Tolley®CPD

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Budget

The Chancellor of the Exchequer, George Osbourne, will hold his second Budget of 2015 on 8 July 2015.

Personal Tax

Common issues when completing SA tax returns (Lecture P896 – 17.00 minutes)

This article covers practical issues that arise when trying to complete the self-assessment tax returns for an individual. All the examples are from real taxpayers.

Taxable and exempt state benefits

Pensions are often paid together with other benefits e.g. Attendance Allowance, but many state benefits, including Attendance Allowance are tax-free.

If working from bank statements, the split may not show up so you will need to get the breakdown issued by DWP

Tax free benefits include:

- Housing Benefit
- Free TV licence for over-75s
- Income Support
- Working Tax Credit and Child Tax Credit -
- Disability Living Allowance
- Child Benefit (if income < £50,000)
- Guardian's Allowance
- Attendance Allowance
- Pension Credit
- Employment and Support Allowance
- Lump-sum bereavement payments
- Maternity Allowance
- Industrial Injuries Benefit
- Severe Disablement Allowance
- Universal Credit
- War Widow's Pension
- Young Person's Bridging Allowance
- Winter Fuel Payments/Christmas Bonus

A Pension statement will include the Attendance Allowance. If this statement is not seen, the advisor might enter too much a taxable income in the SATR.

Annual allowance charge

Excess pension inputs over and above the annual allowance are taxed as the top slice of income

An individual gets relief for pension contributions paid in the tax year, but the annual allowance charge is based on a 'Pension Input Period' – the year-end of the pension plan. Like sole traders, the inputs are based on the accounting period ending in the tax year.

If your client makes contributions at the annual allowance level, it is vital that you know the pension input period of their pension plan.

It is easy to make mistakes in the timing of inputs, leading to an AA charge.

Remember that unused AA can be carried forward 3 years – it was £50,000 to the end of 2013/14 and has been £40,000 from 2014/15.

Example

A client has no unused AA. The PIP of their pension plan is 30 June. On 15 August 2013 the client paid their only pension premium of 2013/14 of £40,000 (£50,000 gross).

The client's basic rate band for 2013/14 would be extended by £50,000 as the premium was paid in that tax year.

But the payment falls into the PIP year ended 30 June 2014 so is tested against the 2014/15 AA limit (which was £40,000).

Unfortunately the client will have an AA charge in 2014/15 of £10,000.

Beneficial loans

The P11D should show the default method of calculating the benefit. This is found by taking the opening balance plus the closing balance, divided by 2, then multiplied by average official rate (was 3.25% throughout 2014/15).

For new loans, assume they are taken out from 6th of the following month and work to nearest month.

Loans repaid – only calculate for the complete months the loan is outstanding for.

You need to check if the P11D benefit has been calculated correctly before entering it on SATR.

The taxpayer has the option of using a day-to-day calculation instead if beneficial – this might be where a large chunk of loan paid off early in the year.

This means the P11D benefit will not be the same as the amount entered on the SATR. It is recommended that you use white space to explain this.

HMRC has the option to insist on a day-to-day calculation – they must instruct employer to use this for the P11D in this case.

Offshore income

You will need a breakdown between interest and dividends where the income is taxed on an arising basis rather than the remittance basis (remittance basis income is always taxed as general income).

Sometimes investment income statements from fund managers are inadequate as no breakdown is given.

If the fund is a 'reporting fund, excess income not distributed is also taxable. It is deemed to arise 6 months after the reporting period of fund. The fund statement needs to clarify its status as 'reporting'/'non-reporting' to ensure the correct income is taxed.

Offshore trust income

An R185 for the beneficiary of an interest in possession trust does not break down foreign income. Trustees are instructed by the form to send a breakdown to the beneficiary.

This is essential if the correct amount of tax is to be paid, so the advisor will need to ensure the client has obtained a breakdown from the trustees.

Contributed by Malcolm Greenbaum

Automatic tax relief for employee expense claims (Lecture P897 – 15.02 minutes)

In his Budget last year, the Chancellor announced a number of measures aimed at simplifying the administration of benefits in kind and employee expenses. This followed on from the January 2014 report by the Office of Tax Simplification (OTS) of the review which they conducted into the tax regime for employee benefits and expenses.

With regard to these matters, there were four main changes which the Government planned to include in FA 2015:

1. abolishing the threshold for the taxation of benefits for employees earning less than £8,500 pa;
2. introducing a statutory exemption for trivial benefits;
3. introducing a system of voluntary payrolling for benefits in kind; and
4. replacing the dispensation system with an exemption for paid and reimbursed expenses.

Rather strangely, FA 2015 does not include the statutory exemption for trivial benefits.

The existing system operates at two levels. Employers can apply to HMRC for a dispensation, allowing them to pay specified expenses to their staff without having to report these items to HMRC and, of course, without having to deduct income tax and NICs.

Unfortunately, HMRC do not make dispensations available to all employers, mainly because of their concern about the misuse of expense payments in connection with tax avoidance.

Employees of a company without a dispensation arrangement are thus charged to tax on their expense claims which they then have to recover from HMRC after the end of the tax year.

This regime was condemned by the OTS in their report. The OTS recommendation was that it should be replaced with a straightforward exemption for qualifying expenses, allowing all employers to determine for themselves whether an expense payment is taxable or not. All employees of all companies would automatically receive tax relief on their legitimate expenses, subject only to checks being made by HMRC on the employer's records.

HM Treasury accepted this recommendation. With effect from 6 April 2016, the dispensation regime is being abolished. Ss65 and 96 ITEPA 2003, which govern the application for, issue of and revocation of dispensations, are repealed (S12(2) – (5) FA 2015). However, HMRC's powers are preserved by S12(6) – (8) FA 2015 to allow them, if necessary, to revoke dispensations retrospectively in respect of those which were in place before 6 April 2016.

S11 FA 2015, which inserts Ss289A – 289E ITEPA 2003, introduces the new automatic exemption for 2016/17 onwards.

S289A(1) ITEPA 2003 provides an exemption for the amount of any paid or reimbursed expenses which would be treated as earnings under the benefits code but where a deduction would otherwise be due under Chapters 2 or 5 of Part 5 ITEPA 2003. An example of such a deductible expense would be any costs necessarily incurred for travel in the performance of an employee's duties. As is invariably the case nowadays, the exemption will not apply if the payment or reimbursement is offered in connection with what are described as 'relevant salary sacrifice arrangements' (see S289A(5) ITEPA 2003).

In addition, S289A(2) ITEPA 2003 provides an exemption for payments of expenses which are calculated in an 'approved way'. An 'approved way' for these purposes is defined in S289A(6) ITEPA 2003. This requires that sums are calculated and paid in accordance with:

- regulations laid down by HMRC; or
- an agreement made under S289B ITEPA 2003.

However, a further requirement is that Conditions A and B must be met. Condition A is that the employer or a third party must have a system in place to check that the employees are actually incurring expenses of the appropriate type and that they would otherwise be allowable (S289A(3) ITEPA 2003). Condition B, which is found in S289A(4) ITEPA 2003, prevents the exemption applying if the person operating the checking system knows or suspects that the employee is not incurring the expense or that the expense is not tax-deductible.

S289B ITEPA 2003 introduces provisions which allow employers to apply to HMRC for a flat rate payment to be made to employees in respect of deductible expenses. As part of this procedure, the employer must provide HMRC with a reasonable estimate of the actual costs incurred.

However, this arrangement may only go ahead once an HMRC officer has approved the application and issued an approval notice. The legislation specifies the information which the approval notice should contain. Where it becomes necessary, S289C ITEPA 2003 sets out the mechanism for revoking approval notices.

S289D ITEPA 2003 brings in a separate exemption for benefits such as the use of company credit cards where the employee would otherwise be entitled to a deduction under Chapter 3 of Part 5 ITEPA 2003. Here, too, there is a 'relevant salary sacrifice' restriction.

Over and above all this, there is a targeted anti-avoidance rule (TAAR) which prevents the exemptions in Ss289A and 289D ITEPA 2003 from applying to expense payments and benefits which are given as part of certain types of arrangement (S289E ITEPA 2003). An arrangement is caught by this TAAR if its effect is to reduce the employee's income subject to tax and NICs and its main purpose, or one of the main purposes, is the avoidance of tax or NICs.

S11 FA 2015 introduces the necessary changes for income tax. Changes will be made to the NIC legislation to mirror aspects of these rules for payments which are subject to Class 1 NICs. For benefits which fall within a liability for Class 1A NICs, current NIC legislation automatically mirrors the income tax position.

Article by Robert Jamieson

Capital Taxes

Taper relief and properties occupied by listed companies

Summary - The FTT found that taper relief did not apply to the disposal of a property occupied by subsidiaries of listed companies.

Mr Richardson, together with a business associate, had purchased a property comprising a shop and an office, which had both been let to tenants. The property had later been sold with the tenants still in occupation and taper relief had been claimed on the disposal under TCGA 1992 Sch A1. HMRC had denied relief on the ground that the tenants were listed companies.

Decision:

The FTT accepted that the tenants were trading companies; however, they were '51% subsidiaries' (ICTA 1988 s 838) of listed companies. The property was therefore not used by 'qualifying companies' and taper relief did not apply to its disposal.

Comments - The case confirms that the definition of '51% subsidiary' for taper relief is that contained in ICTA 1988 s 838 and not that in TCGA 1992 s 170. The appeal did succeed, however, as the FTT found that HMRC had given notice of the enquiry after expiry of the time limit.

Andrew Richardson v HMRC [2015] UKFTT 179

Entrepreneurs' relief for Lloyd's underwriters

Summary - The FTT found that the disposal of syndicate capacity by a Lloyd's underwriter did not qualify for entrepreneurs' relief.

Mr Carver underwrites risk through syndicates. Syndicates are the means by which insurance is written at Lloyd's. In order to join a syndicate, members must purchase 'syndicate capacity'.

HMRC had rejected Mr Carver's claim for entrepreneurs' relief (under TCGA 1992 s 169H) in respect of the disposal of syndicate capacity. Mr Carver contended that he had disposed of a separately identifiable part of his business as he continued to hold capacity in other syndicates. HMRC considered, however, that the disposal of capacity did not constitute 'part of a business', as Mr Carver had not disposed of a 'viable section' of his business but simply of an asset used in it.

Decision:

The FTT noted that the capital gains tax treatment of a Lloyd's business could not be intended by Parliament to diverge conceptually from its treatment for income tax, which is as income from a single source.

Mr Carver must therefore have carried out a single trade, regardless of the fact that he was involved in many syndicates. Furthermore, capacity is not in itself the trade, but a means by which the trade is carried on, in a way partly analogous to goodwill. It is therefore an asset of the trade.

Comments - The case explores the application of entrepreneurs' relief to the trade of Lloyd's underwriters. In doing so, it sets out the key requirements of the relief.

John Humphrey Roberton Carver v HMRC [2015] UKFTT 168

The waiver of a debt and CGT consideration

Summary - The FTT confirmed that the waiver of a debt was part of the consideration for CGT purposes.

Mr Cooling had sold 99.9% of the share capital of 'Target'. Before executing the share purchase agreement, he had entered into an asset purchase agreement with the company to buy several assets. The share purchase agreement provided that the £297,638.95 debt owed by Mr Cooling to Target as a result of the asset purchase agreement would not be recovered by Target. The issue was whether this amount was part of the consideration for the share disposal.

Decision:

The FTT found that the tripartite arrangement under which Mr Cooling would not be required to pay for the assets purchased from Target only made sense in the context of the disposal of the shares in Target. Mr Cooling had therefore received £297,698.95 non-cash consideration in the form of the release from a debt. This was part of the overall consideration for CGT purposes.

Comments - Although the parties had agreed a consideration of £21m, the FTT found that the sale proceeds should be increased by the debt waived by the buyer.

Steven Cooling v HMRC [2015] UKFTT 223

Further entrepreneurs' relief amendments (Lecture P899 – 23.07 minutes)

Associated disposals

Where an individual qualifies for entrepreneurs' relief on the disposal of shares, he can also obtain relief under S169K TCGA 1992 for the associated disposal of an asset used by his company. Typically, this will be property which is personally owned by the individual and has been used by the company for business purposes, but it can also cover the sale of intellectual property such as goodwill which is held outside the company by the vending shareholder.

There are similar provisions for a partner who owns premises or other business assets which are used for the purposes of the partnership trade.

