp Duty Land Tax: First-Time Buyers

For a limited period of two years, the Finance Bill will introduce relief from stamp duty land tax for purchases of residential property up to £250,000 where the purchaser (or all the purchasers) are first-time buyers and intend to occupy the property as their only or main home. This relief will be available for residential purchases where the effective date (normally the date of completion) is on or after 25 March 2010 and before 25 March 2012.

Stamp Duty Land Tax and Partnerships

The rules relating to stamp duty land tax and partnerships have been exploited to contrive a partnership relationship between the vendor and purchaser in order to reduce the chargeable consideration and thus the tax due. The Finance Bill will introduce legislation to prevent the exploitation of these rules, broadly with effect from 24 March 2010.

Overpayments of Stamp Duty Land Tax and Petroleum Revenue Tax

The error or mistake relief rules relating to stamp duty land tax and petroleum revenue tax will be amended with effect from 1 April 2011. The time limit for claiming repayments will be reduced from six years to four years. The requirement that the overpayment must be the result of a mistake in a return, and that it must be made under an assessment, will be removed. The current restrictions on the right of appeal will also be removed. These changes will bring the rules for these taxes into line with those already applying for income tax, capital gains tax and corporation tax.

Clearing Houses and Stamp Duty

The Finance Bill will include legislation to make it explicit that the power to make regulations under FA 1991 to remove multiple charges to stamp duty or stamp duty reserve tax extends to regulations providing relief to members of clearing houses and their nominees. This had been questioned by a recent Select Committee Report, leading to some confusion and uncertainty among participants in financial markets. This clarification will take effect from the date of Royal Assent to the Finance Act, but to provide clarity in respect of regulations that have already been made, the amendments will be regarded as always having had effect.

STOP PRESS

The 50p per month tax on phone lines will not go ahead.

Personal Tax

Company car strategy through to 2012/13

Taxable benefit for the car

The income tax charge on the benefit of having a company car for private use has been announced for all tax years up to and including 2012/13. As such, a robust tax strategy can now be established for a range of companies and their employees so as to fully take into account the tax exposure.

The amount charged as a benefit is based on a % of the list price of the car, graduated according to the level of the car's carbon dioxide emissions. Business mileage levels are ignored, as is the actual private use and the age of the car. The graduation is in 1% steps for every additional 5 grams per kilometre, with a maximum charge of 35%. There is a car price cap of £80,000, but that ceases to apply from 2011/12. That means that a car costing £200,000 (mainly banker territory!) has an annual tax charge on £28,000 to 5 April 2011, increasing then to £70,000.

The level of CO2 emissions qualifying for the basic minimum 15% charge is 135 g/km for 2009/10; 130 g/km for 2010/11; 125 g/km for 2011/12; 120 g/km for 2012/13. There is a lower charge of 10% of list price where CO2 emissions do not exceed 120 g/km, but that level reduces to 99 g/km from 2012/13.

There is a 2% discount if the company car is capable of running on E85 biofuel, but that discount ceases to apply from 2011/12.

Diesel cars emit less CO2 than petrol cars and so would be taxed on a lower % of list price than an equivalent petrol car. However, diesel cars emit greater quantities of air pollutants, and accordingly a supplement of 3% of the list price applies – e.g. a diesel car, which would give rise to a 20% charge on the basis of its CO2 emissions, is instead charged at 23%. The maximum charge for diesel cars is capped at 35%. The 3% supplement did not apply to a diesel car that met the Euro IV emissions standard for cleaner cars, but it did so from 2006/07 if the car was first registered after 31 December 2005, and in all other cases it also does so from 2011/12.

The position for alternative fuel vehicles is that they will usually have CO2 emissions of not more than 120 g/km so start at a base of 10% of list price. They then enjoy a 3% discount, resulting in a tax charge on 7%. That discount ceases to apply from 2011/12. The position of the Lexus RX450h hybrid continues to be unique. It has CO2 emissions of 148 g/km but still receives a 3% discount until 2011/12 plus, as a hybrid, reduced road fund tax and exemption from the London congestion charge. It does 0-60mph in 8.7 seconds.

Electric-only cars with nil CO2 emissions enjoy a 6% discount on the basic 15%, resulting in a tax charge on 9%. From 6 April 2010 (for a 5 year period) the tax charge is on NIL. That also will be the case for an electric van from that date, in place of the current tax charge on £3,000.

Private use fuel tax charge

The tax charge is based on the same % used in calculating the taxable car benefit which therefore takes into account supplements and discounts. The % is then applied to a fixed amount of £16,900 for 2009/10, increasing to £18,000 for 2010/11.

Advisory fuel rates for company cars

Published guidelines are issued by HMRC. The stated aim is to save time for all concerned by setting out figures which they reckon can be used in the majority of cases

They are only advisory, and can apply where the employer reimburses the employee for fuel for business travel in a company car or where the employer requires the employee to repay the cost of fuel for private travel in a company car.

They are reviewed every 6 months, but more frequently at HMRC's consideration if fuel prices fluctuate by 5% from the current rate and that is likely to be sustained.

From 1 December 2009 the rates are as below based on petrol at 108.7p per litre:

Engine size	*Fuel cost per mile*		
	Petrol	*Diesel*	*LPG*
to 1,400 cc	11p	11p	7p
1,401 to 2,000cc	14p	11p	8p
over 2,000 cc	20p	14p	12p

Tax strategies

The electric company car is a rare vehicle, due no doubt to the premium price and limited range before recharging. Both of these issues are being addressed. There will also over the next few years be a wider range of electric cars on the market and more recharging points will be available.

A company car with a nil tax charge will be a very attractive proposition where the recharging issue is not a problem given the particular pattern of private use. In particular, a family company could provide company electric cars for members of the family (including those who do not work for the company) and there is likely to be a place for at least one electric car in most families.

Qualifying low emission cars (QUALECS) give a 100% FYA to the company provided the following conditions are met:

- expenditure incurred to 31 March 2013
- CO2 emissions no more than 110g/km OR it is electrically propelled

For a bi-fuel car there is more than one emissions figure. The lowest certified figure is then used.

The new Stop and Start technology may well in time result in several desirable models qualifying for 100% FYA. The engine is automatically turned off and is in standby mode when the vehicle stops at traffic lights and in traffic jams. The engine instantly starts up again when the brake pedal is released, with the vehicle pulling away once the accelerator is pressed. In testing the Stop and Start system has reduced fuel consumption by 10% for city driving, 6% in a standard combined cycle and up to 15% in heavy traffic.

List of QUALECS

Model	List Price	Likely Discount	Co2 Emissions G/km	0- 60 Secs
Citroen C1 1.0i VT	£7,945	£1,000	106	13.7
Fiat 500 1.3 MultiJet	£9,700	nil	110	12.9
Fiesta 1.4 TDCi Studio	£12,195	£1,700	110	14.9
Fiesta 1.6 TDCi Econetic	£13,795	£2,000	98	12.3
Honda Civic 1.4i VTEC Hybrid ES	£17,970	£1,000	109	12.1
Honda Insight 1.3s	£15,890	£600	101	12.5
Mini Cooper 1.6D	£14,785	£150	104	9.9
Nissan Pixo 1.0 Visia	£6,995	nil	103	11.0
Peugeot 107 Urban Lite	£8,095	£1,200	106	14.2
Polo 1.4 TDi 80 BlueMotion 1	£13,105	£900	99	12.8
Seat Ibiza 1.4 TDi Ecomotive	£11,805	£1,000	98	12.9
Skoda Fabia 1.4TDI Greenline	£12,140	£1,600	109	13.2
Smart ForTwo Coupe 60 mhd Pure	£6,912	£150	103	16.7
Suzuki Alto 1.0 SZ2	£7,245	nil	103	13.5
Toyota Aygo VVT-i	£7,505	£450	106	14.2
Toyota IQ 1.0	£9,615	£450	99	14.7
Toyota Prius 1.8VVT-I T3	£18,590	£1,750	89	11.0
Volvo C30 1.6D Drive Start/Stop	£16,245	£1,000	104	10.7

Many of these cars are diesel-engined, so of course create a tax charge on 13% of list price rather than 10%. Road fund tax is low for these cars, at £35 per annum if between 101 and 110 g/km (£15 if using alternative fuel) or nil if not over 100 g/km.

In the right circumstances, members of a family can have a company car with low tax charges all round (NIL from 6 April 2010 if electric)

Illustration for 2009/10 and 2010/11

Mother runs a small company and decides to provide her 2 children with a company car each – Nissan Pixo 1.0 Vistia. They do not work for the company, and all mileage will be private. She is a 40% taxpayer. The tax position is as follows:

Income tax on mother per car:

List price £6,995 @ 10% = £699 @ 40% = £279 pa

Company's position per car:

100% FYA on £6,995 @ 21% = £1,469

Class 1A NIC on £699 @ 12.8% = £89 pa

Full VAT reclaim on input tax on car servicing etc.

Corporation tax relief on running costs and on £89 above

Contributed by Gerry Hart

Lecture P587 (12.24 Minutes)

Inside the Gaines-Cooper case

In a landmark case that has raised a fierce debate among the accounting community, the Court of Appeal ruled this week that HMRC did use the correct interpretation of the UK's non-resident policy, IR20, in the case of UK born entrepreneur Robert Gaines-Cooper. AccountingWEB spoke exclusively to Gaines-Cooper's chief legal adviser Peter Vaines of Squire, Sanders and Dempsey, who confirmed that his client is seeking leave to appeal to the Supreme Court.

Gaines-Cooper had appealed on the basis that he moved to Seychelles in 1976, but it was ruled that he never qualified for exemption from British taxes as a non-resident since he had not cut ties with the UK.

There was a domicile appeal, which went to the High Court and Court of Appeal back in 2008 but which Gaines-Cooper lost. The current case concerns the issue of residence and, with the Court of Appeal siding with HMRC's interpretation of the law this week, Gaines-Cooper has requested leave to take the case to the Supreme Court. No decision has been made as to whether he has been granted this leave as yet.

One of the key tenets of Gaines-Cooper's legal argument was the retrospective nature of HMRC's actions. "Mr Gaines-Cooper's view of the matter is that he was not aware of any implied conditions needing to be satisfied – and if those conditions had been articulated he would have satisfied them as well. For HMRC to come along later and to impose conditions which had not previously been mentioned is unfair – and it is this unfairness which was the basis of his appeal", said Vaines.

Despite this, HMRC maintains its interpretation has not changed. An HMRC spokesperson told us: "HMRC's interpretation of its guidance on residency in booklet IR20 was correct and the Court has agreed with HMRC that there has been no unannounced change of that interpretation".

Severing family ties
One of the problems in this case was the fact that Gaines-Cooper maintained an estate in Oxford, where his wife and child resided – meaning he had not fully 'cut ties' with the UK, according to HMRC's definition.

Vaines insists that this detail in particular is a red herring. "My client left the UK in 1976 to go to the Seychelles. He took advice and, satisfied that he had met the conditions of IR20, he left". Unfortunately, almost 30 years later, HMRC argued that he hadn't satisfied the conditions because he hadn't severed all social and family ties to the UK. Gaines-Cooper argued there wasn't such a condition in IR20, but HMRC said it was implied. "You can't just impose this new condition and say it was always implied", says Vaines. While HMRC may reserve the right to impose whatever conditions it chooses, backdating the rules is where the problems arise, he argues.

Nonetheless, Gaines-Cooper may now be liable for taxes dating back to 1993 – the total of which could reach an estimated £30m.

The law and politics
Many commentators have suggested that a statutory residence test could be on the cards, a suggestion Vaines welcomes but says is not without its own complexities. "For my part and for the people I advise, they don't need a statutory residence test – they just need some clear rules. Tell us what the rules are and we'll abide by them".

In a case that stretches as far back as 1996, it's interesting that the final hearing (should it indeed be heard at the Supreme Court) happens to be in an election year. Could the pressure be on for HMRC to catch 'tax exiles'? "I don't think that's the case", counters Vaines. "I can see the argument, but I think the revenue and the courts should be above those things and I think they are. There might be pressure to collect more money, but I'm sure there won't be a political influence. That wouldn't be right".

