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BUDGET 2012 **(Lecture P706 – 23.16 minutes) (Lecture B706 – 26.24 minutes)**

The purpose of this note is not to highlight all the information in the Budget but to draw attention to the items that were new. We covered in the January material a summary of the items which were issued as a consultation for inclusion in the Finance Bill

The Finance Bill 2012 was of course published on 29 March 2012.

Inclusions which were not expected:

Personal Tax

Income Tax Rates 2013/14

The rates of income tax for 2013/14 will be: basic rate 20%; higher rate 40%; additional rate 45%; dividend additional rate 37.5%; trust rate 45%; and dividend trust rate 37.5%.

The charge on benefits paid to non-individuals under an employer-financed retirement benefits scheme will reduce from 50% to 45%. Where capital sums are deemed to be income of a settlor, the rate of tax taken as paid by the trustees will also reduce from 50% to 45%.

Basic Personal Allowance, Basic Rate Limit and Upper Earnings Limit for 2013/14

For 2013/14 the personal allowance for those aged under 65 will be increased to £9,205. The basic rate limit will be reduced to £32,245.

The National Insurance contributions upper earnings limit and upper profits limit will continue to be aligned with the level of the higher rate threshold (the total of the personal allowance and the basic rate limit).

Age-related Personal Allowances

For 2013/14 the higher personal allowance available to people aged 65–74 will be restricted to those born after 5 April 1938 but before 6 April 1948. The higher personal allowance for those aged 75 and over will be restricted to those born before 6 April 1938. The amounts of these allowances will not be increased from their 2013/14 levels. Eventually there will be a single personal allowance for all taxpayers.

Child Benefit: Income Tax Charge for those on Higher Incomes

With effect from 7 January 2013, an income tax charge is being introduced as a means of clawing back child benefit from those on higher incomes. Entitlement to the child benefit itself and the amount of the benefit will both remain unchanged. The charge will apply to recipients of child benefit whose income exceeds £50,000 in a tax year and to individuals whose partner is in receipt of child benefit and whose own income exceeds £50,000. In the event that both partners have income over £50,000, the charge will apply only to the partner with the highest income. Partners for this purpose include married couples, civil partners, unmarried couples and same-sex couples not in a civil partnership. Income will be measured by reference to adjusted net income, which is broadly taxable income before deducting the personal or blind person's allowance, adjusted for any pension contributions paid net of tax and Gift Aid donations.

For those with income between £50,000 and £60,000, the amount of the charge will be 1% of the amount of benefit for every £100 of income above £50,000. For example, if total child benefit is £1,752 and adjusted net income is £54,000, the tax charge will be £700.80 (£17.52 x 40).

For those with income above £60,000, the amount of the charge will equal the amount of child benefit received, so that the benefit will be fully clawed back.

The tax will be collected via PAYE and self-assessment. Child benefit claimants will be able to elect not to receive the child benefit to which they are entitled if they or their partner do not wish to pay the tax charge. The claimant can subsequently withdraw that election if they or their partner are no longer liable to pay the charge.

Cap on Unlimited Tax Reliefs

Legislation will be introduced in Finance Bill 2013 to apply a cap on income tax reliefs claimed by individuals for 2013/14 onwards. The cap will apply only to reliefs which are currently unlimited. For anyone seeking to claim more than £50,000 of these reliefs, they will be capped at 25% of income or £50,000, whichever is the greater.

Enterprise Management Incentives

The limit on the value of shares over which an employee may hold options under the Enterprise Management Incentives scheme will be increased from £120,000 to £250,000 from a date to be announced. The Government intends to implement the measure as soon as possible, subject to EU State aid approval.

Qualifying Time Deposits

Legislation is to be included in Finance Bill 2012 to require banks, building societies etc. to deduct sums representing income tax at the basic rate from interest on qualifying time deposits (generally deposits of at least £50,000). The legislation will apply only to such deposits opened or made on or after 6 April 2012.

Company Car Tax Rates

For 2014/15 the appropriate percentage of list price for cars emitting more than 75g of CO_2 per kilometre will be increased by one percentage point up to a maximum of 35%. For 2015/16 and 2016/17 there will be an increase of two percentage points up to a maximum of 37%.

From April 2015, the five-year exemption for zero carbon emission cars and the lower rate for ultra low carbon emission cars will come to an end. The appropriate percentage for zero emission and all low carbon cars emitting less than 95g of CO_2 per kilometre will be 13% in 2015/16, and will increase by two percentage points in 2016/17.

The diesel supplement will be removed in April 2016.

Company Car Fuel Benefit Charge

For 2012/13, the multiplier (the figure to which the appropriate percentage is applied) for calculating the car fuel benefit charge is increased from £18,800 to £20,200. There is a further commitment to increase the multiplier by 2% above the rate of inflation (RPI) for the tax year 2013/14.

Charge on Non-resident Non-natural Persons

The Government will consult on the introduction of a capital gains tax charge on residential property owned by non-resident, non-natural persons, and the consultation will be made in conjunction with the stamp duty land tax enveloping annual charge for high-value residential properties. The charge will be introduced in Finance Bill 2013 with the measure coming into effect in April 2013.

IHT - Spouses and Civil Partners Domiciled Outside the UK

The Government will consult on legislation to increase the IHT-exempt amount that a UK domiciled individual can transfer to their non-UK domiciled spouse or civil partner. The Government similarly proposes to allow individuals who are domiciled outside the UK and who have a UK domiciled spouse or civil partner to elect to be treated as domiciled in the UK for the purposes of IHT. Legislation will be in Finance Bill 2013.

Pensions Tax Relief

Legislation will be introduced in Finance Bill 2013 to amend the rules which currently allow employers to pay pension contributions into their employees' family members' pensions as part of their employees' remuneration package to remove the tax and NICs advantages from these arrangements.

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Business Tax

Tax Simplification for Small Businesses

The Government is to consult on introducing a voluntary cash accounting basis for unincorporated businesses with receipts up to the amount of the VAT registration threshold, with a view to introducing legislation in Finance Bill 2013. It will also consult on a simplified expenses system for business use of cars, motorcycles and the home and on proposals to introduce a tax relief for disincorporation of businesses carried on by companies.

Personal Service Companies and IR35

The Government intends to bring forward a package of measures to tighten up on avoidance through the use of personal service companies, and to make the existing IR35 legislation easier to understand. This will include HMRC strengthening specialist compliance teams, simplifying the way IR35 is administered, and consulting on proposals which would require office holders and controlling persons, who are integral to the running of an organisation, to have PAYE and NICs deducted at source.

Enterprise Zones First-year Allowances

Finance Bill 2012 will introduce legislation to provide 100% first-year allowances for expenditure incurred by trading companies on qualifying plant or machinery for use primarily in certain designated assisted areas within enterprise zones. The qualifying expenditure must be incurred between 1 April 2012 and 31 March 2017, the area in which the plant or machinery is to be used must be an assisted area at the time when the expenditure is incurred, and the plant or machinery must not be held for use in an area outside of the designated assisted area for a period of 5 years.

The usual general exclusions will apply including the exclusion of expenditure on assets for leasing.

First-year Allowances for Low Emission Cars

The 100% first-year capital allowance for businesses purchasing low emission cars will be extended for two years beyond the current expiry date of 31 March 2013, except for leased cars. Also, from the same date the qualifying threshold will be reduced from 110g/km to 95g/km driven.

Emissions Threshold for Main Rate Cars

The threshold for a main rate car will be reduced from 160g/km to 130g/km, and the associated lease rental restriction will also be revalorised in line with this change. These changes will have effect from 1 April 2013 (corporation tax) or 6 April 2013 (income tax).

First-year Allowances for Gas Refuelling Equipment

The 100% first-year capital allowances for plant and machinery used in gas, biogas and hydrogen refuelling stations will be extended for two more years to 31 March 2015.

Corporate Tax

Main Rate of Corporation Tax

The main rate of corporation tax for companies with profits above the upper limit of £1.5m will be reduced to 24% from 1 April 2012, 23% from 1 April 2013 and 22% from 1 April 2014. The main rate for companies with profits arising from oil extraction and oil rights in the UK and the UK Continental Shelf (ring-fence profits) will remain at 30%.

Small Profits Rates

The small profits rate of corporation tax remains at 20% from 1 April 2012. The small profits rate for ring-fence profits remains at 19%.

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Corporation Tax Reliefs for the Creative Sector

Corporation tax reliefs for the production of culturally British video games, television animation programmes and high-end television productions are to be legislated for in Finance Bill 2013, and will take effect from 1 April 2013, subject to State aid approval. Consultation on the design will take place over the summer.

Anti-avoidance

General Anti-abuse Rule

The Government has accepted the recommendation of the Aaronson Report that there should be a General Anti-abuse Rule (GAAR) targeted at artificial and abusive tax avoidance schemes. The Government will consult on draft legislation in the summer of 2012, with a view to introducing legislation in Finance Bill 2013. The GAAR will be extended to stamp duty land tax.

Post-cessation Trade Relief

Legislation will be introduced in Finance Bill 2012 to deny post-cessation trade relief and capital gains relief for payments or events which are made or occur directly or indirectly in consequence of, or in connection with, tax avoidance arrangements the main purpose of which is the obtaining of a reduction in tax liability as a result of post-cessation trade relief.

The amendments will apply to payments made, or events occurring, on or after 12 January 2012 except where a payment is made pursuant to an unconditional obligation in a contract made before that date.

Property Loss Relief against General Income and Post-cessation Property Relief

Finance Bill 2012 will amend legislation to deny agricultural property loss relief and post-cessation property relief for expenses arising, or a payment or an event which is made or occurs, directly or indirectly in consequence of, or in connection with, tax avoidance arrangements, the main purpose of which is the obtaining of a reduction in tax liability as a result of the reliefs.

The amendments will apply to expenses arising and payments made, or events occurring, on or after 13 March 2012 except where expenses arise or a payment is made pursuant to an unconditional obligation in a contract made before that date.

Stamp Duty

Rates for Residential Properties

A new 7% rate of stamp duty land tax is to be introduced for purchases of residential property where the consideration exceeds £2m. The new rate applies where the effective date of the transaction (usually the date of completion) is on or after 22 March 2012, subject to a transitional rule to ensure that the new rate does not apply to contracts entered into before 22 March 2012 but completed on or after that date.

Enveloping of High Value Residential Properties

Where a residential property is purchased on or after 21 March 2012 and the consideration exceeds £2m, a new higher rate of stamp duty land tax of 15% will apply if the purchaser or purchasers are certain types of non-natural person. For this purpose, non-natural persons include companies, collective investment schemes (such as unit trusts) and partnerships in which a non-natural person is a partner. Exclusions from the higher rate will apply for property developers and certain corporate trustees. A transitional rule will ensure that the new rate will not apply to transactions where the contract was completed and signed by all parties before 21 March 2012.

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VAT

Online Registration and Removal of the Threshold for Non-UK Established Businesses

With effect from October 2012, businesses will be able to register and deregister for VAT, and amend their VAT registration details, electronically. In addition, with effect from 1 December 2012 non-UK established businesses will be required to register for VAT regardless of the value of taxable supplies they make in the UK, i.e. such businesses will no longer benefit from the UK VAT registration threshold.

Low Value Consignment Relief

This measure removes, with effect from 1 April 2012, low value consignment relief from mail order goods imported into the UK. This is an anti-avoidance measure which prevents the VAT-free importation of consignment of goods with a value of less than £15 (prior to 1 November 2011, £18).

Cost-sharing Exemption

The cost-sharing exemption provided for in EU Directive 2006/112/EC, art 132(1)(f) is to be implemented in the UK with effect from Royal Assent to Finance Bill 2012. The measure will exempt from VAT the supply of services by a group which consists of persons engaged in exempt or non-taxable activities so long as the services are supplied to group members at cost and for the purposes of those activities.

Conditions may be imposed in connection with the application of the exemption.

Reduced Rate for Energy-saving Materials in Charitable Buildings

Legislation will be introduced in Finance Bill 2013 which will mean that buildings used for a relevant charitable purpose will no longer benefit from the reduced rate of VAT in respect of the supply and installation of energy-saving materials. The reduced rate will continue to apply to the supply and installation of energy-saving materials in residential accommodation, including accommodation operated by charities.

Approved Alterations to Listed Buildings

Zero-rating for approved alterations to listed buildings is to be removed with effect from 1 October 2012.

In addition, the '60% test' for the first sale or long lease of a substantially reconstructed listed building is to be removed, so that zero-rating will apply only if the reconstructed building incorporates no more of the original building than the external walls, together with other external features of architectural or historic interest.

Transitional arrangements will provide for the retention of zero-rating where a contract for reconstruction was entered into prior to 21 March 2012, and at least 10% of the work (by cost) was completed before that date.

Anti-forestalling measures will be introduced in Finance Bill 2012.

Hairdressers' Chair Rental

Legislation is to be introduced with effect from 1 October 2012 to ensure that the provision of chairs in a hairdressing salon to a self-employed stylist is standard-rated. This will be achieved by adding the provision of such chairs in a salon (together with related services) to the list of supplies which are excluded from exemption under VATA 1994, Sch 9, Group 1 Item 1.

Holiday Caravans

With effect from 1 October 2012, the zero-rating of caravans will apply only to those caravans which are designed and constructed for continuous year round occupation. This effectively means that all holiday caravans (not just mobile caravans) will be standard-rated.

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Hot Food and Premises

With effect from 1 October 2012, the meanings of 'hot food' and 'premises' for the purposes of VAT zero-rating will be clarified. From that date:

'hot food' means all hot food, with the exception of freshly baked bread; and

the sale of all food for consumption in areas adjacent to a retailer, or in areas that are shared with other retailers, is standard-rated.

Self Storage

Legislation is to be introduced with effect from 1 October 2012 to ensure that the provision of self storage facilities will be taxed in the same way as other storage facilities. This will be achieved by adding self storage facilities to the list of supplies which are excluded from exemption under VATA 1994, Sch 9, Group 1 Item 1.

Anti-forestalling legislation will come into force immediately.

Sports Nutrition Drinks

Legislation is to be introduced with effect from 1 October 2012 which provides for the standard-rating of 'sports nutrition drinks' (case law currently holds that some drinks in this category are not regarded as beverages, and are therefore not excluded from zero-rating).

From that date, sports drinks that are marketed as products designed to enhance physical performance, accelerate recovery after exercise or build bulk, and other similar drinks, including syrups, concentrates, essences, powders, crystals or other preparations of such drinks will be standard-rated.