The legislation requires various conditions to be satisfied before an associated disposal can attract relief. Until recently, the main one has been that the vendor making the associated disposal must do so as part of his 'withdrawal from participation' in the business carried on by his company or partnership.

HMRC interpreted this requirement in the same way as they did for the corresponding retirement relief provisions. Thus the 'withdrawal from participation' test could be met by simply disposing of part of the individual's shareholding or partnership interest. Indeed, in early 2012, HMRC confirmed that, in the case of shares, the disposal of a single share would suffice – see page 8 of 'Entrepreneurs' Relief – Practical Points' which is a guide for members of the CIOT on technical aspects of the relief raised with HMRC (this guide can still be accessed on the CIOT's website). There is no requirement that the disposal of the owner's business interest has to give rise to a gain or, if it does, that it must be the subject of an entrepreneurs' relief claim. Nor is there any need for the vendor to reduce his workload, ie. he does not have to stop working for the company or partnership.

S41 FA 2015 has made important changes to S169K TCGA 1992 in relation to disposals on or after 18 March 2015. It is now a prerequisite that the disposal of the asset owned personally must be accompanied by a significant reduction in the claimant's participation in the business. This condition is met if the interest disposed of represents, in the case of a company, at least 5% of the company's ordinary share capital carrying at least 5% of the voting rights. With partnerships, the equivalent rule is that a 5% minimum interest in the assets of the partnership must be disposed of. And there cannot be any arrangements for repurchasing further shares in the company or a further partnership interest.

Illustration 1

Anthony is aged 48 and has been the managing director of, and largest shareholder in, his family company for the last 10 years. He holds 35 ordinary shares of £1 each out of a total of 100 in issue.

Anthony also owns the business premises from which his company trades. He has recently been approached by Sainsbury's who would like to acquire the property and convert it into one of their town centre supermarkets. They offer Anthony a substantial sum which, if accepted, would give rise to a gain of £2,850,000.

If Anthony decides not to do any tax planning, he will suffer a CGT charge of 28% on the sale. However, if he is able to bring S169K TCGA 1992 into play, he can claim entrepreneurs' relief on the disposal of the business premises which should reduce his CGT liability by more than £500,000. Clearly, this is an important consideration.

Accordingly, Anthony chooses to give his 25-year old son five shares in the company at the same time as the Sainsbury's sale goes through. Holdover relief under S165 TCGA 1992 is claimed in respect of this family transaction. As a result, Anthony is entitled to claim entrepreneurs' relief on the property sale.

In the past, a gift of one share to his son would have been good enough.

HM Treasury have explained the rationale for the restriction as follows:

'This measure removes an unintended facility under the entrepreneurs' relief rules. Under these rules, the relief could be claimed by an individual on a disposal of a private asset used in a business without the individual permanently reducing their participation in the business by a meaningful amount.

Allowing relief in these circumstances (was) not consistent with the purpose of entrepreneurs' relief on associated disposals, which is to promote the transfer of a business to new proprietors along with all the assets used in that business, including assets which are not owned by the trading entity.

This measure ensures that entrepreneurs' relief is better targeted at people who have genuinely reduced their participation in a business.'

It should be emphasised that there is still no need for the vendor to reduce his working hours in order to qualify for associated disposal relief.

There has been no alteration to the legislation in S169P TCGA 1992 under which entrepreneurs' relief on an associated disposal can be scaled down on a 'just and reasonable basis' in the event of various circumstances such as the charging of rent to the company or partnership for its use of the business premises.

Meaning of 'trading company' and 'trading group'

In the context of entrepreneurs' relief, the terms 'trading company' and 'trading group' are stated in S169S(5) TCGA 1992 as having the same meaning as in S165A TCGA 1992. One of the side-effects of this definition was that, if a company held 10% or more of the ordinary share capital of a joint venture company, a proportionate part of the joint venture company's activities was treated as belonging to the investing company. A joint venture company is a company:

(i) which is a trading company or the holding company of a trading group; and

(ii) at least 75% of the ordinary share capital of which is held by not more than five persons.

Thus, if I Ltd owns 32% of JV Ltd (a qualifying joint venture company), I Ltd was treated as owning 32% of JV Ltd's trading activities – normally, a minority stake would count as an investment.

Structures have been set up under which individuals hold a 5% stake in I Ltd (and they must of course also be officers or employees) so that they will qualify for entrepreneurs' relief when they sell their shares. This is despite the fact that I Ltd does not itself carry on a trade but only has a 32% interest in JV Ltd. I Ltd is treated as a trading company because of its investment in JV Ltd.

With effect from 18 March 2015, activities of joint venture companies in which a company holds shares will no longer be regarded as carried on by the shareholder company (S43 FA 2015). Similarly, activities carried on by a company in its capacity as a partner in a firm will not be treated as trading activities. In HMRC's words:

'Allowing relief in these circumstances (was) inconsistent with the relief's purpose of supporting significant participation by claimants in businesses.'

This new measure will mean that many of the joint venture structures which have been put in place to secure entrepreneurs' relief for individuals who would not otherwise have satisfied the 5% requirement in the main trading company will now be ineffective and will have to be reviewed.

Contributed by Robert Jamieson

Administration

Reasonable excuse: IT issues

Summary - The FTT found that the appellant had a reasonable excuse for the late filing of her return.

Ms Porter was appealing against a penalty imposed for the late filing of her individual tax return. The due date had been 31 January 2014, but she had filed her return on 5 March 2014.

She had repeatedly contacted HMRC prior to the deadline explaining that she was unable to pay the tax due online due to some access issue; and she had been informed that this was due to an IT failure which would be remedied.

Decision:

The FTT found that Ms Porter had 'done her best' to submit her return on time. The IT difficulties that she had encountered were unexpected and had eventually been solved when HMRC had issued her with a new ID number. The taxpayer had established a reasonable excuse.

Comments - Cases in which a taxpayer successfully establishes a reasonable excuse are few and far between. This case may provide a useful precedent to any taxpayer who files a return late due to IT issues.

Joanna L Porter t/a Crafty Creations v HMRC [2015] UKFTT 0170

Reasonable excuse: Agent's late registration

Summary - The FTT found that the late registration of an agent by HMRC constituted a reasonable excuse for the late submission of employer annual returns (EAR).

Perfect Permit had delivered its EAR (forms P35 and P14) late in respect of the years 2008/09 and 2009/10 and had been charged penalties.

Decision:

The FTT observed that the 2008/09 return had been filed on 5 July 2010, over a year late, and so the penalty was due. The failure of the taxpayer's previous agent was not a reasonable excuse and it was up to the taxpayer to seek redress from its agent.

The return for 2009/10 was also filed on 5 July 2010, only 47 days late and by the taxpayer's new agent. The FTT accepted that the new agent had experienced 'genuine and continuing difficulties' in registering with HMRC as an agent. He had started the process on 5 March 2010 and still had not been registered by 5 August 2010. Had HMRC registered the new agent reasonably promptly, it was likely that the return would have been filed on time. HMRC's delay in registering the new agent therefore represented a reasonable excuse.

Comments - Like the previous case, this case is a rare example of 'reasonable excuse' being successfully pleaded. It also confirms that a system failure by HMRC can constitute a reasonable excuse.

Perfect Permit v HMRC [2015] UKFTT 171

Reasonable excuse: HMRC confused taxpayer

Summary – The Tribunal agreed that HMRC had confused the taxpayer

The taxpayer submitted his 2012/13 self-assessment tax return electronically on 20 December 2013. It showed a capital gains tax liability of £1,440. He requested in his return that any outstanding tax be collected through his tax code, but HMRC expected the tax to be paid on 31 January 2014 (TMA 1970, s 59B(4). They issued a late payment penalty against which the taxpayer appealed.

Decision:

The First-tier Tribunal said that HMRC did not act on the taxpayer's request to code out the outstanding tax. Not only did they fail to tell him, but they did not explain why until 1 April 2014. The Revenue sent a reminder for the tax in February 2014 but, because they did not include a copy of this in the papers before the tribunal, it could not be accepted as evidence.

Given that the taxpayer's first PAYE deduction would have been made in April 2014, the judge said it was "understandable" why he made no payment.

In fact, it was not until HMRC responded to his query in March asking for clarification of the position that the taxpayer realised his PAYE code had not been adjusted. After receiving a penalty notice, he appointed an agent and paid the tax at the beginning of June 2014.

The judge said:

"This whole problem could have been avoided if HMRC had notified the appellant that they would not be collecting the tax by PAYE code adjustment. They processed the taxpayer's return on 20 December 2013 so had ample time before 31 January 2014 to notify him."

Although HMRC applied the rules correctly, they should have told the taxpayer before 31 January that the tax had to be paid by then. By taking advice he had taken the action of a "reasonably diligent man wishing to comply with his tax actions". The tribunal concluded he had a reasonable excuse for the late payment of tax and quashed the penalty.

The taxpayer's appeal was allowed.

Comments – The Tribunal will look at the level of knowledge of the taxpayer and the effort that has been made by the taxpayer. That was clearly what occurred in this case and HMRC did themselves no favours by their lack of actions at the appropriate times.

J Crangle v HMRC TC4354

Reasonable excuse: Too much pressure on the adviser

Summary – The Tribunal allowed reliance on an adviser as a reasonable excuse

The taxpayer employed an adviser to file his self-assessment tax returns each year. The return for 2012/13 was submitted late and HMRC imposed a penalty.

The taxpayer appealed on the ground that he relied on his agent to deal with the form. He had delivered his papers to her in sufficient time to complete the return. However, the adviser had had a busier time than usual because her father-in-law had fallen ill at the beginning of 2014 and died in April.

As a result she had less help with her children and, although she thought she had submitted all her clients' returns on time, she discovered in early February that she had missed the taxpayer's return.

Decision:

The First-tier Tribunal found that the agent had not told the taxpayer that she was facing more pressure than usual in January. He believed that he had employed a reliable person to submit his tax returns on his behalf and had no reason to suspect that she had failed to do so in January 2014. The tribunal judge ruled that he had taken reasonable steps to file on time and had a reasonable excuse for the late submission.

The judge warned the adviser that “taking on new clients when under too much pressure is not necessarily the action of a reasonable person”.

The taxpayer's appeal was allowed.

Comments – Normally reliance on a third party such as an adviser would not be treated as a reasonable excuse. However in this circumstance the taxpayer had good reason to rely on his adviser and therefore the tribunal judge ruled that he had taken reasonable steps to file on time and had a reasonable excuse for the late submission.

S Taylor v HMRC TC4375

No reasonable excuse - Penalties stand

Summary – The Tribunal found against the taxpayer through lack of reasonable excuse

The taxpayer appealed against late payment penalties imposed by HMRC under FA 2009, Sch 56 for 2012/13. It claimed reasonable excuse on the grounds of:

- financial, economic and cashflow difficulties;
- HMRC had not made it aware of the penalties; and
- company employee changes.

Decision:

The First-tier Tribunal said there was no reasonable excuse. The company had not shown that it had insufficient funds each time it failed to make its PAYE on time; still less that there was any event over which it had no control that led to the lack of funds. Further, HMRC had warned the company about the risk of penalties and, even had they not done so, it would not be deemed a reasonable excuse because "ignorance of the law was no defence". On staff changes, the tribunal said this did not affect the company's statutory obligation to settle its PAYE on time.

The tribunal considered that HMRC's decision not to exercise its discretion under Sch 56 para 9 that there were special circumstances was not flawed and, had the tribunal exercised its own discretion, it would have reached the same conclusion. The taxpayer's appeal was dismissed.

Contents – Reasonable excuse is exactly that – The comments by the Tribunal make it clear that you have to prove the reasons. The taxpayer company had not really made the appropriate effort to prove that and therefore failed.

Bluu Solutions Ltd v HMRC TC4300

No reasonable excuse - Plenty of time

Summary –Tribunal confirmed penalties as the taxpayer did not have a reasonable excuse for the failure.

On 6 March 2014, HMRC issued notices to the taxpayer to make self-assessment tax returns for the three years ended 5 April 2013. The submission date for each return was, under TMA 1970, s 8(1H), 13 June 2014. The taxpayer filed the returns on 7 July 2014 and HMRC imposed a late filing penalty of £100 for each one.

The taxpayer appealed against the penalties on the ground that she had no self-assessment income for any of the years and was required to complete the forms only because a query had arisen on her pension where tax had been deducted at source. She said it was impossible for her to submit the returns in the timescale allowed.