AccountingWeb, 19 February 2010

Lecture P588 (12.49 Minutes)

Special Annual Allowance Charge: Protected Pension Input Amounts

The Special Annual Allowance rules are in Schedule 35 of Finance Act 2009. Guidance on this legislation is included in Chapter 15 of the Registered Pension Schemes Manual - www.hmrc.gov.uk/manuals/rpsmmanual/rpsm15100000.htm. This will be updated as soon as possible to include additional guidance about this Order. A brief overview of this is however given below.

The Special Annual Allowance Charge (Protected Pension Input Amounts) Order 2010 (SI 2010/429) extends protection against the special annual allowance charge in three particular instances:

– where there is a change in pension provider on or after 22 April 2009,

– for contributions which an individual or an individual's employer was contractually committed to at 22 April 2009 but which had not actually commenced on that date, and

– for certain lump sum contributions made on 22 April 2009.

Change of Pension Provider

Where an individual ceases to make protected contributions into a money purchase scheme (other than cash balance ones) that is not an occupational scheme and within 3 months commences to make regular contributions to another such scheme, those contributions will be protected under the new arrangement to the extent that they are paid at the same rate as agreed under the old arrangement.

Where an individual ceases to be an active member of an occupational scheme and within 3 months becomes an active member of a new scheme either because the individual's employer had entered into a re-organisation of its pension arrangements and the change was a consequence of that re-organisation or because of a relevant business transfer as described in paragraph 12(8A) Schedule 36 FA 2004, then contributions to the new arrangement will be protected. For a money purchase scheme the contributions are protected to the extent that they do not exceed the rate of contributions paid under the old arrangement. For defined benefit and cash balance schemes the input amount under the new arrangement is protected to the extent that it does not exceed what would have been the protected input amount under the old arrangement. However, for defined benefits and cash balance schemes there is an additional requirement that there must be no material difference between the rules under which benefits accrued for the old arrangement and the rules under which benefits accrued for the new arrangement.

If an individual was paying additional voluntary contributions (AVCs) into a money purchase arrangement under an occupational scheme arrangement, any AVCs paid under the new arrangement are protected to the extent that they do not exceed the rate of contributions paid under the old arrangement, provided the new arrangement meets the relevant conditions outlined above.

Similarly if an individual was paying relevant added years' contributions into a defined benefit scheme, added year contributions paid under the new arrangement are protected but only up to the figure that would have been protected under the old arrangement.

Contractually Committed Payments

Where on or before 22 April 2009 an individual's employer had made, in writing, a contractually binding offer to make a lump sum contribution and this offer had been accepted in writing by the individual on or before 22nd April 2009, the payment is a “protected pension input” provided it was made under the terms of the agreement and was paid by any date specified in the agreement.

Where not later than 22 April 2009 an individual's employer has entered into a binding contractual offer to provide new regular contributions or benefits for an employee, those contributions or benefits are “protected pension inputs” provided the arrangement was entered into, in writing, before 22 April 2009 and was accepted, in writing, by the individual also before 22 April 2009, regardless of when any contributions are first paid.

Lump Sum Payments Made On 22 April 2009

Protection for contributions paid less frequently than quarterly made in relation to money purchase arrangements that are not cash balance arrangements in the period beginning on 6 April 2009 and ending on 21 April 2009 is extended to payments made on 22 April 2009 as well.

Stage Management–Revised HMRC guidance on employment status

An agreement was reached between Inland Revenue (as it was then), Equity and the Theatre's National Committee in 1994 that stage managers, deputy stage managers and assistant stage managers who enjoyed similar terms of engagement to actors and who carried out their profession in the same way would be subject to the Revenue Guidance on the Tax Treatment of Theatrical Performers/Artists, published on 31 August 1994. This was on the understanding that, in addition to their normal duties, there was an expectation that stage management personnel at every level would, where required, undertake to perform understudy duties in rehearsals or appear on stage in costume or in blacks.

Where the relevant conditions were satisfied stage management would be accepted as falling within the McCowen & West criteria, as described in the above guidance, and, therefore, self employed for tax purposes but normally liable to Class 1 NICs.

It had become increasingly apparent to HMRC over the intervening years that in some cases there was no contractual obligation or any expectation for stage managers to appear in productions in practice and HMRC raised those concerns at a recent meeting with Equity.

Revised Guidance

At that meeting the various stage management roles in theatre productions were discussed as well as the results of a recent Equity survey of stage management members and consequently HMRC has issued the following supplementary guidance to ensure that the correct tax treatment is applied to stage management for the future:

Stage management will continue to be considered as entertainers in accordance with tax and NIC legislation where they are required to undertake stage management duties as a company and stage manager (dual role), stage manager, deputy stage manager or assistant stage manager in accordance with a standard Equity contract. It is understood that within the Equity terms they may be required to carry out stage management duties in a performance on stage, in costume or may be required to wear blacks.

An engagement solely as a company manager will not be considered an entertainer and, therefore, will be subject to the normal status rules.

Any non-standard contracts will be considered on their own merits and in any case where the contractual requirement to appear on stage is overridden by agreement or through custom and practice the status should be determined by the normal case law process. See HMRC guidance at www.hmrc.gov.uk/employment-status/index.htm.

The guidance notes for Theatrical Performer/Artists only apply where the stage manager, deputy stage manager or assistant stage manager is engaged for no longer than the run of a production or a short fixed period and do not apply to permanent (or long term) engagements.

If any individual stage management member is unsure whether a Particular engagement meets the HMRC criteria to be considered an entertainer they should seek advice from their Equity or Stage Management Association representative or ring the HMRC Helpline on 0845 9154655 begin_of_the_skype_highlighting 0845 9154655 end_of_the_skype_highlighting and ask to speak to a member of the Employment Status Customer Service team.

Employees - resident but not ordinarily resident in the UK–SP1/09 extended

Statement of Practice 1/09 (SP1/09) took effect from 6 April 2009 and covers the tax treatment of employees who are resident but not ordinarily resident in the UK, who have a single contract of employment covering both UK and overseas duties.

When SP1/09 was introduced, the intention was that it would apply for one year, before being legislated in Finance Bill 2010. Since April 2009 HM Revenue & Customs (HMRC) has worked towards this aim, including consultation and meeting with external stakeholders. However, it has not been possible to resolve all the outstanding issues in time to legislate the practice this year.

In these circumstances, the Financial Secretary to the Treasury has agreed that SP1/09 will apply for a further year until 5 April 2011.

HMRC will continue working with stakeholders on the issues which remain unresolved, with the aim being that SP1/09 will be brought into legislation as part of Finance Bill 2011.

Kent v Revenue and Customs Commissioners

The appellant, an independent financial adviser (IFA), belonged to two approved personal pension schemes. Those schemes allowed for members' funds to be transferred to, inter alia, 'an occupational pension scheme approved under Chapter 1 of Part XIV of [TA 1988] to which the Member's Employer contributes or has contributed …' In August 2001 the appellant transferred his accrued benefits to another plan, the H Plan. The transferred benefits were used to purchase a deferred annuity for £55,354.54. The annuity was to pay £18,154.08 pa from the appellant's 75th birthday on 3 October 2010 and was payable by M Ltd, registered and based in Niue. The H Plan was approved by HMRC under TA 1998, Ch 1, Pt XIV with effect from 1 February 2001. HMRC opened an enquiry into the appellant's tax return for the year ended 5 April 2002 and concluded there had been an unauthorised transfer—within the meaning of TA 1988 s 647(2)(a)—of his funds out of two authorised pension schemes on the basis that he was not an employee of H Ltd. HMRC amended his tax return for that year to reflect an additional liability to tax of £18,568.15. In addition the appellant was assessed to a penalty of £5,557.74 under TMA 1970 s 95(1)(a) for negligently delivering an incorrect tax return. The appellant appealed. He submitted, inter alia, (i) he was an employee of H Ltd and his employment as a sales associate—

selling H Ltd brochures giving discounts on short term hotel breaks on commission—was genuine, as evidenced by the fact he had not received a loan back. He could not recall how many brochures he had sold and he had kept no records; he had not reported to a sales manager and had not worked fixed hours; and he had only worked for a few months; (ii) he had lost confidence in the stock market and wanted the security a guaranteed annuity would provide; (iii) he had had a written contract of employment. However he firstly claimed he had lost the contract but he then changed his evidence to say he had left it at home. HMRC produced as an exhibit an employment contract they had following an investigation into the H Plan. The appellant said that his employment contract was identical to that one. HMRC's case was that the H Plan was a pension liberation scheme and the scheme operators persuaded people who wished to realise their pension funds before their retirement age to become sham employees of H Ltd. A participator in the scheme would then request the transfer of his pension funds from his legitimate approved pension schemes to the H Plan which used the would-be employee's funds to buy an annuity which he could then use as security for an interest-free loan. The idea, HMRC alleged, was that the annuity would never be paid to the employee but similarly the loan would never be called in. HMRC alleged that the organiser of the scam would earn commission of 20% of the funds. If successful, the scheme would therefore leave the participators with 80% of the value of their pension fund as cash in hand at the current date rather than with 100% tied up in a pension fund inaccessible until they reached retirement age.

The tribunal found that the transfer of funds was an unauthorised transfer of the appellant's funds out of the two authorised pension schemes for the following reasons: (i) H Ltd and the H Plan were set up with the object of pension liberation. The motivation of the persons behind the operation of the company and its pension plan was no doubt to earn the 20% commission on the funds liberated. It was clear that the object of H Ltd and its directors was not to employ the would-be employees, including the appellant, but to give the appearance of employment sufficient for the would-be employees' accrued pension funds to be transferred into the H Plan; (ii) the appellant was not a witness of truth. He was an unreliable witness. It was inherently improbable that he would be prepared to exchange his funds for an annuity commencing in 2030 to be paid by a company based in Niue. Rather the appellant received his funds as a loan secured on the annuity; (iii) his motive in entering into his arrangements with H Ltd was to liberate his pension fund, and it was not his intention to become an employee of H Ltd but to appear to be an employee of H Ltd; (iii) he was not an employee of H Ltd. There was no employment contract. Even if there was a written agreement between the appellant and H Ltd, it was a sham as the motive of both parties in entering into it was to create the appearance of employment rather than actual employment; (iv) on the facts, there was no employment. The appellant failed to fulfil the necessary prerequisites for a contract of employment to exist, as set out in *Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance* [1968] 1 All ER 433. Condition (i) was not met as he was not required by his alleged contract of employment to devote any time to work and in particular to selling the brochures. At best it was an agreement under which he would be paid if he did sell the brochures. It did not oblige him to spend a minimum amount of time carrying out work for H Ltd. Nor was condition (ii) satisfied as the appellant did not have a manager and did not report to anyone. H Ltd exercised no control over what the appellant did and he was under no obligation to perform any service. Neither party intended to actually be a party to an employment contract with the other: both merely wished to give the appearance of it. It was a sham; and (v) he did not return any income from his connection with H Ltd and he was not paid by H Ltd. Accordingly the appellant was liable to tax under TA 1988 s 647(3) as the transfer out was for his benefit. Furthermore, in the light those findings of fact the appellant was at least negligent in completing his tax return in not drawing the transfer of funds to the attention of HMRC. It followed that the penalty imposed was correct. It followed that the appeal would be dismissed. Appeal dismissed.

Pensions—rates of tax

The Taxation of Pensions Schemes (Rates, etc) Order, SI 2010/536 comes into force on 24 March 2010 and makes amendments to the rate of two tax charges applying to pension schemes with effect from 6 April 2010. The rate of tax applicable when relevant benefits are received by persons other than individuals under EFRB Schemes is increased from 40% to 50%. The rate of tax on short service lump sum refunds is increased from 40% to 50% and the limit for the lower rate of tax is increased from £10,800 to £20,000.

Transactions in securities

When it comes to HMRC proposals for 'simplifying' legislation, one might be forgiven for being more than a little apprehensive. However, if there is one part of the tax code where a good dose of clarity and certainty would be warmly welcomed, it is surely the anti-avoidance provisions on transactions in securities.