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PERSONAL TAX

The new Seed Enterprise Investment Scheme (Lecture P708 – 22.29 minutes)

In his Autumn Statement late last year, the Chancellor announced that he would be introducing a special relief to encourage investment in new start-up companies. Subsequently, the Government published a lengthy Schedule for inclusion in the Finance Bill 2012 which covers most (but not all) of the draft SEIS legislation.

The SEIS provides individuals with three different tax reliefs:

(i) The SEIS offers income tax relief at 50% to taxpayers who subscribe, on or after 6 April 2012, for new ordinary non-redeemable shares in qualifying companies (see (c) below). Relief will be given at 50%, whether or not the individual is an additional rate taxpayer. Each investor has an annual limit of £100,000, but, as with the EIS regime, there will be a carry-back facility to the previous tax year. However, no tax relief is available to anyone who is an employee (or an associate of an employee) of the investee company – note that, for this purpose, directors are *not* regarded as employees. Also disqualified is any person who has a substantial interest in the company (ie. someone entitled to more than 30% of the company's ordinary share capital, issued share capital, voting power or assets in a winding up). The income tax relief cannot be claimed until the company has spent at least 70% of the money raised by the share issue on its business activities and has issued the necessary compliance certificate.

(ii) Gains realised by the individual on the disposal of qualifying shares will be exempt from CGT, provided that this takes place three or more years after the shares were issued.

(iii) For 2012/13 only, there is to be a one-off additional CGT relief: a gain arising on the disposal of any type of chargeable asset in that year will be exempt from tax as long as it is invested in SEIS shares. In particular:

- the gain must arise on a disposal made on or after 6 April 2012 and before 6 April 2013;
- the gain must be invested in new shares which are issued (fully paid up and wholly in return for cash) on or after 6 April 2012 and before 6 April 2013;
- the individual qualifies for SEIS relief in respect of this investment; and
- the new shares are held for at least three years.

The individual is not required to invest the whole of his sale proceeds in the new shares – the only stipulation is that he should invest an amount equal to his gain. Thus, if a rental property is sold for £250,000 and this gives rise to a gain of £75,000, the entire gain will be CGT-exempt as long as the disponor puts at least £75,000 into qualifying SEIS shares. Note that there is no requirement to reinvest the whole gain – in the above example, if the individual only invested £25,000 under the SEIS, one-third of the gain would be exempt from tax but the other two-thirds would remain fully chargeable (unless, of course, some other relief or exemption could apply).

The combined effect of (i) and (iii) above can provide an effective tax relief of as much as 78% for the first year of the scheme's operation.

The official explanation is that the SEIS is intended to be focused on 'smaller early stage companies carrying on, or preparing to carry on, a new business in a qualifying trade'. In order to achieve this focus, there are

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numerous conditions, all of which must be satisfied, before a company can come within the SEIS. The key ones are as follows:

(i) the investee company must have been incorporated within the two years ended on the date when the SEIS shares are issued (this is presumably intended to discourage the purchase of 'off the shelf' companies from company formation agents);

(ii) the purpose of the investee company's existence must be to carry on a trade which is a 'genuine new venture';

(iii) the investee company must not control, or be under the control of, any other company;

(iv) the investee company must not be a member of a partnership;

(v) the investee company must be an unquoted company;

(vi) the investee company must have a permanent establishment in the UK;

(vii) immediately prior to the issue of the SEIS shares, the investee company's gross assets must not exceed £200,000;

(viii) the SEIS shares must be issued wholly in return for cash and must be fully paid up at the time when they are issued;

(ix) at the time when the SEIS shares are issued, the investee company must have fewer than 25 employees (including directors) – however, only the appropriate fraction of a part-time member of staff is counted in this total; and

(x) no EIS or VCT investment should have been made in the investee company on or before the date on which the SEIS shares are issued.

A further significant restriction is that each investee company is subject to a cumulative investment limit, namely that the maximum total funds which it can raise from issuing SEIS shares is £150,000.

The reference in the draft legislation to the investee company carrying on a 'qualifying trade' means that the same requirements and restrictions which apply in the context of the EIS regime (see Ss189 and 192 – 200 ITA 2007) are also relevant here.

As might be expected, the SEIS is subject to numerous anti-avoidance rules which comprise a substantial part of the draft legislation.

Following a successful SEIS share issue, an investee company is to be allowed subsequently to raise further funds under the existing EIS regime. However, the EIS rules are modified so that:

(i) the investee company cannot issue any EIS shares until it has spent at least 75% of the funds which it raised from the SEIS share issue; and

(ii) the maximum amount which the investee company is permitted to raise under the EIS must take into account the moneys raised under the SEIS.

Although, in due course, the life of the SEIS may be extended, it is currently intended that the scheme will apply for a five-year fixed period, namely to shares issued on or after 6 April 2012 and before 6 April 2017.

While the introduction of the SEIS has generally been welcomed, there has been considerable criticism of one particular aspect of the scheme. In the words of one commentator:

‘The cumulative SEIS investment limit of £150,000 per company could prove to be something of a barrier to third party investors such as “business angels”. In particular, given that almost all start-up companies are very high-risk investments, the third party investor will wish to undertake or commission appropriate due diligence before investing. If the total cost of that due diligence amounts to a substantial fraction of the total SEIS tax relief potentially available to the investor, then the whole investment may cease to be viable for the investor.

Hopefully, therefore, the Government may be persuaded to increase the cumulative per company limit significantly, perhaps to £500,000 or £1,000,000. If the cumulative limit is raised significantly, then:

(i) the total cost of due diligence should become less of a barrier; and

(ii) several investors investing together could each bear a fraction of the costs.’

<u>Post Script</u>

The Budget announced that changes will be made to the legislation to:

- qualify if they have subsidiaries
- determine eligibility by reference to the age of any trade rather to the age of the company
- remove reference to the holdings of other entities in calculating asset and employee tests
- allow previous (but not current) employees to qualify and
- allow directors who have qualified under SEIS to continue to qualify under EIS subject to time limits

Contributed by Robert Jamieson

American taking employment in London – Temporary workplace?

An American citizen (L) took up employment with Goldman Sachs in London in 2004. He rented a house in the UK, and claimed deductions for the rent, the costs of travel from the house to his office, and for 'subsistence expenses'.

HMRC rejected the claim and L appealed, contending that since he had intended to return to the USA within two or three years, his office in London should be treated as a 'temporary workplace' for the purposes of s339 ITEPA 2003.

Decision:

The First-tier Tribunal rejected this contention and dismissed L's appeal. Judge Radford held that the London office 'did not qualify as a temporary workplace and therefore the travel and subsistence expenses were not deductible'.

Comments – s339 ITEPA 2003 defines a 'temporary workplace' as 'a place which an employee attends in the performance of the duties of the employment for the purpose of performing a task of limited duration, or for some other temporary purpose'. The First-tier Tribunal upheld HMRC's view that, although the appellant did not intend to stay in the UK for more than three years, the London office from which he worked did not qualify as a 'temporary workplace' for the purpose of this provision. Accordingly, his travelling costs, and the cost of renting a house in London, were not allowable deductions. It is essential to distinguish between a temporary workplace and a permanent workplace to ensure that the expenses are properly allowable as a deduction.

S Long v HMRC (TC01843)

Interpretation of anti-avoidance legislation to gain double tax relief

An individual (S), who was resident in the UK, had helped to form a Delaware limited liability company (H). The US authorities charged tax on S's share of H's profits, treating H as a transparent entity. S claimed double taxation relief for the US tax. HMRC issued discovery assessments for 1997/98 to 1999/2000, and amendments to S's self-assessments for 2000/01 to 2003/04, on the basis that H should not be treated as transparent and that S was not entitled to double taxation relief.

Decision:

The Upper Tribunal upheld the assessments and amendments. Mann J held that, on the facts found by the First-tier Tribunal, S had no 'form of proprietary entitlement' to H's profits. H was not transparent, and S was not entitled to double taxation relief under the US/UK Treaty. S requested a further hearing, contending that he should have been charged under ICTA 1988 s 739, and that any such assessments would have qualified for relief. In HMRC v Anson (No. 2) (Upper Tribunal — 20 February), Mann J rejected this contention, observing that it would appear 'to be extremely odd that a section which in terms is expressed to have anti-avoidance as its purpose can actually be turned to account by the taxpayer invoking it', and holding that HMRC had been entitled to conclude that S had fulfilled the conditions of ICTA 1988 s 741, and that the assessments had been issued on a correct basis.

Comments - The Upper Tribunal upheld HMRC's contention that the investor was not entitled to double taxation relief. For a discussion of the substantive decision, see 'Reviewing the impact of Anson' (Pete Miller) Tax Journal, dated 9 September 2011. The Tribunal also rejected an unusual interpretation of ICTA 1988 s 739, which had been propounded by counsel for the investor. Mann J's comments are self-explanatory.

HMRC v Anson (No. 1) Upper Tribunal

New guidance on Gift Aid declarations: What charities need to do

HM Revenue & Customs (HMRC) Charities published updated guidance on Gift Aid declarations and provided new model declarations on 24 February 2012. This guidance was developed with the help of charity sector representatives to help ensure that charities give a full and correct explanation of the law to their donors before the donor makes the declaration.

Since the publication of the revised guidance HMRC has received a number of queries in regards to these changes and to clarify matters we have provided further information for charities and donors.

It has always been the case that the donor must pay enough tax to cover all of their charitable donations and not just the donations made to that particular charity at that particular time. The mandatory information on the forms ensures that the donor is making an informed declaration, and understands the consequences if they have not paid enough tax to cover all the donations they make under Gift Aid, not just those to one charity or CASC. By incorporating the required information set out in the guidance on the Gift Aid declaration form, charities can be certain that HMRC will not challenge the associated Gift Aid claim on the grounds that the donor gave a valid declaration.

The Gift Aid declaration does not need to incorporate all the information set out in HMRC's model declaration in the guidance if the charity provides that information to donors in a different way, for example if volunteers explain the Gift Aid rules verbally using a set script that includes the mandatory information. But incorporating the information on the form is the simplest way for charities to show they have explained the tax consequences to the donor and ensure that the donor’s Gift Aid declaration is valid.

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Charities do not need to change their existing Gift Aid forms immediately; HMRC will continue to accept Gift Aid claims on donations made using forms based on the wording in the old HMRC model declaration until 31 December 2012. However where possible charities should seek to incorporate any additional information required under the new guidance as soon as possible, or amend their processes to ensure that staff and volunteers are providing the correct information to donors.

Charities might also like to remind donors who have made enduring Gift Aid declarations of the rules on tax to cover, perhaps through their regular mailshots.

Finally, where a charity has already received a Gift Aid declaration based on the old wording in the guidance they do not need to ask the donor to supply a new declaration with the new wording to support that donation for gift aid purposes. It is only new and where charities are replacing enduring declarations going forward that need to be based on the revised wording. Charities may chose to replace their existing enduring declarations with new ones based on the new guidance if they so wish but there is no requirement that they do so.

New definition of a charity will apply to all UK charity tax reliefs from April 2012

The Finance Act 2010, Schedule 6, Part 2 (Commencement) Order 2012. S.I.2012/736 and the Finance Act 2010, Schedule 6, Part 1 (Further Consequential and Incidental Provision Etc) Order 2012/735 were made on 8 March to apply the new definition of a charity under Schedule 6 of Finance Act 2010 to all UK charity tax reliefs and exemptions administered by HMRC not already covered by the definition, from 1 April 2012 onwards.

Personal Liability Notices - Test is subjective

The taxpayer was the finance director of W and Co until he resigned in February 2007. The company went into liquidation owing HMRC National Insurance of some £321,306. In September 2009, HMRC issued a personal liability notice to the taxpayer under s121C Social Security Administration Act 1992. This states that if a company fails to pay National Insurance and the loss can be attributed to neglect or fraud, the company's directors become liable for the outstanding amount.

The taxpayer appealed saying that the failure to pay National Insurance was not the result of neglect or fraud on his part. He said further that he suffered from an addiction which affected his behaviour and this should be taken into account when deciding whether or not he had been negligent in carrying out his duties. HMRC said the negligence and fraud test was an objective one and the taxpayer's state of mind was irrelevant.

HMRC and the taxpayer were subsequently invited to present written arguments on whether the test was objective or subjective.

Decision:

The First-tier Tribunal said that s 121C was a penal measure which could be used to transfer a financial obligation from the employer, i.e. the entity legally liable to pay it, to officers of the company. In relation to the word 'neglect', the legislation used the word 'culpable' which was defined in the Oxford English Dictionary as guilty, criminal and deserving of punishment. Thus 'neglect' did not have an objective meaning, but had to be read as requiring mens rea of the individual involved.

The taxpayer's appeal was allowed.

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Comments – The Tribunal considered the matter in some depth and came to the conclusion that as s 121C is a penal provision, the tribunal should be careful in how the legislation is construed. HMRC's view is that as the legislation is clear, the intention of Parliament expressed in Hansard is not relevant (*Pepper v Hart*). However in *J E Chilcott & Others v R & C Commissioners [2009] STC 453* , subsequently upheld by Lord Neuberger with the following - 'The fact that some might regard the operation of s 144A, according to its terms as penal, merely emphasises that the court should construe it with care and if there is a narrower construction less beneficial to the Revenue, more beneficial to the taxpayer, available then the court should at least seriously consider it, and if appropriate, adopt it.'

O'Rorke (TC1675)

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CAPITAL TAXES

Residence: stockbroker returning to UK with gain on disposal

A British subject (K) had been a partner in a firm of stockbrokers. He had been resident in the UK from 1994 until September 1997, when the firm posted him to an office in Japan. He continued to work in Japan until he resigned from the partnership on 11 July 2005. He returned to the UK on 17 July and stayed at his mother's house in Kent until 30 July, when he went to Italy on holiday. He remained in Italy until 28 August. While he was in Italy, he disposed of a significant holding of shares. HMRC issued a ruling that CGT was chargeable on the disposal, on the basis that K had become resident in the UK when he returned from Japan on 17 July. K appealed, contending that he should be treated as not having become resident in the UK until he returned from his Italian holiday on 28 August.

Decision:

The First-tier Tribunal rejected this contention and dismissed the appeal, finding that while K was in Kent, and before he travelled to Italy, he had agreed to lease a property in Norfolk. Judge Nowlan concluded that 'at some time before 30 July, even if not on 17 July, the appellant formed the intention to stay in the UK permanently and then became resident'.