Decision:

The First-tier Tribunal disagreed that the taxpayer did not have enough time to deliver the returns. HMRC had used their discretion to allow a further seven days for submission and "it was clearly possible for the appellant to submit the returns by that date and therefore on time".

The taxpayer did not have a reasonable excuse for the late returns and there were no special circumstances to allow the penalties to be reduced. The taxpayer's appeal was dismissed.

Comments – Cases like this demonstrate how sometimes the system can be potentially unfair. The penalties applied even though there was no self-assessment income in the relevant years.

IM Cahoon v HMRC TC4355

No reasonable excuse - No proof of postage

Summary – The Tribunal found against the taxpayer because of lack of proof of posting.

On 10 April 2014, the taxpayer received a notice to file a 2012/13 self-assessment tax return. The deadline for filing was 17 July 2014 (in accordance with TMA 1970, s 8(1H)). HMRC alleged that the form was submitted late, on 20 August 2014, so they imposed a late filing penalty.

The taxpayer appealed. He claimed that his wife posted the return to HMRC on 6 May 2014. She had used a post box so was unable to provide proof of postage.

Decision:

The First-tier Tribunal agreed that post going astray might constitute reasonable excuse. However, because the taxpayer was unable to provide evidence of posting, "regrettably" the appeal would be dismissed.

Comments – The comments of the FTT are self-explanatory.

NP O'Keeffe v HMRC TC4356

Double tax treaty relief on dividends

Summary - The FTT found that double tax treaty relief was not available in respect of dividends which represented loan repayments.

The issue was whether Next was entitled to double taxation relief (DTR).

This depended on whether dividends paid by its UK subsidiary Next Near East Ltd (NNEL) were 'dividends' for the purposes of the relevant provisions (ICTA 1988 ss 788–812); and, if so, whether 'underlying tax' paid by NNEL in respect of its own Hong Kong subsidiaries could be taken into account. HMRC claimed that Next had artificially inflated its entitlement to DTR, as some of the dividends were actually loan repayments.

Decision:

The FTT observed that the relevant provisions refer to income, gains and profits and therefore cover 'dividends representing the payment of profit not dividends with some other purpose'. The FTT also noted that the accounting entries showed that the greater part of the dividend represented the repayment of a loan and that this could not be ignored simply because the payment had the form of a dividend.

Comments - In the view of the FTT, 'the question was not whether the payment took the form of a dividend or had the character of income but whether the payment was of profits which had borne tax'**.**

Next Brand Ltd v HMRC [2015] UKFTT 175

One bad debt did not make the total claim

Summary –Tribunal found that part of the claim for bad debts on a self-assessment tax return was valid.

The taxpayer ran an agency providing care workers for families with dependent children who had a mental or physical disability. During 2010/11, two clients failed to pay for services they had received. The taxpayer included the total of the unpaid amounts, £6,713, in box 26 "irrecoverable debts written off" of his 2010/11 tax return and set them off against the profits for the year. HMRC did not accept that the sums were bad debts and amended the assessment.

The taxpayer appealed. He produced evidence to show that £438.38 was irrecoverable and it was agreed it constituted a bad debt.

Decision:

On the remainder, the tribunal found that the client had made payments over time and, without a list of the amounts due and paid, it was impossible for the tribunal to find which debts remained unpaid. The judge concluded "on balance, that the sums which are now outstanding relate to a later period".

The tribunal noted that, because the taxpayer thought he had been told to enter sums in box 26 where the debt was unpaid at the end of the tax year, HMRC accepted no penalty was appropriate.

The taxpayer's appeal was allowed in part because one debt was bad.

Comments – This case demonstrates how all figures on a self-assessment tax return need to be supported by relevant figures as they are exactly that self-assessed and therefore verification could be needed at any point. Reliability of back up documentation must be retained.

M Michiels v HMRC TC4357

FTT's jurisdiction on legitimate expectation

Summary - The FTT found that it had no jurisdiction to consider legitimate expectation.

The appellants had made supplies to a university which they had treated as exempt. HMRC considered that VAT should have been charged. The appellants conceded that the supplies could not have been exempt, as they had not been made by an eligible body. However, the appellants' case was that Mr Aspinal had been informed by an HMRC officer that the supply was exempt, as it was in respect of medical research. This was wrong. They therefore claimed that they had a legitimate expectation that the supply would be treated as exempt.

Decision:

The FTT observed that it does have the authority to consider legitimate expectation in some cases where HMRC has lawfully exercised its powers, such as *Oxfam* [2009] EWHC 2078. *Noor* [2013] UKUT 71, however, establishes that the FTT's jurisdiction does not extend to cases where HMRC has acted beyond its powers, for instance, by giving a misdirection, as was the case here.

The FTT would therefore not consider the part of the appellant's case relating to legitimate expectation and dismissed the appeal as the supply was chargeable.

Comments - Since the inception of the FTT, the extent of its jurisdiction to hear legitimate expectation cases has been the object of much debate. This case clarifies the position.

Nicholas John Aspinal and others v HMRC [2015] UKFTT 162

No chance of success

Summary –Court found against taxpayer's appeal on basis that they had not provided sufficient evidence

In April 2014, HMRC presented a creditor's petition for the winding-up of a company on the ground that it owed corporation tax of about £239,000.

The company appealed against the assessment to the First-tier Tribunal and applied for the petition to be dismissed, arguing that the tax liability was in dispute.

The petition was amended to cover a VAT liability of £1.6m. HMRC said the company had not paid the input tax claimed and was therefore not entitled to set it off against the output tax for which it was liable. This was known as the non-payment issue. The company appealed against this assessment and applied to have the petition dismissed because the VAT had not been agreed.

HMRC made more amendments to the petition to take account of other assessments. They said that no supply existed to allow the company to justify the inputs claimed and accused it and its sister company of having taken part in VAT fraud. This was the non-supply issue. The company appealed.

Decision:

Nicholas Le Poidevin QC in the Chancery Division, Companies Court said it was settled law that a debt disputed on substantial grounds could not give rise a winding-up order. However, this did not entitle the company to do no more than assert that the tax was disputed — it had to provide more information and show it had a substantial case.

In this instance, since the company had failed to provide evidence, it followed that its appeal had no real prospect of success on either the non-payment issue or the non-supply issue.

The taxpayer's application to have HMRC's winding-up petitions dismissed failed.

Comments – This is another case where the lack of evidence was the cause of the failure in the Court. It is surprising that appellants take cases to the Courts and reduce their chance of success by lack of preparation or evidence.

Winnington Networks Communications Ltd v CRC

Jurisdiction of UT to hear appeals against information notices

Summary - The UT found that any decision of the FTT relating to information notices cannot be appealed.

Miss Jordan is a taxi driver. Following her refusal to participate in a business records check, HMRC issued an information notice (FA 2008 Sch 36). The notice had not been approved by the FTT, and Miss Jordan had exercised her right of appeal.

The FTT had held (1) that part of the request which related to non-statutory records should be disallowed, (2) that some of the requested items were not statutory records and (3) that there was no right of appeal in respect of the statutory records. The issue was whether FA 2008 Sch 36 para 32(5) precluded Miss Jordan from appealing to the UT against all three parts of the decision.

Decision:

It was clear that no appeal lay against (1). The UT also found that there was no appeal against a decision of the FTT that an item was (or was not) a statutory record (2). Such a decision would be the result of an appeal under para 29 so that para 32(5) would be engaged. Finally, there was no right of appeal to the UT against the decision of the FTT to strike out an appeal on the grounds that the documents requested were statutory records (3). First, because the appeal would have been brought under para 29; and second, because the appeal would be against the decision of the FTT that the documents were statutory records and such a decision cannot be appealed.

Comments - The UT explained that the purpose of the legislation was to restrict judicial scrutiny to one stage in order to avoid undue delays to HMRC's information gathering process. There was therefore no exception to the rule that the FTT's decisions on information notices cannot be appealed.

Carmel Jordan v HMRC [2015] UKUT 218

Consequence of contempt

Summary - The Court ordered a custodial sentence for the contempt of court.

The claimant, HMRC, presented a petition for £7.7m in respect of a company for unpaid VAT. The court appointed a provisional liquidator to take possession of the assets of the company and to collect and protect them. The order stated that the liquidator was appointed as an officer of the court and that it was a contempt of court for any person to prevent or impede him in carrying out his duties.

The defendants, M and F, were directors of the company. Another defendant, C, was the company secretary. The provisional liquidator, an independent solicitor and a process server attended the company premises and M, in the presence of C, was served with documents, including the order appointing the provisional liquidator. The company made three payments to another company.

The Revenue brought proceedings against the defendants saying the payments had been made in contempt of court. The defendants admitted to breaching the court order.

Decision:

Mr Justice Norris in the High Court said that a contempt of court was not a wrong done to another party to the litigation. It was an affront to the rule of law and to the court. In this instance, a custodial sentence was essential. When officers of a company tried to prevent a liquidator carrying out his duties, a clear message had to be sent to the commercial community that such conduct had serious consequences. It did not matter that the defendants were paying a supplier. They had usurped the role of the liquidator by disposing to a creditor money that did not belong to them. They had done this partly to benefit themselves in the hope that they could delay full liquidation and recover control of the company.

The judge said the defendants had not been "lining" their own pockets directly, so the case was not as bad as it could have been. But their actions were serious "because of the sums involved, because of the proportion of the companies' assets which is affected by your conduct, because of the consequences for the liquidation and because, above all, you intentionally thwarted the purpose of a court order".

The judge sentenced the defendants to six months' imprisonment telling them that they would serve three.

Comments – This case demonstrate that taxpayers play a very dangerous game when they take the actions that they took to avoid unpaid VAT. When officers of a company tried to prevent a liquidator carrying out his duties, a clear message had to be sent to the commercial community that such conduct had serious consequences. The judge said the defendants had not been "lining" their own pockets directly, so the case was not as bad as it could have been. But their actions were serious "because of the sums involved, because of the proportion of the companies' assets which is affected by your conduct, because of the consequences for the liquidation and because, above all, you intentionally thwarted the purpose of a court order".

CRC v Munir and others, Chancery Division

Personal or business?

Summary – The Tribunal found in part for the taxpayer.

HMRC enquired into the taxpayer's 2011/12 self-assessment tax return. They issued a notice under FA 2008, Sch 36 to obtain bank and credit card statements.

The taxpayer appealed, saying the notice breached his right of privacy. He said HMRC had all the information they needed and the statements were private documents and unrelated to his property business.

Decision:

The First-tier Tribunal said, in this instance, the information was “reasonably required” since there was the possibility that the bank or credit card accounts were used for “returnable activities and private ones”.

However, given that the statements would include private transactions, the tribunal varied the information notice permitting the taxpayer to omit certain personal information.

The taxpayer's appeal was allowed in part.

Comments – The request for bank account statements is always a thorny issue because of the different positions that a taxpayer and HMRC will come from. The tribunal judge ruled that he had taken reasonable steps to file on time and had a reasonable excuse for the late submission.

J Smith v HMRC TC4392

Deadline dates for June 2015

1 June 2015

- Payment of CT liabilities for small/medium-sized companies with accounting periods ended 31 August 2014 where payment not required by instalments.
- Check for revised HMRC advisory fuel rates.

7 June 2015

- Electronic filing and payment of VAT liability for quarter ended 5 April 2015.

14 June 2015

- Quarterly CT instalment for large companies (depending on year end).
- EC sales list for quarter ended 30 April 2015 due (paper form).

19 June 2015

- PAYE/NICs/CIS/student loan payments for month ended 5 June 2015 if not paying electronically.
- File monthly construction industry scheme return.

21 June 2015

- File online monthly EC sales list.
- Submit supplementary Intrastat declarations for May 2015.

22 June 2015

- Electronic payment of PAYE/CIS liabilities for month ended 5 June 2015 should have cleared

30 June 2015

- Companies House should have received 30 September 2014 accounts of private companies
- Companies House should have received accounts of PLCs with 31 December 2014 year end.
- HMRC should have received CTSA returns for companies with periods ended 30 June 2014.
- CT61 — quarterly period ends.
- VAT partial exemption annual adjustments for March VAT year end.
- Receipt of returns by savings institutions made under the European Savings Directive for 2014/15

HMRC News

Recognised stock exchanges

HMRC has updated its lists of recognised stock exchanges. Recognition under ITA 2007 s 1005 is for tax purposes only and confers no other status on the exchange concerned. It does not constitute any form of recognition or approval for regulatory or other purposes; nor does it provide any form of approval or recommendation of any of the investments which are listed or traded on that exchange. Whether or not a security is traded on a 'recognised stock exchange' constitutes a qualifying criterion for certain tax purposes, including ISA eligibility, alternative finance investment bonds and venture capital reliefs.