Last year, HMRC issued a lengthy consultation document entitled 'Simplifying Transactions In Securities Legislation'. It contains various HMRC proposals which are intended to streamline and clarify the existing regime. It is hoped to include the revised legislation in FA 2010, although this outcome is still a little uncertain.

The original provisions were introduced in 1960 and were designed to put a stop to arrangements which sought to turn taxable income into tax-free capital – this was, of course, at a time when CGT did not exist. More specifically, they allow HMRC to counteract a tax advantage obtained by a taxpayer in consequence of:

1. a transaction in securities; or
2. the combined effect of two or more transactions in securities; or
3. the combined effect of one or more transactions in securities and the liquidation of a company.

The term 'transaction in securities' has a very wide meaning and includes the purchase, sale, exchange or issue of shares or securities.

The transaction in securities rules do not apply if the two conditions currently set out in S685 ITA 2007 are met:

1. the first is that the relevant transaction must be effected for genuine commercial reasons or in the ordinary course of making or managing investments; and
2. the second is that the obtaining of an income tax advantage must not be the main object (or one of the main objects) of the relevant transaction.

If there is doubt as to whether a transaction (or proposed transaction) might fall foul of the legislation which could lead to the issue of a counteraction notice, an application can be made to HMRC for a clearance that the provisions will not apply to the transaction in question.

One commentator has observed:

> 'Many small to medium-sized practices will, at best, submit only a handful of statutory clearance applications under S701 ITA 2007 to HMRC each year. Some will no doubt be uncertain whether transactions potentially fall within the transaction in securities legislation at all, because (to quote HMRC) the rules are "extremely complex and unnecessarily burdensome".

However, firms – quite understandably – invariably want the comfort of a letter stating HMRC's satisfaction that the transaction(s) is not one in relation to which a counteraction notice should be given. In other words, it is not caught by the anti-avoidance rules.'

It is interesting to examine the statistics. HMRC are on record as saying that, in 2008, nearly 6,000 clearance applications were made, 98% of which were accepted. Furthermore, 90% of the acceptances were processed in fewer than eight days because there was virtually no risk of the transaction in securities provisions applying. Looked at logically, these figures are a damning indictment of the existing regime and the very real uncertainty which it causes.

The proposed changes to be introduced from 6 April 2010 include the following:

- redefining and quantifying the term 'income tax advantage';
- introducing a new 'fundamental change of ownership' rule; and
- replacing 'relevant company' in the legislation with 'close company'.

The revised transaction in securities legislation will in future apply where all the conditions below are satisfied:

- the shareholder must be a party to one or more transactions in securities;
- the shareholder must receive relevant consideration (ie. consideration which is not taxable as income) in connection with the distribution, transfer or realisation of assets of a close company;
- the shareholder must be unable to take advantage of a new 'fundamental change of ownership' exclusion; and
- the shareholder's main purpose (or one of his main purposes) must be to obtain an income tax advantage and such an advantage must actually be obtained.

It is hoped that this approach will avoid the need for clearances to be sought in straightforward cases.

Fundamental change of ownership

A key component of the proposed new regime is the 'fundamental change of ownership' exclusion.

Transactions which meet this rule are completely removed from the anti-avoidance legislation. In broad terms, the 'fundamental change of ownership' rule will be complied with where throughout the two years following the relevant transaction such as a share sale:

- at least 75% of the company's ordinary share capital is held by third parties who are unconnected with the original shareholder; and
- these shares also carry an entitlement to at least 75% of the available distributions and voting rights.

This new 75% rule is based on current HMRC practice which is to grant clearances in those cases where there is a 75% change of ownership. The two-year period ensures that the change of ownership is sufficiently permanent. It is a pity that this previously unpublished practice was not made more widely known, eg. through a Statement of Practice, as it would undoubtedly have saved a great many advisers considerable time and effort in drafting unnecessary clearance applications.

Contributed by Robert Jamieson

Lecture B588 (12.30 Minutes)

Capital Gains Tax

Ahad v Revenue and Customs Comrs

The appellant acquired a right to build a restaurant on land in Milton Keynes from the development corporation, M. M was succeeded by the Commission for the New Towns, C, who approved the appellant's plans for the construction of the restaurant. On 13 August 1992 C granted the appellant and Mr D a 125-year lease in the land for £160,000 payable in instalments and agreed to transfer the freehold to the appellant for the nominal sum of £1 once the development was complete. The terms of a lease include a restrictive covenant, the effect of which was that the appellant and Mr D were prevented from assigning, underletting or transferring the lease. Local residents objected to the appellant's proposed development and he agreed to sell his interest in the land to A Ltd who wanted to build a supermarket on the land. On 29 March 1996 the appellant paid C £50,000 to remove the restrictive covenant from the lease. On the same day he bought Mr D's interest in the lease for £102,000 and sold his resultant share in the land to A Ltd for £360,000. HMRC issued an assessment charging capital gains tax on the gain for the tax year 1995-96. The issue arose as to whether the appellant could claim roll-over relief under TCGA 1992 s 247. The appellant submitted that although the actual person to whom he disposed of the land, namely A Ltd, was not a person who acquired or could have acquired the land compulsorily within the meaning of “authority exercising or having compulsory powers” in s 243(5), that definition should be construed to enable s 247 relief to be given in a case where, as in the present case, the disposal was to some extent involuntary, because of the existence of actual or possible compulsory purchase powers. C had the relevant powers under the New Towns Act 1981 (NTA 1981) ss 36 and 37 and “could be authorised to acquire” the land compulsorily on its own behalf or on behalf of A Ltd. On the facts C “effectively controlled the whole situation”. In the alternative the appellant submitted that C had succeeded to the functions of M, who had the requisite compulsory purchase powers and C must be taken to have acquired them on the succession. HMRC argued that C did not have compulsory powers to purchase land at the relevant time; that the powers under NTA 1981 s 36(3)(a) “to acquire (otherwise than by transfer under this Act) land” with the authority of the Secretary of State were not powers to purchase land compulsorily, but simply powers to acquire land if authorised to do so by the Secretary of State; and that TCGA 1992 s 243(5) should be construed so that an “authority exercising or having compulsory powers”, where it was not a person or body of persons actually exercising compulsory purchase powers, was a person or body of persons who was not only theoretically capable of being authorised to use such powers but would also have used such powers if necessary to acquire the land in question for the purposes for which it was actually acquired; and that M's power to purchase land compulsorily was not transferred to C.

The tribunal found that the roll-over relief on the compulsory acquisition of land under TCGA 1992 s 247 did not apply. The appellant disposed of the land to A Ltd but A Ltd was not an “authority exercising or having compulsory powers” within the definition in TCGA 1992 s 243(5). As A Ltd itself had no compulsory powers, it could only come within the definition if it was, in March 1996, a person for whom another person or body of persons—namely C—”has or have been, or could be, authorised so to acquire it”, which meant authorised to acquire the land, which had been transferred, compulsorily for the purposes for which it was (actually) acquired. The appellant had not shown that C was actually authorised to acquire the land on A Ltd's behalf. Nor was A Ltd a person for whom C could have been authorised to acquire the land compulsorily for the purposes of constructing a supermarket on it. As a matter of law C could not have been authorised to acquire the land compulsorily under NTA 1981 ss 36 and 37 for the purposes of constructing a supermarket on it. Whereas NTA 1981 s 10 clearly provided for a development corporation to acquire land compulsorily by means of an order made by the corporation and submitted to and confirmed by the Secretary of State and required the procedure for authorising compulsory acquisitions laid down in NTA 1981 Sch 4 to be observed, there was no reference to Sch 4 in ss 36 and 37 and so the powers were not compulsory powers. Furthermore, C could not have been authorised to acquire the land compulsorily for the purposes of constructing a supermarket on it on the basis that it had succeeded to the functions of M. The compulsory purchase powers were not transferred from M to C by NTA 1981 Sch 10 as the word “rights” in para 1(1) meant rights in the nature of property, and excluded the statutory right, or power, in a development corporation, with the Secretary of State's consent, to acquire land compulsorily. It followed that the appellant did not dispose of the land to "an authority exercising or having compulsory powers" and therefore the condition in TCGA 1992 s 247(1)(a) was not fulfilled in relation to the disposal in issue. The appeal would be dismissed.

Appeal dismissed.

Tribunal: John Walters QC and Michael Templeman, ***8 December 2009***

Skye Inns Ltd and anor v Revenue and Customs Comrs

The appellant company (S) had acquired two restaurants/pubs which were running at a loss. On 18 December 2001 one of the company directors (R) subscribed shares in S for £1.5 million so that S could purchase the O pub and use the profits from that pub to fund the losses at their two existing restaurants. In February 2002, 48 hours before simultaneous exchange and completion of contract, the vendor pulled out of the sale of O pub. Following the failed acquisition the directors continued with their search for an appropriate pub to buy but eventually decided to abandon that plan and concentrate on improving the existing restaurants. R claimed EIS relief in respect of the December 2001 share subscription. HMRC rejected the claim on the basis that a review of the company's accounts for the year ended 31 March 2003 revealed that the company could not have "employed" 80% of the funds raised in the December subscription in its business, because those accounts showed that on the balance sheet date, S still had £1.2 million on deposit with its bankers, and thus not "employed in the trade". The company and R appealed contending that S had been about to make a major acquisition in February 2002 that would have ensured that 80% of the moneys subscribed on 18 December 2001 would have been employed in S's business within the required 12-month-period to ensure compliance with the enterprise investment scheme (EIS) relief. It was only because the vendor backed out at the last minute that the acquisition fell through. Notwithstanding that, the directors had kept looking for new acquisitions and they certainly never decided to apply the cash fund elsewhere in some form of non-qualifying investment. Therefore the 80% test was met at the very point when the acquisition was about to be made. Alternatively, their continued intention to find a replacement property meant that the requirement was met for that reason; and since they retained that intention, it would be ridiculous for the tax requirements to force them to make an unattractive purchase and, on that basis, the tax test ought to be applied in a fairly flexible manner.

The tribunal considered that in circumstances, such as those in the present case, where the company had not actually yet entered into a contract to make a purchase, moneys that the company merely meant to employ in the business could not be said to be "employed" in that business for the purposes of satisfying the test for EIS relief. On the facts the relevant test could not be shown to have been satisfied in the few days before the vendor backed out of the proposed sale and it certainly could not be satisfied because it remained the directors' intention after February 2002 that some other pub acquisition would be made. It was highly unfortunate that the directors were faced with the unenviable choice of making an acquisition in order to satisfy the tax test, when they were not content that the acquisition was a prudent one, or they had to fail the tax test because they could not find a suitable replacement property. HMRC, however, could not be blamed for imposing that invidious choice on the directors and the company. The tax test imposed a definite time period within which different percentages of the cash raised by a share issued had to be employed in the trade, and no exception was permitted for the situation where the directors wanted to meet the test but were unable to do so. It followed that the appeal would be dismissed.

Appeal dismissed.

Inheritance Tax and Trusts

Freezing operations

In the last two years, there have been significant falls in the value of UK land and buildings. This has led some property investment clients to look at the possibility of 'freezing' that part of their estates for IHT purposes.

Shares in property investment companies rarely qualify for business property relief. Individuals with such assets therefore need to seek other alternatives in order to minimise their IHT liabilities. Typically, this will involve the client pegging the current (low) value of their property company shares and passing on any potential future growth to the next generation. This can be achieved either by an outright gift or by a transfer into trust.

The first step is to create a new class of growth share, usually by way of a bonus issue. These will only be entitled to dividends and participation in any winding up proceeds once the present value of the company has been distributed to the holders of the original shares. The rights attaching to these original shares are therefore altered to restrict their future dividends and winding up proceeds to an aggregate sum equal to the current value of the company – this will have the immediate effect of freezing their value at this amount.

The new shares will initially be worth very little – indeed, they may well have a nil value – but they should grow significantly over the next few years as and when the property market recovers. It is these new shares which are given to the donor's children or, alternatively, placed in trust (particularly if the growth in value could be substantial).

Illustration 1

Brian holds 100% of a company which owns various let residential properties. The value of this company is currently £2,000,000.