Comments - The Tribunal upheld HMRC's view that the appellant, who had been resident in Japan for several years, had become resident in the UK by the time he disposed of the shares. If he had made the disposal a few weeks earlier, he would have avoided the charge to CGT. This case demonstrates the vagaries of the current rules on residence. The Statutory Residence Test which will be legislated shortly and which will operate from 6 April 2013 will give far more certainty. This situation could then potentially be avoided.

R Kimber v HMRC (TC01803)

Determining the year of an assessment

The taxpayer's father owned three flats which he transferred to her by way of a gift. The relevant documentation showed a transfer date of 2 December 2002, but the beneficial interest on flat B was transferred to the taxpayer in July 2000, while that of flats A and C was transferred in July 2002. The transfers gave rise to a capital gains tax liability which was not paid by the father before he died in June 2003.

HMRC raised a capital gains tax assessment for 2002/03 on the taxpayer's late father in July 2007. While the tax was agreed, it remained unpaid. In August 2009, HMRC sent a notice of assessment under s282 TCGA 1992 (recovery of tax from donee) to the taxpayer requiring payment of the tax.

The taxpayer said the assessment was wrong. The valuations of the flats were understated and flat B had been sold in 2000/01. Furthermore, the assessment should have been for 2009/10, the year it was issued, rather than 2002/03, and that no interest on the unpaid tax was due.

Decision:

The First-tier Tribunal said that HMRC were entitled to raise the s 282 assessment on the taxpayer. As to the year the assessment should relate to, s 282 did not specify the year for which an assessment on a donee should be made. However, it was 'a distinct and different assessment from that on the donor'. Its purpose was to provide a mechanism for outstanding tax to be paid, rather than determine a new liability. The tribunal

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judge concluded that the year of assessment should be the year in which the s 282 assessment was made. This meant that interest could only run from the year the assessment is made.

The tribunal decided that as the s 282 assessment was made in August 2009, it followed that it was for 2009/10, not 2002/03.

The taxpayer's appeal was allowed.

Comments – This case demonstrates the importance of determining the exact history of transactions and therefore the tax consequences that follow from that. In this case the assessment made on the daughter in the absence of the payment of tax in respect of the father's estate means that it is an assessment in a completely different capacity with the result that the due date for payment and consequently the interest that might result from late are different.

Z Hamar (TC1529)

Avoidance scheme succeeds

The taxpayer, who was UK resident and domiciled, had realised a substantial gain on the sale of a business, and did not dispute that he had entered into a scheme to avoid capital gains tax by ensuring that the gain was realised by a non-domiciled beneficiary of a trust who did not remit it. The transaction occurred in 2002, prior to the introduction of the remittance basis charge and the targeted anti-avoidance rules on chargeable gains.

The taxpayer exchanged shares standing at a gain for loan notes situated outside the UK and with a value of £1.18m. He claimed that s135 TCGA 1992 should apply to hold over the gain on this paper-for-paper exchange. The loan notes were then sold to a trust for £900.

This sale was a 'backstop' in case the planning failed, to ensure that taper relief would then be given. If the planning had failed, the sale price would have been increased to £1.16m.

The trust borrowed £1.16m from a bank, secured against the loan notes. The trust was then divided into two funds: Part A consisting of the £1.16m and Part B of the loan notes plus the liabilities to the bank.

The trust was an interest in possession trust in favour of the taxpayer, but with an overriding power of appointment. A suitable non-UK-domiciled beneficiary had been found, Mr Gower (AG), who was unconnected to the taxpayer. He was appointed as the beneficiary of Part B of the trust but expressly subject to a lien for the bank borrowing, leaving the taxpayer as the unencumbered beneficiary of Part A. The loan notes were then sold for their face value of £1.18m. The £20,000 difference between this and the bank borrowing was the fee to AG for taking part in the scheme.

The taxpayer claimed that the sale had been made by a non-domiciled beneficiary absolutely entitled to the loan notes by virtue of s71(1) TCGA 1992, and that the lien for the bank borrowings was ignored under s60(2) TCGA 1992, therefore no tax was due. HMRC claimed that, construed purposively, AG had not become absolutely entitled under the meaning of the section.

Decision:

The First-tier Tribunal considered first whether AG had become absolutely entitled to the loan notes under general law, and concluded that he had. They then considered the Ramsay principle, as elaborated in subsequent cases, particularly the review of it by Lewison J in Berry v CIR [2011] STC 105. The statutory principle requires the identification of the transaction which will answer to the purposive construction of the statute, and then a consideration of whether the transaction in question does so. While the interpretation of the statute does not have to be literal, the more comprehensively Parliament has set out the scope of a provision, the less room there is for a non-literal interpretation.

In this case, AG had, both literally and realistically, acquired an absolute right to the loan notes, and there was a clear statutory disregard of the lien of the trustees for the bank borrowings. The transaction did fall within the statutory description, and the taxpayer had not made a capital gain, notwithstanding the tax avoidance motive.

The taxpayer's appeal was allowed.

Comments – This case demonstrates an uncommon beast – a tax avoidance scheme that succeeds in the Courts. It needs to be remembered that the approach to tax avoidance was completely different at the time. You will be aware that the Government has approved the creation of a GAAR and therefore such planning is of the past.

McLaughlin (TC1870)

Some practical points on entrepreneurs' relief **(Lecture P709 – 14.27 minutes)**

The recent publication of the Tax Faculty's TAXLINE 1/12 has highlighted a number of practical points of interest in connection with entrepreneurs' relief. A representative selection of the matters considered appears below.

5% rule for shares

One intriguing conundrum relates to the 5% rule for shares set out in S169S(3) TCGA 1992. Imagine the following situation (and assume that all the other conditions for entrepreneurs' relief are satisfied):

- Adam holds 5% of the ordinary share capital of a company and has done so throughout the period of one year up to the date of the sale of the company's entire share capital.
- In the company, there are holders of share options who intend to exercise their entitlements and acquire shares on the date of sale (ie. shortly before taking part in, and signing, the sale contract).
- The sale contract is entered into at, say, 1200 on the day of sale.
- By virtue of the exercise of the options earlier in the day, Adam holds *less than* 5% of the ordinary share capital at the time of his disposal (ie. when the contract is signed).

Does Adam fail to meet the conditions in S169I(6) TCGA 1992?

HMRC's response is that Adam qualifies for the relief. They confirm that the words ('throughout the period . . . ending with the date of the disposal') must properly be interpreted as meaning that the period in question comes to an end at midnight on the day *prior to* the sale. Adam is therefore in the clear.

Associated disposals

By virtue of S169K TCGA 1992, entrepreneurs' relief is available in respect of a gain on an associated disposal, ie. the disposal of an asset owned personally by an individual which was used in the trade of his company or partnership. The associated disposal must be made as part of the withdrawal by that individual from participation in the business carried on by the company or partnership. The relief is restricted (inter

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alia) where, after 5 April 2008, the availability of the asset – for the whole or part of the period of business use – was dependent on the payment of rent by the company or partnership (S169P(4) TCGA 1992).

It is understood that, with partnerships, the restriction only applies where actual rental income is received by the partner. HMRC's view is that entrepreneurs' relief does *not* have to be restricted where there is an arrangement under which the partner receives a higher profit share in return for the partnership using his property.

HMRC have also confirmed that there is no de minimis limit for the reduction of the individual's shareholding or partnership interest in order to make a qualifying withdrawal from participation in the business.

Claims for remittance basis users

The deadline for making an entrepreneurs' relief claim is linked to the tax year in which the disposal is made, and *not* to the tax year in which the gain accrues to the disposer (see S169M(3) TCGA 1992). This can present a problem where the disposer is a remittance basis user. If a UK-resident non-UK domiciliary sells a foreign qualifying asset and makes a substantial capital gain, he may not know at this stage whether he will ever wish to remit the sale proceeds to the UK. However, if he does eventually do so, he can only be eligible for entrepreneurs' relief on the remittance if he has made a timely claim. The date when the proceeds are remitted is completely irrelevant.

For example, Henri is a UK-resident Frenchman who claims the benefit of the remittance basis. In 2011/12, he makes a gain of £5,000,000 on a disposal of shares in a French company (total proceeds = £8,000,000). He has never previously claimed entrepreneurs' relief and so his full £10,000,000 allowance is available. Henri does not expect to remit the proceeds from the gain for at least four years (having sufficient clean capital to supplement his UK income). If he wants to be able to benefit from entrepreneurs' relief on any future remittance of the proceeds, he has until 31 January 2014 to make his claim. The fact that he will not have remitted the proceeds by that date is immaterial.

Where a claim is required prior to the gain having been remitted, there will be no gain shown on the tax return. The claim should be made by way of a note to the return, with the entrepreneurs' relief computation included.

Contributed by Robert Jamieson

ADMINISTRATION

Real Time Information (Lecture P710 – 12.05 minutes)

The new Real Time information system will commence testing during 2012, with implementation due from April 2013. The following information is extracted from HMRC material on the subject.

Real Time Information (RTI) is a priority Government programme aimed at improving the operation of Pay As You Earn (PAYE). It will make the system better for individuals and easier for employers and HM Revenue & Customs (HMRC) to operate. It also supports the introduction of Universal Credits.

Currently, employers and pension providers send information about tax, National Insurance contributions (NICs) and other payroll deductions to HMRC after the end of each tax year. The result is that HMRC cannot correct mistakes until the employer sends this information.

However, under RTI, employers and pension providers will tell HMRC about tax, NICs and other deductions when or before the payments are made.
RTI will:

- make the PAYE process simpler and less burdensome for employers
- reduce costs for HMRC and enable it to deal with non-compliance (such as late payment and debt collection) more effectively
- support the payment of Universal Credits
- make PAYE more accurate for individuals, over time reducing the number of bills and repayments sent after the end of the tax year
- reduce tax credits error and fraud

Employers and pension providers will send this information to HMRC Online.

Timetable
HMRC currently envisage that all employers and pension providers will have joined the RTI system by October 2013. To make sure that the service is thoroughly tested and issues are resolved, HMRC will pilot the RTI service with volunteer software developers and employers for a year, starting in April 2012.

HMRC also envisage that most employers and pension providers that haven't joined the RTI system during 2012-13 will do so in April 2013, and that RTI will be routinely operating by no later than October 2013. HMRC will notify all employers and pension providers about their obligations in due course.

HMRC will continue to work closely with employers, payroll providers and the software and banking industries over the coming months and throughout the pilot period to help ensure that the process of sending information under the RTI system is as easy as possible.

Employer FAQ’s
Q: What will RTI do?

A: Under RTI, employers and pension providers will tell HMRC about tax, National Insurance contributions (NICs) and other deductions when or before the payments are made, instead of waiting until after the end of the tax year.
RTI will:

- make the PAYE process simpler and less burdensome for employers and HMRC; for example by removing the need for the end of year return (P35 and P14) and simplifying the employee starting and leaving processes
- make PAYE more accurate for individuals, over time reducing the number of bills and repayments sent after the end of the tax year

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- enable HMRC to pursue late payments more effectively
- support the payment of Universal Credits
- reduce Tax Credits error and fraud

Employers and pension providers will send this information to HMRC online.

Q: How does RTI support the payment of Universal Credits?

A: RTI will support Universal Credits by providing the Department for Work and Pensions (DWP) with up to date information about claimants' employment income, enabling them to calculate Universal Credits payments without the need for claimants to supply employment or pension income information.

Q: Why change the PAYE system?

A: RTI will enable HMRC to improve the way that the PAYE system operates and builds on the work already done with the introduction of the National Insurance and PAYE Service (NPS).

Under the current PAYE system employers tell HMRC what deductions they have made from employees pay after the end of the tax year. Only then are HMRC able to review whether the correct deductions have been made under PAYE.

Under RTI, HMRC will be receiving information when, or before payments are made and will be better able to ensure the correct deductions are made from pay. This will mean more employees will pay the right amount of tax and National Insurance in the tax year.

Q: How will RTI be less of a burden?

A: RTI reporting will become an integral part of an employer's normal payroll activity. When employers run their payroll the payroll software will gather the information required and send it to HMRC. This will be done using the internet through the Government Gateway or by using Electronic Data Interchange (EDI) on or before the date payment is made.
There will be transitional costs of introducing RTI but analysis indicates the system will be cheaper for employers and HMRC to operate once it is bedded in.

For HMRC it will mean that there are fewer individual customer records needing an end of year recalculation to determine what underpayments or overpayments have arisen.

<u>What changes will be made to the operation of PAYE under RTI (Section added 3 August 2011)</u>

Q: Will employers report all payments as part of their normal payroll activity?

A: Yes, employers and pension providers will send details of all payments made through the payroll irrespective of the amount of pay or pension.

Q: Will employers have to complete a form P46 when taking on a new employee who doesn't have a P45?

A: No, employers will not have to complete a form P46 and send it to HMRC. But they will need to obtain the P46 information from the employee and use it to complete the starter information which will be sent as part of the RTI payment submission, with details of the employee's first payment, when the payroll is run.

Q: Will employers use the form P38A (employers supplementary return) under RTI?

A: No, employers and pension providers will not need to complete an end of year return (P35 and P14) or P38A supplementary return, as they will tell HMRC about all payments made each time their payroll is run.

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Q: What will employers have to do at the end of the tax year?

A: Employers and pension providers will be expected to:
- indicate on their last payment submission on or before the 5 April that this is the final submission for the tax year
- provide each employee and pensioner with a form P60
- complete and file any forms P11D and P11D(b) due under the existing PAYE arrangements

Timetable for the introduction of RTI

Q: When will it happen?

A: Employers and pension providers will begin to use the RTI service in the period April 2013 to October 2013. All employers will be using the RTI service by October 2013.

RTI pilot

Q: How can employers be sure the service will work?

A: To make sure that the RTI service is thoroughly tested and issues resolved before April 2013, HMRC will pilot it with volunteer software developers and employers and pension providers for a year, starting in April 2012.

Q: How can employers be part of the pilot?

A: Plans for the April 2012 pilot are already well advanced and no additional employer volunteers are needed. However HMRC are looking at how to bring more employers onboard later in the 2012-13 tax year.

Q: I act as an agent on behalf of a number of employers and currently make all of their PAYE submissions for them. Do I need permission from my clients before I could take part?

A: Yes. An agent would need to have the agreement of the client employer.

Q: How were the pilot employers and software developers selected?

A: HMRC approached software developers to establish which products they would like to include in the pilot. The software developers then approached clients to see if they would be willing to volunteer. In addition, some employers approached HMRC direct as a result of the formal consultation.
In order to get the best of the pilot, it must be representative of a wide range of employers. HMRC used the following criteria to make sure that all significant types of employer are involved:
- software used
- employer size
- employee turnover
- geographical location
- those using bureaux

RTI reporting

Q: How will employers send information to HMRC using RTI?