Employee benefit schemes case goes to Supreme Court

HMRC has been granted leave to appeal the Court of Appeal's decision in *DB Group Services (UK) Ltd v HMRC* and *HMRC v UBS AG* [2014] EWCA Civ 452. That case concerned employee benefit schemes implemented by UBS and Deutsche Bank to limit their liability to income tax and NICs on the payment of bonuses.

HMRC wins rate-booster case

HMRC has been quick to publicise its success in a tax case involving Next Brand Ltd, which is part of the Next group, over its use of a tax avoidance structure known as a rate-booster. The FTT ruled in HMRC's favour after finding Next's scheme artificially moved money around the group, so the company could try to claim tax relief on overseas profits. It is now facing a £22.4m tax bill.

HMRC's director general of business tax, Jim Harra said: 'This case shows how HMRC takes effective action against big businesses that try to avoid paying tax through convoluted, artificial avoidance schemes. HMRC expects all businesses to steer well clear of such schemes.'

This is the second rate-booster case to reach the FTT. The tribunal also ruled against P&O in 2013, which has appealed and is awaiting a decision. About £130m in tax is at stake across 20 rate-booster cases, which were waiting on the *P&O* and *Next* decisions. Around 70 rate-boosters have already been conceded by companies rather than go to court, which has brought in more than £500m in tax.

HMRC to scrutinise internationally mobile high earners

City law firm RPC has said there has been a 29% rise in the number of tax investigations into internationally mobile high earners by HMRC in the last year, and that the firm 'does not expect any let up in HMRC's investigations of this class of high earners'.

RPC says HMRC's specialist personal tax international compliance unit investigated 764 cases in 2014/15, up from 593 investigations in 2013/14 and 438 in 2012/13; and that the increase in the number of investigations has been driven by a clampdown on individuals that HMRC believes are wrongly claiming to be non-resident and non-domiciled in the UK. These include British citizens who now live abroad and international businessmen who have residences in the UK as well as other countries.

European Commission strategy for single digital market

The European Commission has set out its digital single market strategy for Europe with the publication of its *Commission staff working document* (www.bit.ly/1P09KWQ) and *Communication* (www.bit.ly/1clD1tZ).

Planned VAT changes include: extending the current single electronic registration and payment mechanism to cross-border online sales of physical goods; setting a common EU wide VAT threshold; and abolishing the small consignments relief for non-EU imports. The Commission will also review the VAT mini one-stop shop and 2015 place of supply rule changes.

Changes are planned to be introduced in 2016 and require approval of all 28 member states.

Multinationals split over BEPS

Taxand's annual global survey of multinational CFOs has shown that multinationals are split as to whether BEPS will create a more sustainable global tax system. 52% of respondents agreed that it would do so; while 48% disagreed. This compares with *Tax Journal*'s own survey of 75 tax directors/heads of tax, where 55% said they were sceptical that the OECD's BEPS project would meet its objectives.

While the OECD aims to achieve a more sustainable global tax landscape, the lack of clarity on key issues will mean further confusion for multinationals as to how operationally they should implement BEPS. The Taxand survey found that while 80% thought that tax initiatives intended to fundamentally reform the international tax architecture are desirable, only 55% think this is achievable. Meanwhile, 83% of respondents believe that enhancing global tax transparency will increase the cost of compliance.

'Education, education, education'

New CIOT president Chris Jones has said he stands for 'education, education, education'. In his inaugural speech at the CIOT's AGM this week, he clarified further, adding: 'Education of the public as to their obligations to the tax system … Education of tax agents as to the scale and nature of the changes we face in this new digital age …. [Finally] education of HMRC that they need an honest friend to help them on this journey … We are here to help, we want to make it work, just like they do, so let's work together, listen and learn from each other.'

EU and Switzerland sign automatic tax information exchange agreement

On 27 May the EU and Switzerland signed a historic new tax transparency agreement, which will significantly improve the fight against tax evasion. Under the agreement, both sides will automatically exchange information on the financial accounts of each other's residents from 2018. This spells an end to Swiss bank secrecy for EU residents and will prevent tax evaders from hiding undeclared income in Swiss accounts. The agreement was signed this morning by Commissioner Pierre Moscovici and Janis Reirs, Latvian Minister of Finance on behalf of the Latvian Presidency of the Council for the EU, and by the Swiss State Secretary for International Financial Matters, Jacques de Watteville.

Pierre Moscovici, European Commissioner for Economic and Financial Affairs, Taxation and Customs, said: *"Today's agreement heralds a new era of tax transparency and cooperation between the EU and*

Switzerland. It is another blow against tax evaders, and another leap towards fairer taxation in Europe. The EU led the way on the automatic exchange of information, in the hope that our international partners would follow. This agreement is proof of what EU ambition and determination can achieve."

The automatic exchange of information is widely recognised as one of the most effective instruments for fighting tax evasion. It provides tax authorities with essential information about their residents' foreign income, so that they can assess and collect the taxes that are due on them.

Under the new EU-Swiss agreement, Member States will receive, on an annual basis, the names, addresses, tax identification numbers and dates of birth of their residents with accounts in Switzerland, as well as other financial and account balance information. This new transparency should not only improve Member States' ability to track down and tackle tax evaders, but it should also act as a deterrent against hiding income and assets abroad to evade taxes.

The new EU-Swiss agreement is fully in line with the strengthened transparency requirements that Member States agreed amongst themselves last year. It is also consistent with the new OECD/G20 global standard for the automatic exchange of information.

The Commission is currently concluding negotiations for similar agreements with Andorra, Liechtenstein, Monaco and San Marino, which are expected to be signed before the end of the year.

HMRC and tax agents **(Lecture P900 – 12.56 minutes)**

The following is extracted from an article in Tax Journal on 6 March 2015 by HMRC's Director General for Business Tax, Jim Harra, talks about the department's plans to incentivise agents to provide a service which benefits them, their clients and HMRC itself.

How does HMRC view the role of agents in the tax system?

Agents play a central role in the tax system. Our customers clearly value how agents can relieve them of the burden of managing their own tax compliance. And HMRC values the fact that agents know what they're doing, which cuts down on the effort that we have to make in corrective work, compared to dealing with unrepresented taxpayers.

I think there's more value to be had for the tax system from tax agents. When an agent is managing the tax affairs of businesses, HMRC really shouldn't have to intervene to resolve non-compliance that could have been identified and sorted out by their agent.

The key thing for me in the future is making sure we've got the maximum value we can from having an agent in the relationship between HMRC and the taxpayer.

What will agents be doing in the future?

HMRC's plan is to launch new personalised digital services for our customers, which means that it will be much easier and more intuitive for them to interact with the tax system.

'Your tax account', already has over 2m users. I don't believe this means that taxpayers will suddenly decide they're going to do everything for themselves and don't need an agent any more.

But I think taxpayers will be looking to agents to either deliver them a lower-cost service or, more likely, a service which adds value to the one they get now. They will instead look to agents to help them to deal with the more complex issues and actively help them to stay on the right side of compliance.

HMRC wants to provide a better opportunity for agents to manage upfront the compliance risks their clients might present, because this is better for the client, better for HMRC and better for the agent, which can market this service.

When an agent represents a taxpayer, we will want to know what services that agent is providing. We'll be giving agents recognition for the value-added work they're doing, and we believe their clients will be willing to pay for this, because they will feel the benefit of a lighter touch from HMRC.

How will you get agents to change?

At the moment, it's difficult for HMRC and taxpayers to differentiate between tax agents. HMRC can't see which agents are adding more value than others.

We want to be able to differentiate between the agents that do offer value-added services and those that don't, and to incentivise all agents to provide these services — and adhere to high standards.

Part of this incentive would be making sure that those agents that provide more get the credit for doing so — whether that involves being able to take on a wider range of functions for their clients via our online services, or by receiving fewer low value interventions from HMRC.

What's in it for tax agents?

In order for them to be able to offer added-value services, we've got to help make it commercially viable for them. No doubt, there is still a future for the basic business model, which involves simply turning a set of information into a filing. But we want more customers to ask for more from their agents in the future, by looking for a filing that they can be sure that HMRC will be happy with — not just one that's filed on time, with payments made on time, but one that's accurate and complete. Exactly how we work with agents will vary, though, according to their needs, their compliance history and the value they add to the administration of the tax system.

How will you introduce new ways of doing things?

We want to build in the role of the tax agent when rolling out new digital services. 'Agent online self-serve' (AOSS) is a new online service aimed principally at professional tax agents, which will eventually replace the existing online service and act as the foundation stone for a range of expanded and improved services for agents in the future.

The first AOSS service will be tested in pilot form by a small number of agents this spring. We will continue to develop and test the service throughout 2015.

What do you mean by standards? How will you enforce them?

We will set the professional standards that we expect agents to meet to be able to transact with us. We are working with the representative bodies to agree these standards across the industry, for example by developing the *Professional conduct in relation to taxation* guidance.

Does HMRC have any ambition to regulate the tax profession?

No. HMRC has no intention of being the regulator for the tax agent industry. But we must intervene where we see standards that fall below an acceptable level, which may involve restricting access to some services where necessary.

Some agents are concerned you're simply trying to outsource some of HMRC's work to them. Is that fair?

The tax system creates a market and a role for tax agents. We want them to perform their role in a way which helps the tax system to run as well as it can. But we're certainly not in the position of just trying to transfer cost out of HMRC onto agents and their clients.

There are a lot of represented taxpayers receiving compliance interventions from HMRC. The more we can get agents up that value chain, the more we can remove the need for those interventions. It's about relieving the burden on taxpayers and incentivising agents to deliver the kind of service that clients will expect in the future.

If an agent makes an innocent error on a self-serve matter, will they be penalised?

No one should be penalised for an innocent error., whether they are an unrepresented taxpayer or an agent representing a taxpayer. Clearly, anybody can make a mistake and we should respond in a proportionate way. If we have evidence someone is deliberately doing something wrong to try to cheat the system, then we'll take tough action.

What we don't want to see is taxpayers — and their agents — being concerned that they'll get a disproportionate response from HMRC if they make an innocent error after taking proper care.

When will agents get a secure electronic communication service with HMRC?

Our aim is to provide this as part of AOSS, although this function will not initially be part of the service. These services will be released in stages, once they have been fully tested and feedback from agents has been fed into the solution every step of the way.

Business Taxation

Vocalspruce decision now final

The Supreme Court has refused the taxpayer permission to appeal in *Vocalspruce* [2014] EWCA Civ 1302, 'because the application does not raise an arguable point of law of general public importance which ought to be considered by the Supreme Court at this time bearing in mind that the case has already been the subject of judicial decision and reviewed on appeal'. The Court of Appeal ruling is therefore final.

In that case, Vocalspruce, a subsidiary of a London-based property business, lost against HMRC over an avoidance scheme used by a number of large businesses. The court found that, under the related party rule, the scheme, which involved the intra-group acquisition of loan notes, was actually taxable and thus failed. The notes were transferred in consideration for the issue of shares at a premium, paid up by capitalising profits and appropriating those to a share premium account. HMRC said the tax at stake was £85.4m.

Deloitte has reported that 'a number of cases' stood behind this lead case, but since the relevant legislation — on the tax treatment of loan relationships — has been heavily amended, the decision is 'of historical importance only'.

Business taxes: film partnerships and loss relief

Summary - The UT found that the partners were not entitled to loss relief and that they had not had a legitimate expectation that the relief would be available.

The issue was whether two partnerships, which had acquired and leased films under sale and leaseback arrangements, were entitled to loss relief in respect of losses which arose on the acquisition of the films. If so, their partners could claim sideways relief under ICTA 1988 ss 380 and 381 to set the losses against their taxable income from other sources.

The purchase of an asset which a person intends to exploit over a period of time is normally treated as capital expenditure. However, ITTOIA 2005 s 134 provides that in the case of a film, the expenditure should be regarded as revenue in nature. Furthermore, ss 138 and 140 allow loss relief to be claimed in advance of the normal rules. Relief is not available, though, if the expenses are not incurred wholly and exclusively for the purposes of a trade or if the losses are not connected with or arising out of a trade.

Decision:

The UT found that the FTT had been entitled to conclude that the partnerships had not been carrying on a trade, so that no loss relief was available to the partners. This was so, even though a transaction of that type could have constituted a trade. In particular, it accepted the FTT's factual finding that the commercial nature of the agreements was 'the payment of a lump sum in return for a series of fixed payments over 15 years'.