New 'B' shares are issued to Brian, with his original ordinary shares being redesignated as 'A' shares. The company's Articles of Association are then amended so that the 'B' shares are entitled to dividends and capital on a winding up only to the extent that the 'A' shares have already received £2,000,000.

At this stage, the 'B' shares will be worth little or nothing. Brian therefore makes a gift of these shares to a discretionary trust for the benefit of his adult children and their issue.

Six years later, Brian dies when his company is worth £3,500,000. The 'A' shares have paid dividends amounting to £750,000 since the reorganisation. As a result, the 'A' shares in Brian's estate are valued at £2,000,000 – £750,000 = £1,250,000 and the 'B' shares held by the trust are worth £2,250,000. The 'B' shares have captured the company's subsequent growth in value of £2,250,000 and the 'A' shares have been frozen at their original value of £2,000,000 less the dividends received by Brian.

The IHT saving is 40% x £2,250,000 = £900,000.

In Illustration 1, the bonus issue of the new shares and the reorganisation of the original share capital fell within the provisions of S127 TCGA 1992, as a result of which there was no disposal for CGT purposes at that time. The subsequent gift of the 'B' shares to the trust was a market value disposal, but any gain would be nominal given that the deemed proceeds were very small (or nil). If necessary, holdover relief under S260 TCGA 1992 would be available provided that the settlor, the settlor's spouse and any of their minor children were excluded from benefit.

From an IHT point of view, the initial reorganisation is a non-event, but the gift of the shares to the trust is an immediately chargeable transfer. However, on the assumption that the settlor has his full IHT nil rate band available, it is unlikely that detailed negotiations will need to be entered into with HMRC's Shares and Assets Valuation about the value of this transfer.

It will be sensible to involve a share valuation specialist from the outset, both to value the company and to confirm the low initial value of the 'B' shares.

In many cases, a single trust will be appropriate, but there can be a advantage in creating several pilot trusts on consecutive days with, say, £10 each followed by a gift of the 'B' shares to all the trusts equally one day later. This develops the principle established in *Rysaffe Trustee Company (CI) Ltd v CIR (2003)* that it is possible to 'bag' a full IHT nil rate band for each trust and so reduce, possibly substantially, future 10-yearly charges. The *Rysaffe* case involved five pilot trusts and this is probably a good compromise.

One final point to mention is the importance of making clear to clients that their future dividend entitlement from the shares which they have retained is capped under this arrangement. If they have received substantial dividends from their property investment company over the years, how comfortable do they feel about the source of their income drying up at some stage in the future?

Contributed by Robert Jamieson

Lecture P589 (14.28 Minutes)

Another use for pilot trusts

Imagine that a client (John) has shares in a private trading company which are currently worth £1,000,000. The company is likely to be sold in the next few years. If John put these shares into a life interest trust for the benefit of his children at a time when his cumulative total of chargeable transfers was £125,000, there would be no entry charge because of the availability of 100% business property relief.

However, when, in five years' time, the shares are sold for cash of £4,000,000, the IHT charge at 2009/10 rates on a capital distribution of £3,500,000 (£4,000,000 less CGT of, say, £500,000) is:

		IHT
	£	£
b/f	125,000	–
Initial value	1,000,000	160,000
	£1,125,000	£160,000

This gives an initial rate of 160,000/1,000,000 x 100 = 16%

The rate of tax actually payable is 16% x 30% x 20/40 = 2.4%

The IHT paid by the beneficiaries on the capital distribution would be 2.4% x £3,500,000 = £84,000.

If John had instead set up five pilot trusts on consecutive days with £10 going into each one and if he had then put one-fifth of his shareholding (worth, say, £120,000) into each of the trusts on the sixth day, the tax position following the sale of the company would be that there was no IHT to pay on the subsequent capital distribution. With reference to each trust, John's position is:

	£
b/f	125,000
Initial value settled	10
Initial value of addition	120,000
	£245,010

In other words, the rate of IHT on each exit charge is 0%.

Contributed by Robert Jamieson

Lecture P590 (9.51 Minutes)

Administration

Huntley Solutions Ltd v Revenue and Customs Comrs

In 2008 HMRC opened an enquiry into the appellant's tax returns for the accounting periods ending 31 December 2004, 2005 and 2006 pursuant to FA 1998 Sch 18, para 24(1). HMRC also sent copies of the notices to the appellant's accountants, M, requesting further information. M failed to produce some of the specified information and HMRC issued notices under FA 1998 Sch 18, para 27 requiring the appellant to produce this information. One of M's accountants rang HMRC explaining that he had a heavy work load and HMRC extended the deadline. In the continuing absence of the requested information, on 3 December 2008 HMRC issued penalty notices under FA 1998 Sch 18, para 29 imposing a £50 penalty in respect of each of the three outstanding periods. In January 2009 HMRC issued further penalty notices imposing daily penalties amounting to £300 in respect of each of the three accounting periods. The appellant appealed contending that M, which had been instructed by it, was unable to provide the information and documents to HMRC because of an overwhelming tax enquiry workload and that provided it with a reasonable excuse for the failure to provide the documents and the information to HMRC as required by the para 27 notices. HMRC, while accepting the difficulties faced by M, submitted that the circumstances did not give rise to a reasonable excuse for the appellant. As the appeal concerned the appellant's reliance on a third party, the tribunal directed the parties to provide written submissions addressing whether that could be a reasonable excuse in light of the decision in *Rowland v Revenue and Customs Comrs* [2006] STC (SCD) 536. The appellant submitted M had faced an extreme and contentious case load without a suitably qualified person to administer tax enquiries and personnel issues meant that any reasonable expectation of a fair response to an enquiry could not begin for some months. It was reasonable for it to rely on M to provide the information and documents to HMRC as it was not something within the scope of its expertise. HMRC submitted that *Rowland* dealt with extremely technically complex legislation whereas the information and documents required in the present case were a straightforward matter, requiring no knowledge or considerations of legislative technicalities.

The tribunal considered that reliance on a third party was capable of being a reasonable excuse for direct tax purposes. However, on the facts of the present case the information and documents required from the appellant by the para 27 notices were straightforward and easily understood. Therefore it was not reasonable for the appellant to rely on M to provide that information when it should have been able to comply with the notices itself. In those circumstances the appellant did not have a reasonable excuse for the failure to provide the information and documents to HMRC. It followed that the appeals would be dismissed; *Rowland v Revenue and Customs Comrs* [2006] STC (SCD) 536 distinguished.

Appeals dismissed.

Tax treatment of capital distributions

There will be clarifying legislation in Finance Bill 2010

A ministerial announcement has been made that clarification will be included in Finance Bill 2010 to the effect that the interpretation of the tax treatment of capital distributions that applied before 2005 will be restored. Under this interpretation capital distributions were regarded as of an income nature unless a specific rule said otherwise (such as for example in a winding up). It will be applied retrospectively subject to an opt out to ensure the new legislation does not give rise to increased tax liabilities in respect of those earlier transactions.

The new legislation should also clarify the tax treatment of capital reductions effected under the new provisions in Companies Act 2006.

The Financial Secretary to the Treasury (Mr. Stephen Timms): There is, at the moment, considerable uncertainty in relation to the corporation tax treatment of distributions. This uncertainty is causing significant problems to UK business and this statement is intended to establish with certainty a result that will be consistent with established expectations of HMRC practice.

In the Finance Act 2009, the Government introduced a new distribution exemption regime. Since then most income distributions received by UK companies are exempt from corporation tax unless they are linked to tax avoidance. The rules ensure that the UK corporate tax regime remains competitive and represent a significant reduction in the compliance burden faced by UK companies.

As intended, the exemption regime excludes distributions of a capital nature, which are subject to the chargeable gains rules where other exemptions may apply. However, the introduction of the new legislation has prompted HMRC to look more closely at the issue of whether a distribution is of a capital nature.

Before 2005 it was possible to interpret the law as saying that all UK distributions were income in nature unless a specific rule said otherwise-for example, distributions in a winding up. In 2005 a Tax Law Rewrite Act, in clarifying the law, made that view impossible to sustain. Despite this, prevailing practice remained unaltered and so UK distributions have generally been regarded until recently as income in nature and potentially exempt from corporation tax.

In the absence of a rule treating distributions as income, companies in receipt of capital distributions may now face an unexpected tax charge. In some cases, it has become clear that commercial transactions have been put on hold until the tax consequences become clear, with a corresponding effect on the normal business of those companies.

In order to resolve the issue, the Government will introduce legislation in the Finance Bill with a view to restoring previous expectations about the way that distributions are taxed. The changes will apply retrospectively where appropriate and will be subject to an opt out to ensure that UK retrospective application of the new legislation does not increase tax liabilities. These new rules will give UK companies the clarity they need to carry on their normal business.

Take care to avoid a penalty

This short summary provides details of the new inaccuracy penalty and has been updated for changes from 1 April 2010.

You could be charged a penalty if you don't take reasonable care with your tax affairs.This guide will help you understand what you can do to avoid a penalty.

We can charge a penalty if your return or other tax document is inaccurate and as a result you don't pay enough tax, or if you don't tell us a tax assessment we have sent to you is too low.

How does it work?

You will have to pay the additional tax and any interest that is due. If we charge a penalty it will be a percentage of the additional tax. The penalty rate now depends on the type of inaccuracy. The more serious the reason for the inaccuracy the higher the penalty can be. We will not charge a penalty if you took “reasonable care” to get things right but still made a mistake.

If you sent us an incorrect document we will charge a penalty if the inaccuracy:

- is because you were careless and failed to take reasonable care
- is deliberate – you intentionally sent us an incorrect document
- is deliberate and concealed – you intentionally sent us an incorrect document and tried to conceal the inaccuracy

What is reasonable care?

"Reasonable care" varies according to the person, their circumstances and their abilities. But we expect everyone to make and keep sufficient records for them to provide a complete and accurate return, and to update them regularly.

Some of the ways you can show you took reasonable care, and avoid a penalty include:

- keeping accurate records to make sure your tax returns are correct – see the record keeping guidance at
- checking what the correct position is when you don't understand something

If you discover errors in a document after you have sent it in, please tell us promptly. Otherwise, we will treat any of the errors that you made despite taking reasonable care as careless inaccuracies, and may charge a penalty.

Remember, if you use an agent such as an accountant, it is still your responsibility to make sure that the return they produce on your behalf is correct.

When will we reduce a penalty?

We can reduce a penalty if you tell us about an inaccuracy, especially if this is unprompted. A disclosure is unprompted if you tell us about the inaccuracy when you have no reason to believe we have discovered, or are about to discover it. Everything else is a prompted disclosure.

We can reduce a penalty from the maximum if you:

- tell us about any inaccuracies
- help us work out what extra tax is due
- give us access to check your figures

The table [which can be found on Tax News Online] shows the range of penalty percentages that can be applied to an inaccuracy.

Can we suspend penalties?

We may suspend a penalty for a careless inaccuracy for up to two years. We will set conditions for you to improve your systems to stop the same mistakes happening again.

If at the end of the suspension period you meet all the conditions, we will cancel the penalty. We cannot suspend penalties charged because of deliberate inaccuracies.

How will I know if I have a penalty?

We will discuss your tax with you to work out the correct amount. We will talk to you about any penalty that may be due before we send a penalty notice so you can understand what has happened and why we are doing this.

How can I appeal?

You can choose to have the penalty reviewed within Revenue and Customs or can appeal against it to an independent tribunal. See our factsheet HMRC 1 at www.hmrc.gov.uk/factsheets/hmrc1.pdf

What changes in April 2010?

We will be able to charge a penalty on a third party from 1 April 2010.

We can only do this if a third party deliberately withholds information from or deliberately supplies false information to another person who has to complete a return or send us a document. We have to demonstrate that the third party intended to cause that other person's return or document to be inaccurate.

We may publish your name as a deliberate tax defaulter if we discover that the extra tax due from deliberate or deliberate and concealed inaccuracies is more than £25,000, and you did not fully disclose and assist us in establishing the true tax position – see Deliberate tax defaulters Q & A at www.hmrc.gov.uk/about/tax-defaulters-q-a.htm.

When does it apply?