A: In April 2013 there will be two methods of reporting:
- internet through the Government Gateway
- Electronic Data Interchange (EDI), which will be available until at least 2014

In addition to this, HMRC is working with the banking and software industries to develop - in the longer term - a service which will enable employers and pension providers who pay their employees or pensioners electronically (for example through Bacs) to send RTI alongside the payment instruction.
This would enable employers and pension providers who pay their employees or pensioners in this way to send RTI automatically at the same time as electronic payments are made to their employees.

Q: Will I have to pay my employees though Bacs?

A: No.

Q: Can employers still use HMRC's Basic PAYE Tools?

A: Yes. HMRC is developing Basic PAYE Tools (HMRC's free PAYE software for small employers) so that it is capable of RTI reporting.

<u>Security and the integrity of the systems used</u>

Q: Can the Government Gateway handle the number of RTI returns that will be made?

A: Yes, HMRC is confident that the Gateway can accommodate RTI volumes.

Q: How will HMRC know the data is correct?

A: HMRC will work with employers to help improve data accuracy - for example by identifying common errors or trends.
HMRC will also be undertaking a series of compliance checks after the employer has sent the data.

<u>Employee information - getting it right</u>

Q: Why is it important to check the details I hold about my employees are accurate?

A: It has always been important to make sure the information that you send HMRC about your employees is accurate to help ensure that your employees pay the correct Income Tax and NICs. Improving the accuracy of the information you hold and send to HMRC will help match the information to the correct HMRC record. This could save you money by helping to reduce the number of employee enquiries you receive.

This is not just important for tax and NICs. From October 2013, RTI will support Universal Credit by providing the DWP with up to date information about claimants' employment income. Ensuring your employee information is correct will help to ensure they receive the right amount of credit.

As part of the process for an employer joining RTI, HMRC will align the records of employees held on the NPS system and the records held by employers. HMRC will publish more information about the 'employer alignment' process soon.

In the meantime HMRC recommends that you start to prepare for RTI by checking the information you hold.

Help and support - addressing the essential data quality issues
Working with employers, pension providers, software developers and industry bodies, HM Revenue & Customs (HMRC) has developed some good practice, guidelines and templates to help improve data quality issues. The materials come in an easy-to-download and customised format to support you, your employees and stakeholders to get it right the first time. The following documents are available to download as PDF’s from http://www.hmrc.gov.uk/rti/dip/data-quality.htm

- How to record employee information accurately (PDF 39K)
- Accurate employee information matters - it can save you time (PDF 39K)

- Providing your employer with accurate personal information - it's important to get it right (PDF 187K)
- How to record pension recipient information accurately (PDF 178K)
- Accurate pension recipient information matters - it saves you time and money (PDF 195K)
- Providing your pension provider with accurate personal information - getting it right will save you money (PDF 187K)

Contributed by Rebecca Benneyworth

No message – Presumption of receipt of form?

The taxpayer partnership, which had filed its P35 employer end-of-year returns online and in good time for the years 2005/06 to 2008/09, appealed against a late filing penalty in respect of its 2009/10 return on the basis that it had been filed in April 2010. HMRC claimed that the return had not been received and that as no message had been received by the partnership acknowledging receipt, it should have known that the return had not been filed successfully.

Decision:

The First-tier Tribunal judge accepted that the partnership genuinely believed that it had filed the 2009/10 P35, having kept a copy of it for its records. She noted that when a return is filed, the taxpayer will receive one of two messages: one says the return has been successful, the other will say the return was rejected. No mention is made that if no message is received at all, the person filing the return should contact HMRC to see if there is a problem. Having not received any message, the partnership quite reasonably did not realise there was anything wrong.

The tribunal judge concluded that the taxpayer had 'intended to honour his tax liabilities' and had reasonable excuse for the late filing of the return.

The taxpayer's appeal was allowed.

Comments – We are having a lot of cases involving the late filing of P35s. Many of them which are successful that are because the taxpayer has done all they could in the circumstances but have been confounded by the quality and integrity of the software or HMRC’s attitude. There is an assumption by HMRC that taxpayers will know the system inside out and therefore they should be aware of whether the relevant documentation has been properly filed. It worth remembering also this year that ESC B46 was abolished last year which gave the extra seven days of grace.

Wayne Sneddon and Steve McMinn trading as The Bridge House Bar and Dining Room (TC1618)

Insufficient training on returns – Reasonable excuse

The taxpayer appealed against penalties, totalling £2,000, imposed for the late filing of P35 returns in respect of the tax years 2008/09 and 2009/10.

The clerk of the parish council concerned said she had reasonable excuse for filing the returns late. She had informed HMRC of a change to her address and, as all payment booklets had arrived at her correct address, assumed they were all she needed. After receiving the penalty letter in February 2011, she found that the P35 forms had been sent to her former address. She finally submitted the relevant returns in June 2011. This delay was caused by difficulties she experienced in coping with online filing.

Decision:

The First-tier Tribunal found that there was a reasonable excuse for the delay and that the returns had been filed within a reasonable time after the excuse ceased.

The taxpayer's appeal was allowed. The judge added that it appeared that the parish clerk had received no effective training in respect of her office as clerk to the parish council. She had struggled to understand and fulfil all her duties with regard to PAYE. He said that the chairman of the council should ensure that the clerk received adequate training to carry out her role to prevent the recurrence of further problems.

Comments – Another case demonstrating that taxpayers may necessarily know all that is expected of them by HMRC and in this case it was compounded by HMRC not sending the relevant documentation to the right address.

Mayfield Parish Church (TC1702)

Employers will be told sooner about late PAYE returns

The joint initiative between HM Revenue & Customs (HMRC), the professional bodies and tax charities launched in late 2011, set a number of service objectives for delivery during 2012. One of these was to work together to address concerns about the delay in informing employers that their PAYE end of year returns are late, and therefore subject to penalties. The background to this issue is that where employers do not file their annual P35 return by 19 May, they incur penalties of £100 per 50 (or fewer) employees for every month (or part month) that their return is late. In some cases, employers were unaware their returns were late until they received a first penalty letter in September covering four months worth of accrued penalties.

HMRC can now announce a number of agreed measures to deal with this problem. To help employers comply with their obligations, HMRC will:

- Change the date when they issue the 'Notification to complete form P35 Employer Annual Return 2011/12' from mid-February to mid-March 2012, so that employers will receive it much nearer to the end of the tax year.
- From 28 April 2012, where they believe a 2011-12 P35 remains outstanding, they will issue an ‘Employer Annual Return Reminder’. From 31 May 2012, introduce a 'P35 Interim Penalty Letter' which will be issued over a five day period, so that it reaches employers within a month of the filing deadline. The letter will state that the employer has incurred a late return penalty and explain what to do to avoid it increasing. HMRC has worked together with the professional bodies on the content of this letter and it has been tested on employers and payroll agents to make it clear and employer-focussed.
- Improve the online guidance for submitting P35s online, including specific advice about the test-in-live service to reduce the number of employers who believe their test submission is the live submission. The on screen messages within the HMRC online product will also make it much clearer that even when a successful test transmission has been made, a live transmission is still required. HMRC would encourage those using commercial payroll software (where the text of test/live messages may vary) to sign up for HMRC’s email alert facility to help them avoid this problem.
- Instruct Employer Helpline staff to tell employers about filing dates when setting up new employer schemes, to help them avoid a penalty.
- For next year, improve the information on the P35 and the reminders to include a warning that the first penalty notice will cover four months.

Taken together, these measures should help employers to avoid incurring unnecessary penalties and significantly reduce the number of cases where penalties in excess of £100 are charged.

Misdirection by HMRC

A self-employed radio presenter (S) claimed deductions for expenditure on clothing, cosmetics, hairdressing, and subsistence expenses. HMRC issued amendments to her returns for 2006/07 to 2008/09 disallowing the deductions. S appealed, contending that when she began self-employment in 2001, she had been informed by a HMRC officer (C) that she could claim a deduction where she spent money for the specific purpose of making public appearances, and that she could claim subsistence expenses if she was working at least five miles away from her normal place of work.

Decision:

The First-tier Tribunal accepted S's evidence, holding that as a matter of law, the expenditure was not deductible, applying the principles laid down in Mallalieu v Drummond [1983] STC 665 and Caillebotte v Quinn [1975] STC 265, but finding that S had been given incorrect advice by an HMRC officer. Judge Cannan expressed the view that he 'would expect HMRC to amend the review decision to allow (S's) claim under these headings for 2006/07'. However, by the time S came to complete her returns for 2007/08 and 2008/09, she was aware that HMRC had queried the claims which she had made for 2006/07, and she had been told by the officer conducting the enquiry that 'the wardrobe costs and subsistence expenses were not allowable for tax purposes'. Therefore S was no longer entitled to rely on the incorrect advice which C had given her. Judge Cannan observed that 'it would be unfair on taxpayers generally if (S) were able to insist on entitlement to relief where none would otherwise be available in the absence of clear unambiguous advice to the contrary'.

Comments - This appears to be an important case on the principle of 'misdirection', where the appellant has been misled by an HMRC officer. In this case, an officer who seems to have been ignorant of 20th century case law had apparently given the appellant seriously misleading advice which led her to believe that she could claim deductions for items of expenditure which the courts have held to be disallowable. The Tribunal held that, in view of the clear evidence of misdirection, the disputed expenditure should be allowed for the first of the years of assessment in question. However the Tribunal dismissed the appeal for subsequent years, since the appellant had by then been correctly advised by a different HMRC officer that the expenditure was not allowable, and it would be 'unfair on taxpayers generally' if she could continue to claim deductions for the amounts in question.

Ms L Stones v HMRC (TC01806)

Problem with getting UTRs

The agent for the taxpayer partnership submitted forms CWF1 (registering for self assessment if self-employed) and 64–8 to HMRC soon after the formation of the partnership. HMRC confirmed that they received the forms in September 2009 and advised the partners that they would receive a letter from HMRC with a UTR number, which they should notify to the agent.

The partners did not receive any such notification, so the agent called HMRC. The agent was told that there was a backlog and paperwork would be dealt with as soon as possible. The partnership wished to file its return on paper, as it would otherwise have to buy third party software to enable it to file online. However, as the partnership UTR was not received until after the paper filing deadline of 31 October 2010 it was impossible to submit the return on time.

The individual partners' tax returns were submitted online in January 2011. These included partnership income details and tax was paid on the partnership profits on 31 January 2011. The agent said that the first written notification of the UTR number was in response to their appeal and that immediately this was received the partnership tax return was filed on paper in May.

HMRC said that a reasonable person would have queried the missing UTR sooner, rather than leaving matters until mid-January 2011 to submit another CWF1 with the request for a partnership UTR number.

Decision:

The First-tier Tribunal decided that the agent had done everything possible to notify HMRC of the partnership formation. The partnership return could not be submitted until the UTR number had been received and the tribunal accepted that the partnership did not receive a notice to file a return, a paper partnership return or a UTR number.

The records showed that HMRC processed the CWF1 and form 64–8 submitted in September, but did not indicate that a partnership return or UTR number was sent to the partnership or its agent. The tribunal concluded that the partnership had shown reasonable excuse.

The taxpayer's appeal was allowed.

Comments – This case is a classic demonstration of the relevant data being needed to even start the process of completing a return. This is not a new problem and as the Tribunal judge pointed out the agent had done everything possible to fulfil his obligations. It is not surprising that in the circumstances the Tribunal held that the taxpayer had reasonable excuse.

C Norton t/a Oracle Fieldwork (TC1708)

E markets initiative

People trading on the internet who haven't paid all the tax they owe have been offered the opportunity to come forward and pay up under an HM Revenue & Customs (HMRC) campaign.

Under the time-limited opportunity, the e-Markets Disclosure Facility, online marketplace traders can pay the tax they owe and benefit from lower penalties available to those who come forward, rather than wait for HMRC to catch up with them.

Marian Wilson, head of HMRC Campaigns, said:

“This campaign is part of a wider HMRC initiative to provide support and guidance to the public on tax evasion and is aimed at people using online marketplaces to buy and sell goods as a trade or business and who fail to pay the tax owed.

“Those who only sell a few items and who are not traders are unlikely to be liable to pay tax on what they sell and will not be targeted by this campaign.

“Our aim is to make it easy for online traders to contact us and make a full disclosure of income, thereby putting their affairs in order.”

Under the opportunity, online marketplace traders can come forward at any time between 14 March and 14 June to tell HMRC they want to take part.

They then have until 14 September to give details of the tax owed and arrange for full payment, including any interest and penalty due. If they make a full disclosure of what they owe before 14 September, some will receive no penalty at all, with most receiving a penalty of no more than 10 per cent of the tax owed.

After that date, using information pulled together from many different data sources, HMRC will investigate those who have failed to respond. The department has recruited additional investigators and will pursue those who have failed to declare their earnings and pay up. Penalties of up to 100 per cent of the tax owed or even a criminal investigation could follow.

To take part:

- People must register with HMRC to “notify” that they plan to make a voluntary tax disclosure by 14 June.
- They then have until 14 September to tell HMRC about tax due and make arrangements to pay any tax interest and penalties owed. This is called “making a disclosure”.

How do they do this?

- From 14 March, online by completing a notification form at:

  http://www.hmrc.gov.uk/campaigns/notify.htm

- Phone HMRC on 0845 601 2944. A dedicated team is available to give information.

A YouTube video is available giving guidance to people wondering whether their buying and selling on an e-marketplace website can be seen as trading – http://www.youtube.com/watch?v=uptdjVD2LgI

HMRC will also hold an online Twitter Q&A on the e-Markets Disclosure Facility on 28 March. Details will be published in advance on HMRC’s Twitter account at @HMRCgovuk.

More than £500m has been raised by HMRC from voluntary disclosures, and a further £105m from follow-up activity. Previous campaigns have targeted offshore investments, medical professionals, plumbers and VAT defaulters.

Toolkits

HM Revenue & Customs has published the updated Expenses and Benefits from Employment Toolkit and the National Insurance Contributions and Statutory Payments Toolkit to help agents complete their clients' 2011-12 returns.

HMRC application to strike out appeals against forms P800

Three individuals sought to appeal against forms P800.