No further arguments were required following the release of the Court of Appeal's decision in *Eclipse Film Partners* [2015] EWCA Civ 95, which recommended a 'realistic approach to the transaction'. The UT added that even if the partnerships had been conducting a trade, they would not have been doing so on a commercial basis, as the transactions were intended to produce a loss in net present value terms. This analysis was not affected by the fact that the individual partners were accruing 'extra benefits' as a result of the tax reliefs. Those reliefs were obtained by 'deliberately causing the partnership to trade in an uncommercial manner'.

The two judges disagreed as to whether, in any event, one of the partnerships had incurred the expenditure for the acquisition of a film (as opposed to that of an income stream). The president exercised its casting vote on this issue, finding that the partnership had incurred the expenditure for the purchase of a film. This was because it had acted bona fide in the belief that it was acquiring valuable rights.

The taxpayers also claimed judicial review on the ground that HMRC's denial of relief was at odds with its own published guidance in HMRC's *Business Income Manual* (BIM). The UT pointed out that unlike IR20, which was aimed to give taxpayers guidance on residence, the BIM was intended for the use of HMRC staff — although it was made available to the public. The UT observed that the BIM stressed in several places that the relief was aimed at tax deferral only. Furthermore, the BIM included clear statements that transactions involving tax avoidance would be closely scrutinised and that the guidance may not be applied to them. The argument that this statement suggested that HMRC reserved the right to treat similar transactions differently was robustly rejected. 'Taxpayers may not like that statement but they could not say that they derived a legitimate expectation that was at odds with it.' Finally, the UT found that HMRC had reasonably thought that tax avoidance was at play. Several features indicated that the aim of the transactions was not tax deferment but tax avoidance.

Comments - The appeal failed on both the 'trading issue' and the legitimate expectation issue. On the trading issue, the UT simply reiterated the points made by the FTT on the basis of its factual findings. On the legitimate expectation issue, the taxpayers could not rely on HMRC's description of a plain vanilla transaction (claiming that their arrangements were similar) and ignore the general statement about tax avoidance. They could not 'take out the plums they liked and ignore the duff they did not'.

Samarkand Film Partnership No. 3, Proteus Film Partnership and three partners v HMRC [2015] UKUT 211

Agency workers – A reminder of the new rules

A worker who offers his services to a number of different clients may choose to sign up to an agency who will seek work on his behalf. The work secured for the individual by the agency may only be hours in duration or it may go on for months. Whatever the duration, the worker has a contract with the agency rather than with the individual clients. The agency generally bills the clients for the worker's services rather than the client paying the worker direct. The agency then pays the worker an amount as agreed in the contract between them.

The agency is responsible for assigning jobs on hand to the various workers it has under contract. Agencies are particularly common in the nursing, domestic care and temporary work sectors.

There are particular tax provisions in ss 44 and 688 ITEPA 2003 (the agency provisions) and NIC provisions in SI 1978/1689, Sch 1, Part I (the categorisation regulations). Those provisions can apply to treat the agency worker's income as employment income and, in most cases, make the agency responsible for the operation of PAYE on that income and make the employer liable to secondary Class 1 NIC in respect of the worker's income.

When do the provisions apply?

From 6 April 2014

The Government made changes in FA2014 to the agency worker legislation as part of its drive to prevent employment intermediaries being used to disguise employment as self-employment.

The agency rules now apply if a worker personally provides services to a client and there is a contract in place between the client and a third person (the agency) under which the client pays for the services that the worker provides. The provisions apply equally where a person connected with the client is a party to the contract rather than the client himself and / or if a person connected with the client pays for or provides consideration for the services supplied under that contract.

The agency rules do not apply if, when providing the services in question, the worker is not subject to (or to the right of) supervision, direction or control by any person. But, importantly, where the worker is engaged through an intermediary, HMRC will see this as a presumption that there is control over the worker.

The key difference from the rules that were in place previously is that the focus is now on whether the individual personally provides services to a client under a contract involving a third party rather than on the terms of such a contract.

There are equivalent provisions for NIC, which were also updated with effect from 6 April 2014 to mirror more closely the agency rules for tax purposes. The NIC agency provisions apply when a worker personally provides services to an end client and there is a contract between the end client and an agency under which those services are provided or the end client pays or provides consideration for the services and the worker is entitled to remuneration for providing those services (whether from the agency or anyone else). Again there is a get-out if, in providing the services in question, the worker is not subject to (or to the right of) supervision, direction or control by any person.

When do the agency provisions not apply?

If the income that the worker receives is taxable as employment income anyway, there is no need to consider the agency provisions.

Where the agency simply puts people forward to be considered for particular jobs and the contract for the work is between the worker and the client, the agency provisions do not apply. Instead the employment status tests should be applied to the contract between the client and the worker.

There are specific types of work that are excluded from the agency provisions. The provisions do not apply to work:

- as an actor, singer, musician or other entertainer
- as a fashion, photographic or artist's model
- in the worker's own home, or at a place neither controlled or managed by the client, and not prescribed by the nature of the services

Effect of the agency provisions

The main effect of the agency provisions is to treat as employment income any form of remuneration that the worker receives directly under the contract with the agency or that is connected with that contract.

PAYE

As stated above, in most cases it is the agency who actually pays the worker. For most purposes, the agency is treated as the employer for the purposes of PAYE in respect of income earned by the workers that it supplies to end clients. This means that the agency must deduct income tax and NICs from payments made to the worker and is also liable for secondary Class 1 NIC contributions.

In some cases, however, particularly with longer term assignments, the agency's client may pay the worker direct. If that happens, it is the client who must operate PAYE in respect of the payments made to the worker.

From 6 April 2015, there are further record-keeping and reporting requirements imposed on employment intermediaries such as agencies. Any employment intermediary must keep records for individual workers they place, even when they are not deducting tax and NIC under PAYE and also submit a quarterly return of any workers it has placed in the period but has not already included in any RTI returns.

Extracted from Tolleys Guidance

Intermediaries –Nitty Gritty of the New Reporting (Lecture P898 – 12.04 minutes)

From 6 April 2015, intermediaries must return details of all workers they place with clients where they don't operate Pay As You Earn (PAYE) on the workers' payments. The return is a report (or reports) that must be sent to HM Revenue and Customs (HMRC) once every 3 months.

If you only introduce workers to clients or supply workers to other intermediaries, and you aren't involved in any arrangements that follow, you don't need to send HMRC reports.

Who uploads and sends the report

You need to send a report to HMRC if at any time in a reporting period you:

- are an agency
- have a contract with a client
- provide more than one worker's services to a client because of your contract with that client
- provide the worker's services in the UK - or if the services are provided overseas, that the person is resident in the UK
- make one or more payments for the services (including payments to third parties)

If the workers you supply provide their services at sea in the oil and gas industry wholly on the UK continental shelf, you don't need to send HMRC reports.

You will need to provide the worker's details and payment details for workers where you don't operate PAYE. This includes overseas workers and payments where the worker is working in the UK or working temporarily abroad.

You don't have to include any details of workers who are your own employees.

You don't have to include any payment details where the payments have already been included as part of a PAYE Real Time Information (RTI) submission by any other organisation.

Information that should be included in the report

If you are responsible for sending the report to HMRC, you should include:

- your full name, address and postcode
- the worker's personal details
- the engagement and payment details

If you want to send reports that contain formatting errors and missing data you will be able to. You may receive a penalty if your reports are incomplete or incorrect.

Worker details

These are the personal details of the workers, including partners within a partnership and limited company directors, who personally provided their services to the client. These details must be included no matter how many intermediaries are involved in supplying the worker to the client. The intermediary sending the report must get these details from the worker or from any other intermediary that supplied the worker.

You should include each worker's:

- full name, address and postcode
- National Insurance number - if they have one and you don't know their date of birth and gender
- date of birth and gender - if they don't have a National Insurance number

Engagement and payment details

You must select the reason why you didn't operate PAYE on the workers payments from these options:

A. Self-employed
B. Partnership
C. Limited liability partnership
D. Limited company including personal service companies
E. Non-UK engagement
F. Another party operated PAYE on the worker's payments

If more than one reason applies select the option that comes first on the list. For example, if A and E both apply, select A.

You should also include the:

- worker's unique taxpayer reference - if they are self-employed or a member of a partnership
- start date of work with client
- end date of work with client - if there is one

The start date is the first date that a worker provides their personal services to a client for which they are paid.

The end date is the last date that a worker provides their services to a client for which they are paid.

Where the worker's services are provided on different occasions to a single client in a reporting period the payments should be combined into a single figure.

Where the worker's services are provided on different occasions to more than one client in a reporting period, you can either:

- combine the engagements into a single record with a single payment
- provide a separate line and payment for each client

If a bureau is used to pay another party on the worker's behalf, the name of the company or partnership should be reported, not the bureau.

If the worker was engaged to do the work and their payments have not been reported to HMRC using RTI, any worker engaged through options A to E, you must also include:

- total amount paid for the worker's services - this is the total payment that you contracted for the worker's services including any expenses and VAT
- currency - this must be given in Great British pounds (GBP) or euros (EUR) and if the worker was paid in another currency it should be converted into Great British pounds or euros using HMRC exchange rates
- whether or not VAT has been charged on the payment
- the full name or trading name and address of who the intermediary paid for the worker's services - this may be the worker's company or partnership
- Companies House registration number - only if the worker was engaged to do the work through a limited company (option D)

You may not know how much money the worker actually gets, but you will know how much money you paid to whoever supplied the worker to you. This may be another intermediary, limited company or personal service company, or the worker themselves.

For example, you have a contract with a client to supply 10 workers for £1,000. You supply:

- 5 workers yourself who you pay £100 each - 2 are your own employees you pay using PAYE and you report their payments on your RTI submission
- 5 workers from another intermediary who you pay £450 (£90 for each worker) and PAYE is operated by someone else

Your report to HMRC will include:

- 3 workers you supplied who weren't your employees who were paid £100 each
- 5 workers from the other intermediary who were paid £90 each

How to send reports to HMRC

Following the end of the first reporting period from 6 April to 5 July 2015 you will have until 5 August 2015 to send your first report to HMRC.

You must use HMRC's report template to create the reports. HMRC provide an online service for you to upload and send your report.

The service uses your PAYE reference and Accounts Office reference from when you sign in to the service as part of the report.

When you use the service, you have to state that the information in the report is correct before you can send it to HMRC.

Deadlines and penalties

Deadlines

You must send HMRC your report, or reports, by each reporting period's deadline or you may receive a penalty.

You can replace a report after you have sent it. You must do this before the next reporting period's deadline.

Reporting period	Deadline date	Date you can replace a report by
6 April to 5 July	5 August	5 November
6 July to 5 October	5 November	5 February
6 October to 5 January	5 February	5 May
6 January to 5 April	5 May	5 August

Penalties

If your report is late, incomplete or incorrect you may be charged a penalty.

Automatic penalties have been introduced for not sending a report or for sending a late report. These are given based on the number of offences in a 12-month period. These are:

- £250 - first offence
- £500 - second offence
- £1,000 - third and later offences

If there are 12 months or more between offences, you will only be charged £250 for the first offence in the new 12-month period.

Where there is continued failure to send reports or send reports late you may receive a penalty every day that you don't send a report.

There is a new appeal process for these new penalties.

For incomplete and incorrect reports, manual penalties may apply on a case-by-case basis.

If you replace a report before the deadline of the next reporting period without being asked to, HMRC will consider this when they decide if you have to pay a penalty.

Record keeping

You must keep information, records and documents that prove what you sent to HMRC was correct. HMRC may ask you for this information.

This information should include any documents that show why you didn't operate PAYEon the worker's payments.

You should work with the workers, other intermediaries involved in supplying the workers, and the clients to get suitable evidence. HMRC must be satisfied that you didn't have to operate PAYE on their payments.

You must keep the records in the form that suits you best for at least 3 years after the end of the tax year that they relate to.

Personal service companies

One-person limited companies, or personal service companies, that only supply a client with 1 worker don't have to send reports to HMRC.

If the worker is supplied through an intermediary they will be included in the return of the intermediary that has the contract with the end client.

If a personal service company supplies more than 1 worker, including any subcontracted workers, it will be acting as an intermediary and will have to send reports for each reporting period.