The new penalty system applies to documents with return periods from 1 April 2008, where the documents are due for:

- Capital Gains Tax
- Construction Industry Scheme
- Corporation Tax
- Income Tax
- National Insurance contributions
- PAYE
- VAT

from 1 April 2009, where the documents are due to be filed from 1 April 2009, for: to be filed from 1 April 2010, for:

- Environmental Taxes
- Excise Duties
- Inheritance Tax
- Insurance Premium Tax
- Stamp Duties.

Where can I get more help?

More information on these penalties is at www.hmrc.gov.uk/about/new-penalties. If you prefer to speak to us about your tax, please phone the helpline number on the tax return or letter we have sent you.

Business Tax

Weight Watchers Ltd and others

Weight Watchers UK is part of a long-established international business providing weight reduction and weight maintenance help to its customers, whom it calls members.

Typically members of the public sign up to take part in a Weight Watchers programme and as part of that programme, Weight Watchers UK provides weekly meetings throughout Britain.

Meetings are advertised and run locally with each weekly session normally lasting an hour and consisting of a combination of the following:

- Payment for attendance or alternatively, production of a card showing prepayment by a member;
- Confidential weighing and recording of each member's weight;
- A session led by the Leader to present or discuss information relevant to weight loss
- Sales and purchases of Weight Watchers food and other products.

Each member is encouraged to set a target weight and to lose weight so as to reach that target, and then maintain that new weight.

A member who does this may become a Gold member, and is given certain benefits.

Role of the Leaders

So how are Leaders involved in all of this?

Leaders are recruited to organise and run the weekly meetings.

They are regularly recruited from those who are Gold members, and so are successful in reducing weight and maintaining that reduced weight

A Leader may be responsible for a single weekly meeting or up to 12 weekly meetings with the average being three and four.

It is not uncommon, particularly in better attended meetings, for the Leader to delegate the duties of weighing and recording and of collecting fees to others who are known as Helpers.

So in summary, Leaders run these weekly meetings and are the link between Weight Watchers UK and its members at the meetings.

What Weight Watchers UK provides

Weight Watchers UK has a central national staff to deal with the supply of merchandise, or any issues arising from members about faulty merchandise.

They employ both Regional and Area Service Managers with the Area Service Manager having the only direct links with Leaders in their own area.

Weight watchers provide Leaders with detailed plans for all meetings, including:

- a weekly topic or topics,
- weekly leaflets for provision to all members

Weight Watchers UK protects its intellectual property and does not allow anyone else to use or derive value from it.

The issue

Previous decisions have held that Leaders were employees rather than being self employed resulting in:

- PAYE being payable by Weight Watchers UK (Regulation 80)
- Class 1 NIC being payable by both Weight Watchers UK and the Leaders (Section 8)

However, Weight Watchers and several Leaders have appealed against these decisions, contending that Leaders are self-employed.

The tribunal's findings

The tribunal found that a contractual relationship existed between Weight Watchers and each Leader in two contexts where:

1. Leader personally takes a Weight Watchers meeting
2. Weight Watchers products are held by the Leader for sale or return.

However, where a Leader found a replacement Leader if they did not take a particular meeting, Weight Watchers pays only the Leader who takes the meeting, and it is only the Leader who takes the meeting who has contractual rights as against Weight Watchers in respect of that meeting.

The tribunal found that Weight Watchers has a considerable degree of control over every Leader.

They ensure that at each meeting only the Weight Watchers Programme is delivered and nothing more.

This is a degree of control enforced by the power held by Weight Watchers under the Agreement and Conditions to stop a Leader acting as a Leader permanently at any time without any reason being stated and to prevent a Leader gaining any enduring business advantage from their efforts as a Leader.

The Leader must deliver their personal service in running a meeting to gain any contractual advantage from Weight Watchers,

On balance, the terms and conditions of the contractual relationship between Weight Watchers and its Leaders were characteristic of contracts of service.

And that HMRC's regulation 80 determinations and section 8 decisions were correct.

All appeals were dismissed.

Lecture B587 (8.39 Minutes)

Ductaire Fabrications Ltd v Revenue and Customs Comrs

The appellant company was registered for gross payment status for the purposes of the Construction Industry Scheme ("CIS") pursuant to FA 2004 s 64 and so satisfied the three statutory tests laid down in FA 2004 Sch 11, Pt 3. In July 2006 the appellant was acquired by C Ltd and as there was a conflict of accounting year dates, the appellant's accounting year dates were changed. The appellant filed its corporation tax return (CT 600) for the accounting period ended 30 September 2006 92 late on 31 December 2007. It also paid its corporation tax for the accounting period ended 30 September 2006 and for 31 December 2006 late. In 2007 and 2008 it submitted four monthly contractor returns late, and several payments made under the monthly scheme payments, as well as PAYE payments, were made late. In October 2007 HMRC imposed a penalty of £100 in respect of the late filing of the corporation tax return which remained unpaid until April 2008. On 11 August 2008 HMRC issued CIS 2008 notifying the appellant of its failures and cancelling its registration gross payment status on the basis that it had failed one of the statutory tests, the compliance test, within the qualifying period which was the 12 months to 18 June 2008. The appellant appealed under FA 2004 s 67(1)(b) contending that it had a "reasonable excuse", for the purposes of FA 2004 Sch 11, para 12(3), for its failure to comply and that it had complied with its obligations without unreasonable delay once the excuse had ceased. It further submitted that: (i) the failures in respect of the contractors' returns should be disregarded as there was a six month grace period from April 2007 to October 2007; (ii) although the corporation tax payment was late, it was due to changes with the accounting period and ownership of the company; (iii) most of the PAYE payments and returns due were made within seven days of the due date. Furthermore HMRC were holding a credit balance of £15,254.53 because of an overpayment in the previous year and that could be regarded as reducing the amounts of late payments; and (iv) the withdrawal of gross status would have an adverse effect on its business. HMRC argued, inter alia: (i) no explanation had been given as to how the change in accounting date or the change in ownership affected the company's ability to pay its corporation tax on time. However they accepted that as the corporation tax return itself was submitted, the failure to lodge on or before 30 September 2007 could be disregarded as one of the exceptions within the Income Tax (Construction Industry Scheme) Regulations 2005, SI 2005/2045 reg 32, although the £100 penalty late payment could not be; (ii) the failure to file the contractors' returns on time could not be overlooked when considering the compliance test. A "mailshot" had been issued to all contractors within CIS in April 2007 explaining the position; (iii) unless tax obligations were strictly complied with a company having gross payment status would have an unfair competitive advantage over those who were complying with the obligations; and (iv) the appellant failed the "reason to expect test", under FA 2004, Sch 11, para 12(7), that it would comply, in respect of periods after the qualifying period, with all obligations and requests imposed on it by virtue of its failure to pay the corporation tax for the account period ended 31 December 2007, due on 1 October 2008, and paid in full 98 days late on 7 January 2009.

The tribunal found on the facts that the compliance test had not been met. The failure to pay the penalty for the late filing of the corporation tax return for the account period ended 30 September 2006 was not within the exceptions from the compliance obligations as it was not less than £100. The failures in respect of the late monthly contractors' returns could not all be disregarded, nor could all of the late payments under the monthly scheme payments. In respect of the PAYE payments the first three payments could be disregarded, but remaining ones could not. Whilst, taken on their own, there would have been a reasonable excuse for the failures in respect of the late payment of the £100 for the filing of the corporation tax return and for the late payments of the monthly scheme payments, taking those failures together with the remaining PAYE payment failures and in particular the late payment in respect of the corporation tax the majority of which was paid 287 days late, it was clear the company did not have a reasonable excuse. There might have been a reasonable excuse had the corporation tax been paid on or before 31 December 2007 but there could be no reasonable excuse for a payment made 287 days late. Corporation tax for the accounting period ended 31 December 2006 was paid 196 days late. Although there had been and would be considerable difficulties in respect of the recession, a company had to comply with all obligations imposed on it unless permitted by the Regulations. Furthermore, the purpose of Parliament in creating the legislation was to procure strict compliance with tax obligations by making such compliance the price of obtaining a certificate and there could be an unfair competitive advantage to allow the gross payment status to continue despite clear failures. Accordingly the consequences of cancellation of gross payment status was not relevant to the issue of whether or not there was a reasonable excuse. In addition there was no reason to expect future compliance. It followed that the appeal would be dismissed.

Appeal dismissed.

Corporation Tax

Distributing profits from a limited company; the new calculations

A fresh look needs to be taken when considering how to distribute profits of a limited company, given the forthcoming increases in the rate of income tax and national insurance contributions.

The calculations below are based on marginal rates and do not reflect the basic rate band of the individual or indeed the personal allowance. They should therefore be adapted to reflect the individual circumstances.

What is clear is that the overall saving in distributing profits as dividends instead of as remuneration is widening, and indeed encourages a fresh look at incorporation where the annual tax savings will be even greater than before (quite apart from the ability to sell the goodwill to the limited company and obtain a one-off tax saving). That is surprising given the Government's stated dislike of "tax-inspired" incorporations.

2009/10 & 2010/11 - distributing profits to a 40% taxpayer – total cost

CT rate	*earnings ET to UEL*	*earnings above UEL*	*dividend*
21%	*56.56%*	*47.7%*	*40.75%*
28%	*56.56%*	*47.7%*	*46%*

All of the calculations below concentrate on a limited company paying corporation tax at the small companies rate which applies to annual profits up to £300,000.

2009/10 & 2010/11 - 40% taxpayer: earnings ET to UEL

EARNINGS	*£*	***Tax & NIC*** *£*
Profits	*100.00*	
Remuneration	*88.65*	
Employer nic (12.8%)	*11.35*	*11.35*
	nil	
Remuneration	*88.65*	
Employee nic (11%)	*9.75*	*9.75*
Income tax (40%)	*35.46*	*35.46*
	43.44	*56.56*

Effective tax rate = 56.56%

2009/10 & 2010/11- 40% taxpayer – earnings above UEL

		Tax & NIC
EARNINGS	*£*	*£*
Profits	*100.00*	
Remuneration	*88.65*	
Employer NIC (12.8%)	*11.35*	*11.35*
	NIL	
Remuneration	*88.65*	
Employee NIC (1%)	*0.89*	*0.89*
Income tax (40%)	*35.46*	*35.46*
	52.30	*47.70*

Effective tax rate = 47.7%

DIVIDEND

		£	*£*
Profits		*100.00*	
Corporation tax		*21.00*	*21.00*
Dividend		*79.00*	
Tax credit (1/9)		*8.78*	
Gross dividend		*87.78*	
Income tax @ 32.5%	*28.53*		
Less tax credit	*8.78*	*19.75*	*19.75*

Net dividend: 79.00 – 19.75 = 59.25
(income tax = 25% of cash dividend)

Total cost	*40.75*

Effective tax rate = 40.75% (if self-employed, rate is 41%)

New income tax rate of 50% from 2010/11 on taxable income over £150,000

2010/11 - distributing profits to a 50% taxpayer with taxable income over £150,000 - total cost

CT rate	*earnings ET to UEL*	*earnings above UEL*	*dividend*
21%	*65.42%*	*56.56%*	*49.52%*
28%	*65.42%*	*56.56%*	*54%*

2010/11 - taxable income over £150,000 – earnings ET to UEL

		Tax & NIC
EARNINGS	*£*	*£*
Profits	*100.00*	
Remuneration	*88.65*	
Employer nic (12.8%)	*11.35*	*11.35*
	nil	
Remuneration	*88.65*	
Employee nic (11%)	*9.75*	*9.75*
Income tax (50%)	*44.32*	*44.32*
	34.58	*65.42*

Effective tax rate = 65.42%

2010/11 - the calculation for taxpayer with taxable income over £150,000 – earnings above UEL

		Tax & NIC
EARNINGS	*£*	*£*
Profits	*100.00*	
Remuneration	*88.65*	
Employer nic (12.8%)	*11.35*	*11.35*
	nil	
Remuneration	*88.65*	
Employee nic (1%)	*0.89*	*0.89*
Income tax (50%)	*44.32*	*44.32*
	43.44	*56.56*

effective tax rate = 56.56%

DIVIDEND

		£	*£*
Profits		*100.00*	
Corporation tax		*21.00*	*21.00*
Dividend		*79.00*	
Tax credit (1/9)		*8.78*	
Gross dividend		*87.78*	
Income tax @ 42.5%	*37.30*		
Less tax credit	*8.78*	*28.52*	*28.52*