Decision:

The First-tier Tribunal accepted HMRC's application for the appeals to be struck out under SI 2009/273, rule 8, and specifically declined to follow Judge Redston's decision in RE Clark v HMRC [2011] UKFTT 302 (TC), TC01164. Judge Bishopp held that the form P800 was 'a reconciliation of the taxpayer's PAYE record. It is not the result of the ordinary assessment process, by which — quite outside the PAYE system — a taxpayer's income, gains, allowances and reliefs are determined, a calculation of the tax is made, the calculation is notified to the taxpayer and (subject to appeal) the amount so calculated becomes payable; nor is it akin to the adjustment of a self-assessment return, by closure notice or discovery assessment.' Where an employee was aggrieved as to 'the manner in which the PAYE system is being applied to his affairs', the

correct course was to appeal against a notice of coding, under Income Tax (PAYE) Regulations, SI 2003/2682, regs 18, 19.

Comments - This is an important decision because it effectively overrules the implications of Judge Redston's controversial decision in the RE Clark case, which has received considerable publicity. Judge Redston had suggested that a form P800 was a notice of assessment which should be treated as giving rise to a right of appeal under TMA 1970 s 31. She had directed that the RE Clark case should be relisted for further hearing. However, the facts of that case reflected so badly on HMRC that it is understood that, following her decision, it agreed to waive the outstanding tax, while maintaining its long-held view that a form P800 is not a notice of assessment and does not give rise to a right of appeal.

The Prince case was treated as a 'test case', and after hearing detailed submissions from very experienced counsel on both sides, the Tribunal President (Judge Bishopp) upheld HMRC's interpretation.

M Prince v HMRC (and related appeals) (TC01852)

No mention of interest - consequences

The claimant company, Teesside Powers Holdings, sold shares under a share purchase agreement. In addition, a tax deed was drawn up whereby any tax rebate made to the purchaser would be passed on to the claimant company.

The question arose as to whether the purchaser was also obliged to pass on to the claimant company any interest relating to the repayments. The claimant asserted that the obligation included interest paid by HMRC on overpayments of tax under TA 1988, s 826 in respect of the period covered. The defendants disagreed.

Decision:

The High Court judge noted that the problem was effectively caused by no mention of interest having been included in the tax deed. He said that as the word 'interest' did not appear in the deed, there had been no apparent consensus between the parties about it.

The judge concluded 'the consequence must be that the clause does not apply to such interest with the result that there is no obligation on the buyer to account for it'.

Comments – This demonstrates that when considering a share purchase agreement or other tax deed it is necessary to consider all the ramifications that will flow from the document. It may seem obvious that if one is creating a document that deals with rebates interest should be included but it was not in this case.

Teesside Power Holdings Ltd v Electrabel International Holdings BV and another company, Queen's Bench Division, 20 January 2012

BUSINESS TAX

Enterprise Zones (Lecture B707 – 5.55 minutes)

Enterprise Zones have been heralded by supporters as something of a panacea for the ailing UK economy. They are seen as engines for growth, which will create jobs in deprived areas and rebalance the economy. The zones are designed to lead the move away from the current dependence on financial services in London and the South East and on the public sector in less affluent areas of the country, towards a more geographically equal, investment-led economy.

Sceptics, however, argue that Enterprise Zones are costly to the taxpayer and unlikely to lead to long-term, sustainable growth. They also raise concerns that, rather than creating new jobs, Enterprise Zones will simply lead to the relocation of existing jobs into other more tax advantaged areas.

Background
Enterprise Zones are not a new idea; similar schemes were set up in the 1980s and 1990s. The Coalition Government reintroduced the idea at the 2011 Budget, when the Chancellor named 21 new Enterprise Zones. Since then, the number has increased to 24.

All new Enterprise Zones will benefit from:

- 100% business rates discount, worth up to £275,000 over a five year period, for businesses moving into an Enterprise Zone during the current Parliament
- All business rates growth in the zone for a period of at least 25 years being shared by the local authorities to support economic priorities
- Simplified planning procedures
- Government support to ensure superfast broadband.

Job creation or relocation?

The Government claims the new Enterprise Zones will create 30,000 new jobs by 2015 as a result of the savings available to businesses. However, there is a concern that these jobs will not be new, but will merely be relocated from other areas.

Research based on the Enterprise Zones set up in the 1980s suggests that, while 63,300 jobs were created in Enterprise Zones, only 13,000 were estimated to be new jobs. It is hoped that the larger size of the new Enterprise Zones relative to those in the 1980s will mitigate job displacement, because it should limit the number of businesses relocating within towns in order to benefit from the incentives offered. However, it will be some years before accurate data can be gathered to assess how well the zones succeeded in creating genuinely new jobs.

Enhanced capital allowances (ECAs)

At the 2011 Autumn Statement, the Chancellor announced that enhanced capital allowances will be available to companies in a limited number of Enterprise Zones. Companies in the Black Country, Humber, Liverpool, North Eastern, Sheffield and Tees Valley Enterprise Zones will be eligible to claim a 100% first year allowance (FYA) on qualifying expenditure on new plant and machinery purchased between 1 April 2012 and 31 March 2017. Draft legislation issued on 6 December 2011 sets out further details on these FYAs, which contain several restrictions on their availability.

One of the provisions ensures that the plant and machinery is used for the purposes of either a business "of a kind not previously carried on by the company", or for the purpose of expanding a business already carried on by the company, or for starting up an activity that relates to "fundamental change" in a product, production process, or service of the company. In addition, the machinery cannot be a replacement asset. While these rules are clearly designed to ensure that the investment will genuinely encourage growth within the company, they are particularly restrictive and could prevent many businesses from qualifying for the

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FYA. It is hard to imagine a struggling business deciding to invest in a completely new area, yet these are the very businesses most in need of Government help.

The many restrictions on the availability of the FYA have led some to question how useful they will be. Furthermore, there are concerns that focusing the ECAs on only a handful of Enterprise Zones will lead to a two-tier system. The Government argues that restricting the incentive in this way will focus it on the areas that need it most, ie those most dependent on manufacturing, while keeping costs under control.

In addition, critics claim that offering FYAs is at odds with the Government's commitment to the 'knowledge economy', as the incentives encourage investment in tangible assets, rather than intangible assets, such as research and development, software, design and branding. Meanwhile, supporters argue that the Government is supporting the knowledge economy by other means and it would be politically difficult to abandon the struggling British manufacturing industry, which is heavily dependent on expensive plant and machinery.

Has the Government learnt the lessons of history?

The new Enterprise Zones have been compared to previous schemes of the same name, operated during the 1980s and 1990s. While debate continues as to the effectiveness of the precursors to today's new Enterprise Zones, the Government is keen to dissociate the two schemes.

There is a significant difference between the new Enterprise Zones and those of the 1980s and 1990s, namely there are fewer tax incentives and a greater emphasis on Government removing bureaucracy. This suggests the Government has listened to research undertaken on the 1980s scheme, in which a survey of companies located in 1980s Enterprise Zones indicated that only around a quarter of new jobs were created as a result of the incentives, which were listed as the third most important factor in attracting firms into an area. Site characteristics and market access were both viewed as more important.

Conclusion

The new Enterprise Zones have received a mixed response, with some hopeful of the investment and momentum they may bring to depressed areas of the UK and others skeptical of the cost-effectiveness and long-term impact of the scheme. There is still debate around the success of the 1980s and 1990s Enterprise Zones, so it is likely to be some time before the effect of the new Enterprise Zones can be determined.

You can view all the areas marked as Enterprise Zones by visiting the Treasury website (www.hm-treasury.gov.uk) and as there have been a number of additions in the last few months it would not be a surprise if the number of zones increased too so it is worth checking this list from time to time.

Contributed by Francesca Lagerberg

Tax Treatment of repayments of amounts wrongly paid as VAT

Four companies, which acted for VAT purposes as the representative members of large groups which carried on business as retailers, had accounted for VAT on amounts which were subsequently accepted not to be due, and had received substantial repayments, together with statutory interest. They treated these repayments as outside the scope of corporation tax. HMRC issued amendments to their self-assessments charging corporation tax on the repayments, and the companies appealed.

Decision:

The First-tier Tribunal dismissed the appeals, holding that 'the VAT repayments received by each of the appellants were trading receipts', and that 'the interest payments are chargeable to corporation tax under Case III of Schedule D'. The Tribunal held, on the facts, that the appellants were beneficially entitled to the relevant amounts from the representative members even though there were no express arrangements to this effect, and that the payments were not therefore gifts.

Comments - There is a great deal of money at stake in this case. The case is significant in that it provides authority for the long-held opinion of HMRC that VAT repayments should be subject to direct taxation. A number of further issues remain to be resolved, however. The case does not consider the impact of the requirement under s80(3) VATA 1994 that taxpayers will normally need to pass on any repaid VAT to their customers in order that they are not unjustly enriched. Assuming they do this, would they be entitled to a deduction against their profits for CT purposes for such payments? If so, then they should not effectively be subject to tax on the repaid VAT; if not, then this would mean they are taxable on amounts they are not actually entitled to retain.

Shop Direct Group Ltd v HMRC (and related appeals) (TC01823)

Enough control for employment status?

In 2004, HMRC ruled that the workers provided by the appellant to contractors in the construction industry were his employees and that he was liable to tax and National Insurance in respect of them.

The appellant appealed to the General Commissioners who found for him. The High Court then remitted the case to the General Commissioners for a retrial on the basis that the wrong legal test had been applied. The General Commissioners remitted the matter to the Special Commissioners. The appellant complained about the transfer, but the Special Commissioners went on to hear the case and dismiss the appeal. The appellant applied to have the decision set aside, and the appeal was then listed for hearing before the First-tier Tribunal.

The appellant submitted a medical certificate stating he was too ill to attend the hearing and asked for it to be adjourned. HMRC opposed the adjournment.

Decision:

The First-tier Tribunal decided that the appeal should proceed as the appellant had given no indication of when he might be well enough to attend a hearing and an indefinite adjournment was not in the interests of justice.

At the appeal, the tribunal found that the appellant exercised sufficient control over the workers, who were unskilled labourers, to make them his employees. According to the evidence the appellant provided sub-contract groundwork services, not labour per se.

The taxpayer's appeal was dismissed.

Comments - This has become something of a long-running saga. The General Commissioners had held that the workers were self-employed but three different judges have disagreed. In the latest instalment, Judge Walters upheld the regulation 80 determinations which HMRC had issued. This case is an excellent illustration of the appeal process – the case was first heard by the General Commissioners and then by the High Court, returning to the FTT (although initially redirected back to the Special Commissioners) and then the High Court and then the FTT again. Not many cases will have such an extensive history (in this case probably a unique history pattern) but of course the issue of employment v self employment is a crucial one in determining the tax consequences.

Wright and another (TC1660)

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IR35 thoughts following JLJ Services Ltd **(Lecture P707 – 8.49 minutes)**

The basis for deciding on the difference between employment and self-employment is a track of case law that runs back for generations.

Over that period, a number of principles have been developed that enable the courts, HMRC and taxpayers to come to reasonable decisions relatively easily in most cases. The key here is that there is generally a fair degree of consistency on all sides.

In order to make life easy, HMRC has produced a booklet ES/FS1. This contains a number of questions that together will enable most people to make informed decisions about their status.

Employed - if you answer yes to most of the questions you are likely to be employed:

- Do you have to do the work yourself?
- Can someone tell you where to work, when to work, how to work or what to do?
- Can someone move you from task to task?
- Do you have to work a set number of hours?
- Are you paid a regular wage or salary?
- Can you get overtime pay or bonus payments?
- Are you responsible for managing anyone else engaged by the person or company
- that you are working for?

Self-employed - if you answer yes to one or more of the questions you are likely
to be self-employed.

- Can you hire someone to do the work, or take on helpers at your own expense?
- Can you decide where to provide the services of the job, when to work, how to work
- and what to do?
- Can you make a loss as well as a profit?
- Do you agree to do a job for a fixed price regardless of how long the job may take?
- If you can't answer yes to any of the above questions, you are still likely to be
- self-employed if you can answer yes to most of the following questions.
- Do you risk your own money?
- Do you provide the main items of equipment (not the tools that many employees
- provide for themselves) needed to do the job?
- Do you regularly work for a number of different people and require business set up
- in order to do so?
- Do you have to correct unsatisfactory work in your own time and at your
- own expense?

While there may be slight disagreement about the balancing of these questions and tax treatment in specific situations, they are generally accepted by all parties.

However, if the JLJ Services case is to become a precedent, this will all change and the determinants for employment versus self-employment will be completely different.

In the case, the judge suggests that in the context of contract workers a new series of criteria should be considered. Readers will understand that the basis of deciding whether a contract worker or IR35 worker is employed or self-employed should be identical to that for anybody else.

"The type of situation, where we consider the contract worker analysis to be realistic is the one where:

- an individual has a particular area of expertise;
- that area of expertise is one that he has found has not enabled him to gain full time employment;
- the explanation for not gaining full-time employment is that the area of expertise is likely to be one that various companies might need, but not on an indefinite basis, but rather simply to complete a particular project;
- the type of work for which the worker is engaged is likely to be work outside the core work of the business.
- the individual has only been able to gain work through rendering his specialist expertise available through placement agents;
- the past pattern of work has confirmed all the above points of short engagements with different companies, and many unwanted gaps between engagements;
- the area of expertise is likely to be one where the client would indicate the project to be done, and the hoped-for time frame for completion of the project, but would not expect to be able to supervise or "control" the worker in any way, simply because the expert would be engaged to do something outside the expertise or competence of the company; and
- the company engaging the individual, engaging him for a project, would consider it quite inappropriate to provide holiday pay, pension benefit, and the other normal incidents of employment because they would all be inappropriate for such contract workers".

Contributed by Philip Fisher (PKF LLP)

Research and Development – an introduction **(Lecture B708 – 14.59 minutes)**

Research and development relief is a corporation tax relief, so it is not available to unincorporated businesses. It provides an enhanced relief for qualifying R&D expenditure and, for SMEs, a payable tax credit can be claimed.

A SME for R&D purposes is a company or organisation with less than 500 employees, and either an annual turnover not exceeding €100m or a balance sheet not exceeding €86m. When looking at these limits certain other entities which have a 25% interest in the company, and other entities in which the company have a 25% interest need to be taken into account on a pro-rata basis.

Relief is given as an enhancement to qualifying expenditure. For SMEs relief is 200% of qualifying expenditure, increasing to 225% from 1 April 2012. For large companies relief is 130% of qualifying expenditure.

Qualifying R&D

The first step in making a claim for R&D relief is identifying the R&D projects carried out by the company. An overall project to develop a new product could involve a number of R&D projects as well as other projects that do not amount to R&D. The BIS (Department of business, innovation and skills) guidance published in 2004 provides some useful pointers on what type of projects will qualify for relief.