Contributed by Tony Jenkins

Partnership difficulties (Lecture B896 – 10.00 minutes)

Tax penalty issues can arise for partners in unincorporated partnerships particularly those who have left the firm

The ex-partner typically leaves with a potential final liability for tax BUT is unable to settle matters with HMRC until and unless he is provided – possibly several months later – with details of his tax adjusted share of partnership profits for the accounting period during which he left.

In *Gorman v HMRC (2011) UKFTT 818 (TC),* Mr. Gorman left a partnership in August 2009. The partnership had a final deadline of 31 January 2011 for submission of the 2009/10 tax to HMRC.

What then is the position if the firm is late in filing the partnership return, which is what happened in the case of Gorman . This produces fixed penalties for every partner irrespective of the fact that he or she left before the end of the tax year.

s93A(2) TMA 1970 states “*Each relevant partner shall be liable to a penalty which shall be £100 “* and s93A (8) goes on to state *“relevant partner” means a person who was a partner at any time during the period in respect of which the return was required.*

As to penalties, schedule 55 FA 2009 states : "*Where the representative partner(or successor)fails to make a partnership return, a penalty in respect of the failure is payable by every relevant partner*"...and.... " *an appeal in connection with a penalty ....may be brought only by the representative partner*"

When Gorman’s case was heard at the First Tier Tribunal, he argued that he had a reasonable excuse for the late return on that grounds that he had junior status with no control over the actions of the nominated partner , and also that he was no longer with the firm at the time the return was required to be filed

His appeal was dismissed, with the Tribunal taking a strict interpretation of TMA 1970

The issue of whether a partner other than the nominated partner has a right of appeal over late-filing penalties was again examined in *Dyson v HMRC TC 04336 2015.*

Dyson and Walker formed a partnership while at university together, notifying HMRC of commencement, with Walker as nominated partner. The partnership ran for a year at a small profit.

The partnership return for 2012-13 was filed on paper on 21 May 2014,after which HMRC issued to each partner penalties of two amounts of £100 for missing the filing deadline, £900 for daily failings and £300 for being over six months late.

D sought to appeal the second and third of these.

HMRC argued that he had no right of appeal. D claimed that he had a reasonable excuse in that he had done all that he could reasonably be expected to ensure W filed the partnership return on time.

Were W to appeal the penalties, it would be treated as an appeal in connection with every penalty payable in respect of the same failure (para 25(5) sch 55 FA 2009).

The Tribunal Judge ruled that she was unable to hear the appeal from a non-nominated partner and was also unable to construe the law in a way which gave rights under the European Convention on Human Rights. His appeal failed.

Importance of the nominated partner

The Gorman and Dyson cases confirm the essential role of the nominated partner

New partnerships registration forms (SA400, SA401 and SA402) now include a requirement to provide details of the name and address of the nominated partner on form SA400,but this covers partnerships which commence from late 2010 onwards.

For partnerships which commenced before that date, practitioners should make note of HMRC's updated guidance (January 2015) in the Self-Assessment Manual at SAM 101290

It is clear from the guidance that, in future, HMRC may look more closely on the information supplied to them regarding the identity of the nominated partner.

Historically they have usually accepted the signatory to the partnership return as the nominated partner but it would be a mistake to assume that this will continue as previously. The signed partnership return could indeed in future be rejected for want of the correct stated signatory, bringing with it potential problems for penalties and an extended enquiry window.

Who is the nominated partner?

In the case of a pre 2010 partnership, in the absence of a nomination HMRC have the authority to nominate one of the partners, so where HMRC have not formally recorded the nominated partner it will be best practice to ensure they are advised accordingly.

It would be good practice to ensure that the identity of the nominated partner is stated in the partnership agreement and notified to all partners, both current and future.

Final thoughts

The Office of Tax Simplification, in their interim report on partnerships published in January 2014, commented 'If the representative partner does not appeal – perhaps because they know there are no grounds for a 'reasonable excuse' defence, individual partners cannot appeal even if they believe they have a reasonable excuse in their own circumstances. This can cause significant unfairness'

The views of the OTS were noted by HMRC in its "HMRC penalties : a discussion document" issued in February 2015 and it may be the case that future legislation addresses this problem

Contributed by Brian Ogilvie

ECAs and zero-emission goods vehicles (Lecture B897 – 4.21 minutes)

100% ECAs for capital expenditure on zero-emission goods vehicles (ie. those powered entirely by electricity or by a hydrogen fuel cell) were first introduced in F(No3)A 2010 – see S45DA CAA 2001. The scheme, in HMRC's words, 'is one of a number of measures designed to help businesses reduce their CO2 emissions and to encourage a shift to cleaner goods vehicles'. This relief was originally due to terminate on 31 March 2015 (for corporation tax) and on 5 April 2015 (for income tax). However, the Chancellor announced on 19 March 2014 that the 100% regime would be extended for a further three years, ie. until 31 March 2018 for companies and 5 April 2018 for unincorporated businesses. Indeed, S64 FA 2014 gave the Treasury the power to extend by Treasury Order the duration of this ECA scheme along with three others.

It is therefore interesting to see that S45 FA 2015 specifically includes a statutory provision to prolong the lifespan of 100% ECAs for the purchase of zero-emission goods vehicles.

Presumably, the reason for this is because that section contains additional conditions which must now be satisfied before the relief can be claimed. The effect of these new conditions is that a 100% ECA is not available or, if given, will be withdrawn where qualifying expenditure has been incurred:

- on or after 1 (or 6) April 2015 and a State aid grant is received on or after 1 (or 6) April 2015;
- before 1 (or 6) April 2015 and a State aid grant is received on or after 1 (or 6) April 2015; or
- on or after 1 (or 6) April 2015 and a State aid grant is received before 1 (or 6) April 2015.

In essence, the business has to make a decision whether to claim the 100% ECA or to receive a grant (or other payment) which ranks as a State aid. It is not possible to have both.

Contributed by Robert Jamieson

Loan relationships and late paid interest (Lecture B898 – 9.42 minutes)

On 20 March 2013, the Government announced a review of the corporation tax rules governing loan relationships. There was consultation on a wide-ranging package of measures to update and simplify this regime and also to reduce its susceptibility to tax avoidance. S25 FA 2015 has been introduced as a forerunner of wider changes which are expected to be included in a later Finance Act.

The 'late paid interest' rules were originally brought in as an anti-avoidance measure in 1996 to prevent mismatches between the timing of relief for interest in debtor companies and its taxation in the hands of the creditor. Interest will normally be accrued in the accounts of the company which is due to pay it (and so is allowed for corporation tax), even though it may not be paid to the recipient and taxed until much later. Accordingly, Ss372 – 379 CTA 2009 set out four separate scenarios involving loans from 'connected' companies where the interest accrued in the accounts is paid more than 12 months after the end of that accounting period.

If this is the case, the interest is only allowable in the accounting period in which it is actually paid, ie. the accruals basis does not apply.

The four scenarios referred to above are where:

1. the two companies are connected under S466 CTA 2009 (S374 CTA 2009);

2. the creditor is a participator in a close company (S375 CTA 2009);

3. one of the parties has a 'major interest' – see S473 CTA 2009 – in the other (S377 CTA 2009);

4. the loan is made by the trustees of an occupational pension scheme (S378 CTA 2009).

However, FA 2009 significantly limited the scope of these late interest rules when they were found to be incompatible with EU law. As a result, Ss374 and 377 CTA 2009 have only applied in fairly restricted circumstances for the last six years.

The main form of interest to be caught nowadays is where it is payable to a creditor who is resident in a 'non-qualifying' territory (this effectively means a tax haven). Following FA 2009, companies have generally been able to obtain relief on an accruals basis on all interest payable to UK and overseas group members and affiliates (irrespective of when the interest is actually paid).

In recent years, these rules have been regularly used by some groups to, in the words of HMRC, 'manage and manipulate the emergence of profits and losses'. Loss relief legislation permits excess amounts (including trading losses and non-trading loan relationship deficits) to be set against a company's other profits of the same period or surrendered to other group companies on a current year basis. A carry-back facility is also available. All these rules provide immediate relief. However, if trading losses or non-trading loan relationship deficits are not used in any of these ways, they can only be carried forward until such time as the company in which they arose is able to set them against future profits from the same source.

For this reason, groups utilising structures which have companies in 'non-qualifying' territories have been in the habit of deliberately deferring payment of interest so that losses can be timed to arise in accordance with profits elsewhere in the group which can then absorb them. This effectively sidesteps the intention behind the group relief rules, namely that relief should only be available for in-year losses and other items. Nor does it accord with the anti-avoidance intention of the late paid interest legislation discussed above.

Accordingly, S25(6) FA 2015 repeals Ss374 and 377 CTA 2009 in relation to loans entered into on or after 3 December 2014. For loans which started before 3 December 2014, the original legislation will continue to apply in respect of interest accruing up to 31 December 2015. However, where material changes are made to an existing loan between 3 December 2014 and 31 December 2015 (inclusive), the repeal will have effect from the date of the change (S25(10) FA 2015).

Contributed by Robert Jamieson

Corporation tax – loss refresh prevention (Lecture B899 – 15.19 minutes)

The Government have introduced new legislation in S33 and Sch 3 FA 2015 in order to, in the words of HM Treasury, 'counteract the advantage for companies of entering into contrived arrangements to circumvent the:

- carry-forward rules . . . which limit the way in which relief can be given; and
- group relief rules in Part 5 of CTA 2010 which only allow relief to be surrendered by a group company against profits arising in the same overlapping period, and not the surrender of relief that has been carried forward'.

What is being attacked are certain tax-motivated arrangements under which companies seek to 'refresh' accumulated tax losses brought forward by effectively converting them into current year deductions. These typically involve the creation of both taxable profits (which can be eliminated by brought forward losses) and current year tax-deductible amounts which are offset against other profits in the company concerned or in related group companies. Many of these arrangements were loans. An illustration of the type of tax planning at which Sch 3 FA 2015 is aimed is set out in (e) below.

The new rule catches brought forward:

- trading losses;
- non-trading loan relationship deficits; and
- management expenses (S730F CTA 2010 (as inserted by Para 1 Sch 3 FA 2015)).

Specifically, the regime will apply where:

- a company has profits arising as a result of arrangements against which it can offset accumulated losses or other amounts;
- the arrangements give rise to tax deductions in the company or in a connected company;
- the main purpose, or one of the main purposes, of the arrangements is to secure a corporation tax advantage involving the creation of allowable tax deductions and the offset of brought forward amounts against profits; and
- it would have been reasonable to assume that, when the arrangements were entered into, the resulting tax benefits of the arrangements for the companies (taken together) would be greater than any non-tax benefits for those same persons (S730G CTA 2010 (as inserted by Para 1 Sch 3 FA 2015)).

In these circumstances, the brought forward amounts are disallowed.

Illustration

Lawrence Industries Ltd is part of a large group and has existing intra-group borrowing which it entered into for commercial reasons.

The company also has a substantial non-trading loan relationship deficit brought forward which it has no realistic prospect of absorbing in the foreseeable future. The group therefore changes its funding structure to accelerate the recognition of non-trading credits in Lawrence Industries Ltd so as to utilise the brought forward deficit and create a replacement deficit which can be used more flexibly. This could be achieved by Lawrence Industries Ltd's existing loan is replaced by another loan from a fellow group member which is interest-free. In all other respects, the terms of this new loan are the same as the original loan.

Under GAAP, the new loan is recognised at a discounted value. For example, if it has a face value of £10,000,000, it will be recognised as a loan of £9,500,000, being the present value of the company's obligation to repay £10,000,000 in, say, two years' time. The value of this loan then gradually grows to £10,000,000 over the term of the instrument.

Lawrence Industries Ltd claims that the excess of £500,000 on inception (cash received of £10,000,000 less the value of the debt recognised at £9,500,000) is an upfront taxable credit, to be covered by the deficit brought forward.

The company also claims that the accretion of the loan back to £10,000,000 gives rise to a tax deduction of £500,000 over the life of the loan. This £500,000 will be surrendered to other members of the group as group relief. Thus a brought forward amount has been converted into a fresh current year deduction.

From an overall group perspective, there is no economic benefit to this planning. The arrangement is, in HMRC's words, 'wholly designed to use up old losses and create new ones'. The provisions of Sch 3 FA 2015 will therefore be invoked.

This measure has effect for accounting periods beginning on or after 18 March 2015 (Para 4(1) Sch 3 FA 2015). Any profits of a company with an accounting period straddling 18 March 2015 need to be allocated into notional periods falling either side of that date and the rules then apply to the period commencing on 18 March 2015 – this apportionment should be done on a time basis, unless that would give rise to an unfair result in which case some other 'just and reasonable' basis should be used (Para 4(2) and (3) Sch 3 FA 2015).