Net dividend: 79.00 – 28.52 = 50.48
(income tax = 36.1% of cash dividend)

Total cost	*49.52*

Effective tax rate = 49.52% (if self-employed, rate is 51%)

New NIC rates from 2011/12

- Employer's NIC 13.8%
- Employee's NIC 12% ET to UEL
- Employee's NIC 2% above UEL
- Self-employed NIC 2% above UPL

2011/12 - distributing profits to a 50% taxpayer with taxable income over £150,000 - total cost

CT rate	*earnings ET to UEL*	*earnings above UEL*	*dividend*
22%	*66.60%*	*57.81%*	*50.16%*
28%	*66.60%*	*57.81%*	*54%*

2011/12 - taxable income over £150,000 – earnings ET to UEL

		tax & NIC
EARNINGS	*£*	*£*
Profits	*100.00*	
Remuneration	*87.87*	
Employer nic (13.8%)	*12.13*	*12.13*
	nil	
Remuneration	*87.87*	
Employee nic (12%)	*10.54*	*10.54*
Income tax (50%)	*43.93*	*43.93*
	33.40	*66.60*

Effective tax rate = 66.60%

2011/12 - taxable income over £150,000 – earnings above UEL

		tax & NIC
EARNINGS	*£*	*£*
Profits	*100.00*	
Remuneration	*87.87*	
Employer nic (13.8%)	*12.13*	*12.13*
	nil	
Remuneration	*87.87*	
Employee nic (2%)	*1.75*	*1.75*
Income tax (50%)	*43.93*	*43.93*
	42.19	*57.81*

Effective tax rate = 57.81%

DIVIDEND

		£	*£*
Profits		*100.00*	
Corporation tax		*22.00*	*22.00*
Dividend		*78.00*	
Tax credit (1/9)		*8.67*	
Gross dividend		*86.67*	
Income tax @ 42.5%	*36.83*		
Less tax credit	*8.67*	*28.16*	*28.16*

Net dividend: 78.00 – 28.16 = 49.84
(income tax = 36.1% of cash dividend)

Total cost	*50.16*

Effective tax rate = 50.16% (if self-employed, rate is 52%)

Contributed by Gerry Hart

Lecture B589 (9.21 Minutes)

Lion Co v Revenue and Customs Commissioners

In September 1998 the appellant company purchased a freehold property for £850,000 with the intention of making a payment in kind to one of its directors, Mr L, by way of a discretionary bonus of the property, once repairs and improvements—which cost approximately £750,000—had been carried out. On 31 July 1999 the appellant transferred the property to Mr L and his wife to hold as joint tenants by way of discretionary bonus. At the date of transfer the property was independently valued at £1.2m, which was approximately £400,000 less than the £1.6m cost incurred by the appellant. The appellant sought to write off the expenditure incurred on the additions in excess of its market value on transfer to Mr L in the accounts for 31 October 1998 and 31 October 1999 (accrued as to £309,041 in the accounts for 1998 and £115,498 in the 1999 accounts) in computing its profits. The written down amounts were reflected in the profit and loss account for each of the years in question as 'Write Down of property held for disposal to estimated net realisable value', and so went to reduce profit before tax (or, in 1998, resulted in a loss before tax). The property was accounted for in the balance sheet for 1998 as a current asset under 'Property held for disposal to directors' at its net realisable value of £1.2m. As the property was transferred during 1999, it no longer appeared in the 1999 balance sheet. HMRC issued assessments disallowing the claim on the basis that the expenditure was of a capital nature. The appellant appealed. It was common ground that the property was not acquired or held by the appellant as trading stock. The appellant contended, inter alia, that (i) the entire purpose in acquiring, repairing and improving the property was to remunerate Mr L in kind by making a discretionary bonus of it. Remuneration of employees was a revenue expense and the costs of remunerating an employee in kind were similarly revenue in nature; (ii) the costs incurred on acquiring and altering the property were a form of circulating, not fixed, capital; (iii) that the loss or write down of the value of the property, as much as the payment of the bonus itself to Mr L, ought to be regarded as revenue expenditure. It was impossible to separate the loss from the bonus and apply different treatment to each; (iv) it only held the asset for a short period of time; (v) the accountancy treatment, whilst not determinative of the capital/revenue distinction, was and should be very relevant. HMRC argued: (i) the property was acquired by the appellant as a capital asset because it was acquired as an investment (albeit as a short term one) rather than as a trading asset; (ii) the loss did not arise from trade as the appellant did not deal in property; (iii) the loss was a capital loss on disposal of a capital asset; and (iv) the case had to be determined by reference to established case law and not accountancy practice.

The tribunal considered that the write-downs of the value of the property were on capital and not revenue account, and accordingly were non-deductible. The deduction related, not to an expense, but to the writing down of the value of an asset, which was not trading stock of the appellant. As the appellant's trade did not include dealings in land the starting assumption was that expenditure on the acquisition and improvement of the property should be regarded as capital expenditure. On the facts there were no contra indicia that pointed in a different direction to outweigh that starting assumption. The fact that the asset was owned for a short period only, and was intended from the outset to be held temporarily, could not alter the character of an asset held on capital account to one of revenue account. Nor, on the authorities, could the purpose of the transaction be determinative, although it was one element to be taken into account. The purpose was to pay a bonus to Mr L. The bonus that was paid, by means of the transfer in specie of the property, was on revenue account to the extent of the value transferred. The means adopted for the payment of the bonus was the acquisition and improvement of an identifiable asset of enduring quality. That expenditure, and the loss or write down in value, was accordingly on capital account. Furthermore, that conclusion was not affected by the accounting treatment of the property as a current asset. The criteria that applied for accounting purposes and which would result in an asset being treated as a current asset were not the same as, and did not reflect, the distinction as a matter of law between capital and revenue. The relevant accounting criteria in the present case concerned the early realisation of the property. As a matter of law, such criteria could not change the nature of the asset or be determinative of the capital/revenue question. It followed that the appeal would be dismissed.

Appeal dismissed.

Value Added Tax

Partial Exemption - changes to the de minimis rules

Changes to the "de minimis" rules for partial exemption are being brought in with effect from 1 April 2010. They are set out in HMRC Information Sheet 04/2010, which has been reproduced below.

This is part of an ongoing project to simplify the partial exemption rules: it began with a consultation in 2008 and continued with changes to the standard method calculations which were brought in on 1 April 2009 by an announcement made on that date. At least the 2010 changes have come with slightly more notice – they were announced on 8 March 2010.

As with three out of four of the 2009 changes to the standard method, the changes to the de minimis rules are optional, and are a genuine and welcome attempt to simplify the operation of the rules for businesses. The accompanying lecture explains and illustrates the changes set out in the Information Sheet.

VAT Information Sheet 04/2010 VAT:

This HMRC information sheet provides guidance on two changes to simplify the de minimis rules that affect VAT periods commencing on or after 1 April 2010.

1. Introduction

1.1 Who should read this information sheet?

Smaller-sized businesses that currently benefit, or think they may benefit, from the partial exemption de minimis rules. This information sheet assumes you have an existing knowledge of the current partial exemption rules. Further information about partial exemption can be found in Public Notice 706 Partial Exemption.

1.2 What is this information sheet about?

It provides guidance on two changes to simplify the de minimis rules that affect VAT periods commencing on or after 1 April 2010. The changes are optional and can be adopted by businesses without approval from us. The two changes are referred to as:

- simplified tests (section 2)
- annual test (section 3)

1.3 Why are these changes being introduced?

The current de minimis rules require businesses to carry out detailed partial exemption calculations. These changes are being introduced to allow the vast majority of businesses to confirm their de minimis status using far simpler calculations that rely on information that a business has readily to hand.

The changes follow a consultation on ideas to simplify the partial exemption rules, which confirmed strong support for their implementation. They build on changes made last year to simplify the standard method by further reducing administrative burdens on businesses.

2.1 How does the current de minimis test work?

The current test requires a business to calculate how much input tax it has incurred on costs relating to exempt supplies in accordance with its partial exemption method. Provided this input tax is no more than £625 per month on average and no more than 50 per cent of its total input tax, the business is said to be 'de minimis' (or to have 'passed the de minimis test') and can provisionally recover input tax relating to exempt supplies. The test is then re-applied at the end of the partial exemption year (also known as a 'longer period') to establish the de minimis status of the business and any under/over recovery of input tax is accounted for in the annual adjustment.

2.2 What are the simplified tests?

The simplified tests save some businesses the need to carry out a full partial exemption calculation to confirm their de minimis status. If, in a VAT period, a business passes Test one or Test two (set out below) it may treat itself as de minimis and provisionally recover input tax relating to exempt supplies. The business is still required to review its de minimis status at year-end as before and account for any under/over recovery of input tax as part of its annual adjustment (see 2.5).

The simplified tests are:

- Test one: total input tax incurred is no more than £625 per month on average and the value of exempt supplies is no more than 50 per cent of the value of all supplies
- Test two: total input tax incurred less input tax directly attributable to taxable supplies is no more than £625 per month on average and the value of exempt supplies is no more than 50 per cent of the value of all supplies

Note one: 'Total input tax' excludes blocked input tax (such as VAT on the cost of business entertainment) which is irrecoverable.

Note two: 'The value of all supplies' includes taxable supplies made in the UK, supplies made outside the UK which confer the right of recovery (known as 'regulation 103 supplies') and exempt supplies.

Note three: 'input tax directly attributable to taxable supplies' is input tax on costs that are used or to be used exclusively in making taxable supplies. For example, input tax on the cost of goods for resale.

Example one: a business has a VAT period running from 1 April to 30 June 2010. During that period it incurs total input tax of £1,800 which it uses making taxable supplies of £30,000 and exempt supplies of £20,000. For the quarter ending June 2010, the business incurs total input tax of no more than £1,875 (£625 x 3 months) and the value of its exempt supplies is no more than 50 per cent of its total supplies (20,000/50,000 x 100 = 40%). Therefore, the business is de minimis for this period as it passes Test one and can provisionally recover £1,800 input tax on its VAT return without the need to carry out a full partial exemption calculation. This will be subject to review at year-end in accordance with paragraph.2.5.

Example two: a business has a partial exemption year running from 1 May 2010 to 30 April 2011. During that period it incurs total input tax of £30,000, of which £25,000 is on goods for resale which are directly attributable to taxable supplies. It makes taxable supplies of £75,000 and exempt supplies of £60,000. Its total input tax less input tax directly attributable to taxable supplies is £5,000 (30,000 – 25,000) which is less than £7,500 (£625 x 12), and the value of its exempt supplies is no more than 50 per cent of its total supplies (60,000/135,000 x 100 = 44%). Therefore, the business has finalised its de minimis status for the year and is entitled to recover £30,000. There is no need for any further partial exemption calculation for that year.

2.3 How do the new tests interact with the current test?

The new tests supplement the current test. A business is de minimis if it passes Test one, Test two or the current test, and if it passes any one test there is no need for it to consider the other two. Even if a business fails Test one and Test two, the information gathered is still required to carry out a full partial exemption calculation for the current test.

2.4 If I pass Test one or Test two in a VAT period do I still need to do a partial exemption calculation?

No. The tests have been introduced to save the need for partial exemption calculations in these circumstances.

2.5 Do I still need to do an annual adjustment?

At the end of your partial exemption year, you need to apply the de minimis test to the year as a whole.

- If you pass Test one for the year, you can recover all of your input tax relating to exempt supplies and are not required to carry out any further partial exemption calculations.

- When applying Test two, you first need to review how much of the input tax you have incurred over the year is directly attributable to taxable supplies. Then, if you pass Test two for the year, you can recover all of your input tax relating to exempt supplies and are not required to carry out any further partial exemption calculations.
- If you fail Test one and Test two for the year, then you need to carry out a full partial exemption calculation for the year to determine whether you pass the current de minimis test (see 2.1) and account for any under/over recovery of input tax as part of your annual adjustment in the normal way.