An R&D project is one which seeks to achieve an advance in the overall knowledge or capability in science or technology. The work must seek to resolve an uncertainty or achieve an advance in science or technology. Relief is not available for work to resolve the company's own uncertainties or lack of knowledge. The projects must also relate to the company's trade.

The company must be able to describe the methods adopted to resolve the uncertainties, and will need to demonstrate that the individuals involved in the R&D projects have requisite background, qualifications and recent experience to be able to resolve the difficulties. HMRC may ask for details of how the projects have been approached, and will expect to see a documented, systematic approach.

It is not necessary that the R&D project was a success in order to be able to claim relief.

Costs qualifying for R&D relief

Once the company's R&D projects have been identified, it is necessary to allocate qualifying costs to those projects. Only categories of expenditure set out in the legislation qualify for enhancement.

Employee costs – salaries and NIC costs for employees directly and actively engaged in carrying out R&D.

Materials and utilities – consumable or transformable materials, which will include not only physical materials, but also electricity, gas, water. Materials and utilities do not include telecommunications or data services.

Subcontracted R&D expenditure – a SME can claim 65% of relevant expenditure on R&D activities provided by a subcontractor. However, if the subcontractor is connected with the company, or the parties have elected for connected parties treatment, actual qualifying expenditure incurred by the subcontractor can be claimed.

Capital expenditure

Where a company capitalises revenue expenditure on R&D it can claim an enhanced deduction on qualifying expenditure in the year it is incurred. Relief would not be available when the qualifying expenditure is released to P&L.

Where a company acquires capital assets that are used for R&D it can claim a 100% first year allowance.

Contributed by Paul Howard

Management and service charges **(Lecture B709 – 9.49 minutes)**

Management charges between related businesses are relatively common, and are sometimes used in a tax planning context. For example, management charges are often considered if, companies are 'associated' for small profits marginal relief purposes, to minimise tax liabilities by ensuring that more profits are subject to a lower rate of corporation tax overall.

HMRC appears to accept commercial levels of management charges in some cases, such as a "reasonable recharge regime" involving group service companies (BIM38230). In addition, HMRC acknowledges the use of service companies by partnerships, where the service company provides office accommodation and clerical services, although the management charges to the partnership should not be more than their cost plus a "modest uplift"(BIM72070). However, difficulties can arise if, for example, management charges appear excessive or non-commercial, or if the charges are intermittent or vary widely.
To qualify as an allowable deduction for the paying business, the "wholly and exclusively" test must be satisfied. In addition, it should not be overlooked that the management charge must satisfy normal principles of commercial accounting.

In *William Craig v Revenue & Customs* [2012] UKFTT 90 (TC), the taxpayer was a sole trader, operating a landscaping and ground maintenance business with a year end of 30 April. He was also a director and shareholder of a company (WB Ltd).

The company issued invoices to the taxpayer as follows:

30 April 2006	To Professional Fees – year ended 30 April 2006. Consultancy costs...*	£59,000
1 May 2007	To Professional Fees – year ended 30 April 2006 and 30 April 2007. Consultancy costs…*	£51,000

* Both invoices were for consultancy costs in respect of work contracts involving the taxpayer's sole trader business and Health Boards, Housing Associations and other institutions.

HMRC enquired into the taxpayer's 2006/07 tax return, including his accounts for the year ended 30 April 2006. The First-tier tribunal accepted HMRC's conclusion that the April 2006 invoice for £59,000 had been included in the taxpayer's draft accounts and tax return, and that the May 2007 invoice for £51,000 was a late adjustment not reflected in the draft accounts at all, but only reflected in the tax return.

HMRC adjusted the taxpayer's 2006/07 tax return by disallowing almost all the total of the two invoices (£110,000). Interestingly, that sum was instead time-apportioned from 15 March 2006 (i.e. the date on which WB Ltd was incorporated). HMRC's adjustments resulted in the following revised deductions in the sole trader accounts:

Year ended 30 April 2006	[£110,000 - £96,466]	£13,534
Year ended 30 April 2007	[£59,000 - £13,534]	£45,466
Year ended 30 April 2008		£51,000
		£110,000

The taxpayer appealed against the amendment to his 2006/07 tax return. There was no dispute that the profits had to be computed in accordance with generally accepted accounting practice (under what was previously *FA 1998, s 42*; now *ITTOIA 2005, s 25*), which required the accruals basis to be considered. HMRC had adopted a straight line apportionment basis for profits. On the other hand, it was argued for the taxpayer that the transfer of £110,000 between the two entities was a "value judgment" which the taxpayer was entitled to make at his discretion. Unfortunately for the taxpayer, the tribunal favoured HMRC's approach. The taxpayer's appeal was therefore dismissed.

HMRC's approach of spreading the deduction over three trading years is perhaps surprising. However, a similar approach was accepted by the High Court in an earlier case (apparently not considered in the *William Craig* case). In *Stephenson (HMIT) v Payne, Stone, Fraser and Co* [1968] 44 TC 507, a firm of chartered accountants used a service company to provide the firm with staff, heat and light, fixtures and fittings, etc. The firm agreed to pay the service company £47,000 in one accounting year, although the services rendered in that year cost only £32,000. The service charge for the following accounting year was fixed at £21,000, having regard to the payment of £47,000 exceeding the cost of services in the previous year by £15,000, and that the service company's policy was that it would not make an undue profit at the firm's expense. The Revenue refused to allow the whole of the £47,000 in the relevant year, contending that no more than £32,000 fell to be deducted from profits for that year.

The High Court noted that the attribution of outgoings between periods of account was a matter to be determined on ordinary principles of commercial accountancy. The Court considered that the service company profit charge of £15,000 was not a profit charge at all, but an allocation of part of the actual cost of the services for the subsequent period of account. It was held that only £32,000 of the expenditure, plus a 'nominal profit' for the service company, could properly be deducted for the year in question.

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Generally accepted accounting practice is not the only possible basis of challenge. As mentioned, management charges must satisfy the wholly and exclusively test in *ITTOIA 2005, s 34*or *CTA 2009, s 54*. For example, HMRC could seek to apply ‘transfer pricing’ principles to management charges (see BIM42140, for example). That guidance also indicates, in the context of group service companies, that if the provision of services is not part of the provider’s trade or investment business or an ‘adventure in the nature of trade’ in its own right a deduction may be denied for expenditure incurred by the provider in providing those services under CTA 2009, s 54 or s 1219 (although HMRC acknowledges that this scenario is “extremely unlikely”). Alternatively, HMRC could possibly argue that such charges are ‘disguised’ remuneration of controlling directors, with a view to imposing PAYE Income Tax and NIC liabilities thereon. Management charges should therefore be handled with care.

Contributed by Mark McLaughlin

Overseas pension scheme – QROP?

The claimant taxpayer was the trustee of a pension scheme in Singapore (ROSIIP). The issue in the instant proceedings was whether ROSIIP was a qualifying recognised overseas pension scheme, for the purposes of the Finance Act 2004. That turned on whether ROSIIP satisfied conditions laid down in regulations made under the 2004 Act, the Pension Schemes (Categories of Country and Requirements for Overseas Pension Schemes and Recognised Overseas Pension Schemes) Regulations, SI 2006/206 (the 2006 Regulations). The High Court held that the scheme did not satisfy two of the relevant conditions laid down in the 2006 Regulations, and therefore held that it was not a qualifying overseas pension scheme. In particular, it held that it did not satisfy “condition B” of reg 2(3) of the 2006 Regulations, in that there had been, contrary to the 2006 regulations, a system for the approval or recognition by, or registration with, relevant tax authorities of pensions schemes, or “primary condition 1” of reg 2(3), in that it was not open to persons resident in Singapore. The claimant appealed.

The claimant submitted that the Court had erred in finding that condition B was satisfied, since the local system extended only to occupations pension schemes (which ROSIIP was not), and what existed in Singapore could not be described as a “system”. Further, it argued that the Court had erred in finding that the scheme was not open to residents of Singapore.

Decision:

The appeal would be dismissed.

The policy of reg 2(3) of the 2006 Regulations was to allow resort to the default qualification in condition B only if the relevant foreign country had no system at all for approval, recognition or registration, for tax purposes of any kind, of any kind of pension scheme.

Condition B could only be satisfied if there were no system in Singapore for the approval or recognition by, or registration with, relevant tax authorities of pension schemes. Accordingly, the existence of the system meant that condition B could not be satisfied by the claimant.

(2) As regarded primary condition 1 of reg 2(3) of the 2006 Regulations, whether ROSIIP was open to persons resident in Singapore, the judge had been entitled, on the evidence, to reach the conclusion that he had.

Decision of HHJ Hodge QC [2011] EWHC 1463 (Ch) affirmed.

Comments - The CA unanimously upheld the Ch D decision that the scheme failed to qualify as a 'recognised overseas pension scheme' within FA 2004 s 150(8), because it did not meet the requirements of the Singapore Income Tax Act 1948. One of the key reliefs with the pensions legislation is that of a QROPS. Under the current pensions legislation a transfer of a member's benefit rights in a registered pension scheme to a pension scheme which is established outside the UK and not registered in the UK may also be a recognised transfer, if the receiving scheme is a qualifying recognised overseas pension scheme. Accordingly the status of the overseas pension scheme is important for UK tax purposes

TMF Trustees Singapore Ltd (aka Equity Trust Singapore Ltd) v HMRC (CA)

European Commission formal request to amend the UK legislation

The European Commission has formally requested the United Kingdom to amend its legislation providing for exit taxes on companies.

The UK legislation at stake results in immediate taxation of unrealised capital gains in respect of certain assets when the seat or place of effective management of a company is transferred to another EU/EEA State. However, a similar transfer within the UK would not generate any such immediate taxation and the relevant capital gains would only be taxed once they have been realised.

The Commission considers that the United Kingdom has failed to fulfil its obligations under EU rules by maintaining these restrictive provisions. Exit taxes may breach the freedom of establishment as they make it more expensive to transfer a company seat or place of effective management to another Member State than to another location in the UK.

The Commission's request takes the form of a reasoned opinion (second step of EU infringement proceedings). In the absence of a satisfactory response within two months, the Commission may refer the United Kingdom to the Court of Justice of the European Union.

Unallowable purposes and tax relief schemes

A UK company (H) was a subsidiary of another UK company (OI) which in turn was owned by a Jersey company (J). It sought the advice of accountants on 'maximising the movement of funds from the UK to Jersey'. In December 2003 H borrowed £2,000,000 from a bank in order to pay a dividend of £1,999,500 to OI, which in turn declared a similar dividend which it paid to J. Four days later H borrowed £1,999,500 from J and used this to repay the bank. H agreed to pay J £2,150,000 after 363 days. The companies entered similar transactions in subsequent years, and H claimed a deduction for the difference between the amount it had borrowed from J and the amount repayable to J. HMRC issued a closure notice rejecting the claim on the basis that the transactions had had 'an unallowable purpose' within what is now CTA 2009 s 441. H appealed, contending that it had made a commercial decision to fund dividend payments by short-term loans.

Decision:

The First-tier Tribunal reviewed the evidence in detail and dismissed the appeal, observing that 'it is perfectly possible for a transaction to have a legal identity but not necessarily have a commercial purpose', and holding on the evidence that H had had a 'tax avoidance purpose' for entering the relevant transactions.

Comments - CTA 2009 s 441 provides that where a company's loan relationship has an 'unallowable purpose', the company may not include any credits or debits in respect of that relationship which are 'attributable to the unallowable purpose'. The Tribunal held that the legislation had to be construed purposively, and upheld HMRC's view that the loan relationship in question had an 'unallowable purpose'. This legislation was previously considered in Explainaway Ltd v HMRC (TC01267), which was discussed in Matthew Hodkin's article in Tax Journal, dated 23 September 2011.

AH Field (Holdings) Ltd v HMRC (TC01800)

Manufactured dividends paid under stock loan agreement

A UK investment company (F) entered into an 'overseas securities lender's agreement' with a Netherlands bank (AB), which carried on business through a UK branch and was an 'approved UK intermediary' within Income Tax (Manufactured Overseas Dividends) Regulations, SI 1993/2004, reg 2(1). Under the agreement, F became the legal and beneficial owner of certain preference shares in a Cayman Islands company (B) until 29 March 2004, and was required to pay a 'manufactured dividend' to AB in respect of any dividend paid on the shares during the currency of the loan. The agreement was a contract for the transfer of overseas securities, within ICTA 1988 Sch 23A. F subsequently entered into an agreement with B under which it agreed to subscribe for an identical batch of preference shares in B. F then sold the original shares in B to an Irish bank (AI) for £50,314,975. B paid dividends totalling £51,000,000 to AI, and F paid 'manufactured dividends' of the same amount to AB, in accordance with the loan agreement. F then transferred the second batch of shares in B to AB, thereby completing the loan agreement. F claimed a deduction of £51,000,000 as management expenses (which it surrendered to its parent company as group relief).

HMRC issued an amendment to F's self-assessment to exclude the deduction, considering that the 'dividends' which B had paid were actually returns of capital and that the 'manufactured dividends' which F had paid did not qualify as management expenses. F appealed, contending that its sale of the shares to AI had been necessary to provide funds; that the transactions had given rise to a chargeable gain of £49,314,875, which it had declared on its return; that the dividends which B had paid were 'overseas dividends', and that the effect of SI 1993/2004, reg 4(1)(c) was that it was entitled to the deduction for management expenses which it had claimed. The First-tier Tribunal accepted these contentions and allowed the appeal, holding that the dividends were income rather than capital, and that the transactions were not a 'sale and repurchase of securities' for the purposes of ICTA 1988 ss 730A and 737A.

Decision:

The Upper Tribunal and CA both dismissed appeals by HMRC. Moses LJ held that 'the reality was the distribution of share premium as dividends, as (B) was free to do under Cayman Islands companies law. That mechanism establishes that the payments were income. The correct identification of the dividends as income, notwithstanding that they were paid out of share premium account, mirrors the situation in United Kingdom company law prior to 1948.' The CA has unanimously dismissed HMRC's appeal in HMRC v First Nationwide.

Comments - HMRC contended that dividends which had originated from a capital reserve were capital in nature, so that they failed to qualify as management expenses (and would not fall within the corporate dividend exemption under CTA 2009 s 931A(2)). The CA unanimously rejected HMRC's contentions, and also rejected HMRC's attempt to apply ss 730A and 737A ICTA 1988to the transactions.