Sch 3 FA 2015 is presented as anti-avoidance legislation aimed at 'contrived' arrangements. However, the rule could also prevent companies from being able to gain effective relief for tax losses which arose in genuine commercial circumstances, given that it focuses on the way in which the losses are used rather than the manner of their creation. Note that HMRC have indicated that it is not targeted at 'simple' arrangements such as shifting a profitable trade or an income-producing asset into a company with accumulated tax losses.

In some instances such as those where the arrangements do not involve any newly created tax-deductible amounts, it should be relatively straightforward for taxpayers (and their advisers) to conclude that the rule does not apply. However, in the case of more complex arrangements involving new tax deductions and groups of companies, there will be a need for companies to address the more difficult question of 'main purpose' as well as comparisons of tax values with non-tax values at a group level.

There is also an element of retrospection in Sch 3 FA 2015. It is clear that the legislation can apply to arrangements which were entered into several years ago but which are still giving rise to profits and deductible amounts.

Contributed by Robert Jamieson

VAT

Compound interest on VAT wrongly paid

Summary - The Court of Appeal found that Littlewoods was entitled to compound interest on VAT wrongly paid.

Littlewoods had paid VAT which was not due. HMRC had repaid the principal amount together with simple interest. Littlewoods claimed that it was also entitled to compound interest.

There were four issues:

1. **Were Littlewoods' restitution claims excluded by VATA 1994 ss 78 and 80 as a matter of English law and without reference to EU Law?** The Court of Appeal found that the net effect of the provisions was that the only cause of action available to the taxpayer for the repayment of the principal sums was that afforded by s 80(1) and so restitutionary claims for repayment of VAT were barred by s 80(7). Furthermore, s 78(1) excluded common law claims for interest.

2. **Did the exclusion of the claim by VATA 1994 violate the principle of effectiveness by depriving Littlewoods of an adequate indemnity for the loss occasioned through the undue payment of VAT?** The Court of Appeal noted that 'adequate indemnity' was not a rigid 'straitjacket' which required compound interest in every case. However, s 78 did deprive Littlewoods of an adequate indemnity.

3. Sections 78 and 80 could not be construed so as to conform with EU law because the exclusion of common law claims for interest was a cardinal feature of the legislation. The provisions must therefore be disapplied. Furthermore, the Court of Appeal did not have the power to disapply the domestic bar to the enforcement of Littlewoods' rights on a selective basis. The choice of remedy therefore belonged to Littlewoods which chose to make a mistake-based restitution claim because this was not time-barred, whereas a *Woolwich* claim would have been.

4. Finally, on quantum, the Court of Appeal found that HMRC should not be treated as if it were an involuntary recipient of overpayments of tax. Consequently, 'objective use value' applied to the valuation of the time value of the overpayments made to HMRC and compound interest was payable. Finally, interest should continue to run after the date of the repayment of the principal amounts of overpaid VAT on such amounts of accrued interest as remained outstanding.

Comments - This is the latest instalment of a judicial saga which includes two High Court decisions and a preliminary ruling by the CJEU. The tax at stake is colossal: £1.2bn in compound interest. HMRC has said it will seek leave to appeal.

Littlewoods and others v HMRC [2015] EWCA Civ 515

VAT challenges for a newly registered business (Lecture B900 – 16.47 minutes)

Challenge 1 – how much input tax can be claimed on pre-registration expenses?

A welcome opportunity for a newly registered business is to be able to claim input tax on certain pre-registration expenses:

- **Goods** – which have been purchased within the four year period before the date of registration, which have been used in the business during that time, and are still owned by the business on its first day in the VAT club. The definition of 'goods' includes both stock and fixed assets.

- **Services** – the time window is capped at six months before registration, and the service cannot relate to a sale that has been invoiced before registration.

Here are three examples of incorrect input tax claims within the above rules:

1. A friend of mine started his business on 1 January this year and immediately became VAT registered – but he could not claim input tax on the laptop and other computer equipment bought in the previous four years as they did not relate to his business at the time of purchase because there was no business. In other words, private expenditure cannot be turned into business expenditure at a future date.

2. A computer consultant claimed input tax on the cost of subcontractor fees incurred in the six month period before registration, which would normally be fine. However, the problem was that the services in question related to completed jobs which he had invoiced before he became registered. If you think about it logically, this is fair because HMRC will not be getting output tax on these jobs so it is a bit cheeky expecting them to allow input tax to be claimed by the business in question.

3. A hairdresser setting up a new business and spending a large sum of money on fitting out her salon will need to recognise that a lot of the expenditure will relate to capital building services rather than goods ie where the six month window is relevant rather than four years. There is no problem with input tax recovery using the four year window on actual physical items such as hairdryers and chairs but definitely an issue with spending on eg decorating, electrical and plumbing works.

Note – as a planning point, don't forget that a business such as the hairdresser in the final situation can register for VAT as soon as it has an 'intention' to make taxable supplies ie which is likely to be the date when the business owner signs the lease/rental agreement with the landlord and therefore knows that it has a clear trading plan. A VAT registration from the first day of business activity avoids any challenges with the pre-registration rules.

Pre-incorporation expenditure

It is obvious to state that a limited company cannot register for VAT or incur expenditure until it is formally incorporated. So what is the situation in relation to goods or services that may have been supplied to the employees setting up the company before incorporation?

The good news is that a company can claim input tax on such expenses on its first VAT return if the tax relates directly to the business to be carried on by it following incorporation and VAT registration. The six-month and four year windows apply in exactly the same way as considered earlier. The key condition is that the expense must have been purchased with the intention of making taxable supplies ie it was not a private purchase made by an employee who is now transferring the asset to the incorporated business.

Challenge 2……..voluntary registration?

Looking again at the first two situations in the previous section, there is a potential opportunity to avoid an input tax problem, which is to apply for a retrospective VAT registration. However, this can only be done at the time the first VAT1 form is submitted to HMRC – it is no good asking for a particular date of registration and then, after it has been given as requested by HMRC, to try and get it adjusted in the future.

A business that has never needed to register on a compulsory basis (ie annual taxable sales have never exceeded the registration threshold on any rolling 12-month basis) has the right to choose its date of VAT registration going back up to four years. So if today is 1 July 2015, I can ask for a date as far back as 1 July 2011. And for our computer consultant, that means he could then issue VAT only invoices to his customers for historic jobs (hopefully they are all VAT registered and able to recover input tax), therefore allowing him to claim input tax on his costs. And for the hairdressing salon, it can ensure that the date of registration is timed so that no purchase invoice is dated more than six months before its registration date and therefore the goods v services dilemma becomes irrelevant.

Challenge 3 …..what about the flat rate scheme?

There are a number of planning points with the scheme:

- A business can claim a 1% discount on its relevant flat rate percentage in the first year of VAT registration.
- A business using the scheme for its first VAT period can claim pre-registration input tax on this return in the same way as a non-scheme user ie four years for goods and six months for services as considered above. This is the only time a scheme user can claim input tax other than when it buys capital goods costing more than £2,000 including VAT.

There is sometimes a misunderstanding among advisers that the 1% discount can be claimed by a business in its first year of using the scheme. This is incorrect – it is only in the first year of VAT registration. And if a business joins the scheme part way through its first year in the VAT club, then it gets the 1% discount for the balance of the first year period that remains.

Example

John became VAT registered on 1 January 2015 and he joined the flat rate scheme at the beginning of his third VAT period ie 1 July 2015. He can apply a flat rate percentage of 13.5% for his next two returns ie until 31 December 2015, and a rate of 14.5% will then take effect from 1 January 2016.

Contributed by Neil Warren

Date of taxable sales

Summary – The First-tier Tribunal agreed with HMRC that the key date for the taxpayer's supply of services was 1996

The taxpayer, a property consultant, registered for VAT as a sole trader in March 2011 with expected sales of £75,000 in the next 12 months.

He claimed input tax on legal fees incurred in litigation against Manhattan Loft Corporation Ltd (MLCL). The dispute began in 1996 and concerned a finder's fee to which the taxpayer believed he was entitled for finding a site at St Pancras Station for the refurbished St Pancras Hotel.

HMRC disallowed the claims because the costs were not relevant to his VAT-registered business. The taxpayer argued that, if he was successful in his legal action, the fees received would be above the VAT registration threshold, and require an output tax declaration, giving him the basis for an input tax claim. HMRC maintained that the taxpayer was not a taxable person at the time the alleged agreement with MLCL was made in 1996, and there was no entitlement to an input tax claim on the costs now being incurred.

Decision:

Although the legal fees were supplied when he was registered for VAT, they were incurred in his attempt to enforce an agreement made in 1996. HMRC were correct to disallow the input tax claim.

The taxpayer's appeal was dismissed.

Comments - Neil Warren, independent VAT consultant, said: “A key challenge with input tax is to find a 'direct and immediate link' between an expense and an onward supply that is taxable. Advisers often take the view that input tax can be claimed on all expenses when a business is registered for VAT, apart from non-deductible input tax on, say, business entertaining, but this is not always the case. The link with a taxable supply must be clearly established.”

CD Lissack v HMRC TC4334

Written approval required

Summary – Approval to use an apportionment scheme by a business had to be in writing

A seaside café offered eat-in and takeaway meals. It submitted VAT returns on the basis that its standard-rated sales were 30% of turnover.

After several invigilation visits, HMRC concluded that the percentage should be 90%. They issued an assessment for £28,963, covering a four-year period under VATA 1994, s 73. This gave HMRC the power to assess tax on the basis of “best judgment” if they considered a return was incomplete.

The taxpayer appealed on the basis that HMRC had approved the use of an apportionment scheme based on the percentage of standard-rated purchase invoices during a telephone conversation in 2004.

HMRC said approval to use an apportionment scheme had to be in writing. This had not been done so the taxpayer was not entitled to operate one. In any event, the business did not meet the conditions to use such a scheme outlined in *VAT Notice 727*. A catering adaption scheme could have been applied for but there was no evidence of this having happened.

Decision:

The tribunal upheld the assessment and dismissed the taxpayer's appeal.

Comments - Neil Warren, independent VAT consultant, said: “The warning from this case is that, even though a business submits low payment returns for a number of years, getting a good result in the process, HMRC will issue an assessment covering a four-year period if and when they identify a problem. It would be very unusual for a café with seating for 30 people to have only 30% standard-rated sales.

McDonald and McDevitt trading as The Picnic Basket v HMRC TC4333

Free supplies to staff taxable

Summary - The FTT found that free supplies of clothes to staff were taxable.

French Connection provided staff members with a clothing allowance for each season to enable them to choose items from the company's stock, which they must wear when working. It appealed against HMRC's decision that the provision of clothing to staff was a taxable supply under VATA 1994 Sch 4 para 5, which treats the disposal of 'goods forming part of the assets of a business' as a supply of goods.

The FTT rejected arguments that art 16 of the Principal VAT Directive pointed to an exemption from the above charge in circumstances where the goods were provided for the purpose of the business. The FTT added that whether or not the clothes were uniforms, the passing of their ownership to staff was a supply of goods. In any event, the clothing did not identify the staff and the fact that it was worn by staff as 'brand ambassadors' did not make it a uniform. However, the FTT accepted that, in circumstances where the allowance had been less than £50 per year, the 'business gifts' exemption applied.

Finally, the value of the supplies should be assessed at the time that the clothes were provided to staff and by reference to the cost of replacement to French Connection. The conditions under which the staff must take the clothing were irrelevant to the cost to French Connection.

Comments - This case provides a rare example of a supply made for no consideration, which is nonetheless taxable, regardless of its purpose.

French Connection v HMRC [2015] UKFTT 173

Private college entitled to education exemption

Summary - The FTT found that some of the courses provided by Bell's fell within the education exemption.

Bell's was a private college approved to offer Education Development International qualifications. It offered vocational courses such as English for Speakers of Other Languages (ESOL), painting and plumbing.

Decision:

The FTT found that Bell's was not a 'school' providing 'secondary education' by reference to the definition in the Education Act 1996. The FTT noted that the fact that the college offered work placements to under 16s did not make it a 'school'. Furthermore, the courses offered by the college were either part time or too specialised to constitute 'education'.

Bell's was not a 'college or university' either, as it was not integrated by any university. The arrangements it had with several universities which ensured that its students obtained credits for courses attended at Bell's were not sufficient. The legislation required a substantial level of integration with one particular university. Finally, Bell's did not teach university type courses, but rather provided a pathway to getting onto degree courses.