2.6 When do the new tests take effect?

The simplified tests may be applied to VAT periods commencing on or after 1 April 2010.

2.7 Why is Test one not set out in the legislation?

A business that passes Test one must, in all cases, pass Test two and so it was unnecessary to set it out in the legislation.

3. Annual test

3.1 What are the current rules?

The current rules require a business to apply the de minimis test in each VAT period. If it passes the test it is de minimis and can provisionally recover input tax relating to exempt supplies in that period. This is subject to an end-of-year partial exemption calculation to review its de minimis status and any under/over recovery of input tax is accounted for in the annual adjustment.

3.2 What is the new annual test?

The annual test gives most businesses the option of applying the de minimis test once a year, instead of four or five times a year (depending on when a business decides to account for its annual adjustment). It allows a business that was de minimis in its previous partial exemption year to treat itself as de minimis in its current partial exemption year. This means it can provisionally recover input tax relating to exempt supplies in each VAT period, saving the need for partial exemption calculations.

3.3 Do I need to review my de minimis status at year-end?

Yes, you are still required to review your de minimis status at year-end in accordance with paragraph 2.5 and if you fail the de minimis test for the year you must repay the input tax relating to exempt supplies that you provisionally recovered in-year. However, there is no need carry out in-year partial exemption calculations.

Example three: A business was de minimis in its partial exemption year ending 31 March 2010. It has the option of applying the annual test and treating itself as de minimis during the year ending 31 March 2011. This means that it can provisionally recover input tax relating to exempt supplies in each VAT period during that year without the need to carry out a partial exemption calculation. The business is then required to review its de minimis status at year-end and, if it fails the de minimis test for the year, repay the input tax it has incurred during the year that relates to exempt supplies.

3.4 What are the conditions on using the annual test?

There are three conditions on using the annual test. The business must:

- pass the de minimis test for its previous partial exemption year
- consistently apply the annual test throughout any given partial exemption year
- have reasonable grounds for not expecting to incur more than £1million input tax in its current partial exemption year

If any of these conditions are not met then the business is required to apply the de minimis test in each VAT period, which remains the default position.

3.5 What else do I need to consider?

The main risk of using the annual test is that a business provisionally recovers input tax relating to exempt supplies in-year, but then fails the test at year-end and is required to repay this input tax to us. If you think you are likely to fail the test at year- end and repaying the input tax would cause you difficulties, then it would not be advisable to take up the option of the annual test.

3.6 When does it take effect?

A business may adopt the annual test for partial exemption years commencing on or after 1 April 2010, if it was de minimis in its previous partial exemption year.

Lecture B590 (15.52 Minutes)

Changes to the operation of the option to tax/definitions of housing association

HMRC Brief 08/2010 announces the simplification of the operation of the option to tax, the simplification of the 6 month cooling-off period to revoke an option to tax, and changes to the definition of a housing association from 1 April 2010.

This Revenue and Customs Brief announces three changes to Schedule 10 of the VAT Act 1994 which deals with the liability of supplies of land and buildings and one change to Group 5 to Schedule 8 of the VAT Act 1994 which deals with the zero-rate for construction services. These changes are:

- simplification of the operation of the option to tax
- simplification of the 6 month "cooling-off" period to revoke an option to tax, and
- changes to the definition of a housing association.

These amendments all come into effect on 1 April 2010.

Background

Schedule 10 to the VAT Act 1994 deals primarily with the option to tax on supplies of land and buildings. Following a series of amendments to block aggressive tax avoidance schemes, this legislation had become increasingly complex and was identified by business as a key area for simplification.

Following consultation with business a re-written version of Schedule 10, in Tax Law Re-write style, was introduced on 1 June 2008. The revised version is easier to follow and employs a more logical layout and simplified language.

Simplification arising from the operation of the option to tax

Following the introduction of the new Schedule 10, HMRC has continued to discuss with business ways in which the legislation could be further improved and simplified. In the course of our discussions additional concerns were also identified relating to certain aspects of the option to tax rules. As a result, a small number of minor amendments are being made which are intended to both simplify the legislation and facilitate business needs. A further change is also necessary as a result of the Housing and Regeneration Act 2008 and the redefining of the term "relevant housing association".

In making the changes set out below it was necessary to balance the business need for flexibility with the requirement that revenue should be protected.

The changes that have been made are as follows:

- occupation of minor parts of buildings (no more than 10% of the total area) by persons that have provided finance for developments is now disregarded for the purposes of the option to tax anti-avoidance provision. A new sub-paragraph 15(3A) has been introduced into Schedule 10 and new tertiary legislation introduced, (see VAT Information Sheet 02/2010 - Annex A).
- the conditions for revoking an option to tax during the "cooling-off" period have been amended. The requirement that land must not have been used has been removed (Schedule 10 paragraph 23(1)(b)). The additional conditions set down in tertiary legislation have also been amended, (see VAT Information Sheet 02/2010 - Annex B).

- the definition of "relevant housing association" has been amended in Schedule 10 paragraph 10(3). The term "registered social landlord" will be replaced from 1 April for England only with "private provider of social housing" as defined by the Housing and Regeneration Act 2008. This consequential change ensures English housing associations continue to enjoy the same VAT reliefs as they do at present in common with housing associations in the rest of the UK. A similar change is also being made in Group 5 to Schedule 8 of the VAT Act 1994 where we are also taking the opportunity to update the reference for Scotland as well.

More detailed explanations and amended tertiary legislation relating to the first two bullet points above are contained in VAT Information Sheet 02/2010.

How will the changes be effected?

All the changes to Schedule 10 and Group 5 to Schedule 8 are being made by separate Treasury Orders and will both be effective from 1 April 2010. The changes to tertiary legislation will also take effect from the same date.

A revised Public Notice 742A Opting to tax land and buildings will be issued in due course.

Further Information

Further information can be obtained on our website www.hmrc.gov.uk or through the Helpline on Tel 0845 010 9000

Information Sheet 02/10 provides guidance and further detail. It supersedes or complements existing guidance as appropriate. A revised Notice 742A Opting to tax land and buildings and new guidance will be available as soon as possible.

VAT status of University Trading Subsidiary Companies

HMRC Brief 09/2010 announces their revised policy with regard to the supply of education by a university subsidiary trading company. It applies to supplies on or after 11 March 2010.

This Revenue & Customs Brief announces our revised policy with regard to the supply of education by a university subsidiary trading company. VAT Information Sheet 03/10 provides further detail.

Summary

Following developments in VAT case law and in methods by which education is delivered by universities, we have reviewed our policy on the treatment of supplies of education delivered by companies that are owned or controlled by a university. This review has identified a need for a change in policy, and as a result the VAT liability of supplies of education will change in certain circumstances. The new policy applies to supplies made on or after the date of this Brief subject to transitional arrangements (see below).

Who should read this?

This Brief should be read by any university owned company that delivers education and any university owning such a company.

Background

Supplies of education are exempt from VAT when provided by a UK university and any college, institution, school or hall of a university. (Note (1)(b), Group 6, Schedule 9, VAT Act 1994). Following the review, we have concluded that, in many cases where a university trading company provides education, they are acting as a "college, institution, school or hall of a university." As a consequence it is an "eligible body" for the purposes of Group 6 Schedule 9 VATA 1994. This means that any education or training provided by the university subsidiary trading company is an exempt supply of education. Please see VAT Information Sheet 03/10 for further detail.

Implications

This policy change is limited to those companies that

- are owned/controlled by a university
- provide university level education leading to a qualification awarded by a university or a nationally recognised body
- have close academic links with their parent university; for example, where students on the company's courses are registered/enrolled with the parent university, subject to its rules and regulations and awarded qualifications by it

Please see VAT Information Sheet 03/10 for further detail.

Once a university subsidiary company is regarded as an eligible body within Note (1)(b):

a) All supplies of education and vocational training provided by that company are exempt from VAT.

b) Any supplies which fall within Group 6 of Schedule 9 VATA 94 should be treated as an exempt supply. (For example supplies of goods which are closely related to the supply of education under item 4.)

Other supplies, in particular consultancy services, provided by a subsidiary company of a university remain subject to VAT at the standard rate.

Transitional arrangements

The policy change comes into effect formally from the date of this Brief. An affected company may also apply it with retrospective effect and make the relevant adjustments to its VAT accounting, subject to the statutory time limits.

However we recognise that many university companies have budgeted on the basis that their supplies would be taxed. Therefore, as a transitional measure, affected companies may continue to apply the old policy (that is taxation at the standard rate) to supplies, which are to be delivered before 1 August 2010.

If a tax point is created for courses (including closely related supplies) to be delivered both before and after 1 August 2010, only that part of the supply which comprises courses which are delivered before 1 August 2010 may be subjected to the previous policy that is taxed.

This transitional measure will not apply if used for tax avoidance purposes, including any attempts to forestall the impact of the policy change. In addition, any pre-invoicing and/or prepayments which have been made in anticipation of the issue of this Brief and which do not comprise the normal commercial practice of the company that is the company is attempting to create a tax point in anticipation of this formal announcement of the policy change will be considered to be tax avoidance and we will apply the policy change to any supplies covered by such pre-invoicing and/or prepayments delivered after 1 August 2010.

Capital Goods Scheme

VAT Information Sheet 03/10 gives guidance on what, if any, impact this change of policy will have on capital items used by university owned or controlled companies in delivering university education.

Further information

For further information please contact:

Dave O'Neil (www.hmrc.gov.uk/asplib/mailer/mailer_form.asp?dpt=DAVE_O%27NEIL), on 0191 4198971

VAT Tribunal decisions: Rank (gaming machines) issued December 2009

Following the decision in Rank Group Plc (TC00301), HMRC will process claims already received in respect of VAT paid on gaming machine takings. HMRC is appealing against the decision to the Upper Tribunal.

Revenue & Customs Brief 40/2009 issued on 14 July 2009 advised of a High Court decision in the case of Revenue and Customs Commissioners v The Rank Group [2009] All ER (D) 65 (Jun), confirming there had been a breach of fiscal neutrality in the tax treatment of the supply of Mechanised Cash Bingo (MCB) and gaming machines.

In respect of gaming machines, as the judgment related to an appeal against an interim ruling of the VAT Tribunal, we advised that no claims for output tax wrongly accounted for would be considered until the Tribunal issued a final ruling in respect of Rank.

The First Tier Tribunal issued this in December 2009 (TC00301: Rank Group Plc), finding that Fixed Odds Betting Terminals (FOBTs) were similar to, and in competition with, taxable gaming machines. We are appealing against this decision to the Upper Tribunal. Additionally, the Court of Appeal is due to hear the appeal against the earlier findings of both the VAT Tribunal and the High Court.

We intend, on the basis of the findings of both the VAT Tribunal and the High Court (and subject to the appeals), to consider those claims already received in respect of VAT paid on gaming machine takings.

Background

Rank, which operates gaming machines, claimed there was inconsistency in the way VAT was applied to these, as compared with certain comparator machines and FOBTs which were exempt from VAT.

In 2008, the VAT Tribunal ruled there had been a breach of fiscal neutrality as a result of the difference in treatment. This ruling was upheld by the High Court last year although this itself is subject to a further appeal. The principle of fiscal neutrality requires similar supplies to be treated the same for tax purposes to avoid any distortion of competition.

The law was changed from 5 December 2005 and from that date the treatment of comparator machines, FOBTs and gaming machines has been the same (and subject to VAT).

Implications of this judgment

As FOBTs came into commercial use in the UK in November 1998, this date agreed by the Tribunal, we will now consider existing claims submitted within required time limits for repayment of VAT paid on gaming machine takings for the period from 1 November 1998 to 5 December 2005.

Claims that have previously been rejected (for whatever reason) and which are not under appeal will not be considered. No new claims for the repayment of VAT paid for the period between 1 November 1998 and 5 December 2005 can be made.

The aim is to process all existing claims, where satisfactory evidence to support the claim has been provided, by 31 March 2011.