HMRC v First Nationwide. EWCA

Freedom of establishment

The CJEU held that Article 49 of the TFEU did not preclude 'legislation of a Member State under which the amount of tax on unrealised capital gains relating to a company's assets is fixed definitively, without taking account of decreases or increases in value which may occur subsequently, at the time when the company, because of the transfer of its place of effective management to another Member State, ceases to obtain profits taxable in the former Member State; it makes no difference that the unrealised capital gains that are taxed relate to exchange rate gains which cannot be reflected in the host Member State under the tax system in force there'. However, Article 49 did preclude 'legislation of a Member State which prescribes the immediate recovery of tax on unrealised capital gains relating to assets of a company transferring its place of effective management to another Member State at the very time of that transfer'.

Comments - Article 49 of the Treaty on the Functioning of the European Union provides that 'restrictions on the freedom of establishment of nationals of a Member State in the territory of another Member State shall be prohibited'. The CJEU gave detailed guidance on how this provision should be interpreted with regard to the taxation of unrealised capital gains.

National Grid Indus BV v Inspecteur van de Belastingdienst Rijnmond / kantoor Rotterdam (CJEU Case C-371/10),

Principal objective of merger

The CJEU held that Article 11(1)(a) of Directive 90/434/EEC 'is to be interpreted as meaning that, in the case of a merger operation between two companies of the same group, the fact that, on the date of the merger operation, the acquired company does not carry out any activity, does not have any financial holdings and transfers to the acquiring company only substantial tax losses of undetermined origin, even though that operation has a positive effect in terms of cost structure savings for that group, may constitute a presumption that the operation has not been carried out for "valid commercial reasons" within the meaning of Article 11(1)(a).

It is incumbent on the national court to verify, in the light of all the circumstances of the dispute on which it is required to rule, whether the constituent elements of the presumption of tax evasion or avoidance, within the meaning of that provision, are present in the context of that dispute.'

Comments - Directive 90/434/EEC, which laid down provisions for the tax treatment of mergers, transfers of assets and share exchanges, was repealed by Directive 2009/133/ EC with effect from 14 December 2009. This case is therefore mainly of historical interest, but the judgment gave useful guidance on whether a transaction had been undertaken for 'valid commercial reasons'. The CJEU held that it was for the national court to determine whether the transaction indicated 'the constituent elements of the presumption of tax evasion or avoidance'.

Foggia — Sociedade Gestora de Participacoes Sociais SA v Secretario de Estado dos Assuntos Fiscais (CJEU Case C-126/10)

Refusal of late claim to group relief: application for judicial review

The claimant taxpayers were wholly owned subsidiaries of D Holdings plc. In March 2006, the taxpayers' accountants submitted tax returns and accounts for D Holdings and the taxpayers for the year ended 31 March 2005. These included a consortium claim for group relief in respect of losses made by A Ltd, CCC Ltd and CD Ltd, although it was accepted that the claim was incorrect. A disclosure of tax avoidance schemes document was also submitted.

One year later, the claimants and D Holdings submitted corporation tax self-assessment returns for the year ended 31 March 2006, claiming group relief for losses made by CCC Ltd and CD Ltd. Again, the group relief claimed by D Holdings plc exceeded its entitlement to absorb the losses.

When the taxpayers realised the errors had been made, they submitted revised computations for each year of claim. These were made in March 2009 and constituted the formal claims.

HMRC refused the claims on the basis that they were out of time under FA 1998, Sch 18 para 74. The taxpayers applied for judicial review, submitting that HMRC's methodology was flawed and that the taxpayers had legitimate expectation that the claims would be accepted.

Decision:

The Queen's Bench Division said no mandatory requirement demanded that HMRC give any reasons for refusing to accept an out-of-time claim. In this instance, it was clear that HMRC had not been satisfied that there were exceptional reasons why the claim had not been made within the specified time. Furthermore, the Revenue had pointed out errors in the original claims, but this did not amount to legitimate expectation that new claims would be accepted. With regard to the errors, it was for the taxpayers to submit correct claims rather than expect HMRC to point out what needed to be amended.

Blair J held that 'in a commercial setting such as this, the responsibility for formulating a claim for group relief correctly must lie with the group. It was for the group to apportion losses in a way that maximised relief, not the Revenue'. He also observed that there was 'no reason in principle why the tax avoidance factor should not be taken into account in deciding whether to admit a late claim or not. In reaching its decision, HMRC must be entitled to take account of the fact that (for example) the relevant losses have not been incurred in the course of the group's trading activities, but have been acquired for the purpose of increasing the claim to group relief.'. The taxpayers' application for judicial review was dismissed.

Comments - This case demonstrates the importance of ensuring that group relief claims are arithmetically correct, and that there are no errors which might result in possible relief being 'wasted' or 'stranded'. The Tribunal upheld HMRC's view that the company could not submit an amended claim, to utilise relief which would otherwise have been wasted, after the expiry of the statutory time limit.

R (oao Bampton Group Ltd) v King (HMRC) (and related applications) (QB)

VAT

Voluntary registration retrospective opportunity

The taxpayer, a well-established charity, rehoused dogs which had been strays or abandoned. It asked for a donation, usually of £150, from the new owners to cover the vet costs it incurred before giving the dog to its new owner. The charity said it used the word 'donation', rather than payment, to emphasise the activities of the charity. A potential owner who refused to make the donation was deemed unable to afford to keep a dog and the rehoming process would be ended, although an arrangement might be made to enable the individual to foster a dog.

The charity did not claim gift aid on these 'donations', but did so on other payments donated. This was because donations in respect of rehoming the dogs were not made voluntarily.

On the basis that it was making zero-rated supplies of dogs in return for payment, the charity applied to register for VAT retrospectively so that it could reclaim four years of input tax. HMRC refused the application saying the charity was rehoming dogs in return for a voluntary donation.

Decision:

The First-tier Tribunal noted that according to HMRC's guidance in Notice 701/1, para 5.9.1 'a donation is outside the scope of VAT provided that it is freely given, with nothing supplied in return'. The tribunal accepted the taxpayer's evidence that there was nothing optional about the payment required from potential new dog owners. It was also clear that the owners got something, i.e. a dog, in return for the payment. Thus it decided that the payments made by the owners were neither 'freely given' nor were they given 'with nothing supplied in return'.

The taxpayer charity was making a supply of dogs to new owners and was entitled to register for VAT and recover its input tax.

Comments - Neil Warren, independent VAT consultant, said that the case highlighted 'the opportunity for any taxpayer to register for VAT retrospectively, up to a period of four years, as long as the registration is made on a voluntary basis'.

Three Counties Dog Rescue (TC1653)

Whether part-time judge required to register

A qualified barrister (M), who was totally blind and did not practise as a barrister, sat as a part-time immigration judge. For direct tax purposes, the Inland Revenue had initially treated him as an employee of the Department of Constitutional Affairs, but in 2004 they accepted M's claim that he should be treated as self-employed. Subsequently HMRC issued a ruling that M was required to register for VAT, and also imposed a penalty for failing to do so. M appealed, contending that he was not carrying on any business.

Decision:

The First-tier Tribunal accepted this contention and allowed M's appeal. Judge Clark observed that as a tribunal judge, M was holding an office, so that it was 'difficult to understand' why the Revenue had accepted his claim to be treated as self-employed. M was not 'a person independently carrying on an economic activity' and was not liable to be registered for VAT.

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Comments - The Tribunal accepted the appellant's contention that, since he was not practising as a barrister, he was not carrying on any business. The case also illustrates the importance of considering both the direct tax and the indirect tax consequences of any given situation. The appellant had managed to persuade the Inland Revenue (as it then was) that he should be treated for income tax purposes as a self-employed barrister, although (as Judge Clark observed) a judge holds an 'office'. The consequence of his being treated as self-employed for income tax purposes was, not surprisingly, that HMRC also sought to treat him as self-employed for VAT purposes. Judge Clark's decision appears to suggest that HMRC should cease to treat the appellant as self-employed for income tax purposes.

Dr AA Majid v HMRC (TC01839)

Two are not one

The taxpayers, a husband and wife partnership, owned a farm. The business included the provision of self-catering holiday accommodation, as well as a haulage operation and the farming of cattle and sheep. In addition, the wife ran a bed and breakfast business as a sole trader from the farmhouse. As the turnover was less than the VAT registration threshold, this business was not VAT registered.

After a VAT visit, HMRC declared that the farming partnership and the bed and breakfast business should be treated as a single entity. The taxpayers appealed.

HMRC cited a number of reasons for ruling that the two businesses were one for VAT purposes, for example:

- the bank accounts for the farm partnership and the bed and breakfast were joint accounts in the names of both taxpayers;
- the same bookkeeper was employed for both businesses;
- money was sometimes transferred from the bed and breakfast account to the farm account;
- the self-catering cottage and the bed and breakfast were on the same website and presented as a single business;
- the same building was used for the self-catering cottage and the bed and breakfast business;
- there was a combined insurance policy; and
- the farm business would not be viable without the bed and breakfast business.

Decision:

The First-tier Tribunal agreed that it was reasonable for HMRC to be satisfied that the farming business and the bed and breakfast business were a single taxable entity. The taxpayers' appeal was dismissed.

Comments - Neil Warren, independent VAT consultant, said 'a key failure in the arrangement was the inclusion of the self-catering cottage in the farm partnership, a move that was clearly designed to ensure the remaining bed and breakfast income earned by Mrs Howard was below the VAT registration limit. This illustrated an artificial split designed to save VAT rather than a split based on logical commercial principles. The positive result for the taxpayer was that there was no argument put forward by HMRC that there never had been two businesses i.e. output tax was only due on future bed and breakfast income (effective from the date specified in the direction) rather than on a retrospective basis.'

H R Patrick and J R Patrick (TC1699)

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VAT: penalties for errors

A company (AP), which was registered for VAT, sold a property to an associated company for £510,000 plus VAT of £76,500. It failed to include this on its VAT return. HMRC imposed penalties under Sch 24 FA 2007, at the rate of 47.25% of the potential lost revenue, on both AP and its principal director (C), who was also the company secretary of the associated company. They appealed.

The First-tier Tribunal dismissed the appeals. Judge Cannan found that C had been 'doing nothing more than trying to erect a smokescreen to cover the fact that he had deliberately made an inaccurate return'.

Comments – Sch 24 FA 2007 provides for penalties for errors. The First-tier Tribunal upheld a penalty at the unusually high rate of 47.25% of the potential lost revenue.

Astoria Properties Ltd v HMRC (and related appeal) (TC01772)

Appealing out of time against a default surcharge - disproportionality

Surcharges of £69,022 at 2% and £195,351 at 5% had been levied for the periods ended 30 June 2008 and 30 June 2009. The company asked for reconsideration of the second surcharge, but HMRC ruled that there was no reasonable excuse. The Enersys decision was released by the Tribunal on 11 January 2010, and the company wrote to HMRC asking for reconsideration in the light of it on 2 August 2010. HMRC did not reply until 9 November 2010, when they pointed out that they could only carry out one review. The company submitted a notice of appeal on 10 December 2010; HMRC wrote a detailed reply arguing that Enersys had been wrongly decided in January 2011; then HMRC applied for strike-out in their statement of case dated 27 May 2011, mentioning for the first time that the appeal was being made out of time.
Decision:

The chairman decided to refuse the application, which was made over two years late for the first surcharge and a year late for the second one: "TNT is a very large company with, it is reasonable to assume, access to excellent legal and accountancy expertise and I regard that as a relevant factor in considering whether it is fair and just to refuse the application for an extension of time. Both parties' interests and the interests of the administration of justice all come into consideration."

TNT GRS 2008 Ltd (TC01663)

Whether repayment claim made within time limit

An accountant wrote to HMRC in March 2009 stating that a professional golfer (L) had wrongly accounted for VAT on tuition fees which should have been treated as exempt. HMRC did not respond to this letter until November 2009, when it requested further information including a detailed schedule. In March 2010 L's accountant provided the requested schedule. HMRC rejected the claim on the grounds that it had been made outside the statutory time limit.

The First-tier Tribunal allowed L's appeal, holding that the letter submitted in March 2009 had been a valid claim.

Comments - HMRC rejected the repayment claim on the grounds that the appellant had not lodged a quantified claim within the statutory time limit. However the First-tier Tribunal allowed the appeal, holding that the letter which the accountant had written in March 2009 was a valid claim even though it did not quantify the amount.

G Laing v HMRC (TC01696)

VAT Appeals Time Limit **(Lecture B710 – 19.19 minutes)**

This lecture considers the rules for making appeals to the Tribunal, in particular the time limit that applies and the circumstances in which an appeal may be allowed to proceed even if the trader was late making the appeal. The rules are illustrated by a selection of Tribunal decisions from recent years. The lecture concentrates on the most recent ones, which suggest that HMRC have received a number of late appeals from traders who have tried to "jump on the bandwagon". They are likely to resist such appeals.

Late appeal applications

A local Conservative Club applied for leave to appeal out of time against a decision to refuse repayments in respect of *Linneweber* claims. The claim had been made on 28 December 2006 in respect of periods from 1 January 2003 to 30 September 2005, and it had been refused by a decision of 19 July 2007. No formal appeal had been made until 2011.

The Tribunal accepted that the decision letter was misleading. It said that the club would have to write to the reconsiderations team in Birmingham if it wanted to dispute the decision, and made no reference to a right of appeal to an independent Tribunal. Both of these features were wrong. However, the delay was some 3.5 years; the person who filed the claim was an accountant who surely should have at least asked a question about how the decision could be independently reviewed. Leave to appeal out of time was refused.

First Tier Tribunal (TC01531): *Biggleswade and District Conservative Club*

A club claimed back £13,600 in respect of a gaming machine in December 2006. It was refused by letter of 17 January 2007, and an appeal was not made until 5 July 2011. The grounds for making an appeal out of time included the fact that the original refusal letter had not included reference to a time limit for appealing, and the club officials were "not sophisticated in legal matters but relied on the Commissioners to act properly". The Tribunal chairman noted that "the letter making the original claim refers to the claim as a voluntary disclosure and refers to the legal basis for making the claim and was accompanied by a spreadsheet calculation; none of which seem likely to have been things that would be known to a person who had no knowledge of the subject".

The appellant also argued that the case should have been reconsidered in the light of the *Rank* appeal. As the Tribunal had decided in Rank's favour in 2008 and 2009, the chairman considered that this did not give any further justification for the club's late appeal. Leave to appeal out of time was refused.