The FTT found, however, that Bell's taught English as a foreign language even though some of its students already had a basic command of it. Part of its supplies were therefore exempt (VATA 1994 Sch 9 Group 6 note 1(f)).

Comments - Although Bell's was neither a school nor a university, some of its courses fell within the VAT exemption.

Bell's College v HMRC [2015] UKFTT 176

Was an amendment to a repayment claim a new claim?

Summary - The FTT found that the amendment of a repayment claim to add subsequent accounting periods was a new claim and was therefore out of time.

The issue was the admissibility of a claim for repayment for the period 1 October 2007 to 30 September 2013, made by a letter dated 30 January 2014. HMRC applied to strike out the claim on the ground that it was made out of time.

Nairn had lodged a claim on time in 2009, covering the periods from April 1991 to December 1996 and from October 2005 to September 2007. It contended that the 2014 claim was not a new claim.

Decision:

The FTT noted, however, that the 2009 claim dealt only with the periods up until 2007, as any claim must be linked to 'prescribed accounting periods' (VAT Regulations, SI 1995/2518, regs 35 and 37). The FTT accepted that the 'core subject matter' of both the 2009 and 2014 claims was the question of green fees and that the relevant legislation was the same in both cases. However, as the claims related to completely different accounting periods, the appeal fell within the parameters of *Reed 1* [2011] UKFTT 200; and following *Hadley Wood Golf Club* TC02014 05589, the 2014 claim was a new claim.

Finally, the fact that the 2009 claim had been sisted (meaning that proceedings were suspended), pending the outcome of litigation in the CJEU, did not affect the time limits applicable to subsequent claims.

Comments - This case clarifies the distinction between the extension of an existing claim and the submission of a new claim. In doing so, it confirms that delays in relation to a claim do not mean that it can be extended to cover subsequent accounting periods.

Nairn Golf Club v HMRC [2015] UKFTT 185

VAT wrongly paid and the rights of the consumer

Summary - The High Court found that a repayment of VAT to a supplier who had wrongly invoiced it would amount to the unjust enrichment of the supplier (VATA 1994 s 80(3)).

QCL, a supplier of Premier Foods, had invoiced VAT in error. Premier Foods had no statutory right to claim the VAT back from HMRC as only QCL had that right (VATA 1994 s 80). QCL had gone into administration so that a civil claim against it would not provide Premier Foods with an effective remedy.

Premier Foods contended that, in order to rectify the situation, HMRC should refuse to repay QCL unless QCL undertook to reimburse the full amount of the repayment to Premier Foods. If QCL refused, the VAT should be repaid directly to Premier Foods. HMRC proposed, however, to repay the VAT to QCL and to enforce assessments against Premier Foods for the input tax which it had deducted.

Decision:

The High Court observed that *Reemtsma* [2008] STC 3448 establishes that the customer who ultimately bears the burden of the VAT has a right under EU law to recover the full amount of the mistakenly paid VAT directly from HMRC. The fact that Premier Foods would be able to recover only a portion of the VAT from QCL was therefore critical. The concept of unjust enrichment and the *Reemtsma* principle provided the machinery to ensure fiscal neutrality and the mechanism to enable the monies to be paid to Premier Foods. The input tax assessments against Premier Foods must therefore be quashed.

Comments - The confirmation that the bearer of the burden of the VAT has a direct right to repayment of VAT wrongly paid may be relevant to many taxpayers.

The Queen on the application of Premier Foods (Holdings) v HMRC [2015] EWHC 1483

Did the BBC supply education services?

Summary - The UT found that the BBC was an organisation 'defined' by the UK as having similar objects to those of a university (Sixth Directive art 13A1(i)) so that its services were exempt.

The issue was whether the supply by the BBC of production and broadcasting services to the Open University (OU) between January 1978 and July 1994 had fallen within the education exemption (VATA 1994 Sch 9 Group 6 item 4).

The question turned on the following: (1) Was the BBC a body governed by public law within the meaning of the education exemption? (2) If so, did the BBC also have the requisite educational aim? (3) Alternatively, was the BBC another organisation defined by the UK as having similar objects (Sixth Directive art 13A1(i))?

Decision:

In relation to (1), the UT observed that, once it was accepted that a body governed by public law has to form part of the public administration, the BBC could not reasonably be regarded as satisfying that condition, given that it was deliberately established with full operational and editorial independence. In relation to (2), the UT found that the extensive provision of support material by the BBC for its educational broadcasts meant that in practice the BBC provided much of the framework needed for distance learning in a way that fulfilled the educational aims which had always been central to its activities. It could not therefore be said that it merely enabled schools to provide education. Furthermore, this was a rare case where the UT could substitute its own view to that of the FTT on what appeared to be a multi-factorial evaluation of the facts. However, given that the BBC failed on (1), this was of no relevance. Finally, as to (3), the UT noted that the UK had 'defined' the BBC as having 'similar objects' by entrusting it with an education function. It was not necessary for the 'definition' to be made for the purpose of the education exemption.

Comments - The case is a reminder that the scope of the education exemption is defined not only by VATA 1994 Sch 9 Group 6 but also by the Sixth VAT Directive. It also provides an interesting example of the UT substituting its own analysis of the facts to that of the FTT.

HMRC v The Open University [2015] UKUT 263

Can VAT be imposed on both the recipient and the supplier?

Summary - The CJEU found that the Bulgarian tax authorities could not tax the same transaction twice.

GST-Sarviz, established in Germany, provided consultancy services to GST Skafolding, established in Bulgaria. On the basis that GST-Sarviz did not have a fixed establishment in Bulgaria, GST Skafolding paid the VAT due on the supply of those services under the reverse charge procedure.

However, the Bulgarian tax authorities found that GST-Sarviz had a fixed establishment in Bulgaria and was liable for the VAT. They also refused to refund the VAT paid by GST Skafolding, because it did not have the required document.

Decision:

The CJEU observed that, under the VAT Directive, only the supplier of services is, in principle, liable for the payment of VAT, except where the supplier is not established in the member state in which the VAT is due and the state has adopted the reverse charge procedure. The Bulgarian tax authorities had found that GST-Sarviz had a fixed establishment in Bulgaria; it was therefore the only person liable.

The fact that GST Skafolding had paid the VAT on the mistaken assumption that GST-Sarviz did not have a fixed establishment in Bulgaria did not authorise the tax authorities to derogate from that rule.

Finally, the refusal to refund the VAT meant that the supplier effectively bore the fiscal burden of the tax, as it could not claim payment from the recipient. As the risk of loss of revenue was eliminated, such refusal was contrary to the principle of fiscal neutrality.

Comments - This was an unusual case, in that the Bulgarian tax authorities effectively sought to tax the same transaction twice. The CJEU found that this was in breach of the VAT Directive on several grounds.

GST-Sarviz AG Germania v Direktor na Direktsia 'Obzhalvane i danachno-osiguritelna praktika' ***(****C-111/14)*

Place of supply of manufacturing services

Summary - The CJEU found that the place of supply of manufacturing services performed in Hungary was Hungary, even though the manufactured products belonged to a UK company.

SMK, a Hungarian company, provided services as a subcontractor to its sister company established in the UK, SMK UK. SMK UK purchased the raw materials and parts and SMK assembled them to make remote controls. After assembly, the remote controls remained on the premises of SMK, while the recipient of the service, SMK UK, sold them to SMK Europe, a Belgian company, which on-sold them to customers. The products left Hungarian territory and were never transported to the UK; and SMK invoiced SMK UK for the services provided.

The issue was the place of supply of the services provided by SMK. If the general rule set out in the VAT Directive art 52 applied, the place of supply was Hungary as the services were performed there. The question was whether the derogation to the general rule set out in art 55 applied.

Decision:

The CJEU found that it did not apply, as the transport of the goods did not take place within the framework of the transaction relating to the work on the goods, but after it. The CJEU added that the fact that SMK UK was registered for VAT both in the UK and in Hungary did not affect the analysis.

Comments - The dispute took place before the rules on place of supply were completely overhauled with effect from January 2010. Under the now 'old rules', the place of supply of services was the jurisdiction in which they were performed. This case confirms that any exception to the general rule should be narrowly interpreted.

SMK kft v Nemzeti Adó- és Vámhivatal (C-97/14)

The tax on pollution and imported second-hand vehicles

Summary - the CJEU found that the imposition of a pollution tax on imported vehicles only was in breach of TFEU.

Mr Manea had sought to register in Romania a second-hand vehicle that he had purchased in Spain. The Romanian tax authority had made registration conditional upon payment of the tax on pollutant emissions. Mr Manea took the view that the tax was incompatible with TFEU art 110, on the basis that the tax applied to imported vehicles at the time of registration. The tax, however, applied to vehicles registered in Romania only at the time of the first transfer of ownership. Article 110 prohibits all member states from imposing internal taxation on products of the other member states which is in excess of that imposed on similar domestic products.

Decision:

The CJEU noted that the tax was imposed in accordance with the same calculation method: first, on second-hand motor vehicles imported from other member states upon their first registration in Romania; and, second, on motor vehicles already registered in Romania at the time of their first sale. The measure was therefore neutral in terms of competition between imported second-hand cars and domestic ones.

The CJEU found, however, that Romania had breached art 110, as the first transfers of Romanian vehicles had been exempt between 2007 and 2013. This had created an inequality of treatment between domestic second-hand vehicles and imported ones.

Comments - The CJEU confirmed that the difference in treatment favoured the sale of domestic vehicles and was therefore in breach of art 110. The CJEU added that the fact that the Romanian government would be under the obligation to reimburse the tax levied did not necessarily lead to the conclusion that the Romanian economy would be adversely affected. It was therefore not appropriate to limit the temporal effects of the judgment.

Mihai Manea v Instituția Prefectului județul Brașov (C-76/14)

Ascertaining the VAT payable in the absence of purchase price

Summary - The CJEU found that when establishing a liability to VAT by reference to the purchase price of similar goods, the tax authorities were not required to exclude certain cost components.

Prodeco had constructed a building with the intention of selling it. It therefore appeared as stock in its account and its valuation included interim interest paid under a loan agreement entered into for the purpose of constructing the building. The issue was whether the taxable amount should include the interim interest. Under the Sixth Directive art 11A(1)(b), the taxable amount was the purchase price of the goods (or of similar goods) or, in the absence of purchase price, the cost price.

Decision:

The CJEU found that the referring court had been right to hold that the relevant taxable amount was the sale price of similar buildings; that is buildings whose size, location and essential characteristics were similar to those of the building at issue. It was irrelevant whether the purchase price of similar buildings included interim interest. Unlike the cost price criterion, the purchase price of similar goods criterion did not require tax authorities to examine the components of the value.

Comments - The case clarifies the way VAT should be assessed in relation to a building which has been constructed by its owner and therefore has no purchase price. The taxable amount should be ascertained by reference to the purchase price of similar goods. It is only if such comparison is not possible that a cost price approach, which may mean excluding some cost components, will be justified.

Property Development Company NV v Belgische Staat (C-16/14)

The flat-rate taxation of investments and EU law

Summary - The CJEU found that the acquisition of units in offshore investment funds, and the receipt of dividends deriving from them, involved financial services provided by those investment funds so that their taxation came within the scope of TFEU art 64.

Between 1997 and 2003, Mrs Schweier had had an account with a Liechtenstein Bank, containing holdings in investment funds established in the Cayman Islands. Those investment funds did not comply with German statutory obligations so that flat-rate taxation applied. Mrs Schweier contended that this was contrary to TFEU art 64 (on free movement of capital).

The key issue was therefore whether art 64 meant that the relevant German legislation constituted a measure which related to the movement of capital involving the provision of financial services.

Decision:

The CJEU noted that the acquisition of units in non-resident investment funds and the receipt of the dividends deriving from them involved financial services provided by those investment funds to the investor concerned. Furthermore, the legislation, which in applying to capital movements to or from third countries restricted the provision of financial services, fell within the scope of art 64. Finally, the relevant provisions could deter resident investors from acquiring units in non-resident investment funds.

Comments - This case clarifies the scope of TFEU art 64. In doing so, it confirms that the payment of dividends by non-resident investment funds relates to the provision of financial services which is grandfathered under the standstill provisions of TFEU art 64.

Finanzamt Ulm v Ingeborg Wagner- Raith (as successor in title to Mrs Maria Schweier) (C-560/13)