Making claims or adjustments

Where a business has already made a claim to us for output tax wrongly accounted for in respect of gaming machines, this will be considered although further evidence may be requested.

All claims will be subject to the time limit in section 80(4) of the VAT Act 1994 â€” three years where the claim was made before 1 April 2009 or, where the claim was made on or after that date, four years or back to accounting periods ending on or after 1 April 2006 whichever is the shorter.

Protective assessments will also be issued under section 80(4A) of the VAT Act 1994 in order to allow us to recover any payments made should any appeals be successful.

There may be direct tax implications where amounts of over-declared output tax are repaid to businesses and your attention is drawn to Revenue & Customs Brief 14/2009 issued previously.

Further information

We 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.

Where you are in any doubt about the correct treatment please contact the Helpline on 0845 010 9000

HMRC Brief 11/2010 17 March 2010

Health professionals, nursing auxiliaries, care assistants and support workers

HMRC Brief 12/2010 clarifies HMRC's policy on the VAT treatment of supplies of health professionals, nursing auxiliaries, care assistants and support workers by employment businesses.

Background

This brief aims to clarify our policy on the VAT treatment of supplies of health professionals, nursing auxiliaries, care assistants and support workers by employment businesses.

Definitions

The Employment Agencies Act 1973 defines an "employment business" as a "business (whether or not carried on with a view to profit and whether or not carried on in conjunction with any other business) of supplying persons in the employment of the person carrying on the business, to act for, and under the control of, other persons in any capacity". "Employment" is construed widely to include engagement on a contract of employment or a contract for services.

"Health professional" is an individual enrolled or registered on the appropriate statutory register including any and all of the following:

- Dentist or Dental Care Professional - an individual registered with the General Dental Council

- Doctor - an individual registered with the General Medical Council

- Nurse, midwife or community public health nurse - individual registered with Nursing & Midwifery Council

- Individuals registered by the Health Professions Council - including:

- Arts Therapist
- Biomedical Scientist
- Chiropodist/Podiatrist
- Clinical Scientist
- Dietician
- Occupational Therapist
- Operating Department Practitioner
- Orthoptist
- Paramedic
- Physiotherapist
- Psychologist
- Prosthetist/Orthotist
- Radiographer
- Speech & Language Therapist.

"Nursing auxiliary" - an individual who is not enrolled on any register of medical or health professionals but whose duties must include the provision of medical, as well as personal, care to patients.

"Care assistant" is an individual who is not enrolled on any register of medical or health professionals but who provides both medical and personal care to the recipient.

"Support worker" is an individual providing personal care and support services that may or may not be directly connected with the welfare of the recipient.

"Medical care" - in the context of what is provided by nursing auxiliaries and care assistants, includes monitoring the health of patients, for example, by taking blood pressure and temperatures, as well as administering drugs to patients under the direct supervision of a health professional.

"Personal care" - includes washing and dressing, feeding, helping people to mobilise, bed making, toileting etc., but does not include medical care.

Employment businesses in the health and welfare sector: basic VAT position

Staff supplied by an employment business may be either employees of that business, or self-employed and engaged by an employment business. In both cases the workers' services are provided to the employment business, which in turn makes a supply of that worker to the client. If the worker comes under the direction and control of the client, this is a supply of staff. The employment business must therefore account for VAT when appropriate on the full charge to the client as in these circumstances it is acting as the "principal".

However, if the employment business maintains the direction and control of its staff to make a supply of welfare or medical services directly to the final consumer, we would see it as providing health or welfare services rather than merely a supply of staff. In these circumstances, subject to relevant criteria, we would see the business as making an exempt supply of welfare or health services - see Public Notice 701/2 Welfare and Notice 701/57 Health Professionals and the section headed "Supplies of Contracted out Welfare Services" below.

Supplies of registered health professionals (other than nurses, midwives and community public health nurses)

When an employment business supplies registered health professionals as a principal to a third party, where the health professional is working under the control and guidance of the third party, it is making a taxable supply of staff to that third party - not an exempt supply of healthcare or welfare services. It is the third party which is responsible for providing healthcare to the final patient, rather than the business supplying the staff which has no such responsibility.

A taxable supply of staff is made even where the employment business is responsible for ensuring that the workers it provides are properly trained and qualified when they work under the control of the third party.

Supplies of locum GPs

Where an employment business supplies a locum GP to a practice, the employment business' only responsibility is to make a taxable supply of staff to the practice, not exempt healthcare to the final patient.

Supplies of nurses, nursing auxiliaries and care assistants by state regulated agencies

The nursing agencies' concession

By concession (HMRC regularly reviews these), nursing agencies (or employment businesses that provide nurses and midwives, as well as other health professionals) may exempt the supply of nursing staff and nursing auxiliaries supplied as a principal to a third party, if the supply is of:

- a person registered in the register of qualified nurses and midwives maintained under article 5 of the Nursing and Midwifery Order 2001
- an unregistered nursing auxiliary who is "directly supervised" by one of the above, or
- an unregistered nursing auxiliary, whose services are supplied to a hospital (NHS or private), hospice, care home with nursing under item 4 of Group 7, Schedule 9 VAT Act 1994 and form part of the care made to the patient.

The institution to which staff are supplied may be operated by a local authority, NHS body, charity or other organisation operating in the public or private sector.

To qualify for the concession, the employment business must be registered with one of the following organisations:

- Care Quality Commission (formerly the Commission for Social Care Inspection)
- Scottish Commission for the Regulation of Care
- Care Standards Inspectorate for Wales, or
- N Ireland Health & Personal Social Services Regulation & Improvement Authority.

For the supply of nursing auxiliaries or care assistants to benefit from the concession, they must undertake some direct form of medical care, such as administering drugs or taking blood pressures, for the final patient. The concession does not apply to supplies of general care assistants who are only involved in providing personal care such as catering, washing or dressing the patients or who are working in care homes without nursing where they do not require supervision by health professionals to provide their services.

However, where a state-regulated domiciliary care agency supplies the services of its care assistants directly to the final patient, we would see the agency as making an exempt supply of welfare services - see Public Notice 701/2 Welfare and the section headed "Supplies of contracted-out welfare services" below.

Supplies of contracted-out welfare services

As is clear from above, employment businesses in the welfare sector make a taxable supply of staff to third parties, such as local authorities, if the third party is legally responsible for the onward supply of providing care to the final recipient. This is subject to the nursing agencies' concession. The mere fact that an employment business is state-regulated does not mean that its supplies of staff are exempt if they are not covered by the nursing agencies concession.

However, when state-regulated welfare providers provide welfare services to the final consumer, these services remain exempt even if they are contracted and paid for by a local authority or other third party. For example, a local authority may contract out the provision of domiciliary care services for the elderly or disabled to a state-regulated domiciliary care agency. Although the local authority rather than the final consumer may pay the domiciliary care agency charities for the care services, for VAT purposes the care agency has still made an exempt supply of welfare services rather than staff to the local authority. This is because the care agency's staff will still be working directly to the agency itself throughout the provision of the services rather than to the local authority.

Exemption would also apply to cases where a local authority or other body subcontracts the provision of adult placement schemes. Under these schemes a â€˜worker' provides personal care and/or support services to adults living with them or living in their own homes. Currently scheme providers need to be registered with the Care Quality Commission.

Sometimes local authorities make payments directly to people who have been assessed as needing help from social services, and who would like to arrange and pay for their own care and support services instead of receiving them directly from the local council. These arrangements are called direct payment schemes, and any welfare services provided to the recipient by a charity or state-regulated private institution or agency are again exempt from VAT.

The wording of terms and conditions of agreements

We are aware that some employment businesses state in their contract terms that their staff are still working under their control and direction rather than the third party to which their staff are being supplied. If that is the case you are no longer acting as an "employment business" within the definition of the Employment Act 1976. You are reminded that the VAT liability of a supply is not determined conclusively by the terms of any contract or other documentation alone. If the wording of a contract does not reflect any changes in the way that the business actually operates in practice, the VAT liability of a taxable supply of staff will not change.

Correcting errors

If businesses can demonstrate that they have taken reasonable steps to follow our previous guidance and that has resulted in their applying the wrong VAT treatment then we will take that into account when considering whether any corrective action is necessary.

Further information

Our public guidance will be updated in due course. If you are unsure of the correct VAT treatment of your supplies you should consult Notice 701/57 Health professionals and/or Notice 700/34 Staff . You may also contact our Helpline on 0845 010 9000 or by writing to HM Revenue & Customs, National Advice Service, Written Enquiries Section, Alexander House, Victoria Avenue, Southend, Essex, SS99 1BD

Changes to treatment of sports-related services

Changes to the VAT exemption for sports related services are being introduced from 1 September 2010. This will primarily affect affiliation fees charged by sports governing bodies to member clubs but the VAT treatment of other sports-related supplies may also be affected.

Background

Certain services closely linked with and essential to sport or physical education are VAT exempt when supplied by an eligible body (that is, essentially non-profit making bodies not subject to commercial influence) to an individual taking part in sport.

In respect of affiliation fees charged by sports governing bodies to their member sports clubs, we have previously restricted the exemption to fees calculated on a per person basis (provided the services were closely linked to sport). Affiliation fees calculated by other methods, for example, on the basis of the club size or the number of teams fielded, were standard rated for VAT.

However, the ECJ in the case of Canterbury Hockey Club and Canterbury Ladies' Hockey Club [2008] found that the exemption applies more widely. It has ruled that in the context of persons taking part in sport, the exemption includes services supplied to corporate persons and to unincorporated associations, provided that the supplies are closely linked and essential to sport, that they are supplied by non-profit making organisations and the true beneficiaries are individuals taking part in sport.

Implications

The ECJ ruling means that some supplies which were standard rated, for example because they were supplied to a corporate body or unincorporated association, may now be exempt from VAT if the services are closely linked and essential to sport and the true beneficiaries are individuals taking part in sport.

From 1 September 2010, eligible bodies meeting the conditions for exemption outlined in VAT Notice 701/45 Sport must exempt supplies where the true beneficiaries are persons taking part in sport, even if the supply is not made direct to an individual and irrespective of how the fee is calculated. Supplies made to commercial profit-making organisations do not meet the true beneficiary test and will not fall within the exemption for supplies of services closely linked and essential to sport.

Where the affiliation fee confers a number of benefits, which individually would be liable to different VAT treatment, the advice in section 4 of Notice 701/5 March 2002 will help determine whether there is a single or multiple supply. Where the conditions of Extra Statutory Concession 3.35 (apportionment of membership subscriptions to certain non-profit making bodies) are met governing bodies may continue to take advantage of the option to apportion their affiliation fees between the rates of VAT applicable to the individual elements. The ECJ gave some examples of services that do not fall within the exemption, including advice about marketing and the obtaining of sponsors. These will be liable to the standard rate of VAT when ESC 3.35 is applied unless relief is available under another part of the VAT Act.

This policy change may also affect some other supplies closely linked and essential to sport by eligible bodies to corporate persons and unincorporated associations where the true beneficiary is a person taking part in sport. An example could be the letting of sports facilities to a club for the direct use of its members. In these circumstances, the supply is exempt if the club is non-profit making. Otherwise it will be taxable.

Making claims or adjustments

The changes described above must be implemented from 1 September 2010 and there is no requirement to make adjustments in respect of supplies made prior to this date. However, any organisations wishing to implement the judgment before 1 September 2010 (and start exempting affected fees from an earlier date) are entitled to do so.

Where a business wishes to make a claim to us (under section 80 of the VAT Act 1994) for repayment of VAT incorrectly accounted for on sports related services, they may do so, subject to the conditions set out in Notice 700/45 How to correct VAT errors and make adjustments or claims.

All claims will be subject to the four-year time limit in section 80(4) of the VAT Act 1994 and to the set-off provisions in section 81 of the VAT Act and section 130 of the Finance Act 2008.

There may be direct tax implications where amounts of over-declared output tax are repaid to businesses and your attention is drawn to Revenue & Customs Brief 14/10.

We may reject all or part of a claim if repayment would unjustly enrich the claimant.

More details on making claims and 'unjust enrichment' can be found in VAT Notice 700/45 How to correct VAT errors and make adjustments or claims.

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