First-Tier Tribunal (TC01718): *North Reddish Working Men's Club*

A similar decision was reached in another case about a *Rank* claim for over £500,000. The original claim had been made under the *Fleming* rules on 20 March 2009. The Tribunal report states that HMRC responded with a holding letter on 12 March – this is probably a misprint for 12 May. The claim was refused by letter to the company's accountants on 9 July. They claimed never to have received this letter or to have been aware of the decision it contained until 2010. The practice was taken over by another firm, and the company asked the other firm to follow up the claim that they thought was ongoing in May 2011.

The Tribunal decided that failing to follow up a claim for £500,000 for two years represented serious culpability on the part of the claimant. Leave to appeal out of time was refused.

First-Tier Tribunal (TC01612): *Jem Leisure Ltd*

Other bandwagons – applications rejected

Another company asked to jump on a different bandwagon – appealing out of time against a default surcharge on the basis of disproportionality. Surcharges of £69,022 at 2% and £195,351 at 5% had been levied for the periods ended 30 June 2008 and 30 June 2009. The company asked for reconsideration of the second surcharge, but HMRC ruled that there was no reasonable excuse. The *Enersys* decision was released by the Tribunal on 11 January 2010, and the company wrote to HMRC asking for reconsideration in the light of it on 2 August 2010. HMRC did not reply until 9 November 2010, when they pointed out that they could only carry out one review.

The company submitted a notice of appeal on 10 December 2010; HMRC wrote a detailed reply arguing that *Enersys* had been wrongly decided in January 2011; then HMRC applied for strike-out in their statement of case dated 27 May 2011, mentioning for the first time that the appeal was being made out of time.

The chairman decided to refuse the application, which was made over two years late for the first surcharge and a year late for the second one: "*TNT is a very large company with, it is reasonable to assume, access to excellent legal and accountancy expertise and I regard that as a relevant factor in considering whether it is fair and just to refuse the application for an extension of time. Both parties' interests and the interests of the administration of justice all come into consideration.*"

First-Tier Tribunal (TC01663): *TNT GRS 2008 Ltd*

In VTD 14,466, a golf club was held to be liable for output tax on a taxable supply of services in respect of the requirement that members subscribe for an interest-free debenture in the club. The club had argued that the issue of the debenture was an exempt supply, but the Tribunal ruled that making an interest-free loan was also consideration for the taxable supply of sporting services. This was valued at the amount of interest that the club would otherwise have had to pay on the money.

After a case involving debentures issued by the *Rugby Football Union* (VTD 18,075), the club claimed a repayment. Initially HMRC resisted the claim, but later accepted that, from August 2001 onwards, the club would be treated as not making taxable supplies in respect of these debentures. There had been extensive correspondence over several years, but it appeared that the club had never quantified its claim nor formally appealed against a decision not to pay. It eventually dropped the appeal in 2006 because there was no longer any substantial dispute between the parties.

HMRC repaid output tax for the period from 2003 to 2006, but refused to repay for the earlier period because the club had not made a proper claim within the time limit (because it had not quantified the amount reclaimed). The club had also missed the time limit to appeal against the decision to refuse to repay.

The Tribunal examined the background in detail and declined to allow an appeal out of time. There were no grounds in the VAT Act, and the doctrine of legitimate expectations also did not assist the club.

First Tier Tribunal (TC01476): *Harleyford Golf Club*

A company made a voluntary disclosure in October 2003 to claim input tax relating to a share issue in its 09/00 period. Customs refused the claim on the basis of their then view that a share issue constituted an exempt supply. The company did not appeal at the time of that decision, but made an appeal 14 months after it – when the *Kretztechnik* decision of the ECJ made it clear that Customs' view was wrong and the appeal ought to be allowed.

There was no question that the input tax would now be regarded as allowable. The Tribunal took into account the principle of "effectiveness" – the importance of allowing traders the opportunity to enjoy their rights. Even so, it held for Customs. There was a long delay before the original claim, and another long delay before the appeal. The proper course would have been to make a protective appeal after the decision and wait for the *Kretztechnik* case to be decided by the ECJ. Customs, as well as the taxpayer, were entitled to the protection of legal certainty. If the case was decided for the taxpayer, there would be a flood of similar claims from people who had been denied input tax in the past.

VAT Tribunal (19,859): *The Medical House plc*

A company managed investment funds. In May 2005 it filed a voluntary disclosure applying for a repayment on the grounds that some of its services should be exempt under EU law. This was subsequently confirmed by the ECJ's decision in the *JP Morgan Claverhouse* case, released on 28 June 2007. On 5 November 2007 HMRC issued BB 65/07, confirming that it would concede that case rather than return to the Tribunal, but restricting the concession to management of investment trust companies. During 2008 further concessions were made, and in August 2008 HMRC announced that management of venture capital trusts would also be treated as exempt with retrospective effect. This appeared to cover the whole of the 2005 voluntary disclosure.

During this time, HMRC had issued a formal decision to refuse the claim to exemption for VCT management on 5 February 2008. No appeal or formal request for reconsideration was made against this decision until 30 June 2009. A further voluntary disclosure was made in September 2008 covering periods from March 2004 to June 2008, and this was rejected as being out of time. That rejection is the subject of a separate appeal.

The Tribunal had to consider whether to allow the June 2009 appeal even though it was well outside the normal 30-day time limit. It seemed that the discussions between the taxpayer's advisers and HMRC had continued over an extended period without the accountants noticing that time was running against them. They had apparently advised against appealing too early as this might be regarded as confrontational.

The Tribunal examined the principles of precedent cases on the issue, and did not think that there was any reason to accept the late appeal. The application was refused.

First Tier Tribunal (TC00418): *NVM Private Equity Ltd*

Other issues – applications accepted

A company was refused payments of £7.9m of input tax because HMRC suspected it of involvement in a carousel fraud. The company appealed in 2008, but it appears that its accountant failed to keep the directors informed about the progress of the appeal. As a result, the company failed to comply with directions of the Tribunal and had the appeal struck out. It applied to have the appeal reinstated; this was refused by the VAT Tribunal in January 2009 in the absence of the taxpayer, again apparently because the accountant had not told anyone about the hearing. At this time the directors engaged new advisors and applied again to have the appeal reinstated.

The change of Tribunals intervened, and the First Tier Tribunal decided that it did not have jurisdiction to reinstate an appeal in these circumstances. The company appealed again to the Upper Tribunal, which allowed the application and referred the case back to the First Tier Tribunal to hear the substantive appeal. The fault appeared to be with the previous accountants; there was a real risk of injustice to the directors, partly because of the sum of money involved and partly because they would have no chance to clear their names of serious allegations of tax fraud. HMRC's only risk was wasted costs.

Upper Tribunal: *ATEC Associates Ltd v HMRC*

An individual received two post-clearance demands in relation to importations of vehicles. He claimed that he had not appealed against them because he believed they were directed at a company in liquidation, and he did not realise they were personal to him. He finally lodged an appeal in May 2010, some seven months late. HMRC argued that he was out of time and did not have a reasonable excuse. The individual had been disqualified from acting as a director in April 2011, and HMRC argued that he was wholly unreliable.

The Tribunal considered the background and a number of precedent cases. The chairman concluded that there was a real risk of unfairness if the application was not granted, and no significant prejudice to HMRC if it was. There were some anomalies and contradictions in the evidence, but the chairman accepted that the individual genuinely believed that the liability was not due from him, and that was why he had not appealed earlier.

First Tier Tribunal (TC01480): *Matthew Richard Griffiths*

A company was assessed to a substantial amount of VAT. Six months later it was put into liquidation, without ever having formally appealed the assessment. Some two years later the directors applied to appeal out of time. Their reason for the delay was that they had believed the company's accountants had already submitted an appeal.

The judge allowed the application, accepting that the company had been acting reasonably under a mistaken belief. There would be demonstrable injustice if the appeal could not be heard.

First Tier Tribunal (TC00592): *B Fairall Ltd (in liquidation)*

Other issues – applications accepted

A company applied for leave to appeal out of time. When the case first came before the Tribunal it was discovered that the company had been dissolved without the consent of its directors, and had to be reinstated. On its reappearance, the Tribunal noted that the company had failed to make returns on time, had failed to notify the Commissioners of a change of address, had failed to pursue input tax repayment claims, and had failed to serve its notice of appeal within time, even assuming that its own claim as to what constituted the decision under appeal was correct.

It appeared that the company's history was one of administrative confusion. It had originally supplied cash machines which were connected to the Link network, but these were disconnected after problems with the contracts were discovered. Accordingly, the company ceased to trade, and its VAT compliance was left in abeyance, including claims to recover input tax on purchases.

In the absence of any explanation for its delays, the company's application to have its appeal heard out of time was dismissed.

First Tier Tribunal (TC01399): *Pen Associates Europe Ltd*

A company applied for leave to appeal out of time against assessments to VAT and penalties totalling over £60,000 for periods from 11/05 to 05/08. The company had incurred costs in relation to refurbishment of premises used by a subsidiary; this was disallowed because there was effectively an exempt licence to occupy granted to the subsidiary. The holding company argued that there was a "de facto VAT group", but HMRC refused to accept that such a concept existed.

The company wrote numerous times to dispute the decision after it had been made, but did not make a formal appeal until more than three years after the deadline had expired. The Tribunal did not consider that any satisfactory reason had been given for the delay; nor, on the basis of the information about the arguments that were put in outline in this preliminary hearing, did the Tribunal consider that the appeal had any prospect of success. Leave to appeal out of time was therefore denied.

First Tier Tribunal (TC01497): *Scan Corporation Ltd*

A company was refused a repayment of £33m of input tax in a decision dated 29 November 2007. It lodged an appeal on 20 May 2008. HMRC resisted an application to be allowed to appeal out of time; the Tribunal made a number of directions to the trader and its representatives to produce documents and other information, but they did not. When finally a hearing was set for 6 January 2009 to consider the extension of time, the representative did not attend, pleading an attack of norovirus (but without a medical certificate).

The Tribunal saw no reason to extend time and dismissed the appeal.

VAT Tribunal (20,914): *Pan Euro Ventures Ltd*

On 10 December 2009 a trader filed a notice of appeal in respect of an assessment raised on 1 July 1980 in respect of a period in 1978. The trader claimed that his appeal was so late because he had believed that a "*Grepe v Loam*" order against him prohibited him from bringing an appeal in the VAT Tribunal. Such an order constrains its subject from bringing actions in the courts. It appears that he was found at some past point to be a vexatious litigant and was forbidden to carry on going to law.

In 2009 he discovered that the order did not apply to proceedings in the First Tier Tribunal, so he promptly commenced an appeal. The Tribunal refused leave to appeal out of time. Firstly, several of his grounds of appeal would require findings of fact, and it would be very hard to establish the facts after such a long time. Secondly, the order was only made in 1994, and there was no explanation of why he had not appealed before that.

The application for leave to appeal out of time was struck out on the basis that the substantive appeal had no realistic prospect of success.

First Tier Tribunal (TC00442): *D A Gardner t/a Gardner's Transport Co*

A different Tribunal judge considered the arguments again and came to the same conclusion. The trader had not given convincing reasons for his failure to appeal at the time; given the long delay, it would be almost impossible for him to provide enough evidence to succeed in a substantive hearing. The application was dismissed.

First Tier Tribunal (TC00748): *D A Gardner t/a Gardners Transport Co*

A trader was assessed to recover input tax that he had claimed in spite, according to HMRC, of only making exempt supplies. He appealed over a year after the decision, and when told that only the Tribunal could allow such a late appeal to proceed, took nearly another two years to pursue that course. In the correspondence he claimed to be appealing against a default surcharge and a misdeclaration penalty, even though the assessment was only for VAT and interest.

The Tribunal saw no reason to allow the appeal to proceed. There was no evidence of any good reason for the delay, nor any indication that the appeal had any chance of success.

First Tier Tribunal (TC00302): *Obhloise Benjamin Ogedegbe*

A trader ran a pub through a company. The company was dissolved in 2006 owing £56,000 of VAT. The individual disputed the accuracy of this amount, although he never appealed against it. The Tribunal comments that “the Appellant felt seriously aggrieved by that episode and determined to arrange his affairs in the future so that he would never have to deal with HMRC again if he could possibly avoid it”.

Accordingly, he transferred the trading rights of the pub operation to four separate Seychelles companies, which were supposed to operate bed and breakfast, a restaurant, bar and conference suite, and outside catering. When HMRC contacted him in 2007, he claimed that all the companies were trading below the VAT registration threshold.

HMRC tried to establish what was happening, given that the trader had not made any returns for PAYE, NIC or VAT. A fire destroyed some of the records, and the trader did not cooperate in providing any information. Eventually HMRC issued a number of decisions and determinations. The trader wrote a letter of appeal against a NIC decision, but failed to lodge any formal appeal against VAT and other compliance decisions (including a notice of compulsory registration and estimated assessments for VAT return periods).

Eventually he lodged an appeal against the VAT decisions, and HMRC sought to have the appeal struck out on the basis that it was made out of time. The Tribunal considered this procedural issue rather than the substantive dispute.

In respect of some of the applications, the Tribunal allowed the appeal out of time. However, the trader’s lack of cooperation counted against him; the chairman considered that he was not, as he claimed, confused by the process, but was instead well aware of the workings of the tax system and was pursuing a premeditated course of obstruction.

The main VAT issue – the notice of compulsory registration – was accepted by HMRC at the hearing as something on which the trader should be allowed to appeal. If he lost, he would then have to submit VAT returns for the periods concerned and these would be treated by HMRC as replacing the assessments. It would then be possible to have a further dispute about the amounts shown on the returns.

The applications to strike out appeals against a number of PAYE penalties was refused because HMRC could not produce satisfactory evidence about the issue of the relevant notices. However, the application to appeal out of time against a number of assessments and liabilities was also refused because the trader could not show a good reason for his delay.

First Tier Tribunal (TC00624): *David C Pledger*

A trader appealed out of time against the refusal to repay input tax of some £4m in relation to an alleged MTIC fraud. The company had received the decision in January 2008 and had within 30 days informed HMRC of an intention to appeal; the officer replied that it was necessary to make a formal appeal to the Tribunal, but this was not done until March 2010, when HMRC eventually issued a letter to the company threatening enforcement action in respect of the assessed proportion of the disallowed input tax (about £3.1m).

The trader put forward a number of reasons for not appealing earlier, chief amongst them the fact that the company could not afford the legal costs. The chairman commented that he had demonstrated that it was possible to appeal in person without incurring excessive costs by making the application to appeal out of time, and he appeared to be well informed about the procedure and the law. None of his other reasons was any more compelling.

The application to appeal out of time was refused.

First Tier Tribunal (TC00656): *Lighthouse Technologies Ltd*

Contributed by Mike Thexton

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